

WEEKLY OUTLOOK

Strong economic data in the US...

Last week's data indicated that economic activity has strengthened in the US. Housing starts in January met the expectations while manufacturing indices for some States recorded a significant increase. Revival in the US economy has had favorable impact on the labor market as well. Weekly jobless claims, which were below the expectations, confirmed the views that the US economy is close to full employment. Additionally, rising global commodity prices have begun to be effective on inflation. CPI in the US in January posted an annual increase of 2.5%, reaching its highest level in the last 4 years.

Fed governors' statements were also monitored closely last week. Fed Chair Yellen cautioned that waiting too long for an interest rate hike would be "unwise" since it would cause Fed to raise rates rapidly disrupting financial markets and the economy. Yellen also referred to Fed's balance sheet and added that they discussed shrinking the balance sheet in time, in tandem with an efficient monetary policy. Yellen emphasized that Fed's policies will continue to be data-dependent and Trump administration's fiscal policies creates uncertainty. Fed officials, Lockhart and Harker, last week defended that three interest rate hikes are appropriate for 2017. Rising market expectation for an interest rate rise in March pushed the 10-year US note yield up in the first half of the last week. VIX index, a key measure for global risk perception touched its highest level during the week since the beginning of February.

Rising inflation in China...

There is a growing concern about price stability in China, as the country is the determinant of global inflation being the biggest consumer of many commodities in the world. PPI in January rose by 6.9% yoy, rising for the fifth consecutive month and reaching to its highest level since August 2011. Inflation was spread amongst products especially in oil, coal, iron and steel industries.. China has been taking tightening steps after its loose monetary policies in 2016 which put pressure on price stability. Outstanding loan growth in China slowed to 12.6% yoy in January, the lowest level since 2006, as a result of macro prudential measures taken by policymakers to curb new housing purchases and restrain the credit growth. Markets currently consider that Chinese authorities will be prominently tightening the monetary policy in case of continuing capital outflows and high inflation level.

Uncertainties in oil market...

Oil prices fluctuated last week. Earlier in the week, the news that the US and Libya were preparing to increase their oil production significantly caused oil prices to decline. In the second half of the week OPEC's statements were influential in the course of the prices. OPEC, which seeks to balance global oil markets, stated that the production cut-off period could be extended and even daily oil production could

WEEKLY DATA

	10 Feb	17 Feb	Change		10 Feb	17 Feb	Change
BIST-100 Index	87,473	88,830	1.6 % ▲	EUR/USD	1.0638	1.0611	-0.3 % ▼
TRY 2 Year Benchmark Rate	11.39%	11.45%	6 bp ▲	USD/TRY	3.6943	3.6280	-1.8 % ▼
US 10 Year Bond Rate	2.41%	2.43%	2 bp ▲	EUR/TRY	3.9290	3.8495	-2.0 % ▼
EMBI+ (bps)	334	339	5 bp ▲	Gold (USD/ounce)	1,234	1,235	0.1 % ▲
EMBI+ Turkey (bps)	331	326	-5 bp ▼	Brent Oil (USD/barrel)	55.1	54.9	-0.4 % ▼

bp: basis point

be reduced further if the excess supply continues. The next meeting of OPEC, in which the roadmap of oil production will be decided, is scheduled to take place on May 25th. Non-OPEC oil producers, especially Russia, is expected to attend the meeting as well.

Current account deficit is below the forecasts.

The current account deficit was realized as 4.3 billion USD in December, slightly below market expectations. Thus, the current account deficit became 32.6 billion dollars for the whole year of 2016, which is only 0.5 billion USD higher than the level in 2015. Energy imports, which declined due to low oil prices in most of the year 2016, were decisive in the contraction of Turkey's foreign trade deficit. On the other hand, similar decline in tourism revenues in the same period limited the improvement in the current account deficit. It was observed that direct investments declined in 2016, but portfolio investments improved somewhat in the financial account. While domestic banks reduced the amount of loans they had from abroad, it was noted that non-banking private sector continued to borrow from foreign markets. In addition, the capital inflow of 11.1 billion USD recorded in net errors and omissions contributed significantly to the financing of the current account deficit ([Our Balance of Payments Report](#)).

Strong start to the year in budget revenues...

In January, budget revenues increased by 25.8% yoy, while expenditures rose by 11.3%. Thus, the budget made a strong start to 2017 with a surplus of 11.4 billion TRY. The regulations on consumption taxes and the revival in privatization revenues were effective in the rise in budget revenues. The increase in budget expenditures was mainly due to the rise in personnel expenditures and current transfers. In this period, personnel expenditures and current transfers increased by 9.3% and 14.2% yoy, respectively ([Our Budget Balance Report](#)).

Unemployment rate is rising.

Relatively weak in economic activity is causing the labor market to perform poorly. Unemployment rate in Turkey increased year-on-year by 1.6 points to 12.1% in November, reaching its highest level since global crisis. Unemployment in youth population, which basically includes people between the age of 15 and 24, also surged to 22.6%. On sectoral breakdown, employment in agriculture kept its downward trend, while that of manufacturing and construction remained flat. However, rising employment in services sector limited the increase in unemployment.

CBRT Survey of Expectations...

The secondary effects of increased volatility in exchange rates over the last few months have caused the markets' macroeconomic expectations to deteriorate. According to the results of the CBRT Survey of Expectation, economic growth expectation for 2017 remained flat at 2.9%, while inflation and exchange rate expectations continued to deteriorate. While 12-month-ahead USD/TRY parity rose to 3.96, concerns regarding price stability persisted. 12-month-ahead inflation expectation reached to 8.2%, highest for the last 8 years. Moreover, current account deficit expectation maintained its upward trend in this period due to developments in oil prices. It is expected that current account deficit to realize at 35.6 USD billion in 2017.

Recovery in domestic markets...

Turkey's 5-year CDS spread has been at its lowest level since September 2016 as demand for TRY denominated assets increased with the improvement in risk perception in Turkey last week. TRY appreciated against USD and EUR as a result of CBRT's tight monetary policy. In addition, announcement from CBRT on Friday that repayments of rediscount credits for export and foreign exchange earning services, which were lent before 1 January 2017 and will be due by 31 May 2017, can be made in Turkish liras provided that they are paid at maturity also supported TRY. CBRT also said that USD/TRY rate announced on 2 January 2017, which is 3.53, will be applicable for these transactions. This facility is expected to limit the demand for foreign exchange in domestic markets. Companies have a total amount of 4.5 billion USD repayments of rediscount credits for export and foreign exchange earning services in March-May 2017 period, according to CBRT. It is expected that CBRT's foreign exchange reserves will decrease by 4.5 billion USD, assuming that companies will choose to repay in TRY.

Last week, high demand towards Treasury's eurobond issuance confirmed the improvement in foreign residents' sentiment. Treasury borrowed a total of 1.25 billion dollar via the re-issuance of eurobond with 10 year maturity, while the yield on issuance was below expectations with 5.65%. Thus, Treasury completed more than half of its international borrowing projection for 2017. During the past week, TRY appreciated by 1.9% against the exchange rate basket (0.5*USD+0.5*EUR), gaining strength for the third week in a row. The upward movement of the BIST-100 index continued as the stock exchange completed the week at 88,830.

INDUSTRY NEWS

New term in R&D supports...

R&D supports, which are distributed by different institutions and ministries in Turkey, would be provided through the newly established R&D and Technology Fund in the coming period. The Minister of Science, Industry and Technology Faruk Özlü told that R&D supports would be distributed more effectively with this manner. Özlü added that every sector will not be supported by the fund while the focus would be on some high value added sectors such as biotechnology, nanotechnology and information technologies. The Minister also said that in order to meet the financing needs of SME's, KOSGEB will give a loan of approximately 10 billion TRY until the end of March.

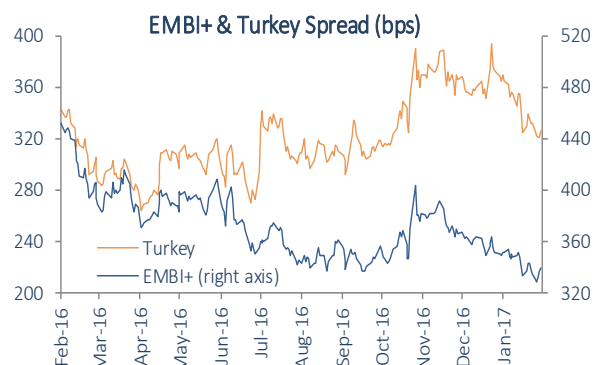
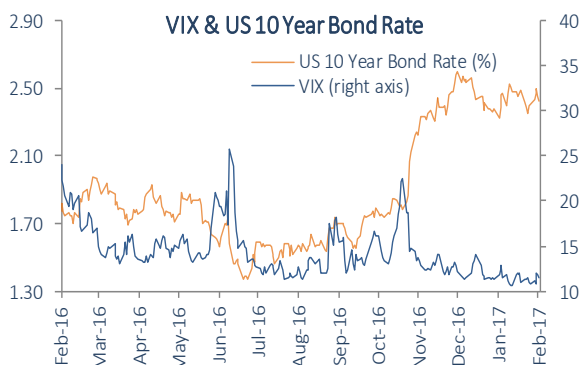
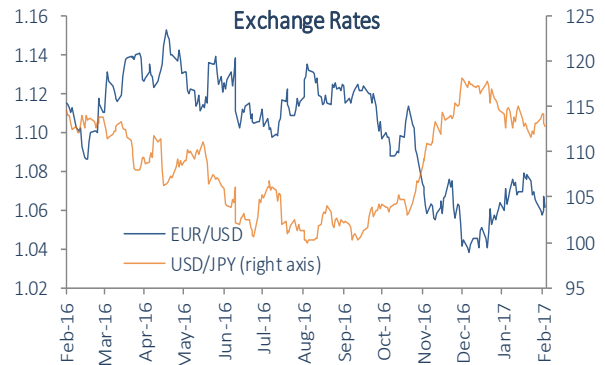
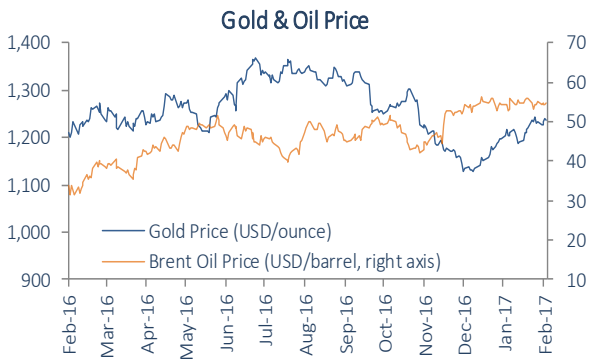
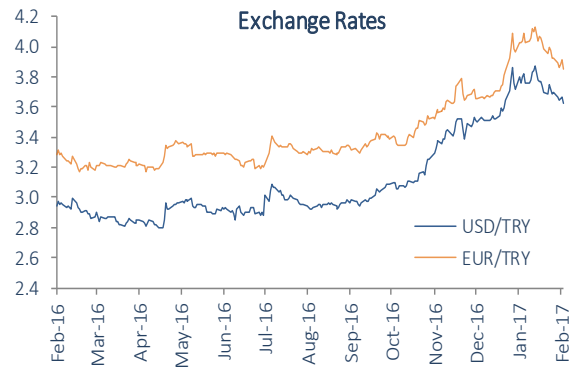
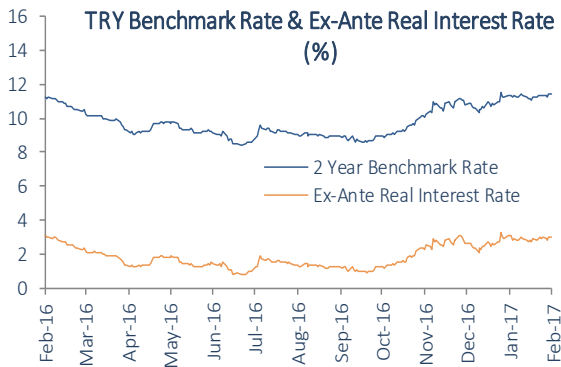
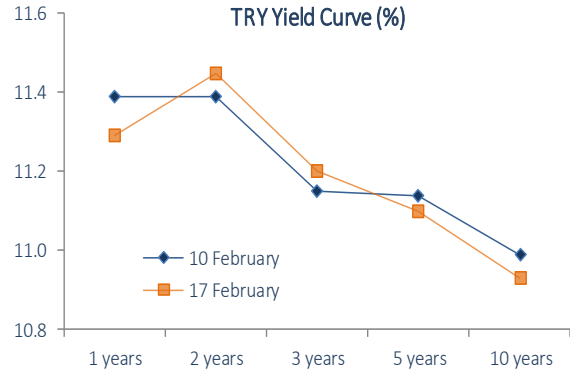
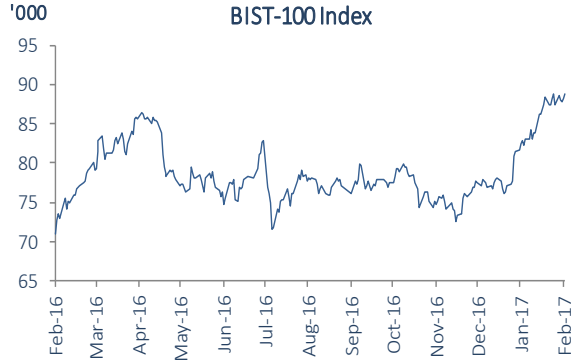
Challenges in the international contracting sector...

The international contracting sector, which is crucial for Turkey in terms of its FX revenues, performed poorly in 2016. According to the report published by the Turkish Contractors Association, volume of new projects abroad decreased by 56% in 2016 yoy to 10.1 billion USD. In the report, it was stated that the adverse developments in Libya, Iraq and Russia, which are among the main markets of the sector, were the main reason of this decline. It is also emphasized that the infrastructure expenditures in energy exporters, where contracting services were strong in previous years, have lost momentum due to decline in energy revenues in 2016. In 2017, on the other hand, international contracting sector is expected to gain some strength thanks to the rebound in oil prices and the recovery in relations with Russia.

Production in the iron and steel sector increased in 2016.

The iron and steel sector, one of the leading sectors in Turkish manufacturing industry, increased its production by 5.3% in 2016 to 33.2 million tons. Thus, Turkey's crude steel production ranked 8th in the world and 2nd in Europe. Manufacture of long steel products remained subdued in 2016, due to the moderate performance in the construction sector, while the buoyant activity in automotive sector supported the demand for flat steel products. In 2017, the construction sector in Turkey is expected to grow mildly in line with the ongoing infrastructure projects and this development is anticipated to support long steel demand. Iron ore and coal prices, which rose significantly in the recent period, are expected to display a moderate performance in 2017 as the increase in steel prices anticipated to lose momentum in this context.

FINANCIAL MARKETS



WEEKLY DATA RELEASES

		Period	Consensus
20 February	Turkstat Consumer Confidence	February	65.7 (A)
21 February	Re-Issuance of Fixed Coupon Bond with September 22nd, 2021 maturity		
	Euro Area Manufacturing PMI (preliminary)	February	55.0
	Euro Area Services PMI (preliminary)	February	53.8
22 February	CBRT Business Tendency Statistics and Real Sector Confidence Index	February	
	CBRT Capacity Utilization Ratio	February	
	Treasury Domestic Debt Redemption (2.2 billion TRY)		
	England CPI	January	1.9%
	US Existing Home Sales	January	
23 February	US Jobless Claims	February III.	
24 February	US New Home Sales	January	

(A) Actual

İŞBANK - Economic Research Division

İzlem Erdem - Division Head
izlem.erdem@isbank.com.tr

Alper Gürler - Unit Manager
alper.gurler@isbank.com.tr

H. Erhan Gül - Asst. Manager
erhan.gul@isbank.com.tr

Dilek Sarsın Kaya - Economist
dilek.kaya@isbank.com.tr

Aslı Göksun Şat Sezgin - Economist
goksun.sat@isbank.com.tr

Bora Çevik - Economist
bora.cevik@isbank.com.tr

Ahmet Aşarkaya - Economist
ahmet.asarkaya@isbank.com.tr

Ayşe Betül Öztürk - Asst. Economist
betul.ozturk@isbank.com.tr

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

This report has been prepared by Türkiye İş Bankası A.Ş. economists and analysts by using the information from publicly available sources believed to be reliable, solely for information purposes; and they are not intended to be construed as an offer or solicitation for the purchase or sale of any financial instrument or the provision of an offer to provide investment services. The views, opinions and analyses expressed do not represent the official standing of Türkiye İş Bankası A.Ş. and are personal views and opinions of the analysts and economists who prepare the report. No representation or warranty, express or implied, is made as to the accuracy or completeness of the information contained in this report. All information contained in this report is subject to change without notice, Türkiye İş Bankası A.Ş. accepts no liability whatsoever for any direct or consequential loss arising from any use of this report or its contents.

This report is copyright-protected. Reproducing, publishing and/or distributing this report in whole or in part is therefore prohibited. All rights reserved.