

WEEKLY OUTLOOK

Fed increased policy rate by 25 bps.

At the last meeting of 2016 held on December 13-14, the US Federal Reserve (Fed) decided to increase the policy rate by 25 basis points. After the meeting, Fed Chair Yellen said that conditions were warranted to raise the policy rate to %0.50-0.75 band, in line with the dual mandate. Referring to the declining unemployment rate in the US and the inflation converging to Fed's long-term target of 2%, Yellen noted that economic growth in US has accelerated since mid-2016. Yellen said interest rate decisions will be shaped by labor market conditions, course of inflation, inflation expectations, and developments in global financial markets. According to the FOMC participants' projections which were published after the meeting, the median interest rate forecast of the members for the end of 2017 was realized as 1.375%. This indicates that FOMC now sees three rate hikes in 2017 instead of the two foreseen as of September. The uncertainty over fiscal policies in Trump era, were also emphasized. Referring to this issue in her speech, Yellen pointed out that the ambiguities over Trump's policies prevented the monetary policy from becoming clear.

Data releases in the US...

According to the US data released in last week, PPI registered 0.4% monthly increase while CPI rose by 0.2% in November. Although the annual increase in CPI has accelerated to some extent, inflation is still below the Fed's long-term inflation target of 2%. Excluding the energy and food prices, core CPI increased by 2.1% yoy in November. Retail sales and industrial production were below expectations in November, while the manufacturing PMI data for the December flash showed strong performance, indicating that private sector production would pick up.

The expectations that Fed will become more hawkish than expected in 2017 support the rise in US Treasury bond rates. US 10-year benchmark bond's yield has risen above 2.6% for the first time since September 2014. In addition, last week the DXY index, which shows the value of dollar against other developed countries currencies, has reached its highest level since 2002.

Recent developments in Italy and Euro Area...

While Paolo Gentiloni has been appointed as the new prime minister of Italy after the constitutional referendum held on December 4th, Moody's downgrading of Italian banking sector's outlook from "stable" to "negative" led to concerns about the sector. On the other hand, the announcement, that the support package of 15 billion euros for the financial markets will be approved on December 22nd, alleviated some of the concerns. In addition, the declaration of Unicredit, that it would go on to issue a significant share of stocks in June, came to the fore as another development that supported the markets.

Euro Area manufacturing industry PMI came above expectations with 54.9, while annual change in CPI has reached its highest level since April 2014 with 0.6%. In Euro Area the effects of the increase in oil prices, the developments related to Brexit and the elections to be held in Netherlands and France will be followed in the coming period.

WEEKLY DATA

	9 Dec	16 Dec	Change		9 Dec	16 Dec	Change
BIST-100 Index	75,727	77,590	2.5 % ▲	EUR/USD	1.0559	1.0447	-1.1 % ▼
TRY 2 Year Benchmark Rate	10.94%	10.84%	-10 bp ▼	USD/TRY	3.4859	3.5058	0.6 % ▲
US 10 Year Bond Rate	2.46%	2.60%	13 bp ▲	EUR/TRY	3.6806	3.6602	-0.6 % ▼
EMBI+ (bps)	367	366	-1 bp ▼	Gold (USD/ounce)	1,158	1,134	-2.1 % ▼
EMBI+ Turkey (bps)	364	365	1 bp ▲	Brent Oil (USD/barrel)	52.4	54.3	3.5 % ▲

bp: basis point

BIST-100 Index increased last week.

Stock market in Turkey started the week with downward trend; however, BIST-100 index surged 2.5% weekly, thanks to the rise in construction and banking stocks. Last week, average compound interest rate in bonds issued by the Treasury on two different days exceeded 11%. This week, domestic markets are waiting for the upcoming Monetary Policy Committee (MPC) meeting of the CBRT, which will be held on December 20th. CBRT is expected to continue to increase interest rates in December after raising interest rates in November for the first time since January 2014.

Expectations for growth and exchange rates deteriorated.

According to the CBRT's Survey of Expectations, year-end USD/TRY expectations in December rose to 3.4602, while year-on-year GDP growth expectations declined to 2.6%. Moreover, the policy interest rate expectation of 8.5% for the next 12 months pointed to the market's expectation of interest rate increases from the CBRT.

Unemployment rate continued to rise.

Unemployment rate in Turkey remained flat at 11.3% in September period which covers from August to October. Despite the 2.7% increase in labor force, 13.5% rise in unemployed population contributed to the increasing unemployment rate. Labor force participation rate in this period was observed at historical high level with 52.8%. On sectoral breakdown, decline in employment in agriculture and manufacturing was noteworthy. Employment in services sector, which accounts for 53% of the total employment, increased thanks to the rise in education sector and administrative and support service activities.

Central government budget posted a surplus in November.

Central government budget posted a surplus of 10 billion TRY in November. During January-November 2016, budget deficit declined by 61% yoy to 2.1 billion TRY. In the first 11 months of the year, budget revenues rose by 15.1% yoy to 508.6 billion TRY while budget expenditures increased by 14.2% yoy to 510.7 billion TRY. Budget revenues displayed a strong performance in November thanks to the rise in tax revenues and restructured debts. Under the assumption that the average growth rate of 15% recorded in the budget revenues in the first 11 months will be sustained in December, budget revenues might exceed the MTP target by 10 billion TRY. On the spending front, taking MTP targets into consideration, it is seen that 70 billion TRY will be available to spend in December. Accordingly, government, having taken steps to support economic activity in the last quarter, has a room to spend about 80 billion TRY in December ([Our Budget Balance Report](#)).

Outstanding loans received from abroad by private sector continue rising.

According to the figures published by CBRT, in October outstanding long-term loans received from abroad by private sector increased by 12.3 billion USD to 207.6 billion USD whereas short-term loans decreased by 3.7 billion USD to 16.8 billion USD. In October, long-term bond stock of banks and non-bank financial institutions increased while non-financial institutions' loan liabilities surged by 9 billion USD. Financial institutions' share in total long-term loans realized as 51.7% whilst share in short-term liabilities reached 81.3%.

INDUSTRY NEWS

BITT Regulation on derivative transactions...

Last week, it was announced that banking and insurance transaction tax (BITT) for the over-the-counter derivative transactions was removed. The elimination of BITT, which is currently 5%, aims to attract the private sector's interest in derivative transactions from abroad to Turkey and to lessen the forward transaction costs of firms which are exposed to currency risks. Similarly, Deputy Prime Minister Mehmet Şimşek revealed last week that they would like to support the real sector firms with FX positions by insuring their positions using derivative instruments. He also detailed that firms with no FX revenues will be limited to have FX loans and hence, private sector's growing FX loans are aimed to be taken under control.

International organizations keep financing domestic investments...

During the panel titled "Private Sector in Turkey: Sustainable Development" hosted by International Finance Corporation (IFC), it was explained that IFC has provided 502 million USD in long-term loans and 145 million USD in short-term loans to Turkey since July 2016. On the other hand, it was explained by European Bank for Reconstruction and Development (EBRD) officials last week that the bank will continue to finance electricity production firms in the northwestern Turkey.

Natural gas imports from Iran declined...

Last week, Iran, Turkey's second largest natural gas supplier, decreased the amount of natural gas provided to Turkey by one third due to the unfavorable weather conditions. Rising demand for natural gas at residences in the winter pushed BOTAŞ to cut gas supply to the state's electricity production company (EÜAŞ). Electricity production has the highest share in the natural gas consumption by 40%. Lack of natural gas for electricity production pushed up electricity prices. Currently Turkey imports 9.6bcm/year natural gas from Iran under the agreement signed in 1996. It comes up almost every year that Iran reduces the amount of gas it supplies to Turkey due to the weather conditions.

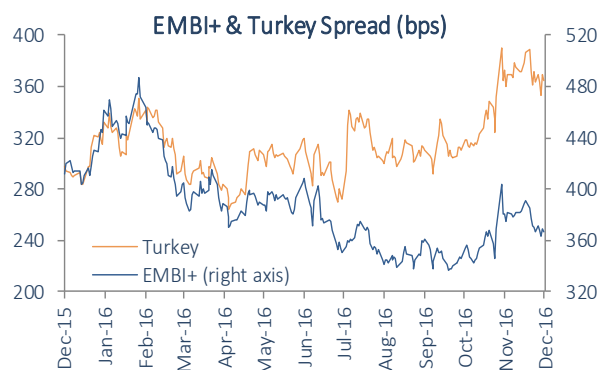
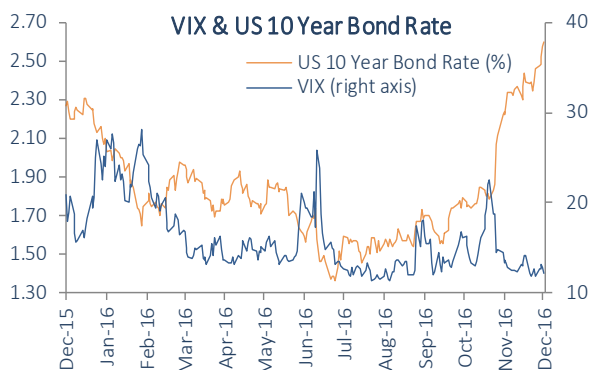
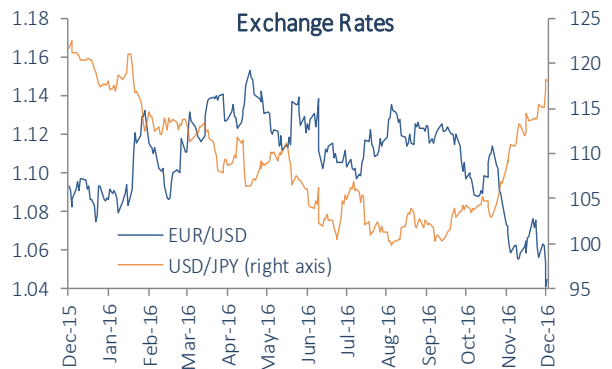
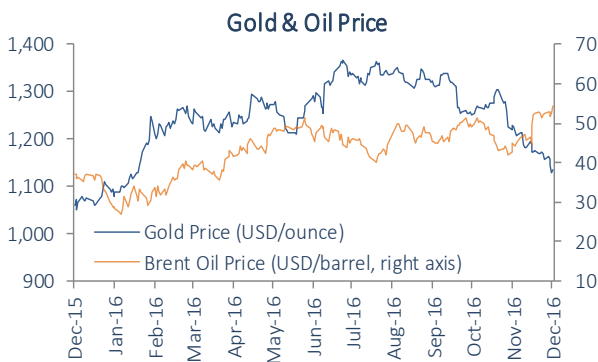
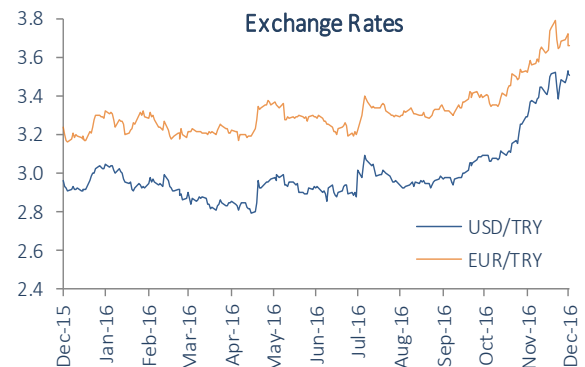
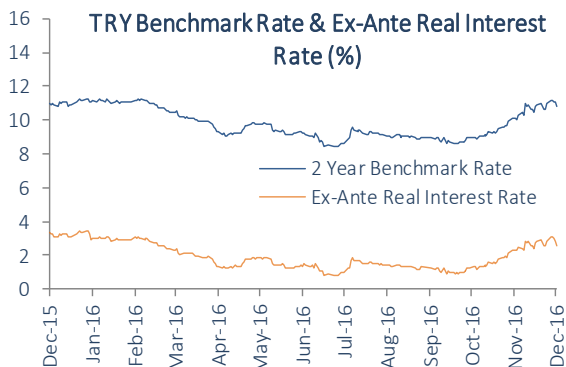
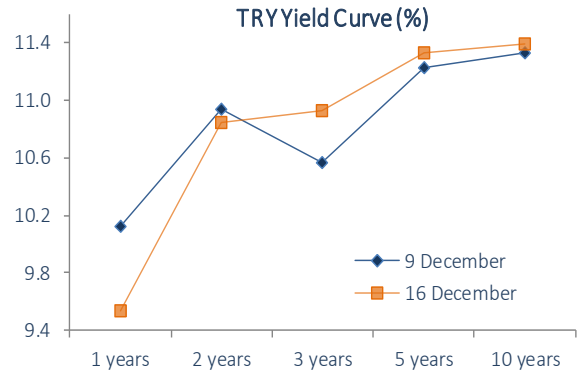
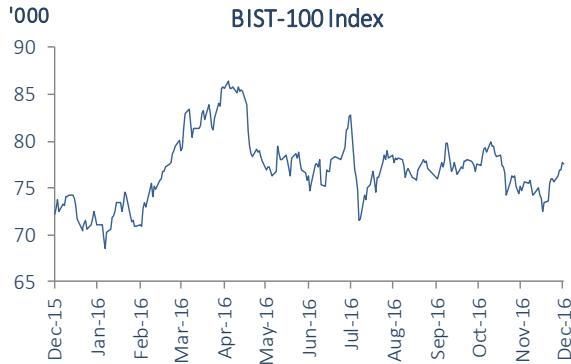
Shopping mall turnover index rose in October.

According to the data published by Council of Shopping Centers (AYD), shopping mall turnover index increased by 1% yoy in October. The sharpest rise by category was observed in the "bags and shoes" by 10% while deferrable necessities at "others" category (furniture, cosmetics, dry cleaning etc.) dropped by 8% yoy. The index's growing pattern in the last two months is considered as a positive development by the sector officials. Recent volatility in currency, on the other hand, was perceived as a factor leading consumers to savings and shopping only for vital necessities.

Automotive sales keep rising in November.

Automotive Manufacturers Association of Turkey (OSD) last week published that automotive production rose by 8% to 1,329,812 at the first 11 months of the year. In terms of sales volume, domestic sales increased by 2% while exports surged by 14%. Exports are estimated to reach its highest level since 2008 to 23.5 billion USD by value.

FINANCIAL MARKETS



WEEKLY DATA RELEASES

		Period	Consensus
20 December	CBRT MPC and Interest Rate Decision	December	
	Japan Central Bank (BoJ) Meeting and Interest Rate Decision	December	
21 December	Turkstat Consumer Confidence Index	December	
	USA Existing Home Sales	November	5.52 million
	Treasury Domestic Debt Redemption (543 million TRY)	December	
22 December	USA GDP-Final	2016 Q3	3.3%
	USA Personal Consumption Expenditure (PCE)	November	2.8%
	USA Personal Income and Outlays	November	0.3%
	USA Durable Goods Orders	November	4.7%
23 December	USA New Home Sales	November	575,000
	USA Consumer Sentiment - The University of Michigan	December	98.1

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