DenizBank Economic Update

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Economic Research and Strategy
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February industrial production rose more than expected...

- Industrial production index rose YoY by 5.8% in February above the market expectation of 4.5%. On a monthly basis, the index rose by 0.5%. In annualized terms, index was up by 4.1%. Unadjusted index rose by 8.5% in February following a 3.6% increase in January.

- While industrial production signals robust economic activity continued in the first two months of the year, leading indicators give a mixed signal. Manufacturing PMI decreased for the third time in a row to 49.2 in March from 50.3 a month ago. A figure below 50 is regarded as economic activity is contracting. On the other hand, seasonally adjusted capacity utilization increased again in April and reached 75.4%.

- Thanks to robust domestic demand and recovery in exports, economic activity continues to be strong in early 2016, after growing by 4% in 2015. A possible slowdown in tourism sector and geopolitical risks may have negative impact in the second half of the year.

Food prices continue to fall, bringing headline inflation down...

- CPI in March decreased MoM by 0.04% contrary to the market expectation of a 0.65% increase. Negative contribution from food prices continued. Annual food inflation dropped to 4.6% from 8.8%.

- Annual inflation decreased to 7.46% from 8.78% driven by the drop in food prices and a stable Turkish Lira. A slight improvement in the pricing behavior was observed as Core I index fell to 9.51% from 9.75%. However, current levels are still high for the core inflation.

- Despite the improvement in headline inflation, Central Bank (CBT) did not revise its year-end forecast in the second inflation report of 2016. Forecast for 2016 and 2017 remain unchanged at 7.5% and 6.0%, respectively. The bank expects inflation to reach the target of 5% by 2018. The high level of core inflation is a concern for the bank. The bank will have to keep its monetary stance tight until a significant improvement is realized. CBT Governor Murat Çetinkaya stated that they expected the core inflation will converge to headline figure by the end of the year.
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Monetary Policy

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

- In its monthly MPC Meeting, CB 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 10.00%
- CBT has made it clear that it aims for a simple, understandable monetary policy with one interest rate. The fall in global volatility levels has decreased the need for an interest rate corridor, so the bank can revert to a simple monetary policy from the current more flexible one. Steps were taken in the last two months thanks to falling inflation and positive outlook in financial markets. CBT states that it will be cautious further down the road in case of a turn for the negative in these conditions.
- Improvement in inflation and increased capital inflows thanks to rising risk appetite towards EM enabled CBT to lower the average funding rate from an average of 8.95% in March to 8.66% in April. Since the bank did not revise its forecast for year end inflation, a significant further decrease in average funding rate would not be likely. As the interest rate corridor narrows and policy moves to a singular rate, it can be expected for the policy rate to be determined in the vicinity of current average funding rate.

External Sector

Current Account Deficit continues to narrow in 2016...

- Current account deficit (CAD) in February came at $1.8 bn. 12 month cumulative CAD narrowed down to $30.5 bn (4.1% of GDP) from $32 bn in January.
- On the financing side, there has been an FDI inflow of $0.1bn in February. Inflow to the bond market was $0.7bn and to the equity market was $0.4 bn. Reserve assets increased in February by $0.6bn.
- 12 month cumulative energy deficit in January shrank by 35% on an annual basis to $30.4 bn.
- Low energy prices continue to drive the narrowing in the current account deficit. Despite the recent recovery in the prices, yearly average for brent oil prices is expected to be $40 per barrel. These levels continue to be a positive factor for Turkish current account. A possible drop in tourism revenues in 2016 may be a downside risk.
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Financial Markets

Debt Market

Benchmark bond yield is at 9.22%.

Currency Market

EM currencies appreciated against US Dollar in April.

Stock Market

MSCI Turkey equity index’ performance was better than other EMs in April.
CAR is at 15.5% in March, compared to 15.6% as the end of 2015.

Share of deposits in funding was at 58% as of Mar16.

Annualized loan growth is at 12.8% as of April 15th.
Loan to deposit ratio is 117% in March.

Headline NPL ratio for the sector is at 3.3%.

As of March, sector’s 12 month cumulative profit increased YoY by 8%. ROE is at 10.8%.