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Global Economy

High level trade negotiations between the US and China are moving in a positive atmosphere with expectations that the two countries can sign a trade agreement before the end of March.

In the last quarter of 2018, the US economy grew above expectations by 2.6% yoy. Leading indicators, on the other hand, draw a mixed picture.

Expectations that the Fed, which announced to pause balance sheet reduction, might halt interest rate hikes this year are strengthening.

Whereas March 29, the Brexit deadline, is closer than a month, it remains unclear whether UK will leave the EU. In the middle of March, many possibilities, including postponing the Brexit deadline to a later date and “no-deal Brexit”, will be voted in the UK Parliament.

Economic activity in the Euro Area continued to lose momentum. While industrial production in the region shows the weakest performance of the last decade, it is considered that the ECB might implement easing policies to support economic activity in the following period.

Starting the month with a flat course, oil prices turned up in the second half of the month thanks to supply-side developments and the US-China talks.

Turkish Economy

In November 2018 period unemployment rate rose by 2 points to 12.3% compared to the same period of 2017.

Contraction in industrial production continued to deepen. According to the calendar adjusted figures, industrial production decreased by 9.8% yoy in December, displaying its worst performance since June 2009.

Manufacturing PMI, which was realized as 46.4 in February, pointed out that the slowdown in the sector continued for 11 consecutive months.

Foreign trade deficit continued to fall in January 2019. Export volume rose by 5.9% yoy to 13.2 billion USD, while import volume was realized as 15.7 billion USD, decreasing by 27.2% yoy.

In 2018, current account deficit was realized as 27.6 billion USD. Portfolio investments displayed a weak performance throughout the year, while official reserves and net errors-omissions stood out in financing the current account deficit.

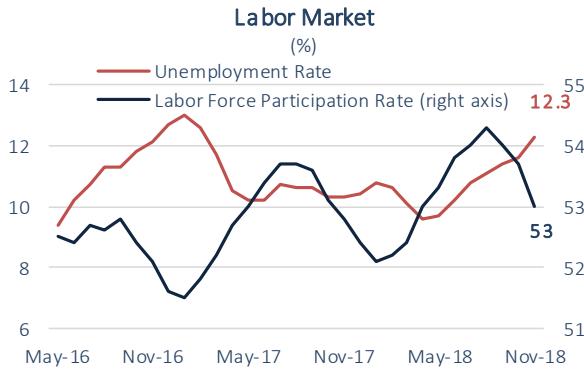
Central government budget gave 5.1 billion TRY surplus in January. Transfer of the CBRT's profit to the budget in advance played a decisive role in this development.

CBRT reduced the Turkish lira reserve requirement ratio by 50-100 basis points in all maturities. In its meeting on March 6, CBRT kept the policy rate unchanged at 24%.

S&P maintained Turkey's sovereign rating at “B+” with a stable outlook.

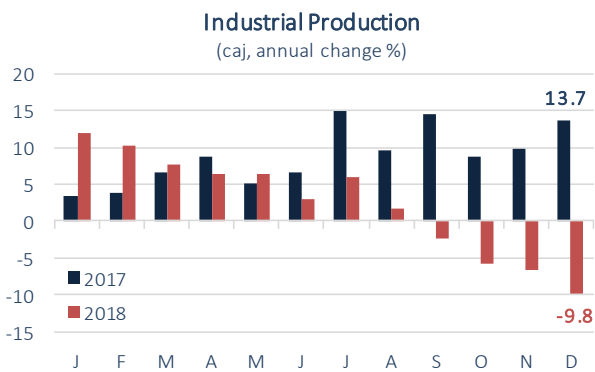
Unemployment rate at its highest level since February 2017...

Unemployment rate rose by 2 points yoy to 12.3% in November 2018 period. Having increased for 7 consecutive months, unemployment rate reached its highest level since February 2017. Labor force participation rate declined to 53%. While seasonally adjusted unemployment rate rose to 12% in this period, labor force participation rate came in at 53.4%.



Industrial production contracted more than expected in December.

Contraction in industrial production continued to deepen. According to the calendar adjusted figures, industrial production decreased by 9.8% yoy in December, displaying its worst performance since June 2009. Thus, in the last quarter of 2018, industrial production contracted by 7.5% compared to the same period of the previous year. In December, annual production decreased in 18 out of 24 sectors. According to main expenditure groups, fall in intermediate goods and capital goods production gained momentum in line with the slowdown in economic activity.



Manufacturing PMI posted an increase in February.

Manufacturing PMI increased by 2.2 points mom to 46.4 in February. Although the index reached the highest level in the last 6 months, it was still below the threshold of 50, indicating that the contraction in the sector continued. During this period, the recovery in new export

orders was remarkable. The said index rose to 50.3 in February, indicating a growth in the sector. The slowdown in the production sub-index also lost some momentum.

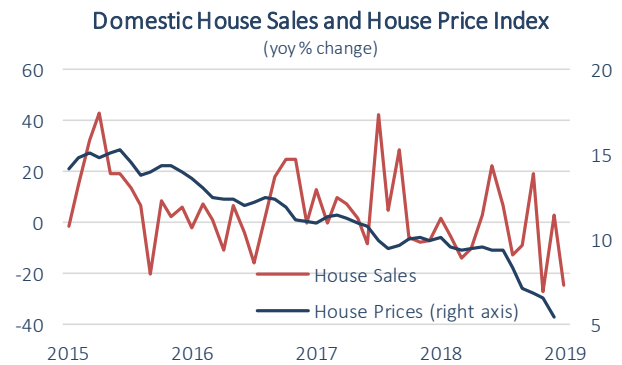
Capacity utilization rate had a slight decline in February.

Seasonally adjusted capacity utilization rate (CUR) decreased by 0.2 points mom to 74.1%. While seasonally adjusted real sector confidence index increased by 1.5 points to 96.9 on a monthly basis in the same period, consumer confidence index fell to 57.8 compared to the previous month. Thus, consumer confidence index remained close to the lowest level in the last 10 years.

House sales remained weak in the first month of the year.

House sales decreased by 24.8% yoy to 72,937 units in January. During this period, mortgage sales dropped by 77.2% yoy, while other sales fell by 2.8%. House sales to foreigners, on the other hand, continued the strong course. House sales to foreigners increased by 81.9% to 3,168 units in the same period.

House price data for December 2018 also confirmed the weak outlook in the housing market. Hedonic price index increased by 5.4% in December compared to the same month of the previous year, while house prices in real terms fell by 12.4%.



Automotive and white goods sales continue to decline.

According to the data published by the Automotive Distributors' Association, automobile and light commercial vehicle sales decreased by 47% yoy in February, despite the reduction in SCT and VAT. According to White Goods Manufacturers' Association of Turkey data, white goods sales fell by 9% yoy in January. In this period, exports and white goods production contracted by 3% and 14%, respectively. Domestic white goods sales shrank by 17% in 2018 despite tax incentives.

Central government budget posted a surplus of 5.1 billion TRY.

In the first month of the year, central government [budget](#) revenues increased by 66.6% yoy to 97 billion TRY, while budget expenditures rose by 62.5% yoy to 91.9 billion TRY. Thus, budget surplus tripled compared

Source: Datastream, Markit, Turkstat

Turkish Economy

to the same month of the previous year and came in at 5.1 billion TRY. Transfer of the CBRT's profit to the budget in advance played a decisive role in this development.

Central Government Budget

	January		% Change
	2018	2019	
Expenditures	56.5	91.9	62.5
Interest Expenditures	6.0	7.3	20.8
Non-Interest Expenditures	50.5	84.6	67.5
Revenues	58.2	97.0	66.6
Tax Revenues	52.0	55.7	7.1
Other Revenues	6.2	41.3	564.8
Budget Balance	1.7	5.1	204.8
Primary Balance	7.7	12.4	61.0

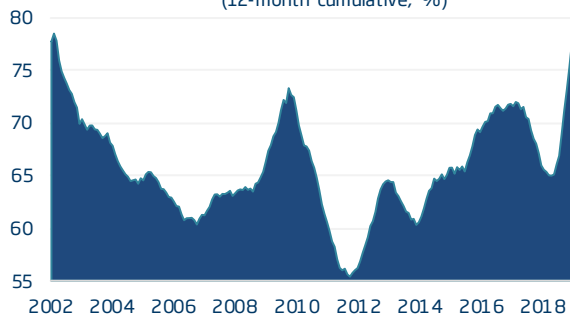
Numbers may not add up to total value due to rounding.

Foreign trade deficit kept contracting.

[Foreign trade](#) deficit has fallen for the eighth consecutive month in January 2019. Export volume rose by 5.9% yoy to 13.2 billion USD, while import volume was realized as 15.7 billion USD, decreasing by 27.2% yoy. Thus, foreign trade deficit decreased by 72.5% compared to the same period of the previous year and became 2.5 billion USD. Import coverage ratio, which was 57.8% in January last year, increased to 84% in the first month of 2019.

Import Coverage Ratio

(12-month cumulative, %)

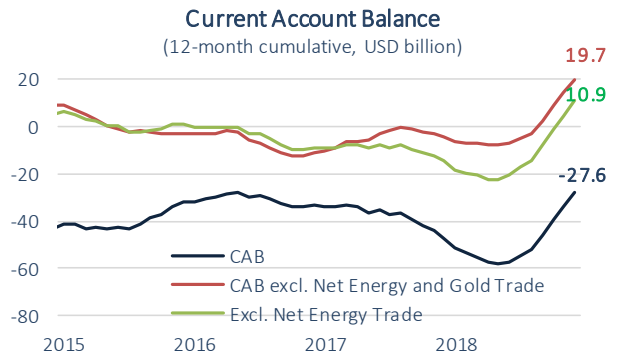


According to the 12-month cumulative figures, exports surged to a historic high of 168.7 billion USD, while imports decreased to 217.2 billion USD. Thus, foreign trade deficit fell to 48.5 billion USD, the lowest level since March 2010. Import coverage ratio reached 77.7%, the highest level since 2002.

According to the provisional data announced by the Ministry of Commerce based on New General Trading System, the foreign trade deficit continued to contract on an annual basis in February. In this period, exports increased by 3.7%, while imports decreased by 18.7%. Thusly, foreign trade deficit narrowed by 69.6% yoy and was realized as 1.8 billion USD.

Current account deficit was 27.6 billion USD in 2018. In 2018, [current account deficit](#) (CAD) decreased by 41.6% yoy to 27.6 billion USD, the lowest level since 2009. Contraction in CAD was mainly driven by the fall in

foreign trade deficit. Besides the slowdown in domestic demand, the annual fall in Brent crude oil prices (almost 30%) was effective in this contraction. Annual rise in net tourism revenues (16.8%) also supported the recovery in CAD. In 2018, CAD excluding net energy trade gave a surplus of 10.9 billion USD. Excluding gold trade from this figure, CAD rose to 19.7 billion USD.



Portfolio investments displayed a weak performance throughout the year, while official reserves and net errors-omissions stood out in financing the current account deficit.

Annual CPI inflation was 19.67%.

[CPI](#) came in below expectations, rising by 0.16% mom in February. According to the Reuters' survey, the monthly CPI inflation was expected to be 0.4%. Domestic PPI (D-PPI) followed a flat course in February, increasing by 0.09% mom.

Having remained above 20% since September 2018, annual CPI inflation declined to 19.67% in February thanks to relatively stable course in Turkish lira, slowdown in domestic demand and measures taken by government. Annual D-PPI inflation, which followed a downward trend since October, continued this trend and declined to 29.59% in February. Thus, annual D-PPI inflation fell below 30% for the first time since July 2018.

January (change %)	CPI		D-PPI	
	2018	2019	2018	2019
Monthly	1.02	1.06	0.99	0.45
Annual	10.35	20.35	12.14	32.93
Annual Average	11.23	17.16	15.66	28.70

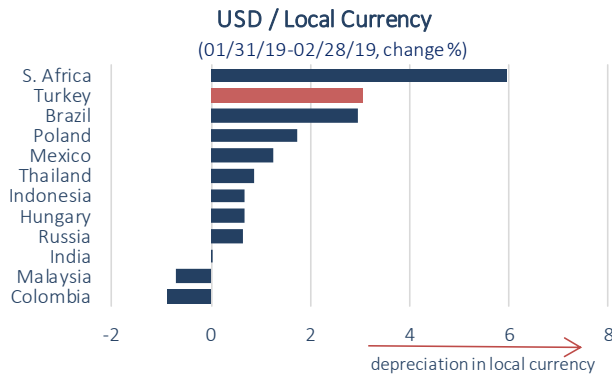
Source: Turkstat, Datastream, CBRT, Ministry of Trade, Ministry of Treasury and Finance

	31/Jan	28/Feb	Change
5-Y CDS (basis points)	303	303	-0 bps ▼
TR 2-Y Benchmark Yield	18.39%	18.79%	40 bps ▲
BIST-100	104,074	104,530	0.4% ▲
USD/TRY	5.1759	5.3340	3.1% ▲
EUR/TRY	5.9391	6.0739	2.3% ▲
Currency Basket*	5.5575	5.7039	2.6% ▲

(*) (0.5 USD/TRY + 0.5 EUR/TRY)

TL depreciated in February.

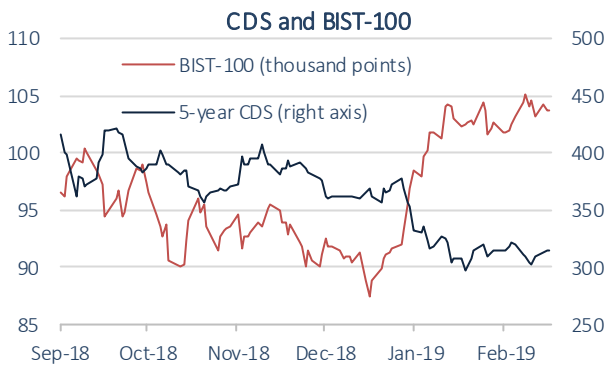
USD/TL, which fell to 5.15 on 31 January thanks to CBRT's statements about preserving the current tight monetary stance, followed an upward trend in the following days due to the appreciation of USD in the global markets in the first half of February and, CBRT's reserve requirement decision. USD/TL increased by 3.1% mom to 5.3340 at the end of the month.



BIST-100 index followed a fluctuating course.

Having posted a rapid rise in January, BIST-100 index followed a fluctuating course. The index rose by 0.4% mom and ended February at 104,530.

Turkey's 5-year CDS spreads, which have been declining since mid-January, fell to 296 on 5 February, the lowest level since July 2018. However, CDS spread was flat and was realized as 303 at the end of February.



Treasury completed its borrowing program slightly below anticipations.

Treasury borrowed a total of 16.4 billion TRY in February. According to the the program, Treasury planned to borrow 17 billion TRY against 22.8 billion TRY debt redemption during this period. While interest rate was realized as 18.34% in the re-issuance of 2-year benchmark bond, 2-year benchmark bond yield was 18.68% in the secondary market on the same day. 2-year benchmark bond yield rose by 40 basis points mom to 18.79% as of 28 February.

2-year Benchmark Bond Yield (%)



CBRT cut the required reserve ratios.

CBRT reduced the Turkish lira reserve requirement ratio by 100 basis points for deposits and participation funds with maturities up to 1-year and for other liabilities with maturities up to (and including) 3-year, and by 50 basis points for all other liabilities subject to reserve requirements. Furthermore, the upper limit of the facility of holding standard gold converted from wrought or scrap gold collected from residents has been increased from 5% to 10% of Turkish lira reserve requirements. While CBRT did not made any statements regarding the impact of the regulation, required reserves of 3.3 billion TRY and 2.3 billion USD are expected to be released.

S&P affirmed Turkey's credit rating and outlook.

S&P maintained Turkey's sovereign rating at "B+" with a stable outlook. S&P stated that Turkey's credit rating could be lowered if the institution sees an increasing likelihood of systemic banking distress with the potential to undermine Turkey's fiscal position. S&P foresees that the economy will contract by 0.5% in 2019, adding that the uncertainties which affect the growth forecast remain. It was also stated that the credit rating may stay under pressure if growth weakens beyond the projections.

Moody's indicated that measures taken by the government in order to increase loan growth had a negative impact on banks' credit ratings. In Moody's' Credit Outlook report, Turkish economy is expected to contract 2% and inflation is anticipated to be 17% in 2019.

Source: CBRT, Datastream, Reuters, BIST

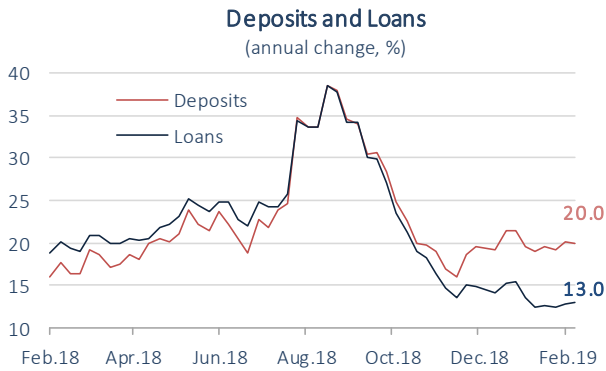
Banking Sector

Annual rise in deposit volume was 20%.

According to the Weekly Bulletin published by the BRSA, as of February 22, deposit volume increased by 20% yoy and by 2% ytd to 2,085 billion TRY. TRY deposits rose by 8% compared to the same period of the previous year and was realized as 1,028 billion TRY. On the other hand, FX deposits in USD terms declined by 4.3% in this period. FX deposits in USD terms increased by 10.2 billion USD compared to year-end.

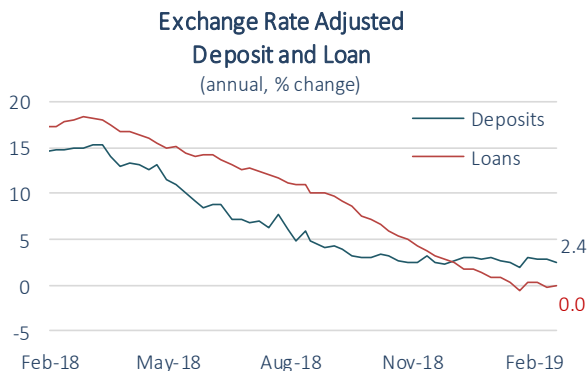
Annual loan growth remained weak.

As of February 22, total loan volume increased by 13% yoy and 0.5% ytd to 2,405 billion TRY. While TRY loans rose by 1.1% yoy to 1,405 billion TRY, FX loans in USD terms declined by 2.2% to 180 billion USD during the same period. On weekly basis, TRY loans seem to recover. In the last 4 weeks, TRY loans surged up by 19 billion TRY.



FX adjusted volumes...

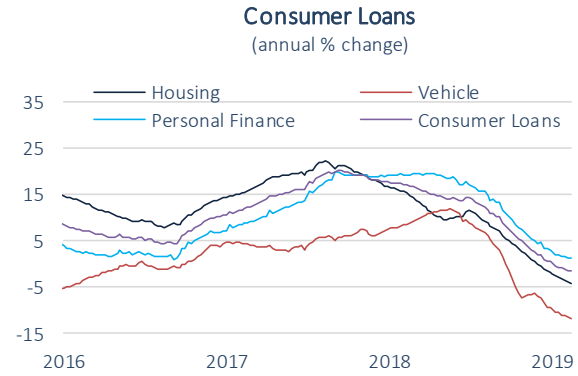
The impacts of foreign exchange developments on banking indicators continued in 2019. According to FX rate adjusted figures annual rise in deposits volume declined to 2.4% while loan volume did not display a significant change as of February 22.



Consumer loans declined on an annual basis.

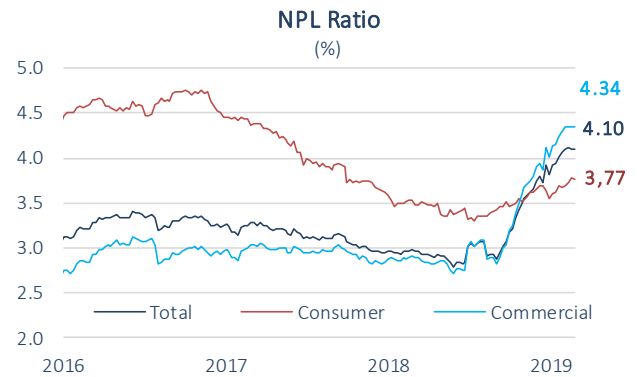
Contraction in consumer loans excluding consumer credit cards since January 11 accelerated. As of February 22, consumer loans declined by 1.7% yoy. During this

period, vehicle loans decreased by 12.1% yoy in parallel with the contraction in the automotive market, while the annual fall in housing loans was 4.5%. Besides, annual rise in personal finance loans which has been declining since August 2018 fell to 1.3%.



Upward trend in NPL ratio continues.

As of February 22, gross non-performing loans surged up by 56.5% yoy to 101.6 billion TRY. Having followed an upward trend recently, NPL ratio reached 4.1% as of February 22. In the same period, NPL ratio for consumer and commercial loans were 4.34% and 3.77%, respectively.



Net foreign currency position...

As of February 22, banks' on-balance sheet FX position was (-) 40,719 million USD, while off-balance sheet FX position was (+) 42,788 million USD. Hence, banking sector's net FX position was realized as (+) 2,069 million USD.

Source: BRSA Weekly Bulletin

Concluding Remarks

Developments regarding trade wars, which have been out of scope for a while, have come to the forefront after the start of negotiations between senior officials of the United States and China in February. In addition to the positive course of the negotiations, postponing the deadline of additional tariffs and the developments which indicate that the trade war between the world's two largest economies can be solved in March were watched closely.

While the damage of the trade war on global economy is widely discussed, the leading indicators show the loss of momentum in economic activity. Although the US economy grew above the expectations in 2018, the data for 2019 display a mixed picture. A similar outlook is still valid for the Euro Area as well where the data for the first quarter of this year indicate a moderate outlook. In China, PMI data indicate that the manufacturing industry started to 2019 with a contraction.

The momentum loss on the global scale increases the expectations that the major central banks will adopt an accommodative monetary policy in the following period. This expectation has an upward impact on commodity prices and support capital flows towards developing countries.

Domestic data show that the slowdown in economic activity has become more evident. Calendar adjusted industrial production, which displayed its weakest performance since June 2009 in December, contracted by 7.5% yoy in the last quarter of the year. On the other hand, the current account deficit was at its lowest level since 2009 with 27.6 billion USD in 2018.

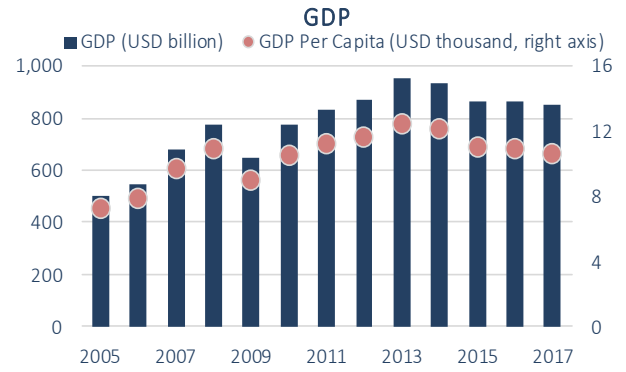
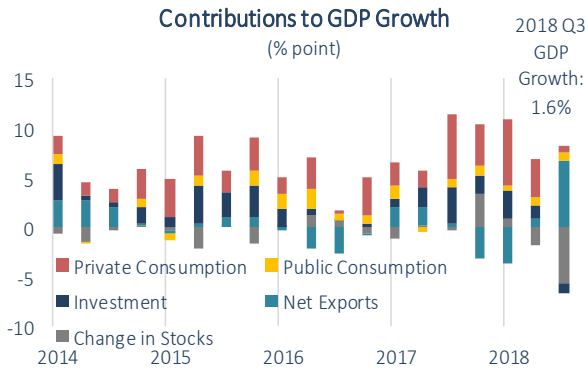
The improvement in the inflation indicators since November due to the rebalancing in economic activity and the relatively stable outlook in the Turkish lira continued in 2019. Momentum loss in food prices thanks to the measures taken played a role in this development.

Forecasts (%)	2018	2019
Growth	2.9	1.0
Current Account Deficit/GDP	3.3	2.0
Inflation (year-end)	20,3 (A)	16.0

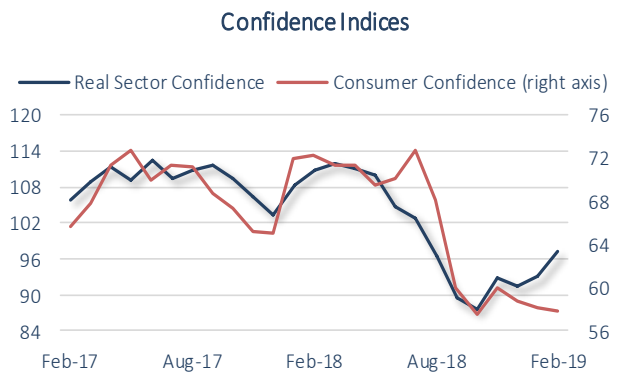
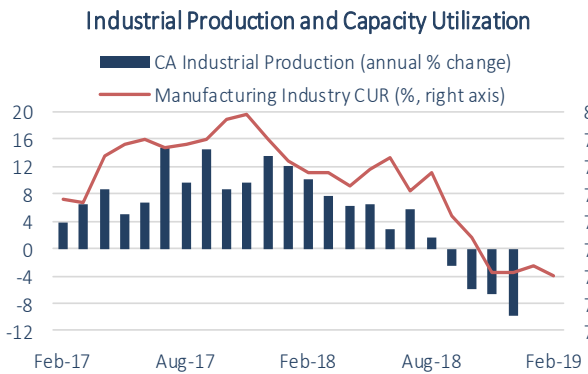
(A) Actual

Turkish Economy- Macroeconomic Indicators

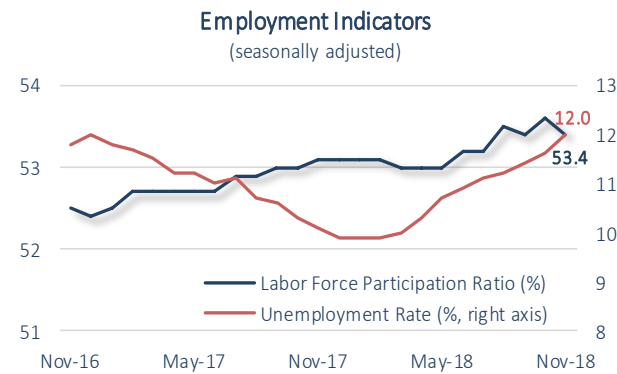
Growth



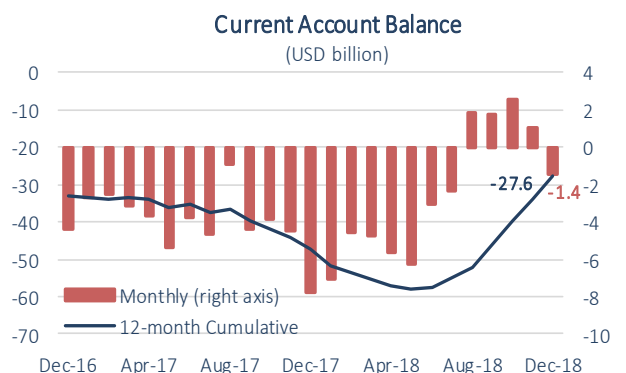
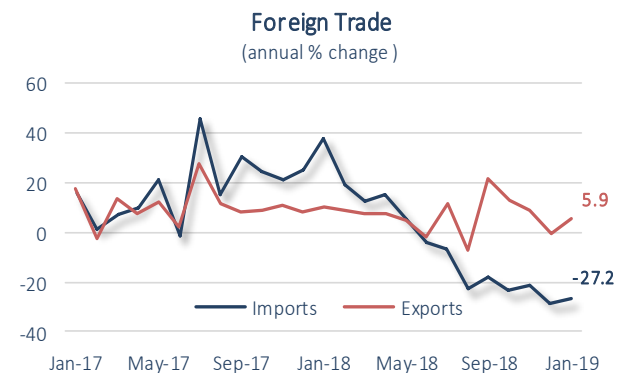
Leading Indicators



Labor Market



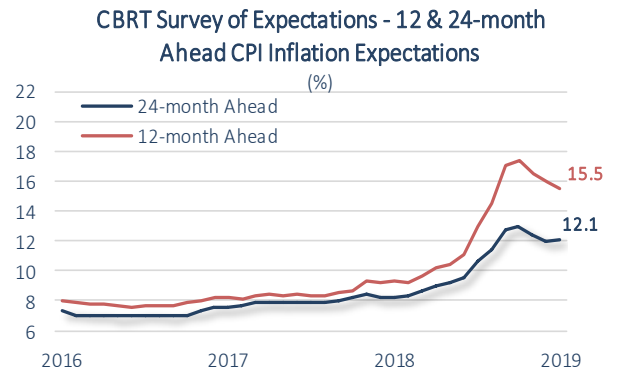
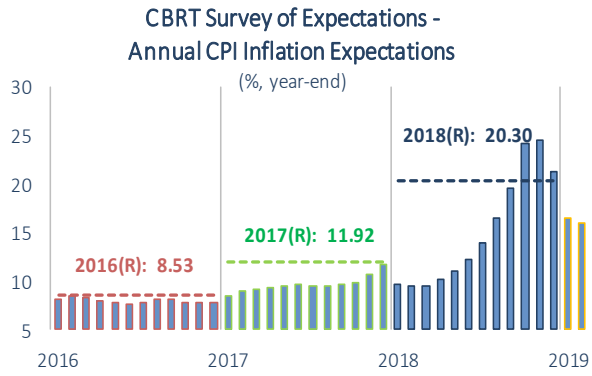
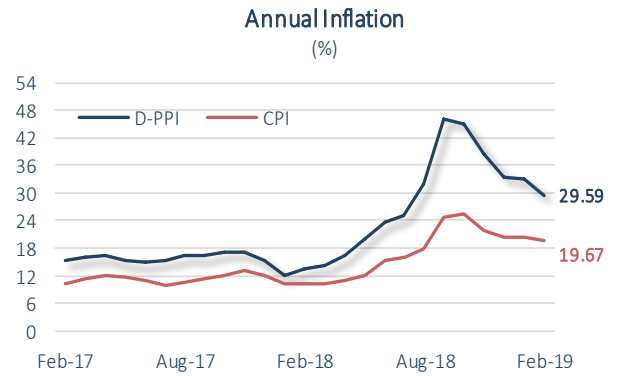
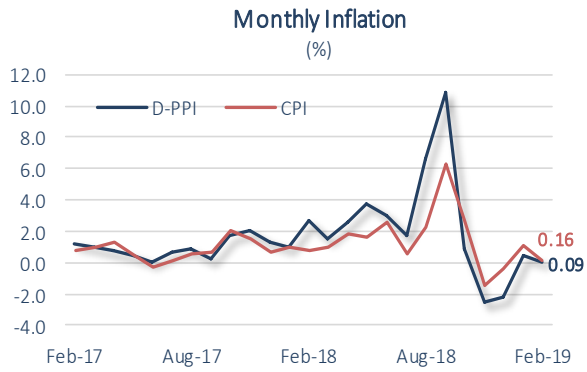
Foreign Trade and Current Account Balance



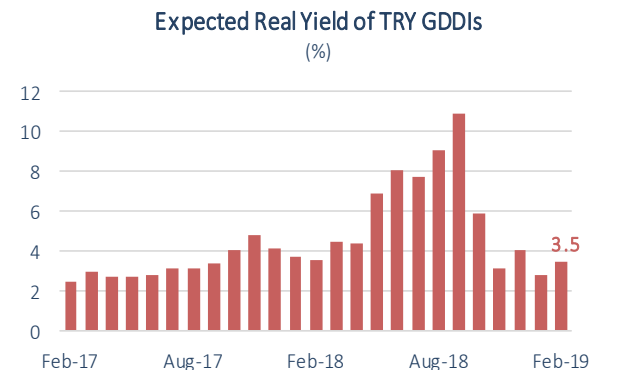
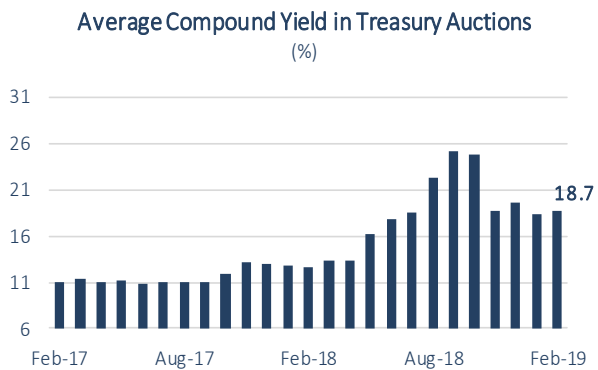
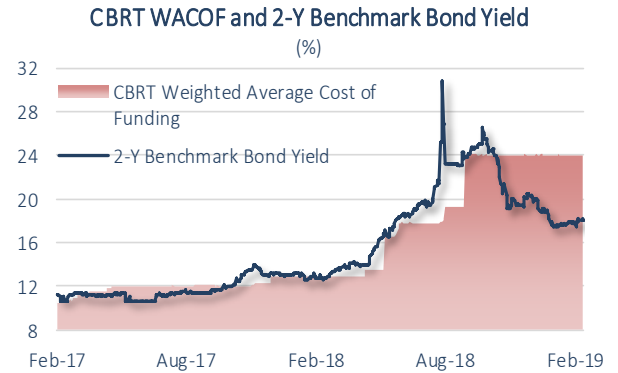
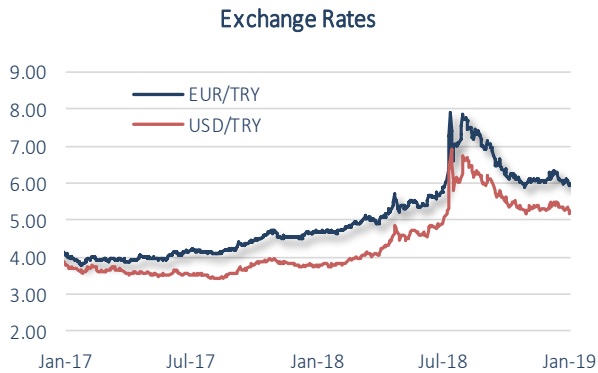
(CA) Calendar adjusted

Source: Datastream, CBRT, Turkstat

Inflation



Foreign Exchange and Bond Market



Turkish Economy - Macroeconomic Indicators

Growth	2013	2014	2015	2016	2017	18-Q1	18-Q2	18-Q3
GDP (USD billion)	950	935	862	863	851	207	204	187
GDP (TRY billion)	1,810	2,045	2,339	2,609	3,107	788	884	1,013
GDP Growth Rate (%)	8.5	5.2	6.1	3.2	7.4	7.3	5.2	1.6
Inflation (%)						Dec-18	Jan-19	Feb-19
CPI (annual)	7.40	8.17	8.81	8.53	11.92	20.30	20.35	19.67
Domestic PPI (annual)	6.97	6.36	5.71	9.94	15.47	33.64	32.93	29.59
Seasonally Adjusted Labor Market Figures						Sep-18	Oct-18	Nov-18
Unemployment Rate (%)	9.1	10.3	10.2	12.0	9.9	11.4	11.6	12.0
Labor Force Participation Rate (%)	48.5	51.0	51.7	52.4	53.1	53.4	53.6	53.4
FX Rates						Dec-18	Jan-19	Feb-19
CPI Based Real Effective Exchange Rate	101.1	105.9	99.2	93.6	86.4	76.4	75.7	77.2
USD/TRY	2.1485	2.3378	2.9189	3.5176	3.7916	5.3199	5.1759	5.3340
EUR/TRY	2.9605	2.8288	3.1708	3.7102	4.5530	6.0815	5.9391	6.0739
Currency Basket (0.5*EUR+0.5*USD)	2.5545	2.5833	3.0448	3.6139	4.1723	5.7007	5.5575	5.7039
Foreign Trade Balance⁽¹⁾ (USD billion)						Nov-18	Dec-18	Jan-19
Exports	151.8	157.6	143.8	142.5	157.0	168.0	168.0	168.7
Imports	251.7	242.2	207.2	198.6	233.8	229.6	223.0	217.2
Foreign Trade Balance	-99.9	-84.6	-63.4	-56.1	-76.8	-61.6	-55.1	-48.5
Import Coverage Ratio (%)	60.3	65.1	69.4	71.8	67.1	73.2	75.3	77.7
Balance of Payments⁽¹⁾ (USD billion)						Oct-18	Nov-18	Dec-18
Current Account Balance	-63.6	-43.6	-32.1	-33.1	-47.3	-39.5	-33.9	-27.6
Capital and Financial Accounts	-62.7	-43.2	-22.7	-22.0	-46.7	-21.0	-16.2	-6.4
Direct Investments (net)	-9.9	-6.3	-14.2	-10.8	-8.8	-8.2	-9.2	-9.5
Portfolio Investments (net)	-24.0	-20.2	15.5	-6.3	-24.5	3.8	0.7	3.0
Other Investments (net)	-38.7	-16.2	-12.1	-5.7	-5.2	11.2	12.2	10.5
Reserve Assets (net)	9.9	-0.5	-11.8	0.8	-8.2	-27.9	-19.9	-10.4
Net Errors and Omissions	1.0	0.5	9.5	11.1	0.6	18.4	17.7	21.2
Current Account Balance/GDP (%)	-6.7	-4.7	-3.7	-3.8	-5.6	-	-	-
Budget⁽²⁾⁽³⁾ (TRY billion)						Nov-18	Dec-18	Jan-19
Expenditures	408.2	448.8	506.3	584.1	678.3	745.4	830.5	91.9
Interest Expenditures	50.0	49.9	53.0	50.2	56.7	71.9	74.0	7.3
Non-interest Expenditures	358.2	398.8	453.3	533.8	621.6	673.5	756.5	84.6
Revenues	389.7	425.4	482.8	554.1	630.5	690.8	757.8	97.0
Tax Revenues	326.2	352.5	407.8	459.0	536.6	575.8	621.3	55.7
Budget Balance	-18.5	-23.4	-23.5	-29.9	-47.8	-54.5	-72.6	5.1
Primary Balance	31.4	26.5	29.5	20.3	8.9	17.3	1.3	12.4
Budget Balance/GDP (%)	-1.0	-1.1	-1.0	-1.1	-1.5	-	-	-
Central Government Debt Stock (TRY billion)						Nov-18	Dec-18	Jan-19
Domestic Debt Stock	403.0	414.6	440.1	468.6	535.4	578.8	586.1	597.9
External Debt Stock	183.2	197.9	238.1	291.3	341.0	470.4	481.0	500.2
Total Debt Stock	586.2	612.5	678.2	760.0	892.7	1,049.2	1,067.1	1,098.1

(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)	2013	2014	2015	2016	2017	Jan.18	Jan.1	Change ⁽¹⁾
TOTAL ASSETS	1,732	1,994	2,357	2,731	3,258	3,867	3,861	18.5
Loans	1,047	1,241	1,485	1,734	2,098	2,395	2,377	13.3
TRY Loans	753	881	1,013	1,131	1,414	1,439	1,441	1.9
Share (%)	71.9	71.0	68.2	65.2	67.4	60.1	60.6	-
FX Loans	295	360	472	603	684	956	937	37.0
Share (%)	28.1	29.0	31.8	34.8	32.6	39.9	39.4	-
Non-performing Loans	29.6	36.4	47.5	58.2	64.0	96.6	99.9	56.1
Non-performing Loan Rate (%)	2.8	2.9	3.1	3.2	3.0	3.9	4.0	-
Securities	287	302	330	352	402	478	496	23.4
TOTAL LIABILITIES	1,732	1,994	2,357	2,731	3,258	3,867	3,861	18.5
Deposits	946	1,053	1,245	1,454	1,711	2,036	2,048	19.7
TRY Deposits	594	661	715	845	955	1,042	1,034	8.4
Share (%)	62.8	62.8	57.4	58.1	55.8	51.2	50.5	-
FX Deposits	352	391	530	609	756	994	1,014	34.0
Share (%)	37.2	37.2	42.6	41.9	44.2	48.8	49.5	-
Securities Issued	61	89	98	116	145	174	175	20.2
Payables to Banks	254	293	361	418	475	563	547	15.2
Funds from Repo Transactions	119	137	157	138	99	97	105	6.7
SHAREHOLDERS' EQUITY	194	232	262	300	359	421	426	18.5
Profit (Loss) of the Period	24.7	24.6	26.1	37.5	49.1	53.5	3.2	-
RATIOS (%)								
Loans/GDP	57.9	60.7	63.5	66.5	67.6			
Loans/Assets	60.5	62.2	63.0	63.5	64.4	61.9	61.6	-
Securities/Assets	16.6	15.2	14.0	12.9	12.3	12.4	12.8	-
Deposits/Liabilities	54.6	52.8	52.8	53.2	52.5	52.6	53.0	-
Loans/Deposits	110.7	117.9	119.2	119.3	122.6	117.6	116.1	-
Capital Adequacy (%)	15.3	16.3	15.6	15.6	16.9	17.3	17.1	-

(1) Year-to-date % change

Source: BRSA, Turkstat

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