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Global Economy

IMF has revised up its global growth forecasts stressing the upbeat prospects.

In US, tax reform and temporary budget bill were high on the agenda in the first half of January while, in the second half, protectionist trade policies and infrastructure investment plans came to the forefront.

The strengthening trend in the US economy and the rise in inflation expectations has led to increases in Treasury bond yields. US 10-year Treasury bond yield, which started 2018 at 2.40%, hit 2.72% on January 31st, the highest level since April 2014.

ECB did not change its monetary policy at its January meeting. At his speech after the announcement, Draghi cautioned against the risks that euro "volatility" poses. Along with the expectations that normalization process of the monetary policy could speed up, EUR/USD parity hovers around the highest levels in four years.

Inflation rate in the Euro Area remains below the target of the Central Bank's "below but close to 2% over the medium term". Economic growth in the region, on the other hand, became 2.5% in 2017 and marked the strongest performance in the last 10 years.

Economic growth in China stood at 6.9% in 2017, accelerating for the first time in seven years.

Oil prices fell during the last days of the month, owing largely to the concerns over excess supply.

Turkish Economy

Employment indicators continued to improve in October 2017 period. Seasonally adjusted unemployment rate hit its lowest level in 1.5 years, decreasing by 0.3 points to %10.3.

Calendar adjusted industrial production increased by 7% yoy in November.

Foreign trade deficit widened by 36.8% in 2017. In this period, export volume increased by 10.2% yoy and import volume surged by 17.7%. Foreign trade deficit continued to follow an upward trend in January, according to the provisional data released by Ministry of Customs and Trade.

Current account deficit expanded by 86.4% yoy in November and came in above the expectations with 4.2 billion USD. 12-month cumulative current account deficit reached its highest level in three years with 43.8 billion USD.

In 2017, budget indicators performed better than suggested in the Medium Term Plan (MTP) targets announced in October. Year-end budget posted a deficit of 47.4 billion TRY, 14.3 billion TRY lower than MTP forecast.

CPI increased by 1.02% mom in January, less than expected. Annual CPI increase continued to lose momentum in this period.

CBRT kept its interest rates unchanged at its meeting held on January 18th as markets have anticipated. The Central Banks reinforced its emphasis on maintaining tight monetary policy stance.

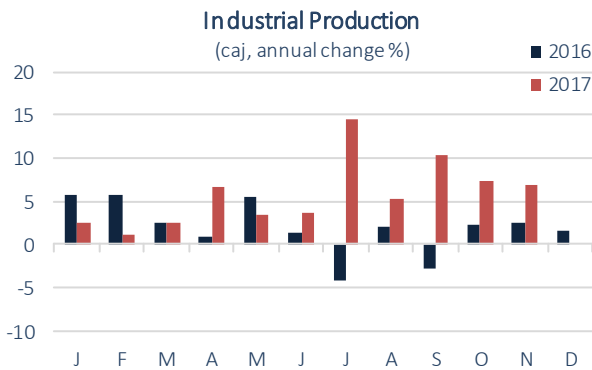
Cross-border operation, which increased its weight on the agenda since the second half of January, had a limited impact on markets.

Recovery in employment indicators continued.

Recovery in employment indicators continued in October 2017 period. Despite the rise of 1 million people in employment yoy, labor force surged up by 1.4 million people during this period. Thus, unemployment rate declined by 1.5 points yoy to 10.3%. Seasonally adjusted unemployment rate hit its lowest level in 1.5 years, decreasing by 0.3 points to %10.3. Labor force participation rate, on the other hand, declined to 53%.

Positive outlook in industrial production...

In November, calendar adjusted industrial production expanded by 7% yoy. Capital goods production showed a positive outlook for the investment demand by recording the highest annual increase among the main industrial groups by 10.9%. Production of durable consumer goods, which had lost momentum in October as the tax incentives ended, contracted in November yoy, putting pressure on industrial production. Manufacturing industry, which constituted more than 80% of industrial production, expanded by 7.1% in November. Production of motor vehicles made the highest contribution to said growth by 1.3 points. Manufacture of machinery and equipment and manufacture of wearing apparel were two other sectors that also made high contribution.



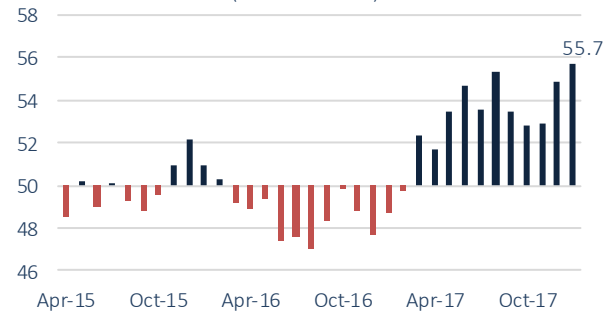
Manufacturing PMI is at its highest level in 7 years.

Having reached the highest level in January since March 2011 with 55.7, manufacturing PMI displayed a positive outlook for manufacturing sector in the first month of 2018. Rising orders from domestic and global markets was behind this higher than expected performance of manufacturing PMI. Depreciation of TL and rising raw material prices seemed to put an upward pressure on costs. However, this increase was reflected to the customers to a great extent.

Sectoral confidence indices, which followed a downward course in the second half of 2017, started 2018 with a strong increase. Services, retail trade and construction sectoral confidence indices rose by 6%, 5.6% and 6.7% in January, respectively. Analyzing the details of indices, it is seen that indicators for the last three months were improved notably, while the expectations for the next three months remained weak.

Manufacturing PMI

(benchmark=50)



House sales rose by 5.1% in 2017.

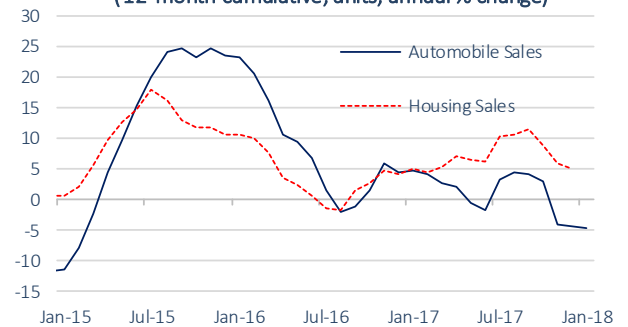
According to Turkstat data, house sales in Turkey decreased by 6.8% yoy to 132,972 in December. In this period, mortgaged house sales contracted by 30.7% while other home sales increased by 5.7%. Throughout 2017, home sales rose by 5.1% and exceeded 1.4 million. In this period, mortgage sales surged up by 5.2% and other sales expanded by 5.0%, exhibiting a balanced outlook. While house sales to foreigners increased by 22.2% last year, Iraqi citizens were the main customers.

Weak outlook for house sales was also reflected in prices. As of November, the annual rise in house prices in Turkey hovered close to the bottom level of 6 years with 11.3%. In Istanbul, the largest housing market, house prices increased by 7.4%, staying below the Turkey average.

Domestic automotive sales also lost momentum in the recent period. In 2017, total automotive market contracted by 2.8% to 956,194 units due to the decline in automobile sales. During this period, automobile sales decreased by 4.5% yoy while light commercial vehicle sales increased by 2.9%. The data for the first month of 2018 also indicated a loss of strength in the sector. In January, automobile sales decreased by 3.6% yoy while light commercial vehicle sales contracted by 12.1%. According to the Automotive Distributors' Association estimates, in 2018 automotive sales will hover around the band of 925-975 thousand units.

Domestic Automobile and Housing Sales

(12-month cumulative, units, annual % change)

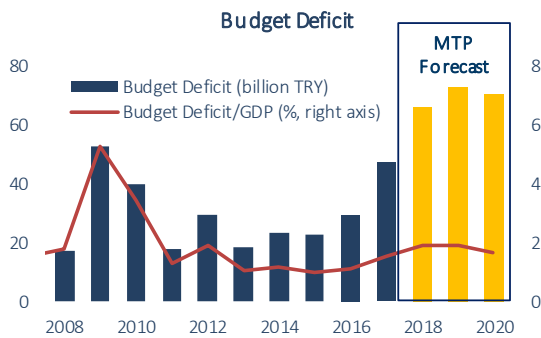


Source: Datastream, Markit, Turkstat, ODD

Budget deficit was below MTP estimates in 2017.

In 2017, [budget indicators](#) performed better than the Medium Term Plan (MTP) targets announced in October. Budget revenues exceeded MTP target by 18.3 billion TRY while budget deficit, which came in 47.4 billion TRY in 2017, was 14.3 billion TRY below the MTP's year-end forecast.

Finance Minister Naci Ağbal stated that they expected the budget deficit to GDP ratio, which is expected to be 2% under the MTP projections, to be 1.5%. The ratio was 1.1% in 2016. We do not expect any significant deterioration in budget indicators in the upcoming period. We anticipate that budget deficit/GDP ratio will remain at around 2% by the end of 2018.



Foreign trade deficit surged by 36.8% in 2017.

The widening trend in [foreign trade deficit](#) continued in December. Thus, annual expansion in foreign trade deficit was 36.8% in this period. Sharp increase in oil prices, the course of gold trade and increasing domestic economic activity led to a steep surge in imports. On the other hand, strong global demand, largely attributable to the recovery in economic activity in European countries, had supported our export performance in 2017.

	December		Δ (%)	Jan.- Dec.		Δ (%)
	2016	2017		2016	2017	
Exports	12.8	13.9	8.6	142.5	157.1	10.2
Imports	18.4	23.1	25.4	198.6	233.8	17.7
Foreign Trade Deficit	-5.6	-9.2	63.5	-56.1	-76.7	36.8
Import Coverage (%)	69.4	60.1	-	71.8	67.2	-

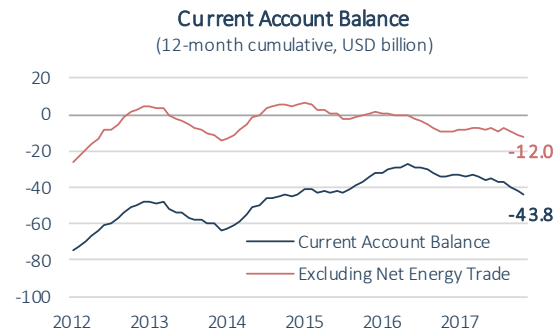
According to the provisional foreign trade data released by the Ministry of Customs and Trade, the foreign trade deficit widened in January by 109% yoy. In this period, exports and imports increased by 10.8% yoy and 38% yoy, respectively. In terms of exports, motor vehicles, boilers-machineries and iron-steel sectors outshined as in 2017, while gold imports kept its pace.

Current account deficit came in above expectations.

In November, [current account deficit](#) came in above expectations at 4.2 billion USD, posting an annual

increase of 86.4%. The rapid increase in oil prices put upward pressure on the deficit during this period. Even though gold imports have lost some steam in November compared to previous months, net gold imports also drove the current account deficit up.

In January-November period, the current account deficit expanded by 37.5% yoy to 39.4 billion USD. 12-month cumulative current account deficit reached its highest level in three years with 43.8 billion USD in November. The deficit excluding net energy trade became 12 billion USD in this period.



CPI was realized below the expectations.

In January, [CPI](#) increased below the market expectations by 1.02% on a monthly basis. Monthly increase in D-PPI was realized as 0.99%. Due to the high-base effect, annual CPI inflation decreased to 10.35%, in parallel with expectations. In the first month of 2018, annual increase in D-PPI, which declined considerably compared to December 2017 to its lowest level for more than a year, was realized as 12.14%.

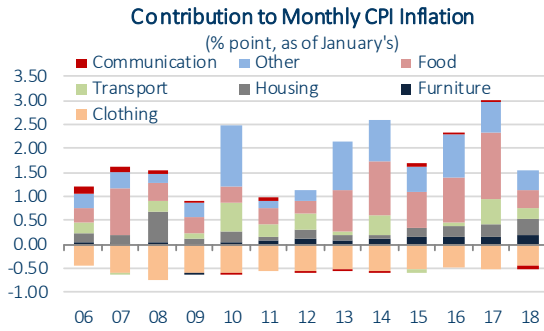
January (change %)	CPI		D-PPI	
	2017	2018	2017	2018
Monthly	2.46	1.02	3.98	0.99
Annual	9.22	10.35	13.69	12.14
Annual Average	7.76	11.23	4.96	15.66

Clothing and footwear prices limited the rise in CPI.

Food and non-alcoholic beverage group, which has the biggest share in CPI basket, made the highest contribution by 38 basis points to the monthly increase in CPI. Rise in electricity fee as well as bridge and highway tolls were effective in the CPI increase. Thanks to the seasonal factors, clothing and footwear group recorded a decrease of 6.02%, limiting the monthly CPI increase by 43 basis points.

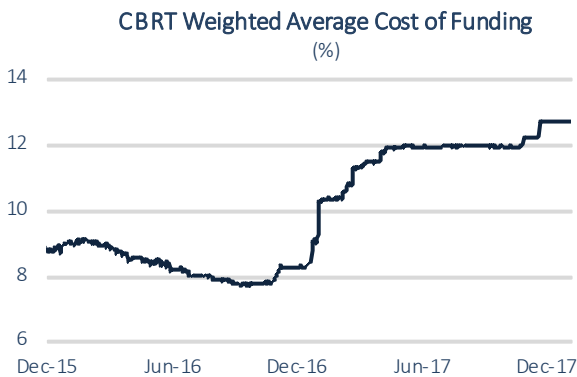
We anticipate that recent trend in annual consumer inflation, which declined in January, will continue through the rest of the first quarter. In this context, we expect CPI to increase by 0.6% in February mom.

Source: Turkstat, Datastream, CBRT, Ministry of Customs and Trade



CBRT kept the policy rates unchanged.

At its meeting on January 18th, CBRT did not change interest rates in line with expectations. Accordingly, policy rate was held at 8% and upper and lower limits of interest rate corridor were kept as 7.25% and 9.25%, respectively. In the statement released following the meeting, it was pointed out that domestic demand continued to expand and economic activity maintained its strength. Also, it was stated that external demand contributed positively to the growth. On the other hand, elevated levels of inflation indicators were highlighted. CBRT suggested that tight stance in monetary policy will be maintained until inflation outlook displays significant improvement independent of base effects and temporary factors. The Committee also reiterated that further monetary tightening will be delivered if needed.



CBRT increased its inflation forecasts.

Central Bank revised its inflation forecasts upward in the first Inflation Report of 2018 published on January 30th. Accordingly, CBRT increased its inflation forecast for 2018 by 0.9 percentage points compared to the October report to 7.9%. The revisions reflected a higher projection for TRY-denominated import prices and further improvement in economic activity as well as the recent rise in the main trend of inflation. For 2019, inflation forecast was increased to 6.5% from 6%. CBRT suggested that, together with a momentum loss in economic activity and deceleration in credit growth, a macro policy framework according to which taxes and administered prices are set consistently with the Medium-Term Program will support the disinflation process.

Decree on non-financial companies' use of foreign exchange loans...

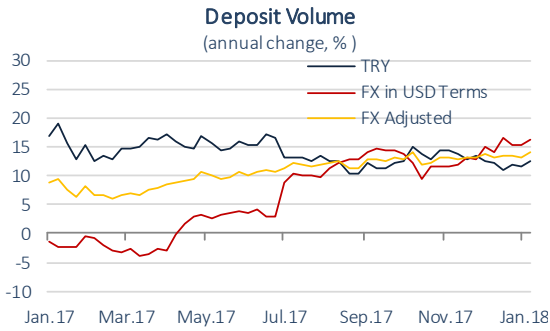
In order to manage the FX position of the real sector, the terms of use for foreign currency loans were tightened. According to the new provisions, companies with less than 15 million USD foreign currency denominated liabilities could borrow only as much as their FX revenues of the last three years. The legislation offers a number of exceptions. Public institutions, banks, domestic leasing and factoring companies, and residents with foreign currency loans equal or higher than 15 million USD are kept out of the scope of this legislation. In addition, the lower limit for FX loans imposed on companies with no foreign exchange earnings was raised from 5 million USD to 15 million USD. This legislation will be operational on May 2nd.

Banking Sector

Deposit volume became 1,829 billion TL.

According to Weekly Bulletin published by BRSA, as of January 26, total deposit volume rose by 1.5% ytd to 1,829 billion TL. Year-to-date expansion in total deposits was 2.1% according to the FX adjusted figures. TL deposit volume increased by 1.4% to 991 billion TRY while the FX deposit in USD terms surged up by 2.9% to 225 billion USD in this period.

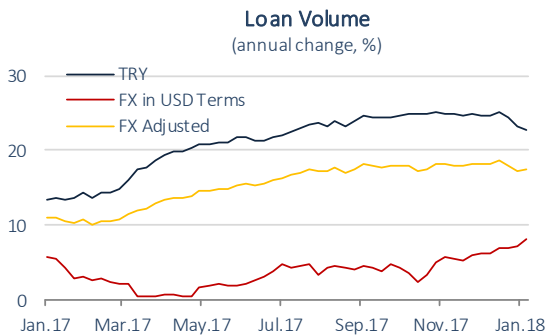
Compared to the same period of the previous year, total deposit volume increased by 206.1 billion TL (12.7%), 110.2 billion TL of which was due to rise in TL deposits.



Annual increase in credit volume declined to 16.3%.

Total credit volume, which rose rapidly in 2017 thanks to the Credit Guarantee Fund, expanded by 0.7% ytd to 2.150 billion TRY as of 26 January. In this period, TL credit volume increased by 0.7% while FX credits rose by 0.9%.

Compared to the same period of 2017, volume of TL credits and FX credits in USD terms increased by 22.8% and 8.1%, respectively. Annual credit volume increase, which was 20.9% at the end of 2017, declined to 16.3% as of 26 January.

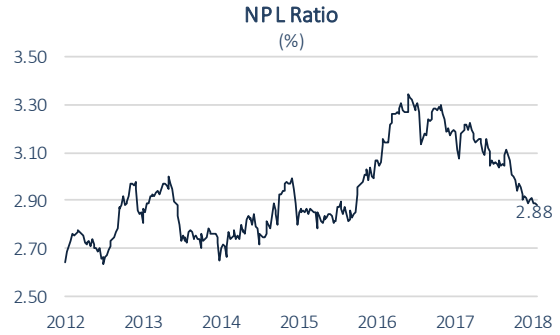


CGF's new guarantee limits have been announced.

The decisions, that returns of credits granted under the CGF scheme can be extended as a new loan and the remaining 50 billion TRY of the previously announced limit of 250 billion TRY was released, were issued in the Official Gazette on January 1st. On January 23rd, under the protocol signed between CGF and Treasury, a limit of 55 billion TRY became available for use. 5 billion TRY of this amount will be obtained from returns.

NPL ratio declined to 2.88%.

As of 26th January, gross non-performing loans was realized as 63.3 billion TRY while non-performing loans ratio, which stood at 2.91% at the end of 2017, declined to 2.88%, the lowest level for more than 2 years. NPL ratio for consumer loans was recorded as 3.49% while NPL ratio for commercial loans was realized as 2.78% as of 26th January.



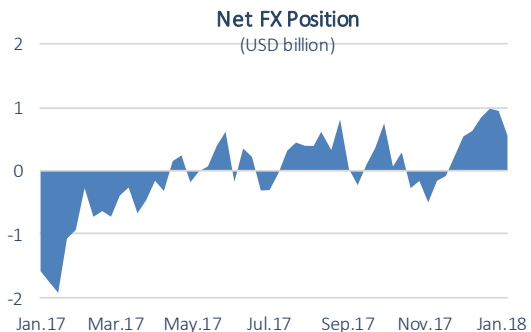
Securities portfolio...

As of January 26, securities portfolio of the banking sector grew by 0.6% compared to the year-end. Portfolio of securities held as collateral has exceeded 173 billion TL in this period.

Also, portfolio securities held in custody accounts increased by 1.7% compared to year end. In this period, the securities portfolio of nonresidents posted an increase of 2.8%, while residents' securities portfolio expanded by 0.9% compared to the end of 2017.

Net foreign currency position...

As of January 26, banks' on-balance sheet FX position was (-) 50,476 million USD while off-balance sheet FX position was realized as (+) 51,030 million USD. Hence, banking sector's net FX position became (+) 554 million USD.



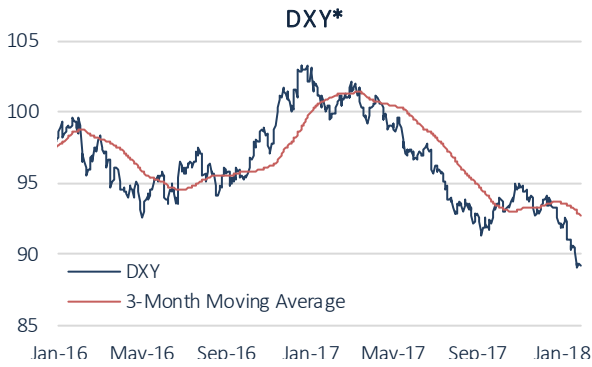
Source: BRSA Weekly Bulletin

Financial Markets

Global markets...

Trading volumes, which remained at low levels in the last weeks of 2017 as global stock markets were on holiday and investors avoided to take new positions, surged up again in 2018. While global stock market indices began the new year with a quick start, stock market indices in US, Europe and Asia hit new records as risk appetite rose.

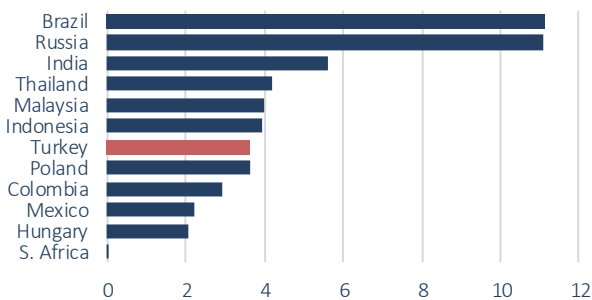
While US dollar was under pressure occasionally in January, DXY index, which shows the value of US dollar against other developed country currencies, decreased by 3.2% as of 31 January compared to the end of 2017. On the other hand, euro gained value in the same period with the impact of the strong economic data in the region and low performance of the US dollar in global markets. EUR/USD parity increased by 3.5% ytd and reached 1.242 as of January 31st.



BIST-100 index continued to rise.

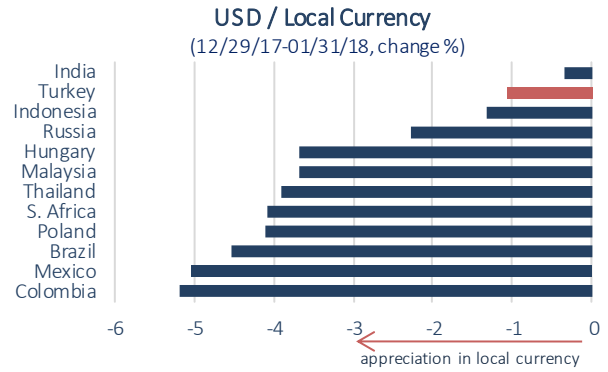
BIST-100 index, which followed a strong course in December and reached record levels at the end of 2017, also started the year at new highs. Despite having exhibited a slight decline, BIST-100 index, which performed strongly throughout the month, recorded the highest closing level of its history with 120.845 as of 29 January.

Stock Market in Emerging Countries (12/29/17-01/31/18, change %)

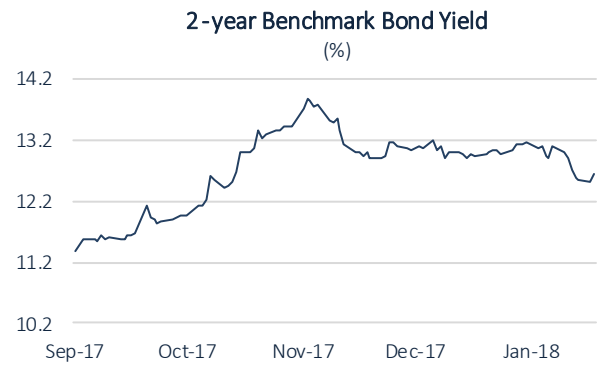


During the last week of 2017, USD/TL declined to 3.70 levels due to the depreciation of US dollar in global markets. However, it surged up in the second half of January due to the rising geopolitical risks in line with the cross border operation. USD/TL fluctuated in the last week of the month and reached 3.75 as of 31st January.

On the other hand, EUR/TL, which stood at 4.5478 at the end of 2017, rose to 4.6608 as of 31 January due to appreciation of euro in global markets.



Compound yield of the 2-year benchmark bond, which closed 2017 at 13.40%, stood at 13.11% at the end of January.



(*) DXY index keeps track of the US dollar's performance against a basket of six currencies (euro, Japanese yen, British pound, Canadian dollar, Swedish krona and Swiss franc).

Concluding Remarks

In the first month of the year, most macroeconomic data on the US and Euro Area economies offered a favorable outlook. IMF's upward revisions to its global growth forecasts, led particularly by the advanced economies, have supported upbeat expectations. Policy makers' decisions also continue to shape the agenda of global economy. Foreign trade protectionism led by the United States and the expectations over the ECB's monetary policy have been rigorously discussed in recent weeks.

Fed, which is expected to raise the policy rate three times in 2018, has not announced any change in its monetary policy at its January meeting just as markets anticipated. In the statement released after the meeting, it was suggested that the economy will continue to gain strength in 2018 and hence the inflation will move upwards. This gave way to an increase in the probability of 2018 rate hikes that markets priced in.

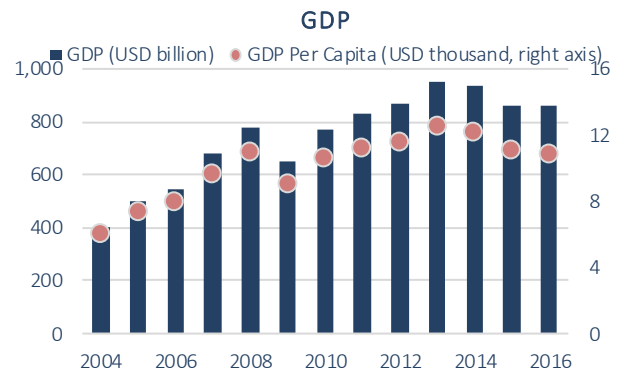
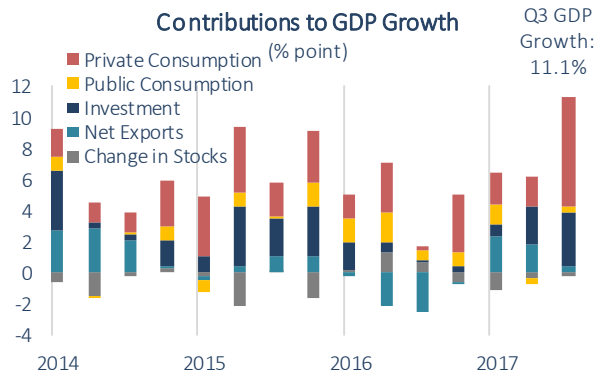
Developments that have taken place since the beginning of the year indicated that the decisions to be made by other central banks of global significance, especially the ECB, will be high on the agenda at least as much as the Fed's normalization process. While relatively hawkish expectations for the ECB policies are driving the euro to its three-year peak, Bank of England will remain under close scrutiny as the conundrum of high inflation and a slowing economic activity creates uncertainty over its future policies.

Turkey has started the year with an intense geopolitical backdrop. This caused occasional fluctuations in domestic markets. On the other hand, economic activity showed mostly positive signs. Exchange rate and inflation developments as well as leading indicators continue to be significant for Turkish economy. The recent stronger emphasis by CBRT on maintaining price stability supports optimism over inflation outlook.

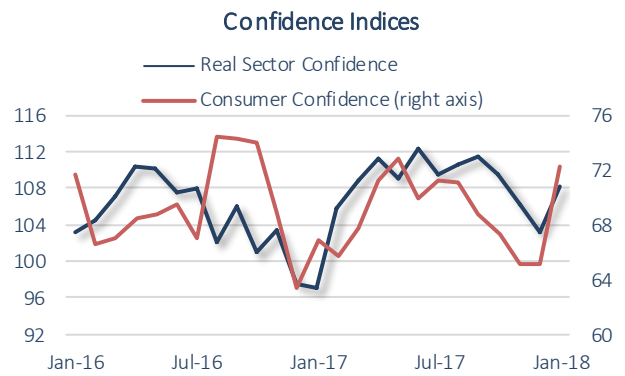
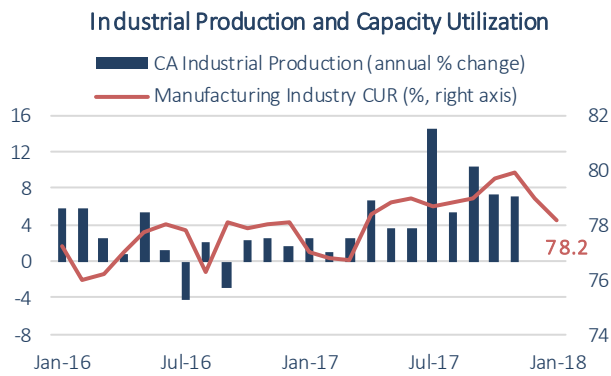
Forecasts (%)	2017	2018
Growth	6.7	4.1
Current Account Deficit/GDP	5.2	5.1
Inflation (year-end)	11.92 (R)	10.20

(R) Realization

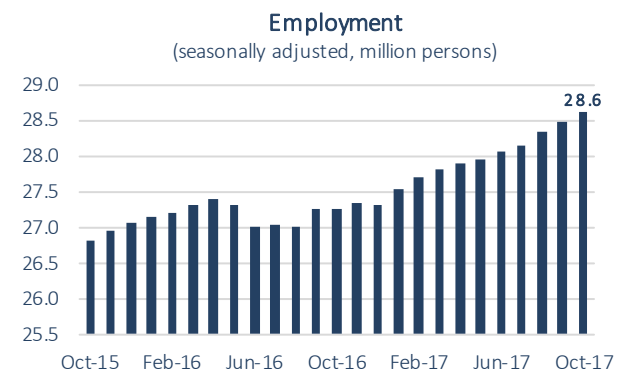
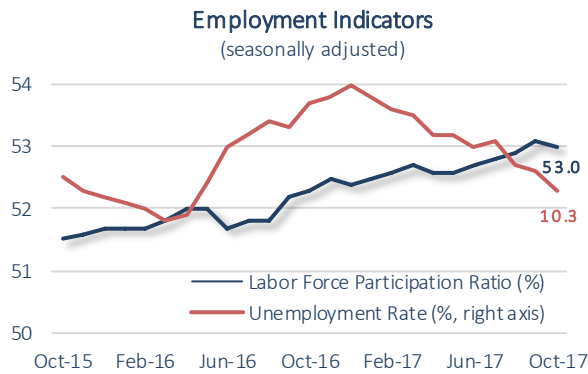
Growth



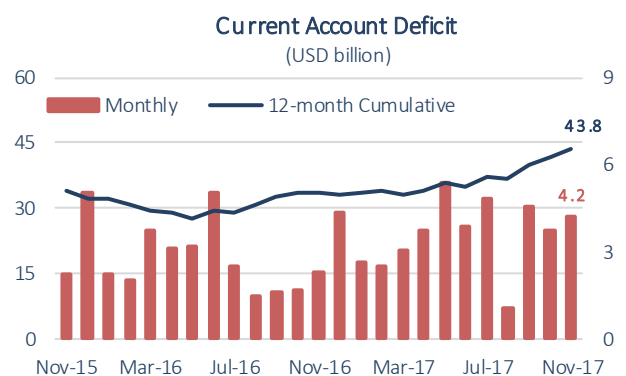
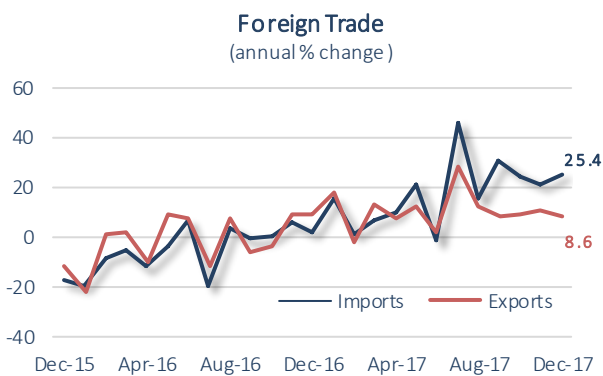
Leading Indicators



Labor Market



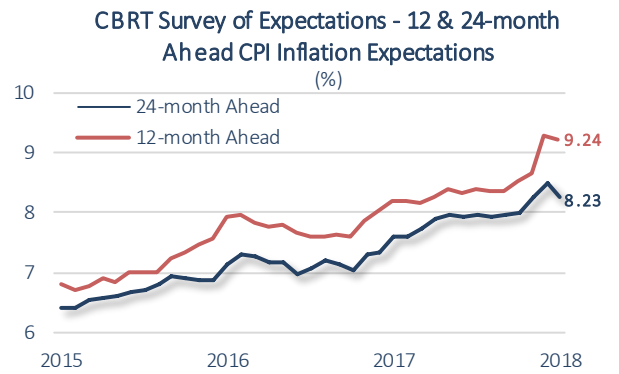
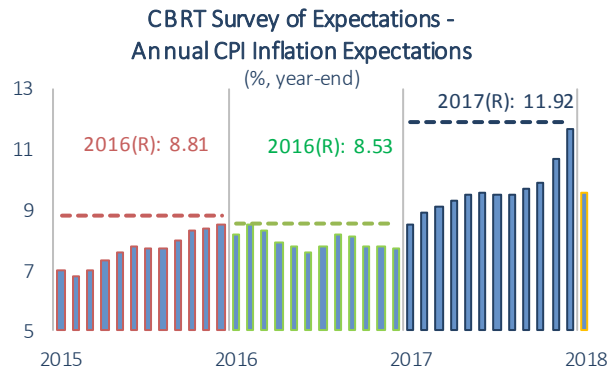
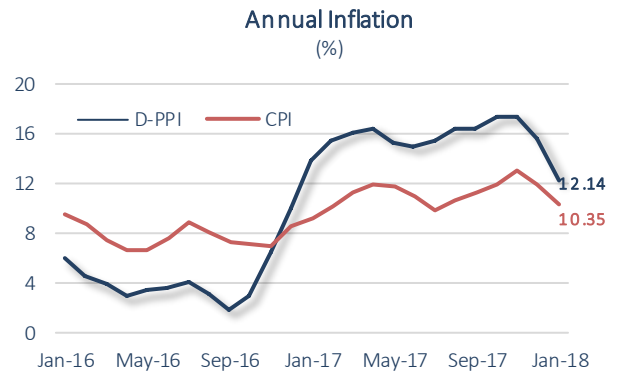
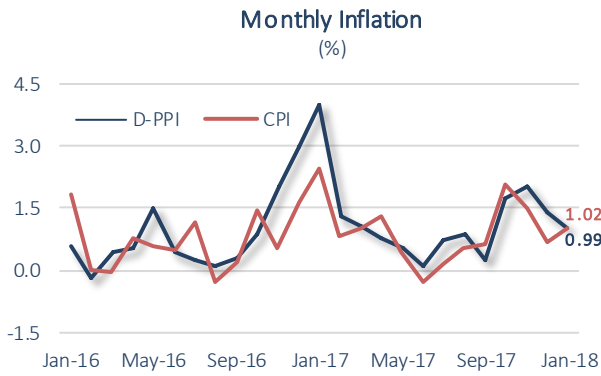
Foreign Trade and Current Account Balance



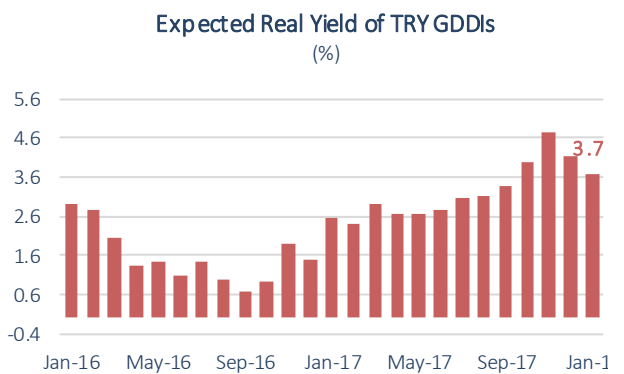
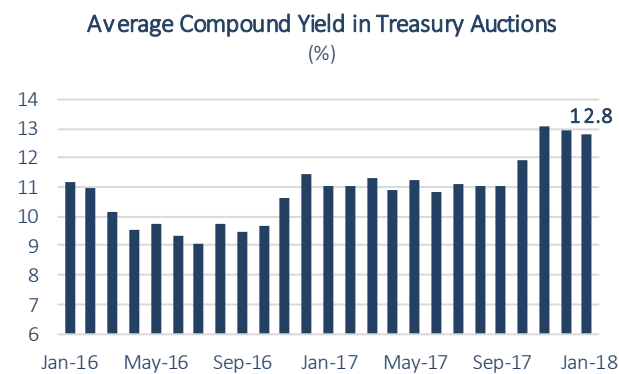
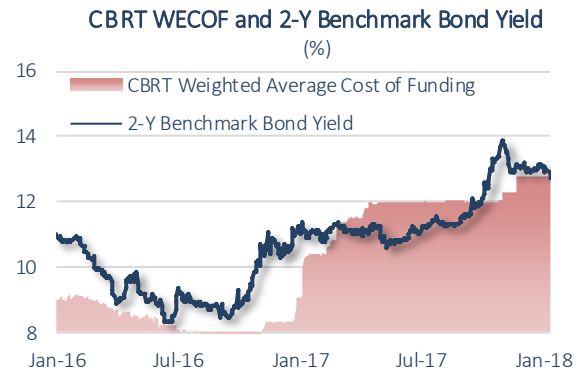
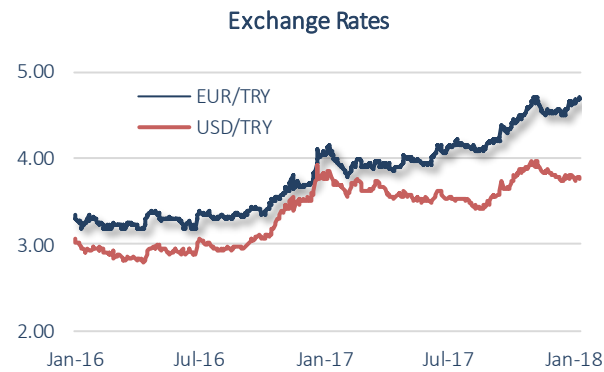
(CA) Calendar adjusted

Source: Datastream, CBRT, Turkstat

Inflation



Foreign Exchange and Bond Market



Turkish Economy - Macroeconomic Indicators

Growth	2012	2013	2014	2015	2016	17-Q1	17-Q2	17-Q3
GDP (USD billion)	871	950	935	861	863	176	205	235
GDP (TRY billion)	1,810	2,045	2,339	2,609	3,040	649	736	827
GDP Growth Rate (%)	4.8	8.5	5.2	6.1	3.2	5.3	5.4	11.1
Inflation (%)						Nov-17	Dec-17	Jan-18
CPI (annual)	6.16	7.40	8.17	8.81	8.53	12.98	11.92	10.35
Domestic PPI (annual)	2.45	6.97	6.36	5.71	9.94	17.30	15.47	12.14
Seasonally Adjusted Labor Market Figures						Aug-17	Sep-17	Oct-17
Unemployment Rate (%)	8.8	9.1	10.3	10.2	12.0	10.7	10.6	10.3
Labor Force Participation Rate (%)	48.5	48.5	51.0	51.7	52.4	52.9	53.1	53.0
FX Rates						Nov-17	Dec-17	Jan-18
CPI Based Real Effective Exchange Rate	111.1	101.0	105.2	97.9	92.1	84.2	84.9	85.5
USD/TRY	1.7847	2.1485	2.3378	2.9189	3.5176	3.9061	3.7916	3.7514
EUR/TRY	2.3530	2.9605	2.8288	3.1708	3.7102	4.6574	4.5530	4.6733
Currency Basket (0.5*EUR+0.5*USD)	2.0688	2.5545	2.5833	3.0448	3.6139	4.2817	4.1723	4.2124
Foreign Trade Balance⁽¹⁾ (USD billion)						Oct-17	Nov-17	Dec-17
Exports	152.5	151.8	157.6	143.8	142.5	154.5	156.0	157.1
Imports	236.5	251.7	242.2	207.2	198.6	225.5	229.1	233.8
Foreign Trade Balance	-84.1	-99.9	-84.6	-63.4	-56.1	-71.0	-73.2	-76.7
Import Coverage Ratio (%)	64.5	60.3	65.1	69.4	71.8	68.5	68.1	67.2
Balance of Payments⁽¹⁾ (USD billion)						Sep-17	Oct-17	Nov-17
Current Account Balance	-48.0	-63.6	-43.6	-32.1	-33.0	-39.7	-41.8	-43.8
Capital and Financial Accounts	-48.9	-62.1	-41.6	-21.9	-22.1	-33.6	-34.7	-39.0
Direct Investments (net)	-9.5	-9.3	-5.8	-12.5	-9.7	-8.5	-9.4	-9.0
Portfolio Investments (net)	-41.0	-24.0	-20.1	15.7	-6.3	-21.2	-20.6	-22.0
Other Investments (net)	-19.2	-38.8	-15.3	-13.4	-6.9	1.4	-1.5	-1.6
Reserve Assets (net)	20.8	9.9	-0.5	-11.8	0.8	-5.3	-3.2	-6.4
Net Errors and Omissions	-0.9	1.6	2.0	10.2	10.9	6.1	7.1	4.7
Current Account Balance/GDP (%)	-5.5	-6.7	-4.7	-3.7	-3.8	-	-	-
Budget⁽²⁾⁽³⁾ (TRY billion)						Oct-17	Nov-17	Dec-17
Expenditures	361.9	408.2	448.8	506.3	583.7	544.4	601.1	677.7
Interest Expenditures	48.4	50.0	49.9	53.0	50.2	50.1	55.3	56.7
Non-interest Expenditures	313.5	358.2	398.8	453.3	533.4	494.3	545.8	621.0
Revenues	332.5	389.7	425.4	482.8	554.4	509.4	574.6	630.3
Tax Revenues	278.8	326.2	352.5	407.8	458.7	430.9	489.3	536.0
Budget Balance	-29.4	-18.5	-23.4	-22.6	-29.3	-35.0	-26.5	-47.4
Primary Balance	19.0	31.4	26.5	30.4	21.0	15.2	28.8	9.3
Budget Balance/GDP (%)	-1.6	-0.9	-1.0	-0.9	-1.0	-	-	-
Central Government Debt Stock (TRY billion)						Oct-17	Nov-17	Dec-17
Domestic Debt Stock	386.5	403.0	414.6	440.1	468.6	530.5	534.5	535.4
External Debt Stock	146.4	183.2	197.9	238.1	291.3	337.1	356.5	341.0
Total Debt Stock	532.9	586.2	612.5	678.2	760.0	842.9	891.0	876.5

(1) 12-month cumulative

(2) Year-to-date cumulative

(3) According to Central Government Budget

BANKING SECTOR ACCORDING TO BRSA's MONTHLY BULLETIN FIGURES

(TRY billion)	2012	2013	2014	2015	2016	Nov.17	Dec.17	Change ⁽¹⁾
TOTAL ASSETS	1,371	1,732	1,994	2,357	2,731	3,269	3,258	19.3
Loans	795	1,047	1,241	1,485	1,734	2,104	2,098	21.0
TRY Loans	588	753	881	1,013	1,131	1,397	1,414	25.0
Share (%)	74.0	71.9	71.0	68.2	65.2	66.4	67.4	-
FX Loans	206	295	360	472	603	707	684	13.4
Share (%)	26.0	28.1	29.0	31.8	34.8	33.6	32.6	-
Non-performing Loans	23.4	29.6	36.4	47.5	58.2	63.7	63.9	9.9
Non-performing Loan Rate (%)	2.9	2.8	2.9	3.1	3.2	2.9	3.0	-
Securities	270	287	302	330	352	394	402	14.3
TOTAL LIABILITIES	1,371	1,732	1,994	2,357	2,731	3,269	3,258	19.3
Deposits	772	946	1,053	1,245	1,454	1,713	1,711	17.7
TRY Deposits	520	594	661	715	845	949	955	12.9
Share (%)	67.4	62.8	62.8	57.4	58.1	55.4	55.8	-
FX Deposits	252	352	391	530	609	765	756	24.3
Share (%)	32.6	37.2	37.2	42.6	41.9	44.6	44.2	-
Securities Issued	38	61	89	98	116	148	145	25.1
Payables to Banks	173	254	293	361	418	479	475	13.7
Funds from Repo Transactions	80	119	137	157	138	98	99	-28.2
SHAREHOLDERS' EQUITY	181.9	193.7	232.0	262.3	300.3	350.9	359.1	19.6
Profit (Loss) of the Period	23.5	24.7	24.6	26.1	37.5	45.2	49.1	-
RATIOS (%)								
Loans/GDP	43.9	51.2	53.1	56.9	57.1			
Loans/Assets	58.0	60.5	62.2	63.0	63.5	64.4	64.4	-
Securities/Assets	19.7	16.6	15.2	14.0	12.9	12.0	12.3	-
Deposits/Liabilities	56.3	54.6	52.8	52.8	53.2	52.4	52.5	-
Loans/Deposits	102.9	110.7	117.9	119.2	119.3	122.8	122.6	-
Capital Adequacy (%)	17.9	15.3	16.3	15.6	15.6	16.4	16.9	-

(1) Year-to-date % change

Source: BRSA, Turkstat

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