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Turkish Economy	2
Financial Markets	4
Banking Sector.....	5
Concluding Remarks.....	6
Graphs.....	7
Tables.....	9

Global Economy

Despite the resumption of talks between the US and China, concerns about the trade war keep rising. The US administration announced that an additional 10% tariffs on 300 billion USD of Chinese products would be imposed as of September 1st.

In its July meeting, Fed cut the policy rate by 25 basis points in line with market expectations. Fed also decided to end its balance sheet unwinding. Fed Chair Powell added that this rate cut is not the beginning of a rate cut cycle.

Although the ECB did not change interest rates at its July meeting, the Bank signaled that expansionary steps would be taken in the following period.

The possibility of a no-deal Brexit strengthened as Boris Johnson became the Prime Minister.

Central banks of developing countries, especially Asian countries which are being affected from trade wars, are lowering interest rates to support economic activity.

Slowdown in the Chinese economy deepened in the second quarter of the year. The country's economy recorded the slowest growth for more than 27 years with 6.2%.

The International Monetary Fund revised its global growth expectations downwards for 2019 and 2020. Having significantly reduced growth expectations for developing countries, the Fund reduced growth rate forecast for global trade volume by 0.9 point for this year.

Escalating tension in the trade war triggered demand-driven concerns, putting downward pressure on oil prices. Gold prices, supported by safe heaven purchases and expectations for monetary expansion, rose to 6-year high at mid-month. In the second half of the month, gold prices posted a limited decrease in the rest of the month due to the rise in USD.

Turkish Economy

Seasonally adjusted unemployment rate reached 13.8% in April, the highest in 10 years, while the youth unemployment rate was 25.5%.

According to the calendar adjusted figures, industrial production contracted by 1.3% in May. On the other hand, monthly increase of seasonally adjusted industrial production supported the view that the slowdown in the economic activity has lost momentum in the second quarter compared to the previous one.

Having realized as 46.7 in July, manufacturing PMI pointed out that the slowdown in the sector has continued.

The contraction in the foreign trade deficit continued in June. As the number of working days fell compared to a year ago due to feast holiday, exports and imports volume contracted by 14.3% yoy and 22.7% yoy, respectively. Hence, foreign trade deficit decreased by 42.5% compared to the same period of last year.

Slowdown in the economic activity continued to support the current account balance in May. Current account balance, which posted a deficit of 6.2 billion USD in May 2018, posted a surplus of 151 million USD in the same month of this year.

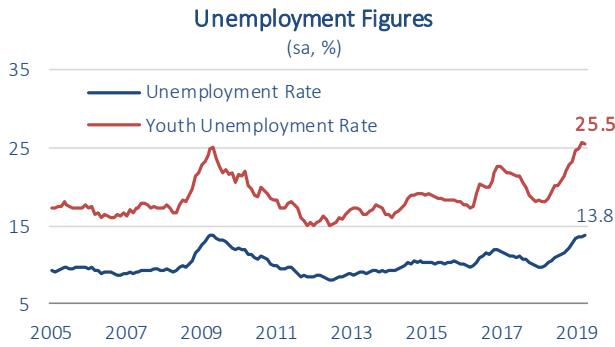
Central government budget deficit was realized as 12.1 billion TRY in June. In the first half of the year, budget deficit reached at historical high with 78.6 billion TRY.

In July, CPI rose by 1.36% mom. Annual CPI inflation was realized 16.6% in the same period. At its meeting held on July 25, the CBRT cut the policy rate from 24% to 19.75%. In its Inflation Report published on July 31, the CBRT lowered its year-end inflation forecast to 13.9%. The inflation forecast for 2020, on the other hand, remained at 8.2%.

Fitch downgraded Turkey's credit rating to BB-.

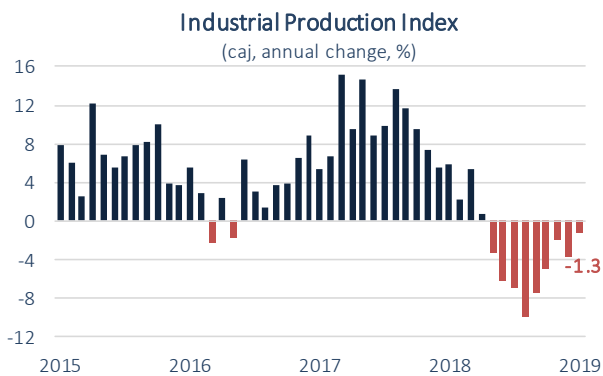
Seasonally adjusted unemployment rate reached the highest level in 10 years.

Unemployment rate increased by 3.4 points to 13% in April compared to the same month of the previous year. Seasonally adjusted unemployment rate rose to 13.8% in April, the highest in 10 years, while the youth unemployment rate was 25.5%. According to seasonally adjusted figures, the number of persons employed decreased in the agriculture, construction and services sectors mom, whereas it increased in industrial sector.



Better-than-expected outlook in industrial production...

According to the calendar adjusted figures, in May, industrial production contracted by 1.3%, showing a better-than-expected outlook. During this period, manufacturing industry and mining & quarrying sub-indices decreased, while the production in electricity, gas and steam industries increased. Thus, the year-on-year decrease of 4.7% in the first quarter of 2019 fell to 2.6% in April-May period. Monthly increase of 1.3% in the seasonally and calendar adjusted industrial production also supported the view that the slowdown in the economic activity has lost momentum in the second quarter compared to the previous one.



Manufacturing PMI declined to 46.7 in July.

Manufacturing PMI, which was 47.9 in June, fell to 46.7 in July, pointing out that the slowdown in the sector have continued for 16 months. During this period, total new orders continued to decline amid challenging market conditions, while new export orders remained flat compared to the previous month. The pace at rise in input costs and output prices softened somewhat.

Retail sales volume have contracted also in May.

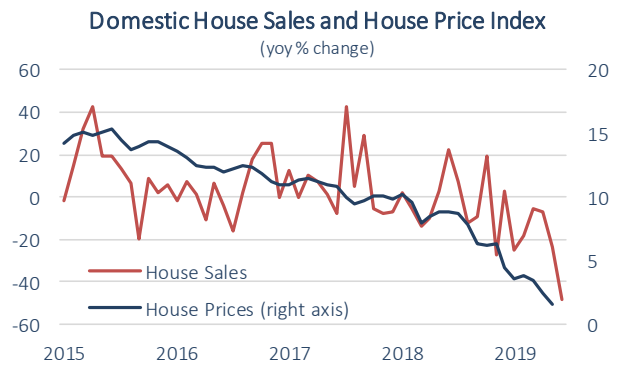
Retail sales volume continued to present a negative outlook due to the weakness in economic activity. Calendar adjusted retail sales volume decreased by 3.7% in May compared to the same month of the previous year, declining for consecutive 9 months. During this period, food, drinks & tobacco sales and non-food (except automotive fuel) sales fell by 3% and 2.3%, respectively. In the same period, automotive fuel sales decreased by 7.8%.

Real sector confidence declined in July.

According to seasonally adjusted figures, real sector confidence index decreased by 3 points to 96.6 in July on a monthly basis. In the same period, seasonally adjusted capacity utilization rate dropped by 0.7 points to 75.9%. Also, consumer confidence index decreased by 1.1 points mom to 56.5 in July.

Housing market remained weak.

Housing market continued to display a weak outlook. According to data released by TURKSTAT, house sales decreased by 48.6% yoy in June. In this period, mortgage sales dropped by 84.6%, while other sales fell by 24.7%. The number of house sold for the first time decreased by 59.2% yoy to 23,265 units, while second-hand house sales decreased by 38.9% to 38,090 units. On the other hand, the strong course of foreigners' demand continued in this period.



The sharp decline in house demand mirrored in house prices. In May, residential property price index (RPPI), which was released by CBRT, increased by 0.5% compared to the previous month. While the index rose by 1.6% on an annual basis in nominal terms, prices decreased by 14.4% in real terms.

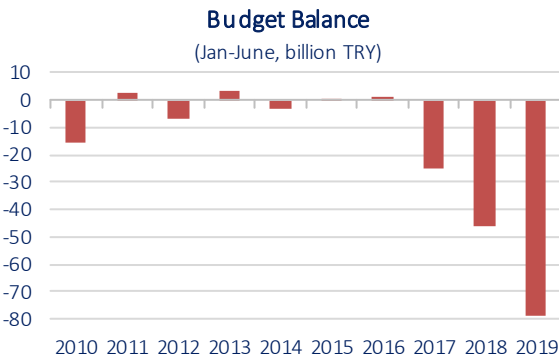
Budget deficit was at historical high in the first half of the year.

Central government budget deficit was realized as 12.05 billion TRY in June. The deficit was 25.6 billion TRY in the same month of the previous year. In this period, budget revenues recorded a slight increase of 7.6% to 55.5 billion TRY while budget expenditures decreased by

Source: Datastream, Markit, Turkstat, CBRT

12.5% to 67.5 billion TRY. Primary deficit, which was 23.2 billion TRY in June 2018, was realized as 7.7 billion TRY in the same month of this year.

The relatively weak performance of budget revenues in the first half of the year led central government budget deficit to increase by 70.5% yoy. Thus, budget deficit in the first half of the year was realized at historical high with 78.6 billion TRY. Primary deficit also rose by 126.6% to 27.8 billion TRY in this period.



Foreign trade deficit was 3.2 billion USD in June .

In June, export volume contracted by 14.3% yoy, the largest decline since January 2016. In the same period, the import volume decreased by 22.7% to 14.3 billion USD. The 9-day holiday was effective on those declines. Foreign trade deficit decreased by 42.5% compared to the same period of the previous year and was realized as 3.2 billion USD. Import coverage ratio, which was 70.1% in June 2018, increased to 77.7% in this period.

	June		Change (%)
	2018	2019	
(billion USD)			
Exports	12.9	11.1	-14.3
Imports	18.4	14.3	-22.7
Foreign Trade Deficit	-5.5	-3.2	-42.5
Import Coverage (%)	70.1	77.7	-

According to 12-month cumulative figures, export volume increased by 4.8% to 169.5 billion USD in June, while import volume decreased by 20% to 198.7 billion USD. During this period, import coverage ratio rose to 85.3%, a historic high level.

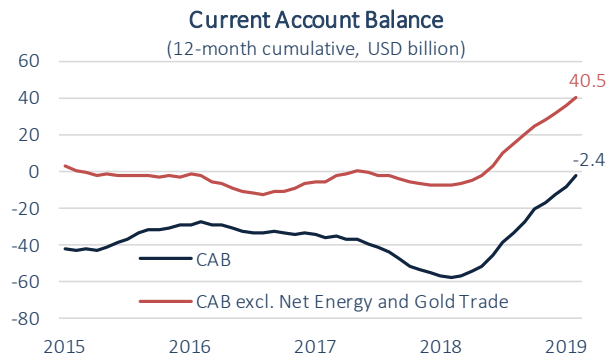
According to the provisional data announced by the Ministry of Commerce, exports increased by 8.3% yoy in July, while imports decreased by 8%. Thus, foreign trade deficit narrowed by 46.5%.

In May, current account balance posted a surplus of 151 million USD.

Slowdown in economic activity continued to be effective on current account balance in May. Current account balance, which registered a deficit of 6.2 billion USD in May 2018, posted a surplus of 151 million USD in the same month of this year. The course of foreign trade

balance and the rise in tourism revenues led this development. According to the balance of payments data, foreign trade deficit decreased by 89.2% to 706 million USD compared to the same period of the previous year, while net travel revenues increased by 16.2%, contributing 1.8 billion USD to the current account balance.

12-month cumulative current account deficit, which continued to decline in May, fell to 2.4 billion USD, the lowest level since February 2003. Excluding net energy and gold imports, 12-month current account surplus reached 40.5 billion USD, the record level of all times.



In July, CPI increased by 1.36% on a monthly basis.

In July, CPI rose by 1.36% mom. According to the Reuters' Survey, CPI was expected to increase by 1.6% mom. Domestic PPI (D-PPI) declined by 0.99% in this period.

July	CPI		D-PPI	
	2018	2019	2018	2019
(change %)				
Monthly	0.55	1.36	1.77	-0.99
Year-to-Date	9.77	6.44	17.56	7.02
Annual	15.85	16.65	25.00	21.66
Annual Average	12.00	19.91	17.41	32.34

Having fallen to the lowest level in one year with 15.72% in June, annual CPI inflation increased slightly to 16.65% in July. D-PPI inflation dropped to the lowest level since May 2018 with 21.66%.

In July, prices in all main expenditure groups except clothing & footwear and food increased. The highest monthly price increases were in transport group with 4.5% and furnishings and household equipment group with 4.2% as tax cuts in related sectors expired during this period. Also, housing group contributed 44 bps to consumer inflation due to the rise in electricity prices. On the other hand, the decline in food and non-alcoholic beverages group prices limited the increase in inflation by 27 bps. The fall in fresh fruit and vegetable prices was behind this negative contribution. Clothing and footwear prices, which declined by 3.2% on a monthly basis, pushed inflation down by 21 bps.

Source: Turkstat, Datastream, Ministry of Trade

	28/Jun	31/Jul	Change
5-Y CDS (basis points)	397	360	-37 bps ▼
TR 2-Y Benchmark Yield	19.68%	15.98%	-370 bps ▼
BIST-100	96,485	102,082	5.8% ▲
USD/TRY	5.7873	5.5854	-3.5% ▼
EUR/TRY	6.5857	6.1806	-6.2% ▼
Currency Basket*	6.1865	5.8830	-4.9% ▼

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

CBRT cut the policy rate by 425 basis points.

At the Monetary Policy Committee Meeting held on July 25, CBRT cut the policy rate, one-week repo rate, from 24% to 19.75%. In the press release published after the meeting, it was noted that recently released data indicate a moderate recovery in the economic activity and the gradual recovery is likely to continue with the help of the disinflation trend and the partial improvement in financial conditions.

CBRT published its third inflation report of the year.

In its third Inflation Report of 2019 published on July 31, CBRT revised down its year-end inflation forecast for 2019 to 13.9%, 0.7 points lower than its April forecast. Inflation forecast for 2020, on the other hand, was left unchanged at 8.2%. Year-end food inflation forecast has been lowered to 15% for 2019 from 16% in the April Inflation Report. The average crude oil price assumptions for 2019 and 2020 revised down to 65 USD from 67.2 USD and to 62.6 USD from 66.2 USD, respectively. The new CBRT Governor Murat Uysal stated that there is a considerable room for maneuver in monetary policy and added that underlying trend in inflation and a reasonable rate of real return were taken into consideration in determining rate cuts.

Fitch downgraded Turkey's credit rating.

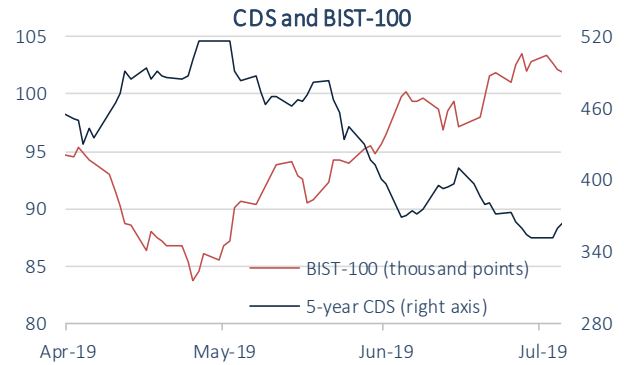
Fitch cut Turkey's credit rating by one notch citing the then CBRT governor's dismissal in its decision. While Turkey's credit rating was downgraded to "BB-", its rating outlook was kept as negative. Pointing out the risks linked to Çetinkaya's dismissal on harming the domestic confidence, which is already weak, Fitch also emphasized rising uncertainties related to structural reforms and management of public finance.

Markets...

Rising risk appetite towards emerging countries and expectations for a strong rate cut by the CBRT supported Turkish markets in July. Following the rate cut decision, expectations for a gradual rate cut cycle provided a further boost to the sentiment. On the other hand, uncertainties regarding the relations with the US, then the CBRT Head Murat Çetinkaya's dismissal, Fitch's downgrade and EU sanctions against Turkey limited the positive mood in the markets. Against this backdrop,

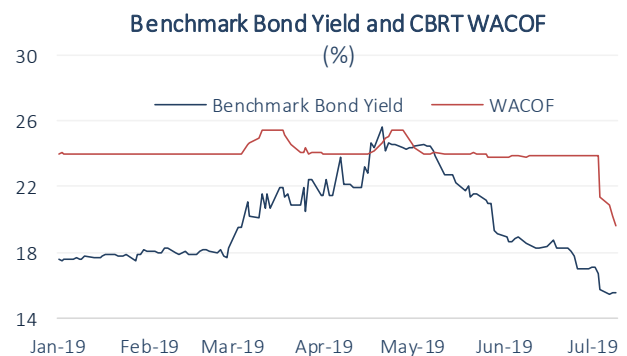
Turkey's 5-year CDS premium followed a volatile path in July. Compared to end-June, Turkey's 5-year CDS premium declined by 37 bps and became 360 on July 31.

The improvement in risk perception towards emerging countries supported the equity market in July. Having also supported by CBRT's rate cut, BIST-100 index reached 4-month high on July 25, exceeding 104,000. The index increased by 5.8% in July, completing the month at 102,082.



Following a fluctuating course in July, USD/TRY fell by 3.5% mom to 5.5854. EUR/TL dropped to 6.1806 in the same period.

Declining since the second half of June, interest rates continued this downward trend in July as the rate cut expectations strengthened. Following the CBRT's decision on July 25, 2-year benchmark bond yield, which continued to decline with further rate cut expectations, dropped to 15.98% as of July 31.

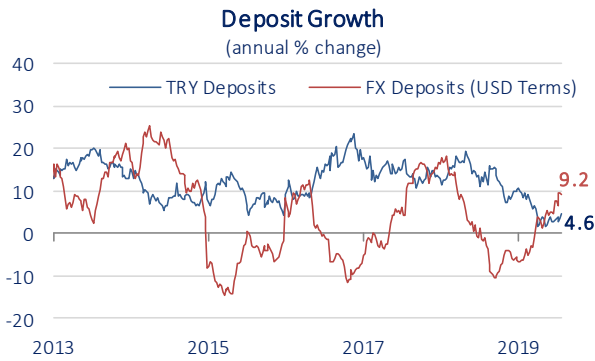


Source: CBRT, Datastream, Reuters, BIST

Banking Sector

Annual rise in TRY deposits was 4.6%.

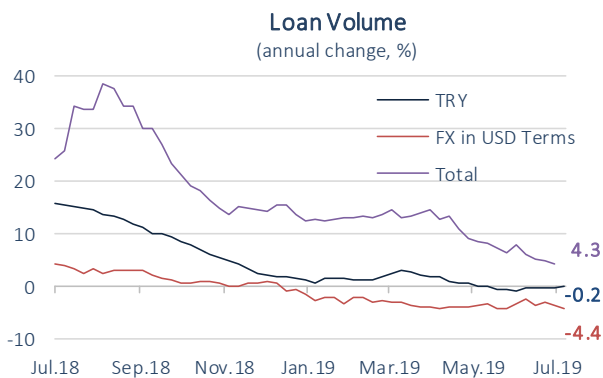
According to BRSA Weekly Bulletin, as of July 26, deposit volume increased by 15.7% yoy and by 12.3% compared to the end of 2018, reaching to 2,296 billion TRY. TRY deposits, which have been displaying a weak outlook since the beginning of 2019, increased by 4.6% compared to the same period of the previous year and rose by 2.9% compared to the year-end. Having fluctuated in 214-216 billion USD band in the last two months, FX deposits in USD terms expanded by 26.3 billion USD compared to the year-end.



Loan growth kept its weak trend.

Annual loan growth continues to decline. According to BRSA Weekly Bulletin, as of July 26, total loan volume recorded the slowest annual rise since the end of 2009, increasing by 4.3%. Total loan volume rose by 5% compared to the year-end and reached 2,512 billion TRY.

As of July 26, TRY loans decreased by 0.2% yoy to 1,513 billion TRY. Recording an annual decline since the beginning of the year, FX loans in USD terms fell by 4.4% to 177 billion USD in the same period. Considering the year-end figures, TRY loan volume rose by 5.2%, while FX loans in USD terms declined by 2.7%.

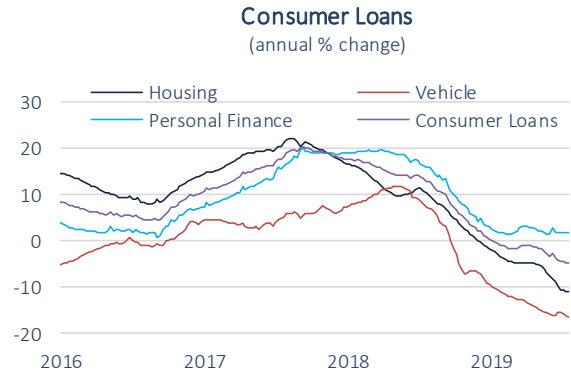


FX adjusted volumes...

According to FX rate adjusted figures annual rise in deposits volume was realized as 6.8% as of July 26. Loans volume declined by 1.7% in the same period.

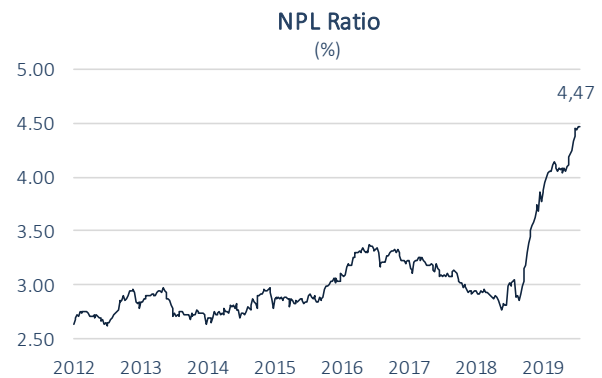
Consumer loans continued to decline on an annual basis.

Contraction in consumer loans excluding consumer credit cards since the beginning of the year continues to accelerate. As of July 26, consumer loans declined by 4.8% yoy. During this period, annual decline in vehicle loans deepened with declining by 16.7% yoy in parallel with the weak course in automotive sector, while the fall in housing loans was 11.2%.



NPL ratio was 4.47%.

Upward trend in non-performing loans continued in the week of July 26. NPL ratio increased to the highest level since June 2010 with 4.47%. As of the same date, the said ratio was realized as 3.77% for consumer loans and 4.65% in commercial loans.



Net foreign currency position...

As of July 26, banks' on-balance sheet FX position was (-)45,136 million USD, while off-balance sheet FX position was (+)48,360 million USD. Hence, banking sector's net FX position was realized as (+)3,223 million USD.

Concluding Remarks

As the trade negotiations between the United States and China resumed in the last week of July, trade war developments came to the forefront. Despite the ongoing talks, the US Government's announcement that it would impose an additional 10% tariffs on 300 billion USD worth of Chinese products and Chinese authorities' vows to retaliate caused pessimism over the negotiations. On the other hand, despite increasing concerns about the global economy, the Fed's interest rate cut and ECB's easing signals limited the deterioration in risk perception. Along with the support of optimistic expectations regarding global liquidity conditions, central banks of emerging countries are also cutting interest rates. At its meeting held on July 25, the CBRT joined this list by opting for a rate cut.

The slowdown in Turkish economy continues, albeit at a slower pace. Seasonally adjusted data indicate that the deterioration in the labor market persists. In July, the manufacturing PMI index remained below the threshold level for the 16th month in a row. During this period, import volume continued to decline, according to provisional data released by the Ministry of Commerce.

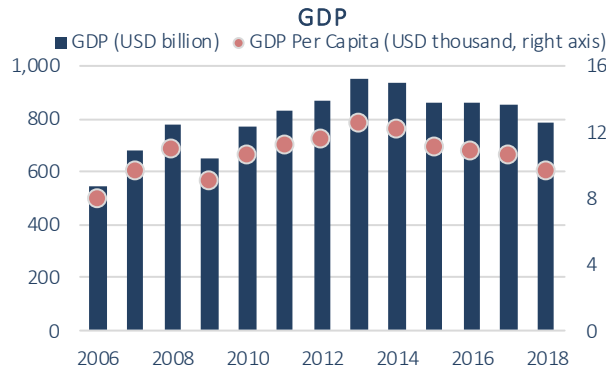
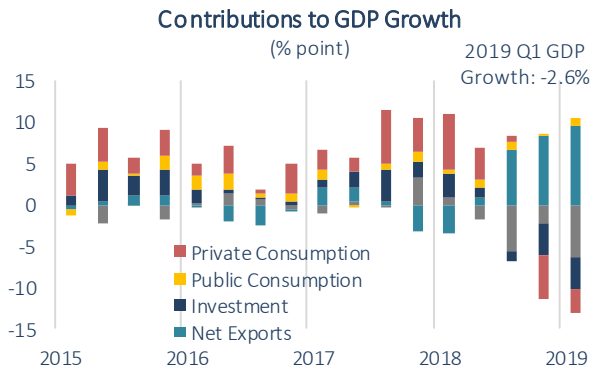
Weak outlook in domestic demand and favorable export figures suggest that the 12-month current account balance may give a surplus in the coming couple of months. On the other hand, budget indicators presented a weak picture in the first half of the year. The Treasury and Finance Ministry estimates that the budget deficit to GDP ratio will exceed the target but will be below 3% at the year-end.

Inflation indicators are also closely monitored. Having increased slightly in July, annual CPI inflation is expected to converge to single-digit levels in the coming months and then to rise somewhat through the end of the year. We believe that 13.9%, the downwardly revised year-end inflation forecast of CBRT in the Inflation Report announced on July 31, is attainable.

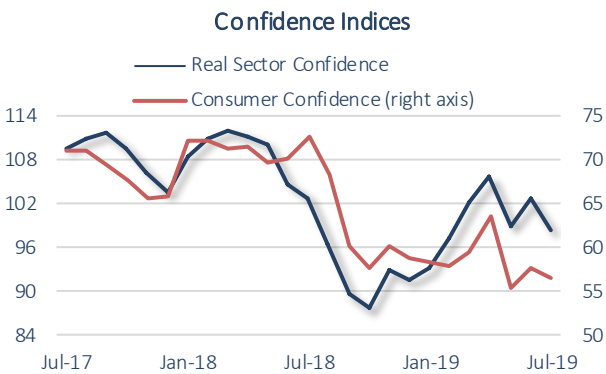
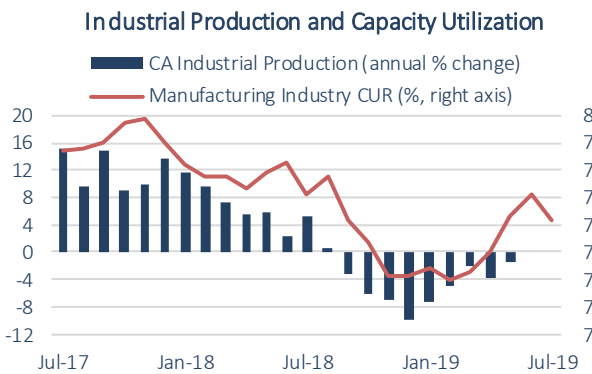
Forecasts (%)	2018 (A)	2019
Growth	2.6	1.0
Current Account Deficit/GDP	3.5	1.5
Inflation (year-end)	20.3	14.0

(A) Actual

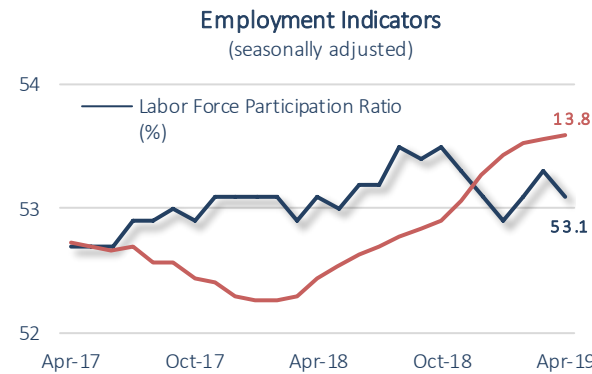
Growth



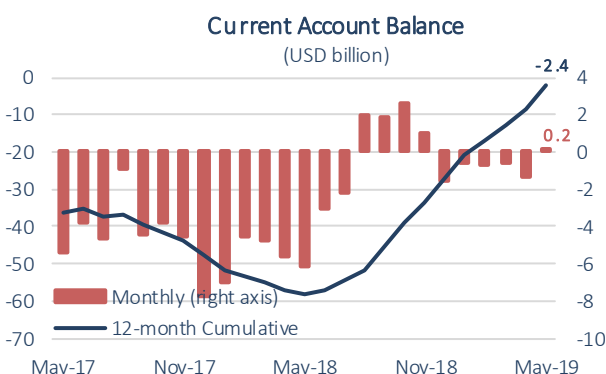
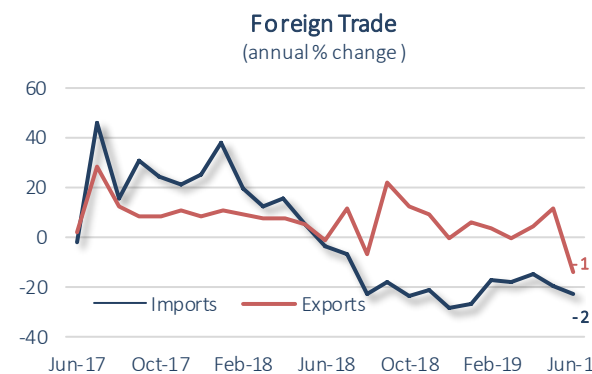
Leading Indicators



Labor Market



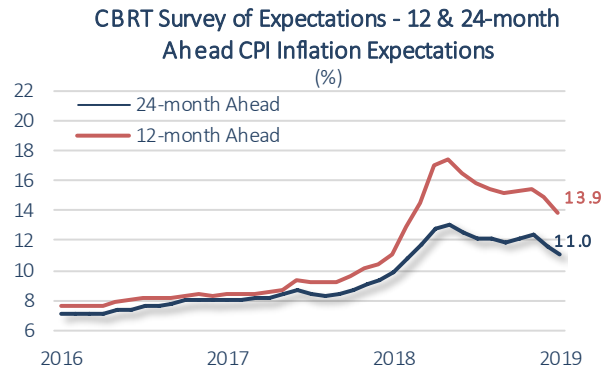
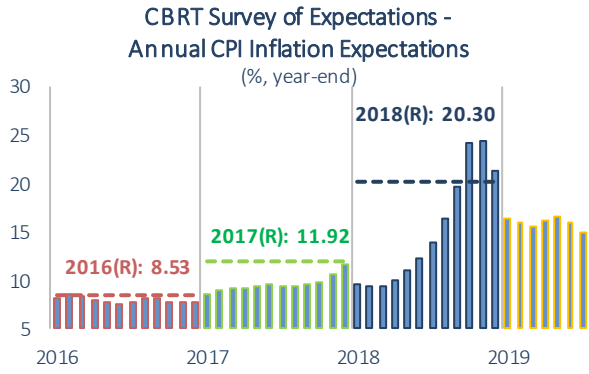
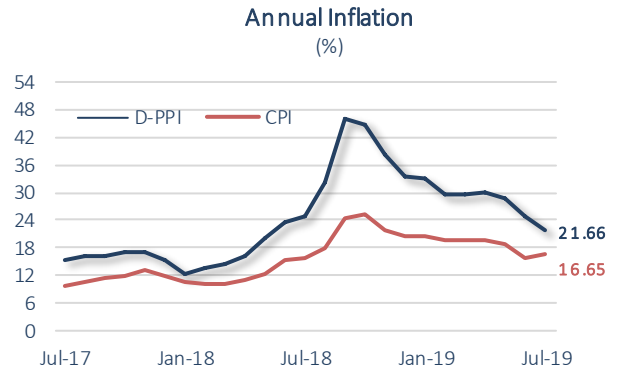
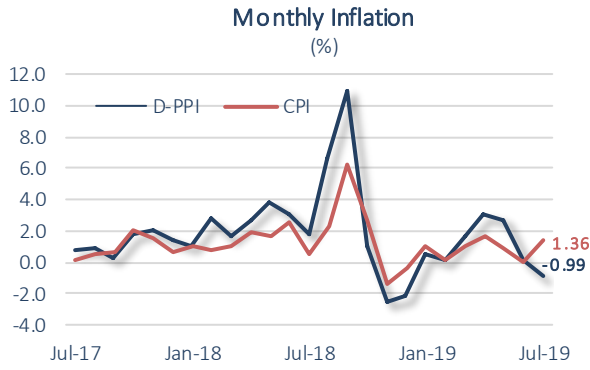
Foreign Trade and Current Account Balance



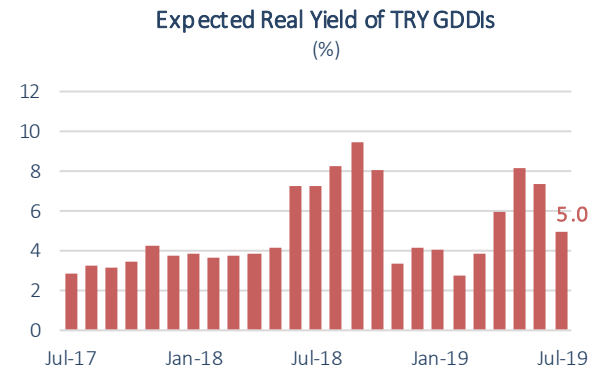
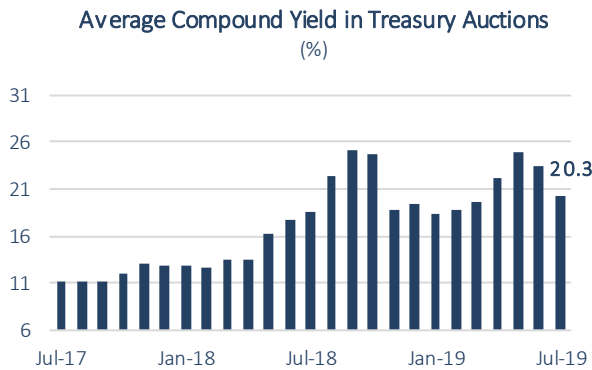
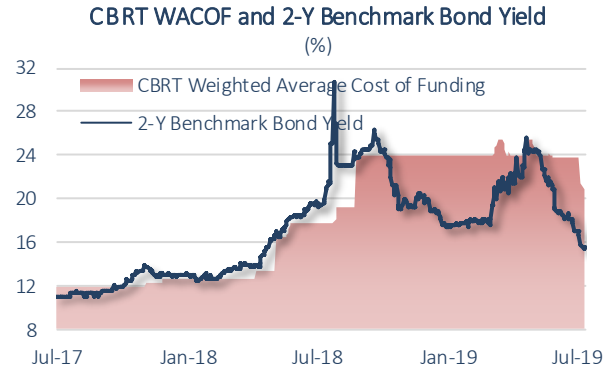
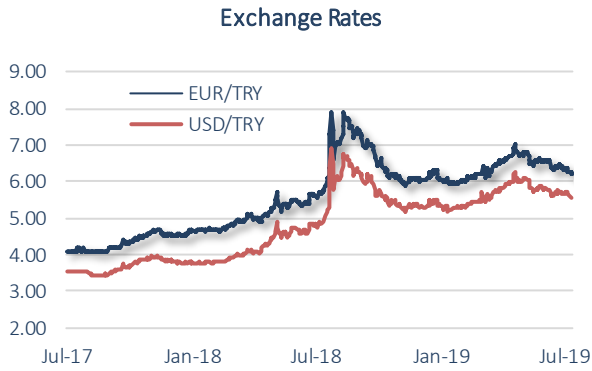
(CA) Calendar adjusted

Source: Datastream, CBRT, Turkstat

Inflation



Foreign Exchange and Bond Market



Turkish Economy - Macroeconomic Indicators

Growth	2014	2015	2016	2017	2018	19-Q1		
GDP (USD billion)	935	862	863	851	784	170		
GDP (TRY billion)	2,045	2,339	2,609	3,107	3,701	915		
GDP Growth Rate (%)	5.2	6.1	3.2	7.4	2.6	-2.6		
Inflation (%)						May-19	Jun-19	Jul-19
CPI (annual)	8.17	8.81	8.53	11.92	20.30	18.71	15.72	16.65
Domestic PPI (annual)	6.36	5.71	9.94	15.47	33.64	28.71	25.04	21.66
Seasonally Adjusted Labor Market Figures						Feb-19	Mar-19	Apr-19
Unemployment Rate (%)	10.3	10.2	12.0	9.9	12.8	13.60	13.70	13.80
Labor Force Participation Rate (%)	51.0	51.7	52.4	53.1	53.1	53.10	53.30	53.10
FX Rates						May-19	Jun-19	Jul-19
CPI Based Real Effective Exchange Rate	105.9	99.2	93.6	86.3	76.4	69.8	72.1	
USD/TRY	2.3378	2.9189	3.5176	3.7916	5.3199	5.8357	5.7840	5.5618
EUR/TRY	2.8288	3.1708	3.7102	4.5530	6.0815	6.5030	6.5868	6.1925
Currency Basket (0.5*EUR+0.5*USD)	2.5833	3.0448	3.6139	4.1723	5.7007	6.1693	6.1854	5.8771
Foreign Trade Balance⁽¹⁾ (USD billion)						Apr-19	May-19	Jun-19
Exports	157.6	143.8	142.5	157.0	167.9	169.6	171.3	169.5
Imports	242.2	207.2	198.6	233.8	223.0	207.1	202.8	198.6
Foreign Trade Balance	-84.6	-63.4	-56.1	-76.8	-55.1	-37.5	-31.5	-29.2
Import Coverage Ratio (%)	65.1	69.4	71.8	67.1	75.3	81.9	84.5	85.3
Balance of Payments⁽¹⁾ (USD billion)						Mar-19	Apr-19	May-19
Current Account Balance	-43.6	-32.1	-33.1	-47.3	-27.3	-13.0	-8.7	-2.4
Capital and Financial Accounts	-43.2	-22.7	-22.0	-46.7	-9.9	-3.8	3.4	7.0
Direct Investments (net)	-6.3	-14.2	-10.8	-8.8	-9.2	-10.2	-10.1	-10.1
Portfolio Investments (net)	-20.2	15.5	-6.3	-24.5	2.9	-3.2	0.6	0.0
Other Investments (net)	-16.2	-12.1	-5.7	-5.2	6.8	18.6	27.5	25.9
Reserve Assets (net)	-0.5	-11.8	0.8	-8.2	-10.4	-9.0	-14.6	-8.8
Net Errors and Omissions	0.5	9.5	11.1	0.6	17.3	9.1	12.0	9.4
Current Account Balance/GDP (%)	-4.7	-3.7	-3.8	-5.6	-3.5	-	-	-
Budget⁽²⁾⁽³⁾ (TRY billion)						Apr-19	May-19	Jun-19
Expenditures	448.8	506.3	584.1	678.3	830.5	330.4	414.0	481.6
Interest Expenditures	49.9	53.0	50.2	56.7	74.0	38.4	46.4	50.7
Non-interest Expenditures	398.8	453.3	533.8	621.6	756.5	292.0	367.6	430.8
Revenues	425.4	482.8	554.1	630.5	757.8	276.0	347.5	403.0
Tax Revenues	352.5	407.8	459.0	536.6	621.3	203.0	262.9	307.7
Budget Balance	-23.4	-23.5	-29.9	-47.8	-72.6	-54.5	-66.5	-78.6
Primary Balance	26.5	29.5	20.3	8.9	1.3	-16.0	-20.1	-27.8
Budget Balance/GDP (%)	-1.1	-1.0	-1.1	-1.5	-2.0	-	-	-
Central Government Debt Stock (TRY billion)						Apr-19	May-19	Jun-19
Domestic Debt Stock	414.6	440.1	468.6	535.4	586.1	653.1	664.5	676.2
External Debt Stock	197.9	238.1	291.3	341.0	480.6	557.4	556.6	543.6
Total Debt Stock	612.5	678.2	760.0	876.5	1,067.1	1,210.6	1,221.1	1,219.8

(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)	2014	2015	2016	2017	2018	May.19	Jun.19	Change ⁽¹⁾
TOTAL ASSETS	1,994	2,357	2,731	3,258	3,867	4,270	4,234	9.5
Loans	1,241	1,485	1,734	2,098	2,395	2,548	2,540	6.0
TRY Loans	881	1,013	1,131	1,414	1,439	1,505	1,508	4.8
Share (%)	71.0	68.2	65.2	67.4	60.1	59.1	59.4	-
FX Loans	360	472	603	684	956	1,043	1,032	8.0
Share (%)	29.0	31.8	34.8	32.6	39.9	40.9	40.6	-
Non-performing Loans	36.4	47.5	58.2	64.0	96.6	111.4	116.2	20.3
Non-performing Loan Rate (%)	2.9	3.1	3.2	3.0	3.9	4.2	4.4	-
Securities	302	330	352	402	478	577	586	22.6
TOTAL LIABILITIES	1,994	2,357	2,731	3,258	3,867	4,270	4,234	9.5
Deposits	1,053	1,245	1,454	1,711	2,036	2,269	2,273	11.6
TRY Deposits	661	715	845	955	1,042	1,031	1,041	0.0
Share (%)	62.8	57.4	58.1	55.8	51.2	45.4	45.8	-
FX Deposits	391	530	609	756	994	1,238	1,231	23.9
Share (%)	37.2	42.6	41.9	44.2	48.8	54.6	54.2	-
Securities Issued	89	98	116	145	174	210	204	17.3
Payables to Banks	293	361	418	475	563	584	565	0.4
Funds from Repo Transactions	137	157	138	99	97	163	161	66.4
SHAREHOLDERS' EQUITY	232	262	300	359	421	439	449	6.8
Profit (Loss) of the Period	24.6	26.1	37.5	49.1	53.5	19.7	24.8	-
RATIOS (%)								
Loans/GDP	60.7	63.5	66.5	67.6	64.7			
Loans/Assets	62.2	63.0	63.5	64.4	61.9	59.7	60.0	-
Securities/Assets	15.2	14.0	12.9	12.3	12.4	13.5	13.8	-
Deposits/Liabilities	52.8	52.8	53.2	52.5	52.6	53.1	53.7	-
Loans/Deposits	117.9	119.2	119.3	122.6	117.6	112.3	111.8	-
Capital Adequacy (%)	16.3	15.6	15.6	16.9	17.3	17.1	17.7	-

(1) Year-to-date % change

Source: BRSA, Turkstat

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