

DenizBank Economic Update

June 2016

- **Economy**
- **Financial Markets**
- **Banking Sector**

Economic Research and Strategy

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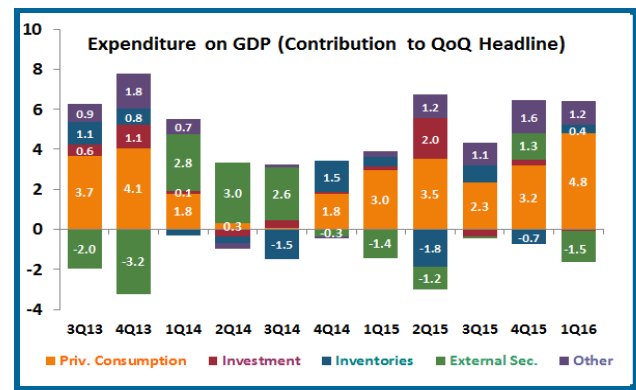
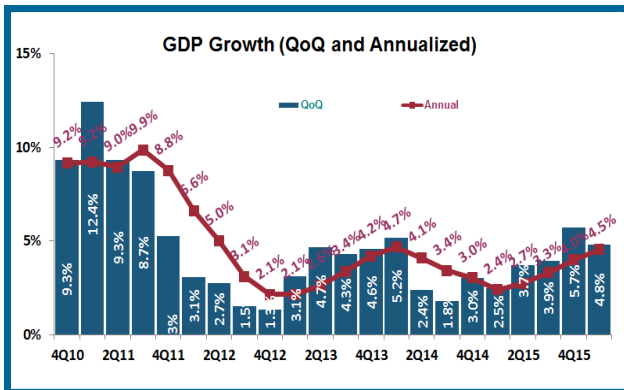
DenizBank 

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DenizBank Economic Update

Economy (I)

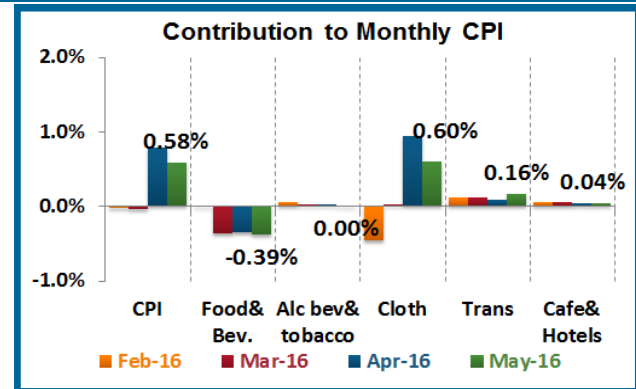
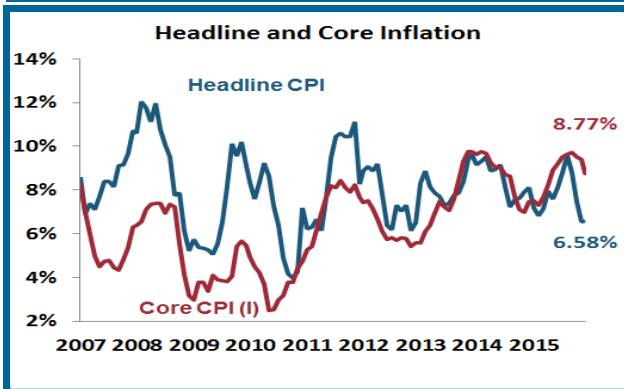
Growth



GDP growth beats expectations thanks to continued robust domestic demand in the first quarter...

- Turkish economy grew by 4.8% in 1Q16 beating the market expectation of 4.4%. Annualized growth rate reached 4.5%.
- Domestic demand continued to be the main driver of growth. Household spending grew by 6.9% Q-on-Q making a 4.8 pp contribution to headline growth figure. This has been the highest contribution since 2011. Public spending increased by 10.9% and made a 1.2 pp contribution. Net exports shaved off 1.5pp of the growth figure. Manufacturing sector grew by 5%, making a 1.3 pp contribution.
- The positive effects of the minimum wage increase at the beginning of the year is observed in GDP figures. Despite retail loan growth has been slow in the first quarter of the year, household spending continued to increase three quarters in a row. A slowdown in household spending can be expected in the remainder of the year, leading to a GDP growth for full year 2016 in a range of 3-4%.

Inflation



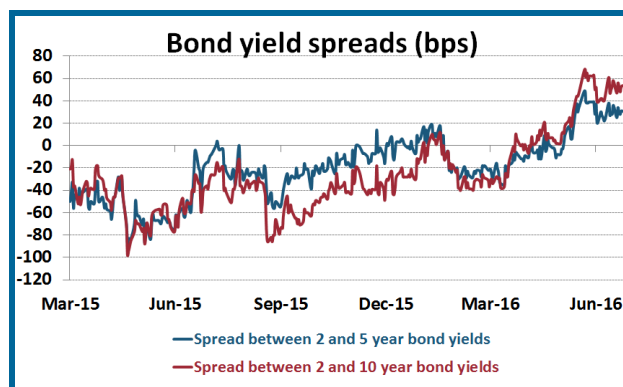
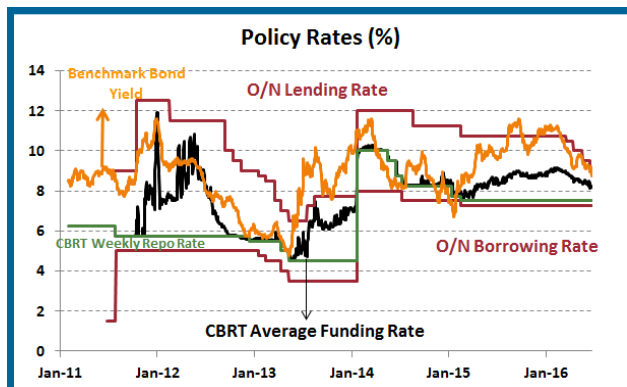
Significant improvement in core inflation, while headline stays almost flat in May...

- CPI in May rose MoM by 0.58%, less than the market expectation of 0.7%. Food prices fell by 1.64% on a monthly basis. Annual food inflation is 2.47%.
- Annual inflation remained at 6.6% in May. With the stable performance in Turkish Lira, an improvement in pricing behavior was observed as core inflation retreated to 8.77% from 9.41% a month ago.
- Food prices act as the main driver in the drop of headline inflation since the beginning of the year. In the coming months this downward trend may be reversed as base effect comes into play. In the aftermath of Brexit decision, Turkish Lira has performed positively along with other emerging markets. This should help bring core inflation down further in June. However, Brexit uncertainty and increasing volatility casts doubt whether this performance can persist or not in the following months.

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Economy (II)

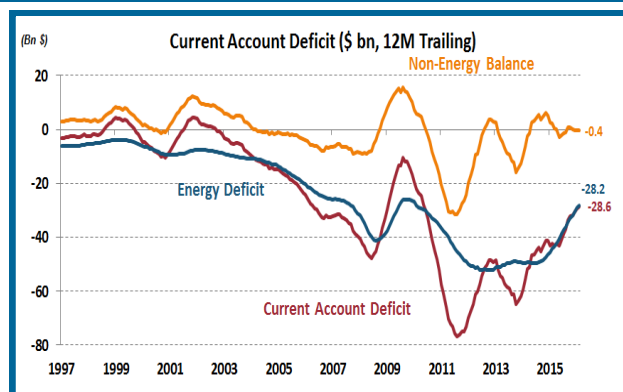
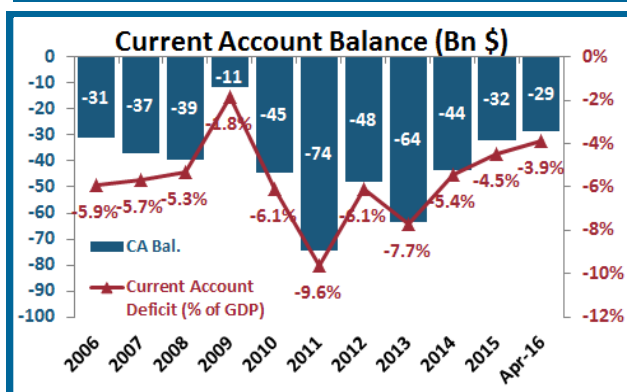
Monetary Policy



Central Bank (CBT) continued the simplification process by a 50 bps cut to the upper end...

- In its monthly MPC Meeting, CBT left the policy rate (one week repo rate) unchanged at 7.5%, in line with the market expectation. O/N lending rate was cut by 0.50% to 9.00%
- As inflation continued to remain below 7% and with the recent improvement in core inflation, CBT continued the steps of simplification process. With the latest 50 bps cut in the upper band, the interest rate corridor has narrowed down to 175 bps from 350 bps at the beginning of simplification. This leaves room for possibly 50 bps more cut in the upper band, before CBT merges different rates and starts a simple monetary policy with a single interest rate.
- CBT continued to remain cautious with its monetary policy. Despite the 175 bps fall in the O/N lending rate, the pace of fall in the average funding rate has been slower. Monthly average of CBT's funding rate has decreased to 8.34% in June from a monthly average of 8.50% in May. With Fed's rate hike expectations delayed and ECB, BOE and BOJ expected to increase their monetary expansion programs, CBT's average funding rate may continue to come down.

External Sector



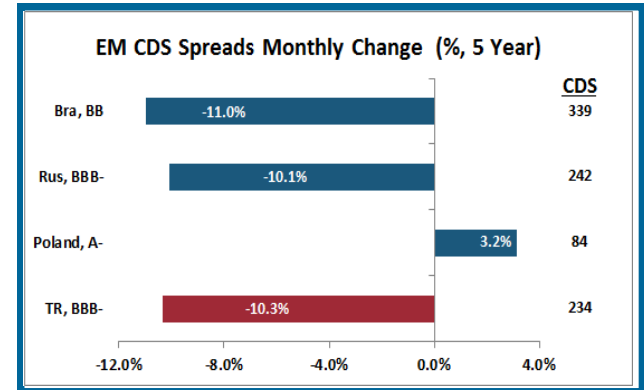
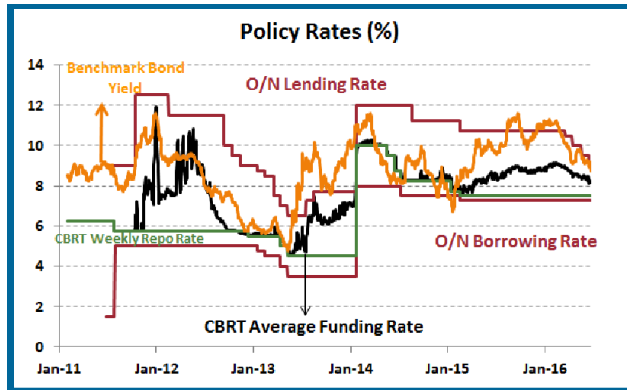
Improvement in the trade deficit and low energy prices continues to drive current account deficit lower...

- Current account deficit (CAD) in April came at \$3.0 bn. 12 month cumulative CAD narrowed down to \$28.6 bn (3.9% of GDP) from \$29.5 bn in March.
- On the financing side, there has been an FDI inflow of \$0.6 bn in April. Inflow to the bond market was \$1.2bn and to the equity market was \$0.5 bn. Reserve assets increased in April by \$0.4bn.
- 12 month cumulative energy deficit in April shrank by 36% on an annual basis to \$28.2 bn.
- As foreign tourist arrivals continue to decrease and tourism revenues fall, an increase in current account deficit may be observed in the second half of the year.

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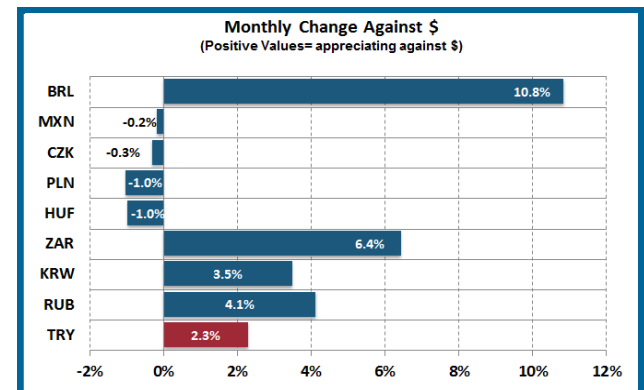
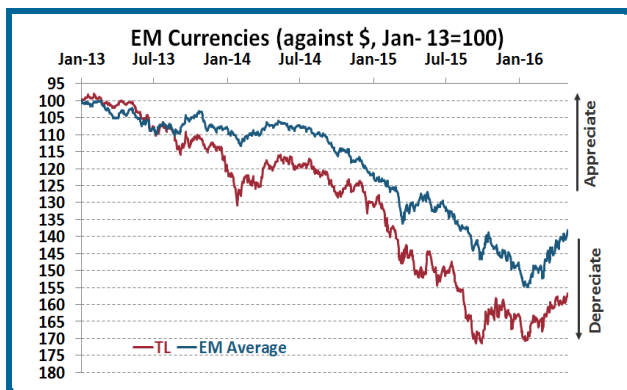
Financial Markets

Debt Market



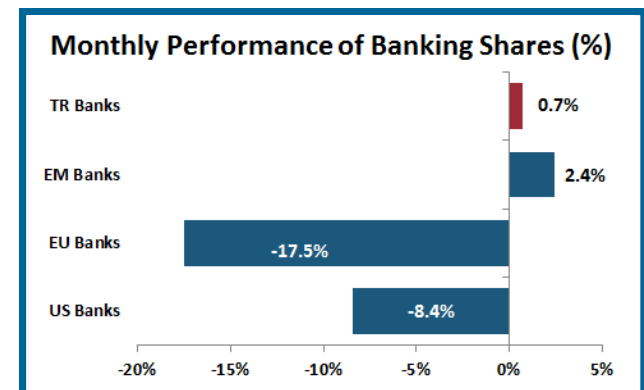
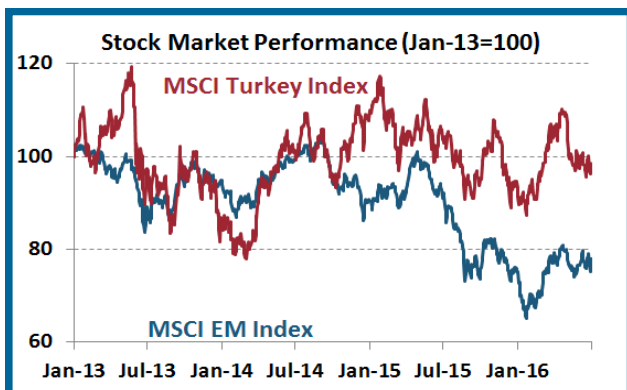
Benchmark bond yield is at 8.75%.

Currency Market



EM currencies appreciated against US Dollar in June.

Stock Market

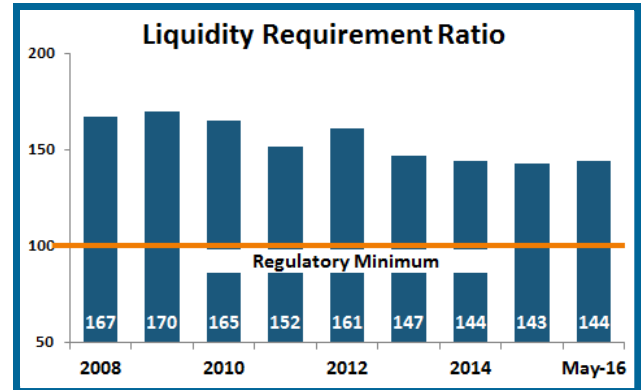
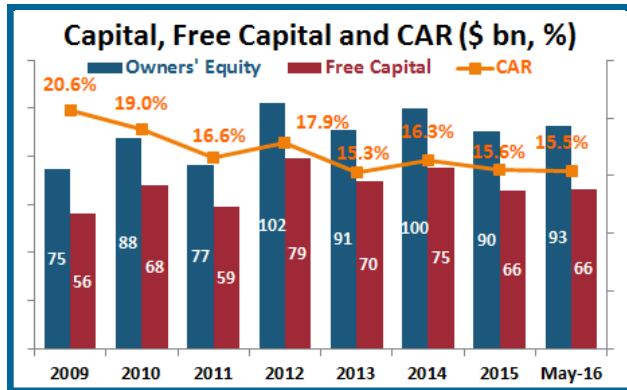


MSCI Turkey equity index differentiated positively from other EMs in June.

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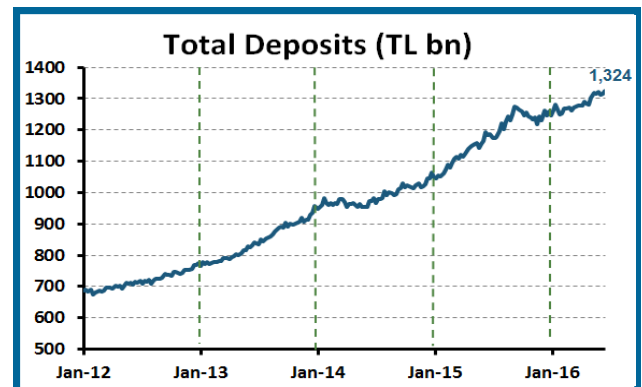
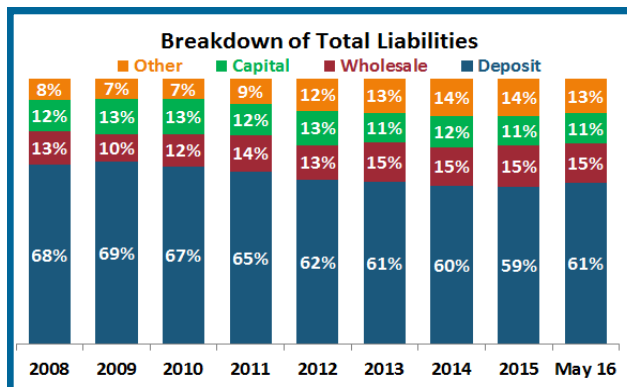
Banking Sector (I)

Capital



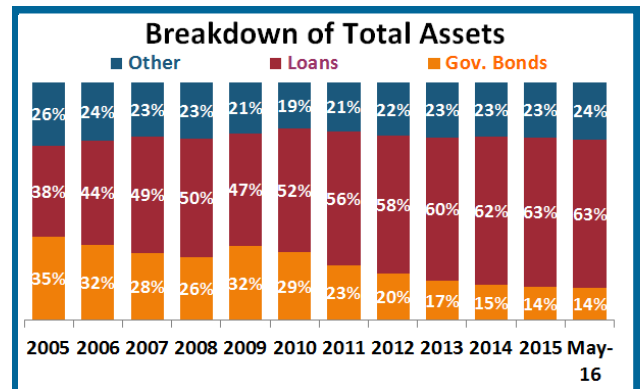
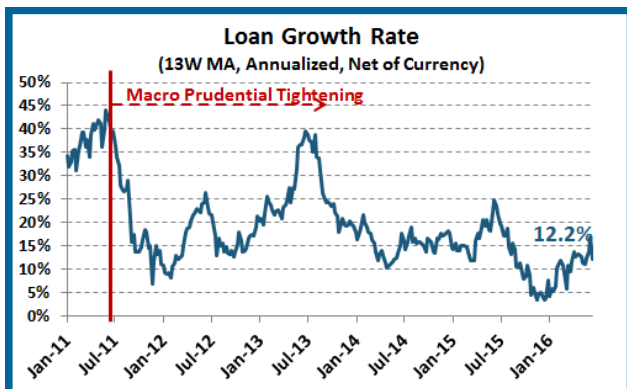
CAR is at 15.5% in May, compared to 15.6% as the end of 2015.

Funding



Share of deposits in funding was at 61% as of May 16.

Lending

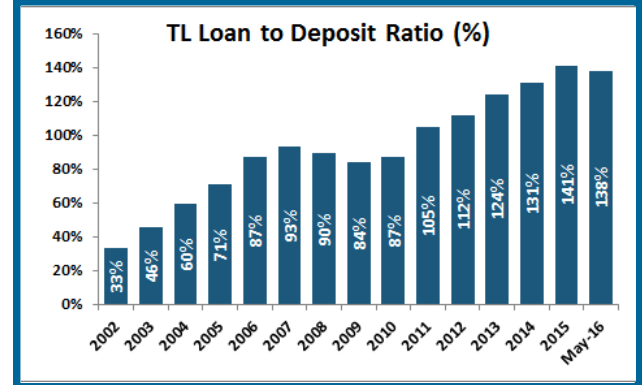
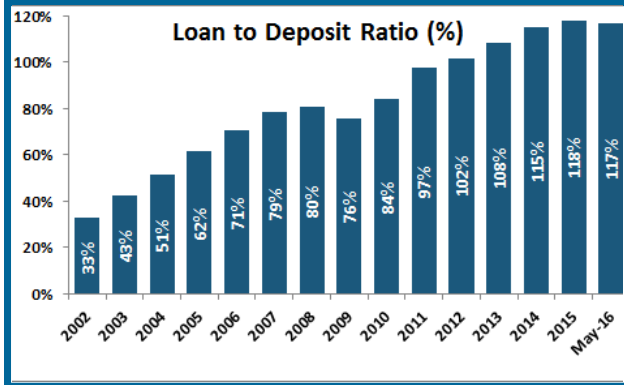


Annualized loan growth is at 12.2% as of Jun 17th.

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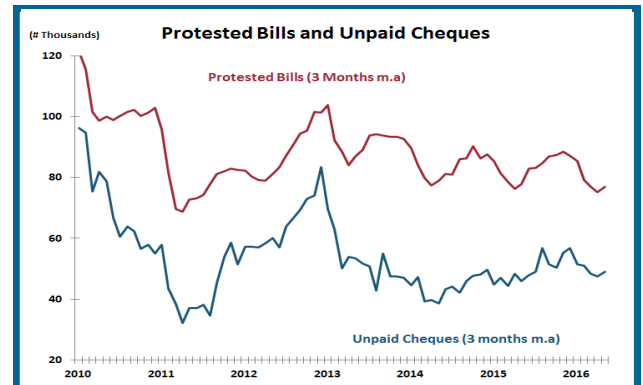
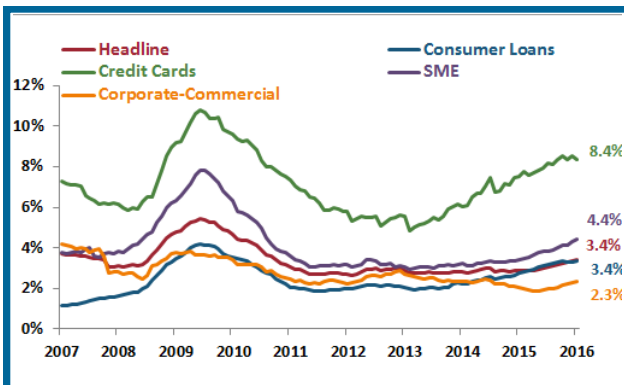
Banking Sector (II)

Loan to Deposit Ratios



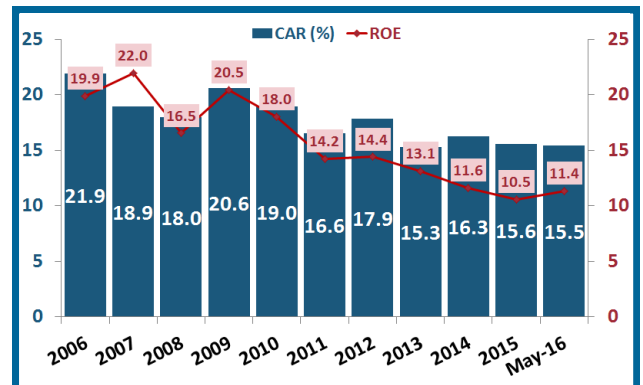
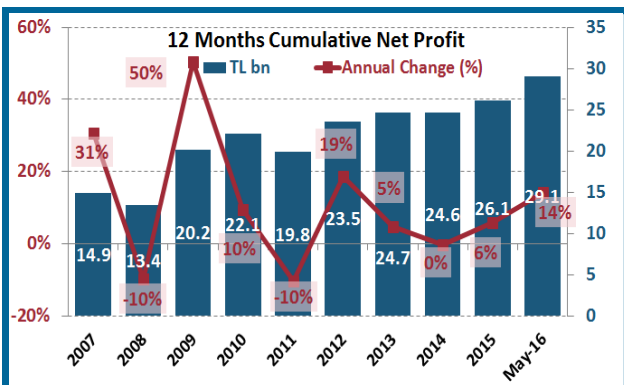
Loan to deposit ratio is 117% in May.

Loan Quality



Headline NPL ratio for the sector is at 3.4%.

P & L



As of May, sector's 12 month cumulative profit increased YoY by 14%. ROE is at 11.4%.