DenizBank Economic Update

October 2017

- Economy
- Financial Markets
- Banking Sector

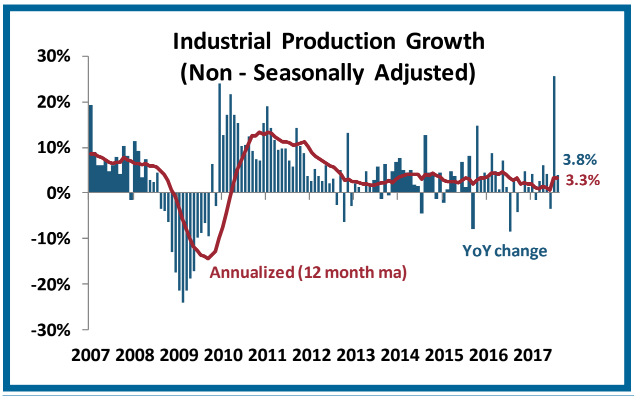
Economic Research and Strategy
Saruhan Özel, Ph.D.
Ezgi Gülbaş
Orhan Kaya
Deniz Bayram

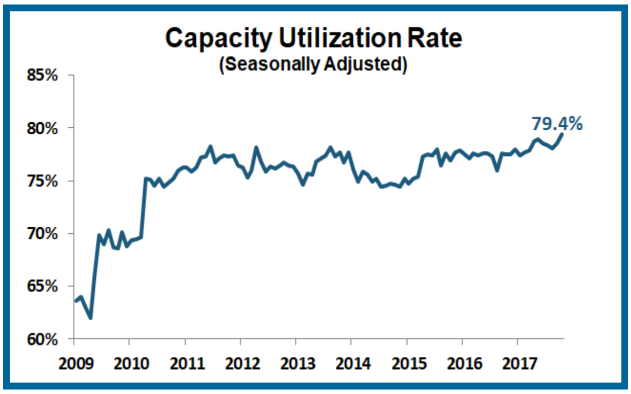
DenizBank Economic Research – (90) 212 348 20 00 or ekonomikarastirmalar@denizbank.com

DenizBank Economic Update

Economy (I)

Growth





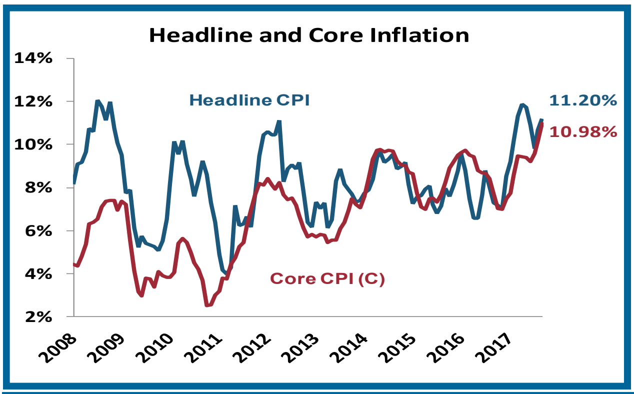
Economic activity accelerates in the third quarter of the year…

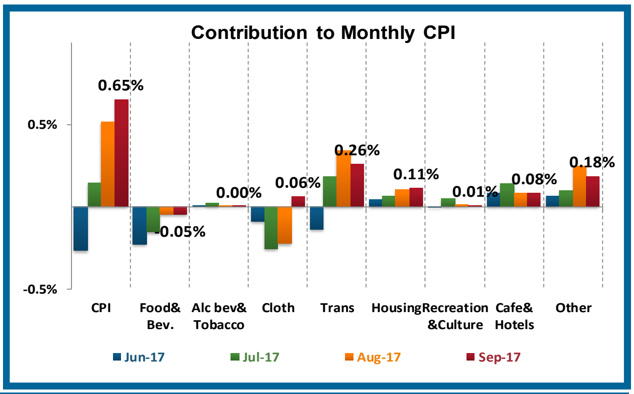
● Seasonally and calendar adjusted industrial production (IP) index contracted MoM by 0.1% in August. The unadjusted index rose 3.8% annually. Annualized IP growth reached 3.3%.

● Early indicators signal economic activity stayed on a high note throughout the third quarter and performance remains to be positive in the last quarter of the year as well. PMI has stayed above 50 for 7 consecutive months. Capacity utilization, first indicator of the fourth quarter from real sector, has gone up to 79.4%. This is the highest level of the data since August 2008.

● Third quarter GDP growth rate, which will be announced on Dec 11th, will likely be this year's peak. With incentives coming to an end, GDP growth rate may start to ease from Q4 onward. Overall, we expect GDP growth to be 5.0% in 2017.

Inflation





Base effect and currency depreciation pushes inflation higher...

● CPI in September increased MoM by 0.65%, in line with the market expectation of 0.63%. Decline in food prices continue. Monthly food inflation was –0.23%.

● Annual inflation jumped to 11.2% from 10.7% a month ago. Annual food inflation went up to 12.5% from 12% a month ago, due to low base effect. Core CPI (CPI excluding food, energy, non-alcoholic and alcoholic beverages, tobacco, gold) increased sharply to 11% from 10.2%. Producers' price index increased YoY by 16.3%.

● The base effect continues to work unfavorably in inflation dynamics. In October and November, inflation is expected to remain in high levels. In December, the impact of base effect will reverse and bring annual rate down, starting a downward trend into 2018. However, the latest depreciation in currency starting mid—September, will likely diminish the impact and duration of this downward trend.

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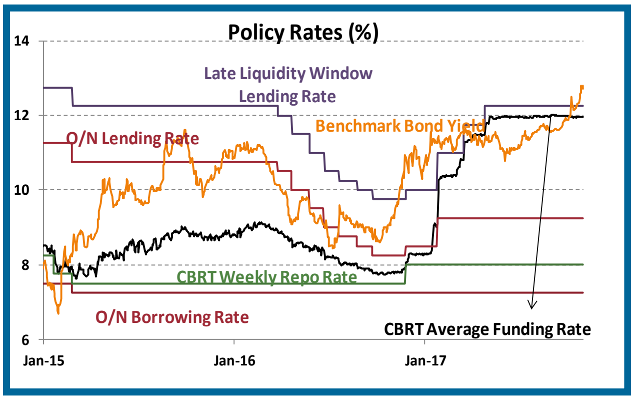
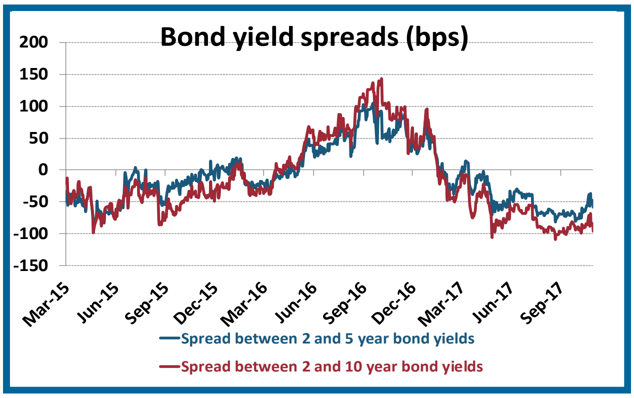
Economy (II)

Monetary Policy





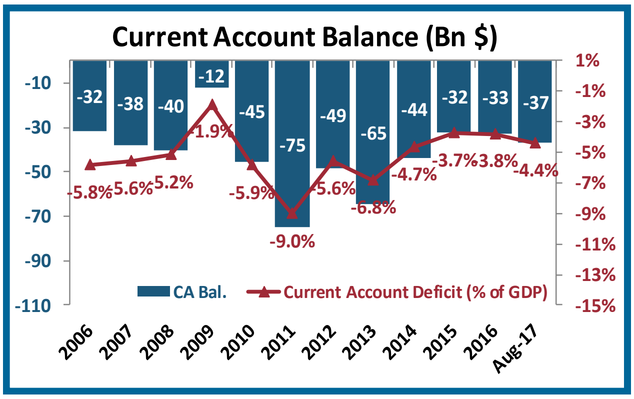
Central Bank of Turkey is committed to tight monetary stance until inflation improves significantly...

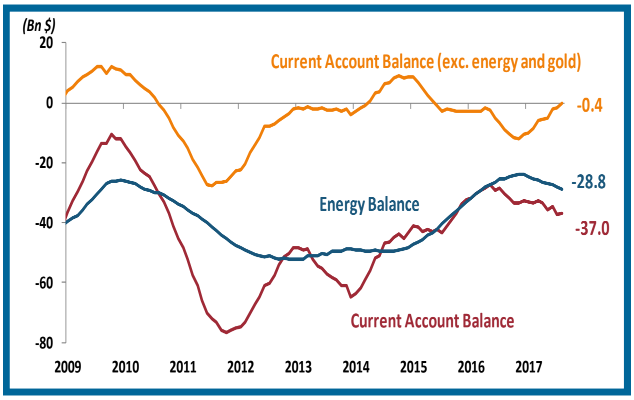
● In its October meeting, Central Bank of Turkey (CBT) kept weekly repo, O/N lending and borrowing rates and late liquidity funding lending rate unchanged at 8.0%, 9.25%, 7.25% and 12.25% respectively. Monetary Policy Committee will convene next on December 14th.

● The decision statement was pretty much unchanged, except for the part where CBT underlines its continued commitment to tight monetary stance.

● The spike in August inflation was higher than expected. In September, core inflation jumped sharply. Currency has depreciated 6% against USD in October, possibly deteriorating pricing behaviour further. The developments in inflation front in the last two months indicate that the expected downward trend of inflation starting from December may be weaker and slower than anticipated. This would require CBT to hold on to tight monetary policy, i.e. keeping average weighted funding high c. 12%.

External Sector





Energy and gold deficit grow wider, but current account deficit is stable thanks to tourism revenues.

● Current account deficit (CAD) in August came slightly below expectations (Bloomberg: $1.4 bn) at $1.2 bn. 12 month cumulative CAD decreased slightly to $37.0 bn from $37.1 bn in July (Aug 2016: $30.3 bn).

● Portfolio inflows peaked in the first eight months of the year, reaching $20bn and continued to be the main source of financing the deficit. Annualized tourism revenues increased to $15.9 bn from $ 15.2 bn a month ago.

● Annualized core deficit narrowed down to $0.4 bn in August from $1.9 bn from a month ago. Annualized gold deficit increased to $7.9 bn from $7.3 bn a month ago. Annualized energy deficit increased to $28.8 bn from $28.0 bn a month ago.

● Annual trade deficit in September has widened, indicating that CAD may widen as well. However, CAD to GDP ratio in the remainder of the year is expected to stay at manageable levels, namely below 5%.

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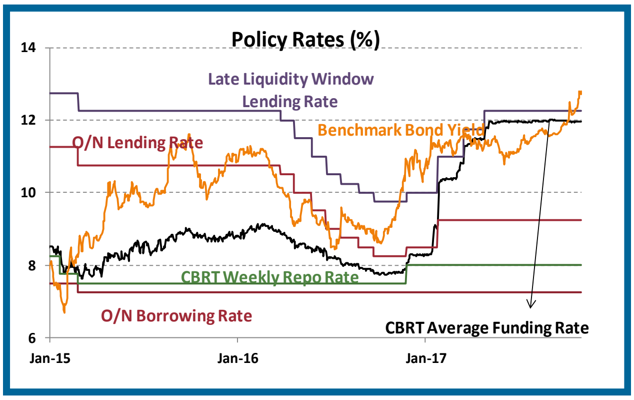
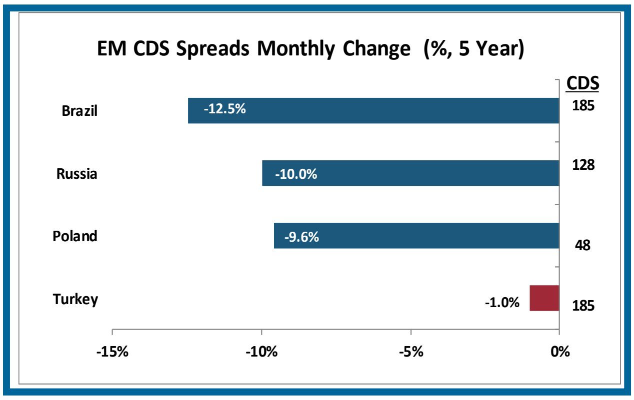
Financial Markets

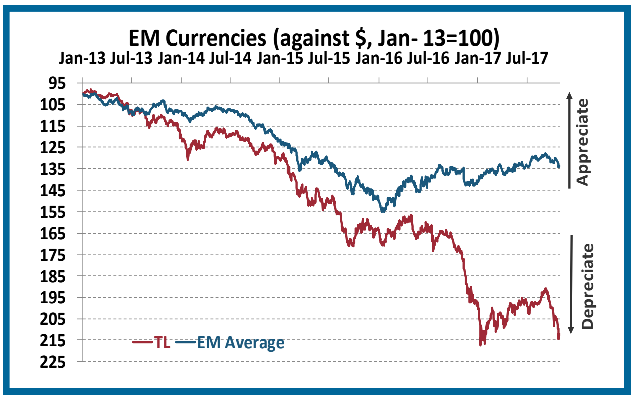
Debt Market

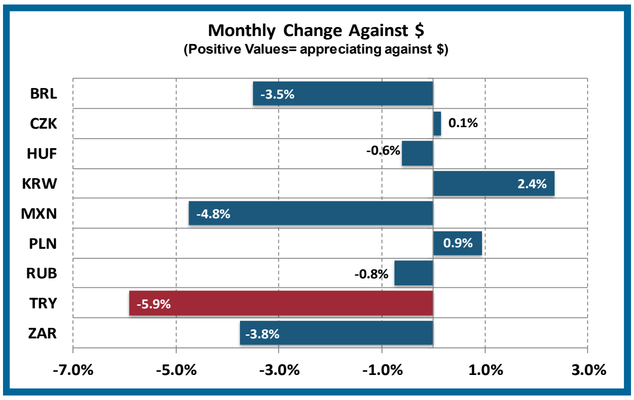




2-year benchmark bond yield is at 12.80%.

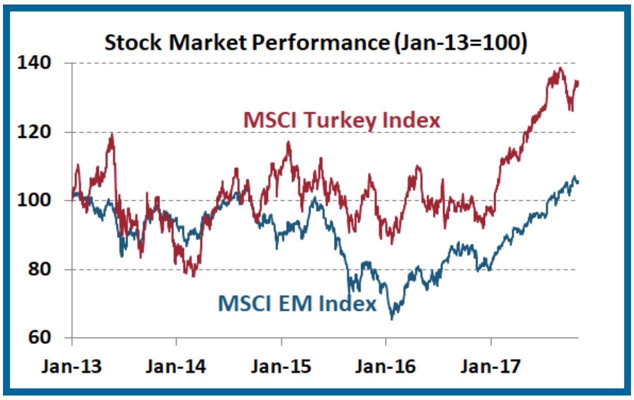
Currency Market

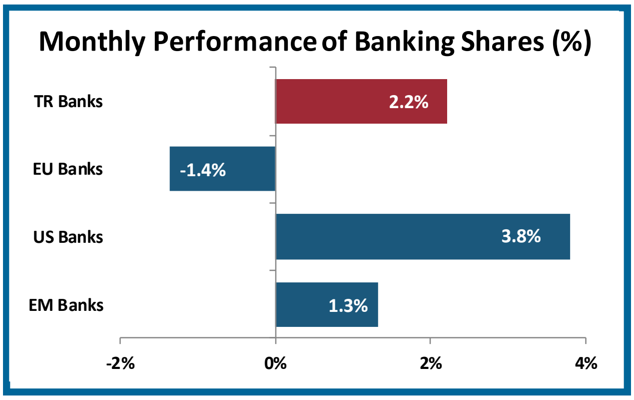




EM currencies continued to depreciate against USD.

Stock Market





Stock market indices performed well in October.

Data retrieved from Bloomberg as of 17:00 (GMT + 3), 31.10.2017

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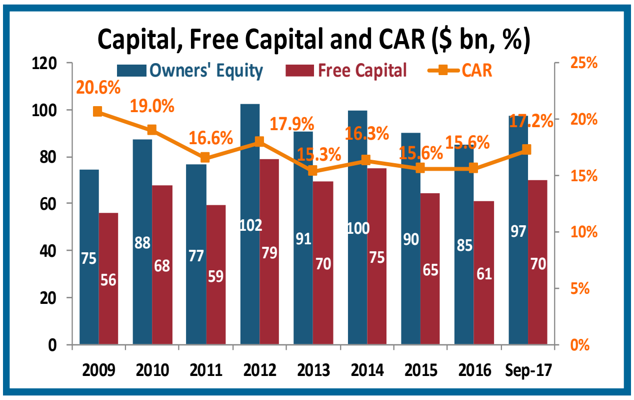
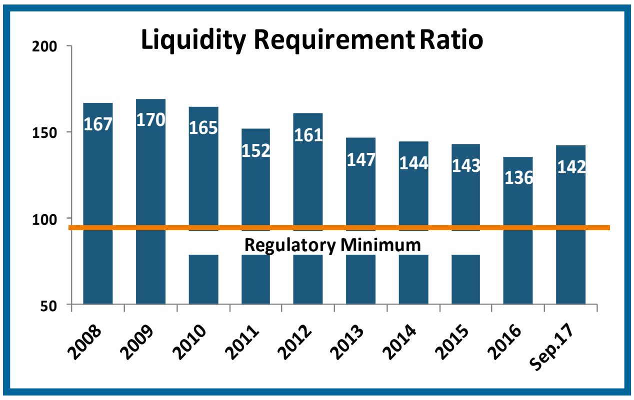
Banking Sector (I)

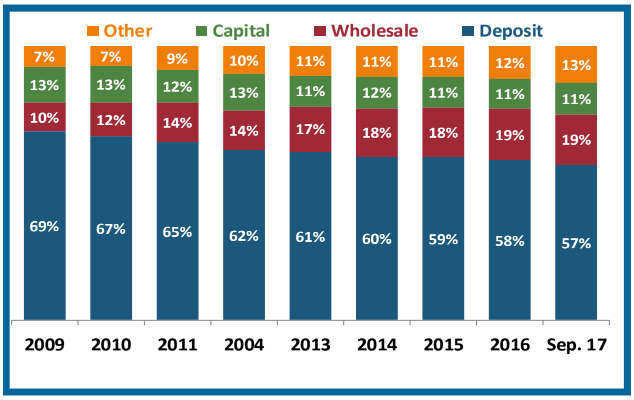
Capital

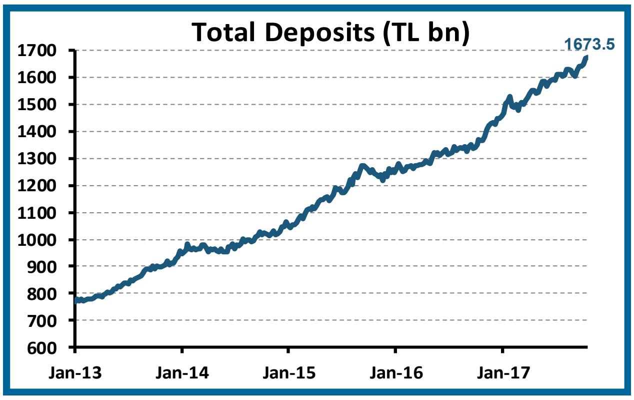




CAR increased to 17.2% in Sep 2017.

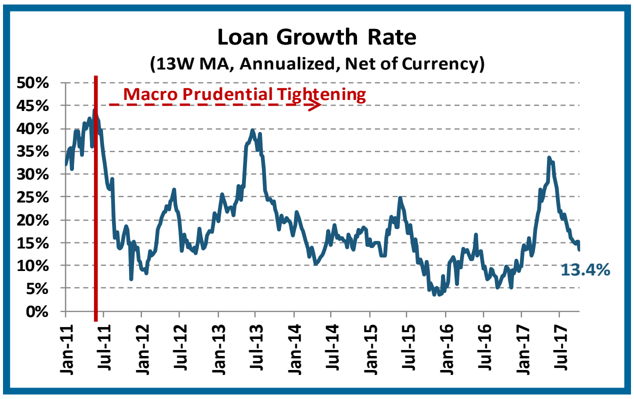
Funding

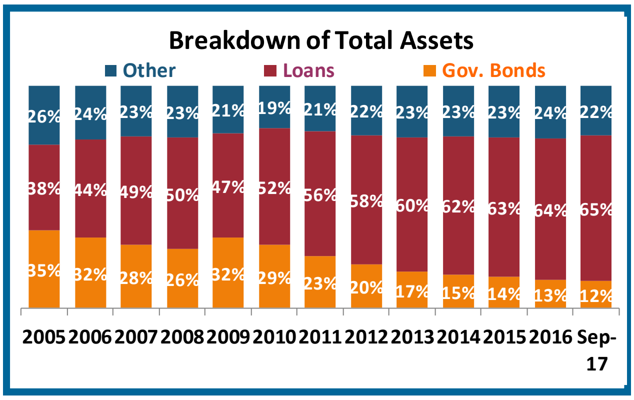




Share of deposits in funding was at 57% as of Sep 2017.

Lending





Annualized loan growth is at 13.4% as of Oct 20th.

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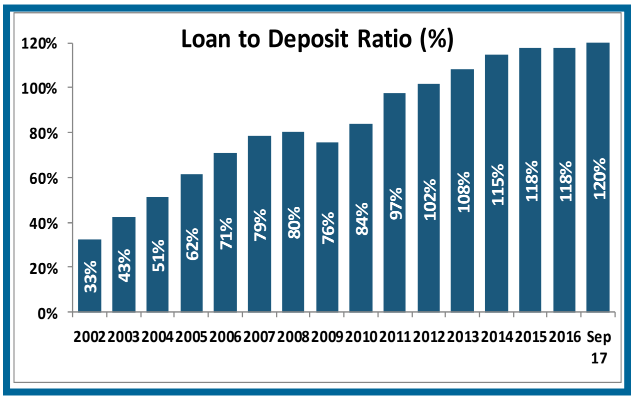
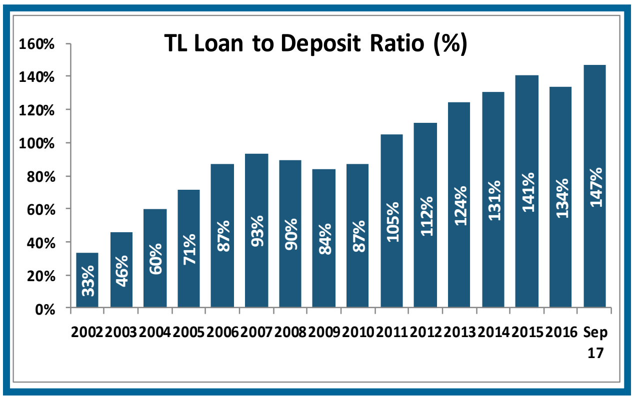
Banking Sector (II)

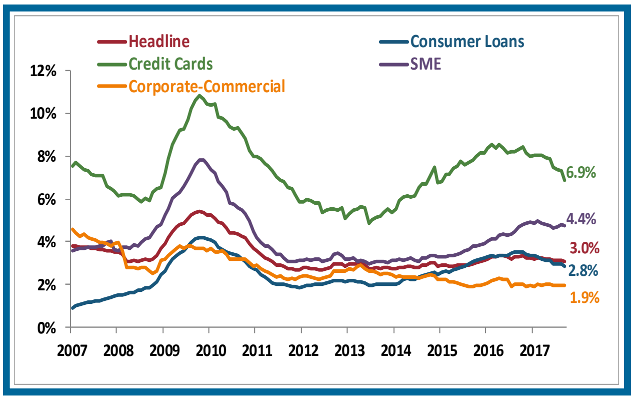
Loan to Deposit Ratios

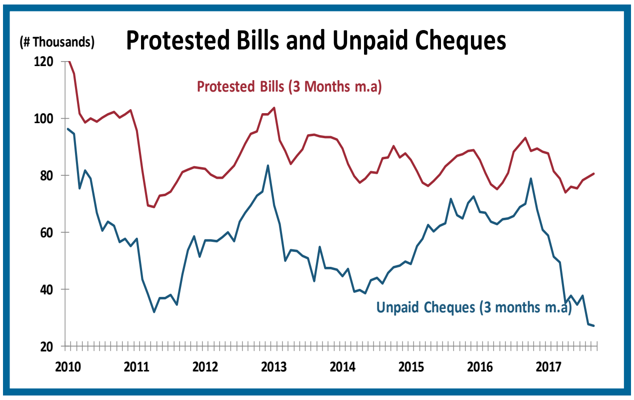




Loan to deposit ratio is 120% in September.

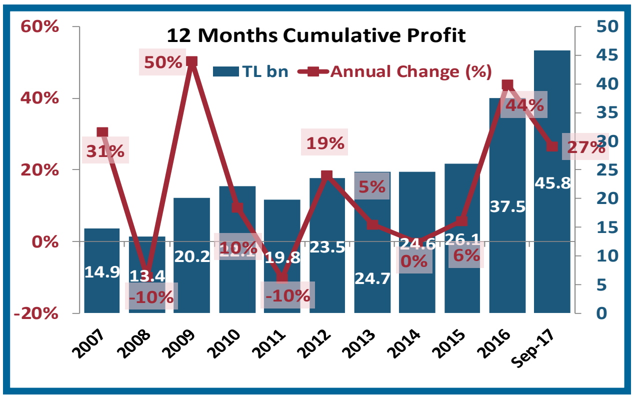
Loan Quality

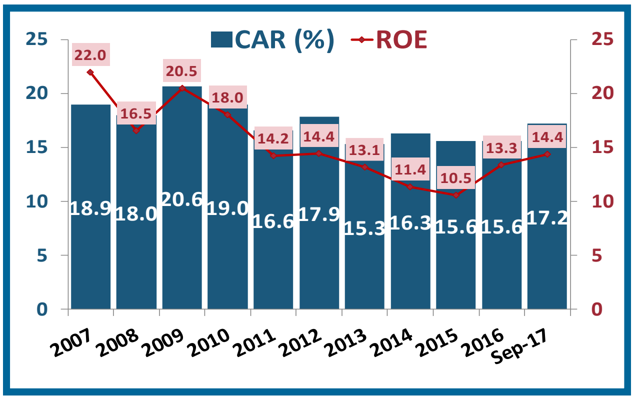




Headline NPL ratio for the sector is at 3.0% as of Sep 2017.

P & L





In Sep 2017, banking sector's annual profit increased YoY by 27% while ROE is 14.4%.