

DenizBank Economic Update

November 2017

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

Economic Research and Strategy

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Deniz Bayram

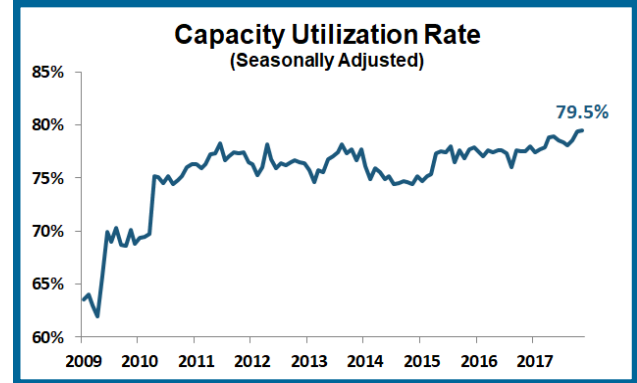
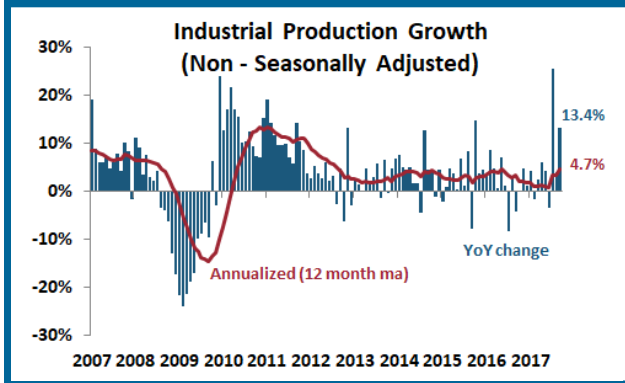
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DenizBank Economic Update

Economy (I)

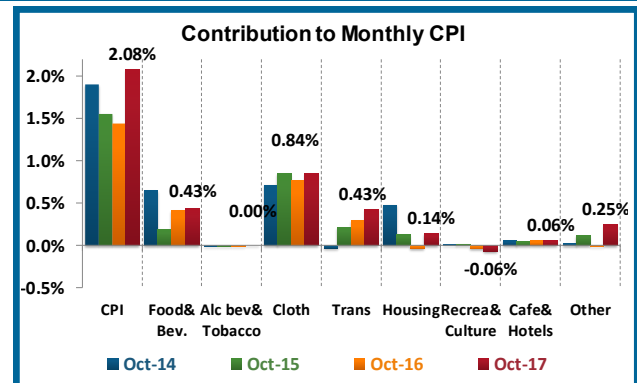
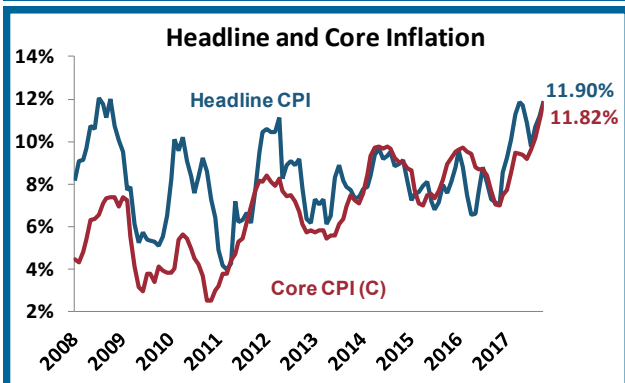
Growth



Economic activity accelerated in the third quarter of the year...

- Seasonally and calendar adjusted industrial production (IP) increased MoM by 0.6% in September and the unadjusted index rose YoY by 13.4%. Overall in 3Q17, the unadjusted index surged 13.7% annually, the highest in the last 26 quarters. Industrial production data indicates GDP growth will accelerate in the third quarter (Q1 YoY: %5.2, Q2 YoY: %5.2).
- Early indicators suggest economic activity remains to be positive in the last quarter of the year, as well. PMI has stayed above 50 since March 2017. Capacity utilization in October and November, has gone up to 79.4% and 79.5% respectively, the highest level of the data since August 2008.
- Third quarter GDP growth rate likely to be this year's peak. Looking at the pace of loan growth (net of currency effect) which slowed down to c.19% on average in 3Q17 from c.13% on average since the beginning of 4Q17, GDP growth rate may start to ease from 4Q onward. Overall, we expect GDP growth to be above 5.0% in 2017.

Inflation



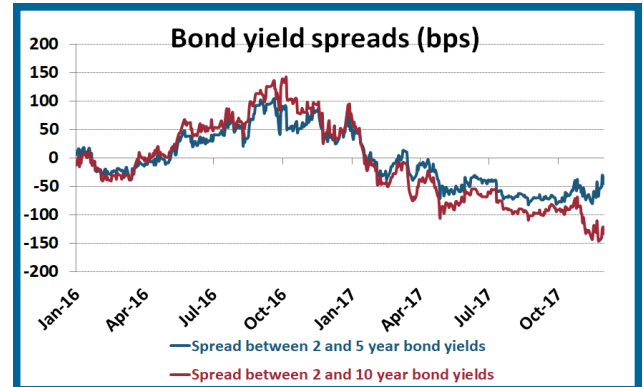
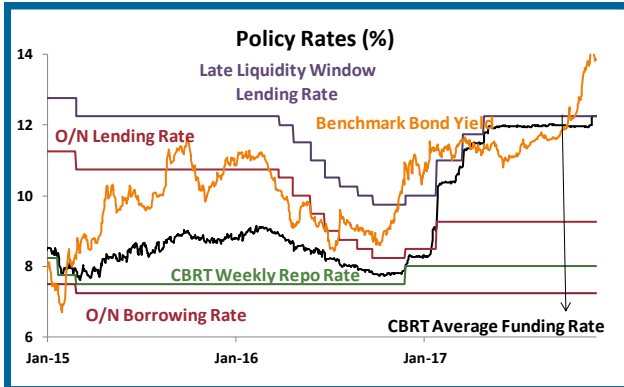
Currency depreciation and base effect pushes inflation higher...

- In October, CPI increased MoM by 2.1%, in above the market expectations of 1.7%. After a five consecutive months of decline, due to seasonal effects food prices increased by 1.97%, contributing 0.43 points to the monthly CPI.
- Annual inflation jumped to 11.9% from 11.2% a month ago, its highest level since 2008. Annual food inflation went up to 12.7% from 12.5% a month ago. Core CPI (CPI excluding food, energy, non-alcoholic and alcoholic beverages, tobacco, gold) rose sharply to 11.8% from 11%, its peak in 13 years. Producers' price index increased YoY by 17.3%.
- Inflation may go up further in November until the favorable base effect will kick in from December onwards. However, annual inflation is likely to be double digit (10.6%) territory at the end of 2017 before falling to single digit levels at the beginning of 2018. However, further depreciation in currency and deterioration in the core inflation dynamics are upside risks to our forecasts.

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Economy (II)

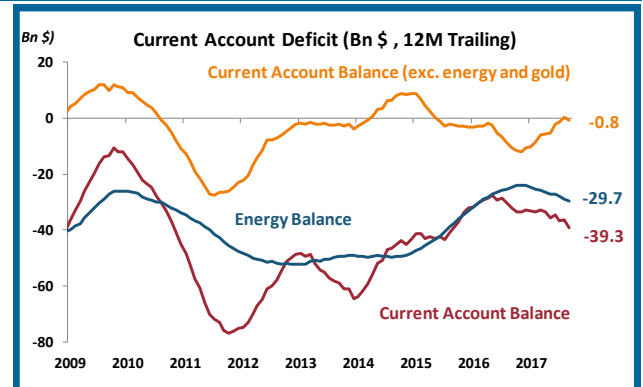
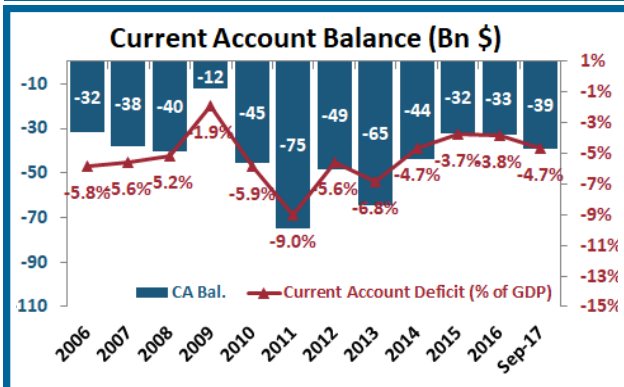
Monetary Policy



Central Bank of Turkey is committed to tight monetary stance until inflation improves significantly...

- In its October meeting, Central Bank of Turkey (CB) kept weekly repo, O/N lending and borrowing rates and late liquidity funding lending rate unchanged at 8.0%, 9.25%, 7.25% and 12.25% respectively. However, CB keeps a tighter monetary policy stance by not opening weekly repo auctions and using late liquidity window for funding. In November, CB eliminated banks' borrowing limits in Interbank Money Market for O/N transactions thus increasing the weighted average cost of funding to 12.25% from 12.0%. CB took further measures against weakening TL such as allowing exporters to repay rediscount credits in TL, lowering upper limit and the tranches for the FX maintenance facility within the ROM and starting TL-settled non-deliverable forward auctions.
- In November Inflation Report, TCMB revised its year-end inflation expectation up to 9.8% from 8.7% in July. Given the ongoing depreciation in TL that may lead to further deterioration in pricing behaviour, CBT is expected to hold on a tight monetary policy.

External Sector



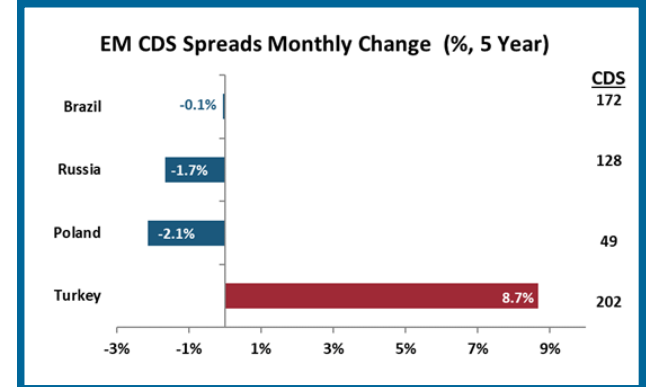
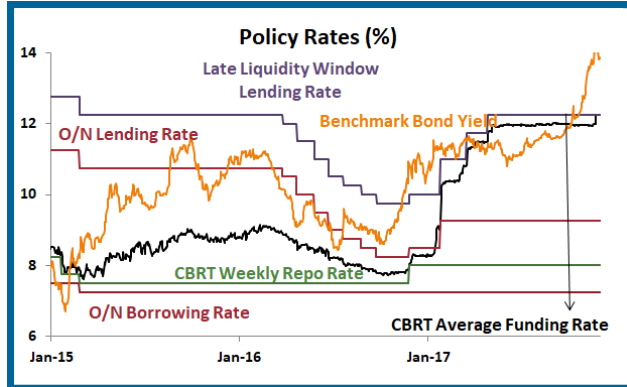
External trade deficit has widened, but current account deficit remains at manageable levels thanks to increasing tourism revenues.

- Current account deficit (CAD) in September came slightly above expectations at \$4.5 bn. 12 month cumulative CAD widened to \$39.3 bn (4.7% of GDP) from \$36.3 bn in August (4.4% of GDP). Portfolio inflows reached to \$22 bn annually and continued to be the main source of financing the deficit.
- In September, annualized core balance, which has been improving for the last 11 months and gave a surplus of \$0.3 bn in August, gave a deficit \$0.8 bn. Energy and gold imports continued to build an upward pressure on CAD. Annualized energy deficit widened to \$29.7 bn from \$28.8 bn while annualized gold deficit increased to \$8.7 bn from \$7.3 bn a month ago. On the other hand, annualized tourism revenues increased to \$17 bn from \$16.3 bn in August, partly compensating the increase in trade deficit.
- In October, annual trade deficit continued to widen, indicating that CAD would increase as well. However, with the help of recovery in tourism revenues, CAD to GDP ratio in the remainder of the year is expected to stay at manageable levels, namely between 5-5.5%.

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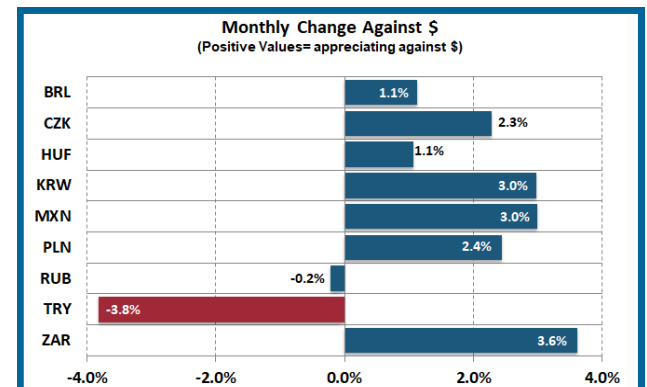
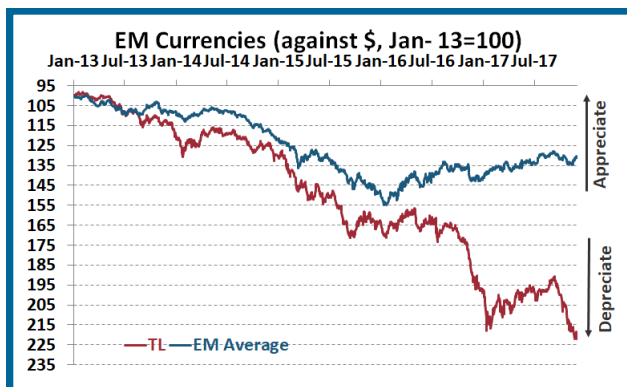
Financial Markets

Debt Market



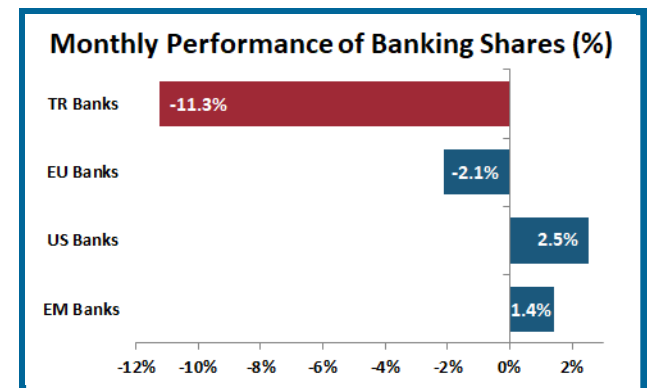
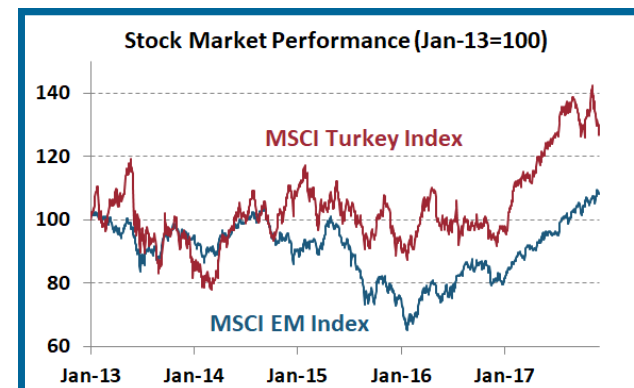
Turkey's 2-year benchmark bond yield rose sharply to 13.6%.

Currency Market



In November, while other EM currencies gained value, TL continued to depreciate against USD.

Stock Market

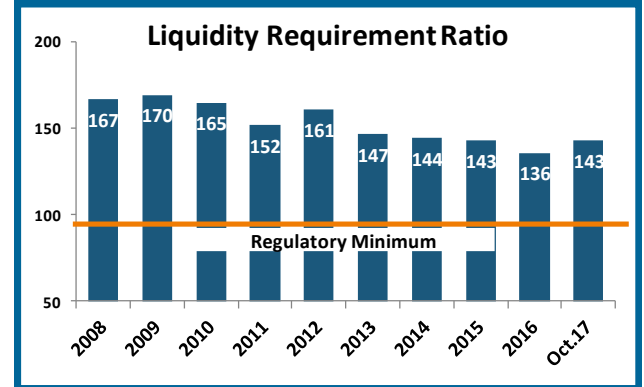
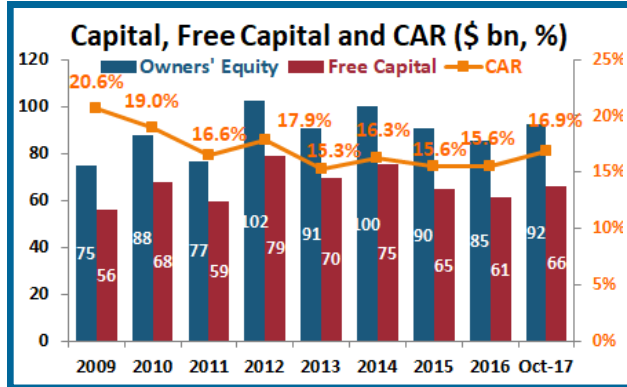


MSCI Turkey index went down by 7% while other EM stock markets continued to performed well.

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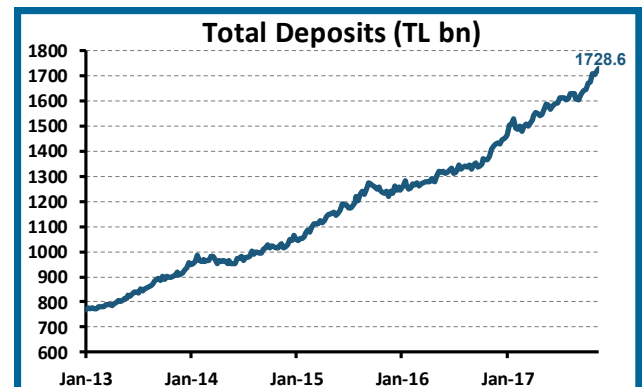
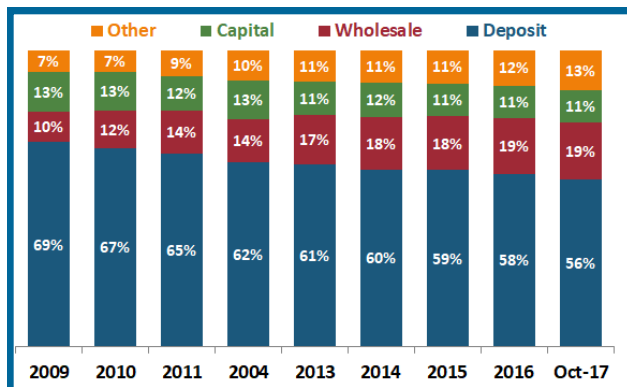
Banking Sector (I)

Capital



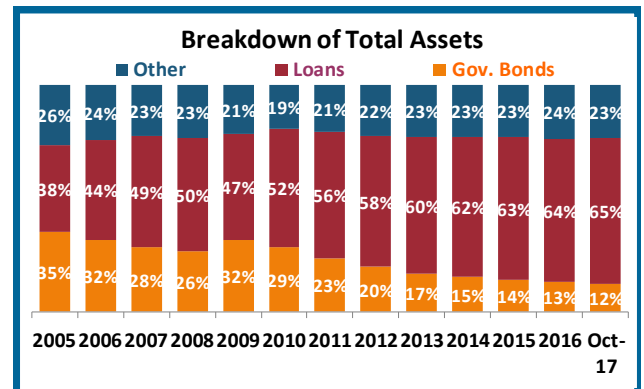
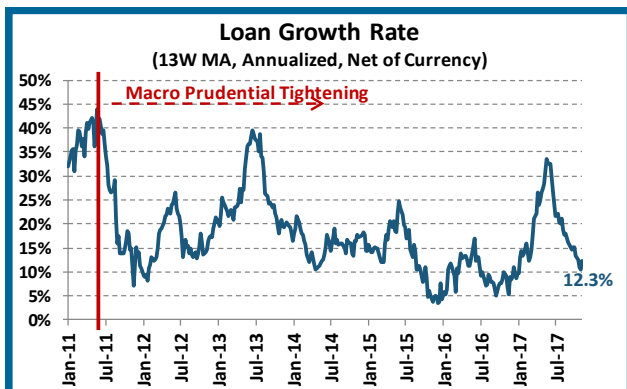
Turkish banking sector CAR was at 16.9% in October.

Funding



Deposits increased YoY by 22% to TL 1.73 trillion in October. Share of deposits in funding was at 56%.

Lending

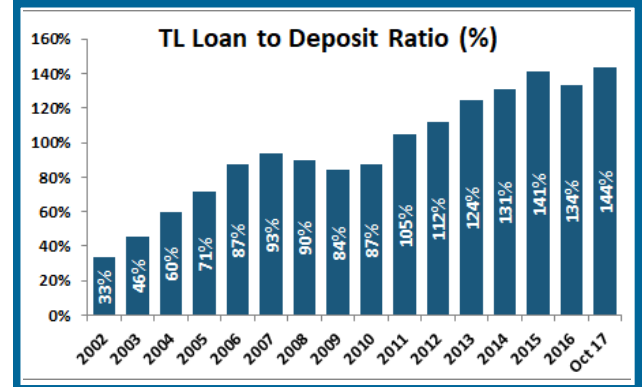
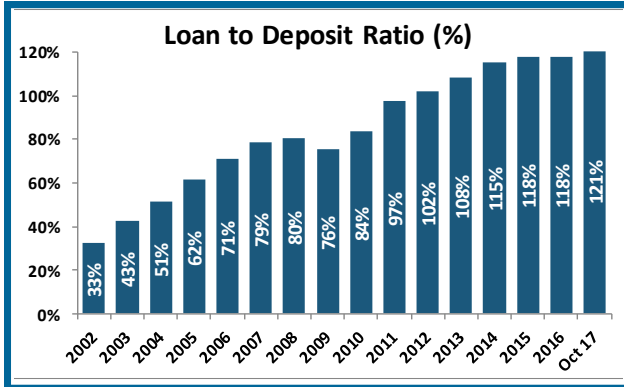


Annualized loan growth decelerated to 12.3% as of Nov 17th.

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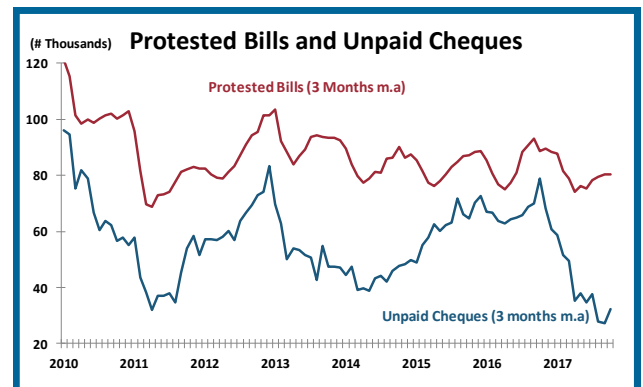
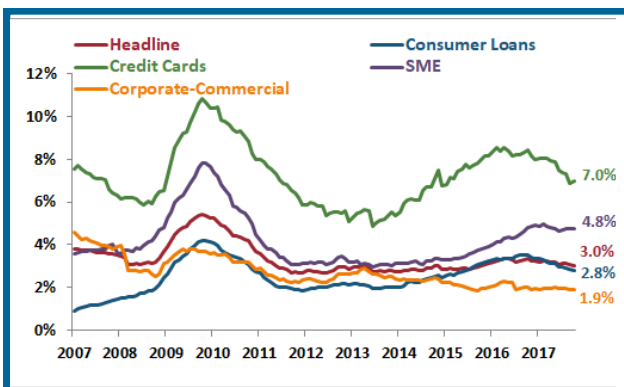
Banking Sector (II)

Loan to Deposit Ratios



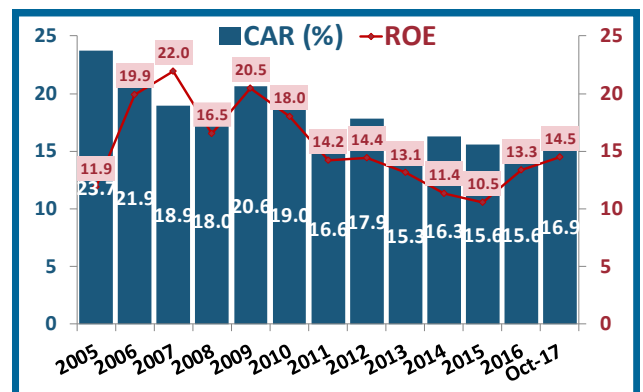
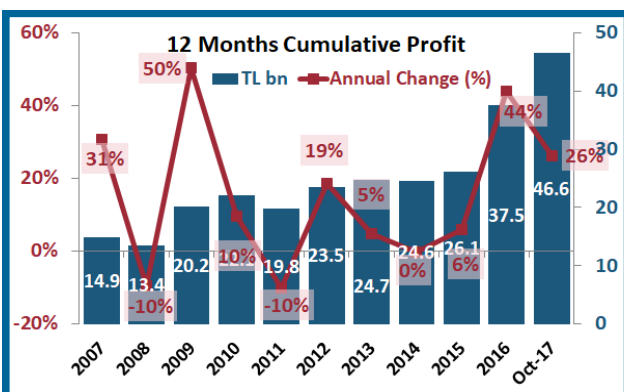
In October, loan to deposit ratio (LDR) was at 121% while TL LDR was at 144%.

Loan Quality



Headline NPL ratio for the sector remains stable at 3.0% as of Nov 17th.

P & L



In October, banking sector's annual profit increased YoY by 26% to TL 47 bn while ROE was up to 14.5%.