DenizBank Economic Update

July 2017

- Economy
- Financial Markets
- Banking Sector

Economic Research and Strategy

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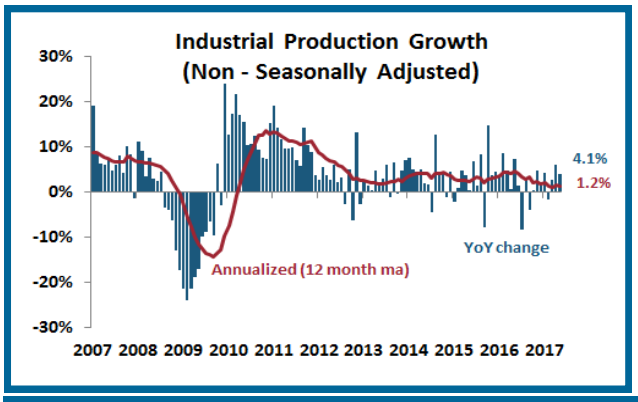
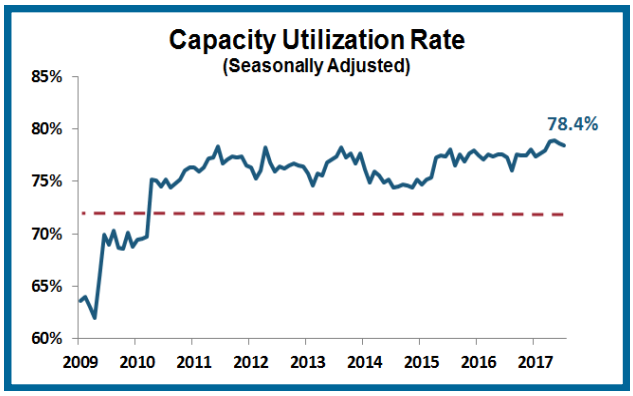
DenizBank Economic Update

Economy (I)

Growth



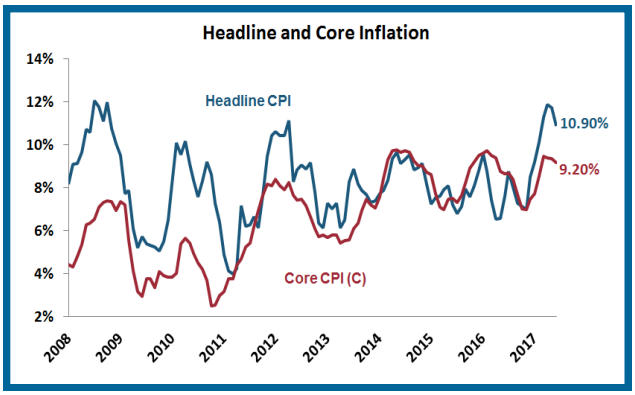


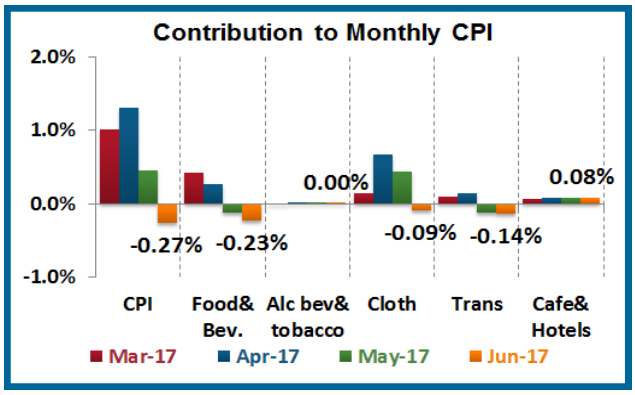
Economic activity continues to gain pace in the second quarter...

● Seasonally and calendar adjusted industrial production (IP) index contracted by 1.5% in May. The unadjusted index rose 4.1% annually in May. The rise in the unadjusted index in the first two months of the second quarter was 5.0% compared to the same period of 2016. Before Turkish Statistical Institute revised Turkish GDP series in December 2016, the unadjusted IP index served as a clear indicator of growth rate. However, in 1Q17, the rise in the index was a mere 1.7%, while GDP growth rate was 5%. The trend in IP suggests the industry sector will contribute positively to growth in 2Q, though the level is difficult to foresee. Turkish Statistical Institute announced IP index along with seven other indices will be updated in early 2018.

● Early indicators signal expansion is solid in economic activity. PMI, which has been above 50 since March, has reached its highest level since July 2014 with 54.7. Loan growth rate (13-week avg, annualized, net of currency effect) has been 28% throughout 2Q on average. Robust growth in retail and commercial loans is a gauge of increase in economic activity.

Inflation





Slow downward trend in annual inflation continued in June...

● CPI in June decreased MoM by 0.27%, in contrast to market expectation of a 0.4% increase. Food prices decreased by 1.06%, declining two months in a row and bringing annual food inflation down to 14.3% from 16.9% a month ago.

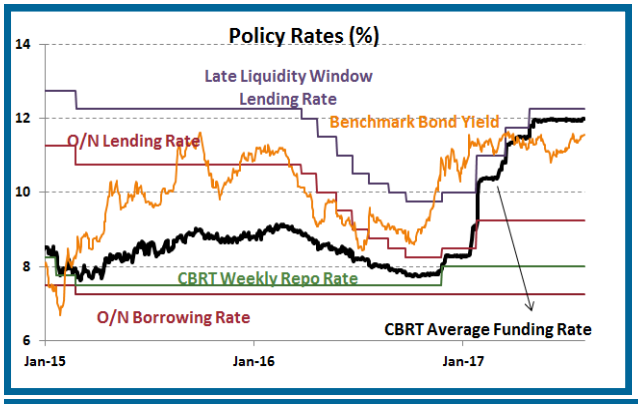
● Annual inflation dropped to 10.9% from 11.7% a month ago. Core Inflation indicator C (CPI excluding food, energy, non-alcoholic and alcoholic beverages, tobacco, gold) decreased to 9.20% from 9.38%. Producers' price index increased YoY by 14.9%.

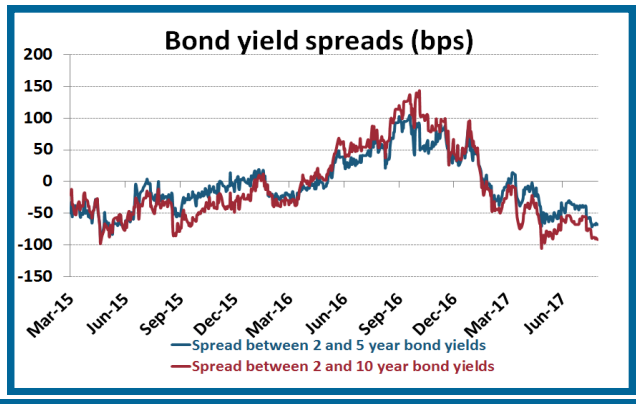
● Historical data and market expectation (Bloomberg survey of 19 participants) imply that inflation may continue to decrease in July. In the remainder of the year though, a reversal of the recent downward trend may be expected until December where due to favorable base effect annual inflation may retreat to single digit levels. The current high level of both headline and core inflation, continuing deterioration in inflation expectations are a clear sign that CBT should keep its current tight stance.

DenizBank Economic Update

Economy (II)

Monetary Policy





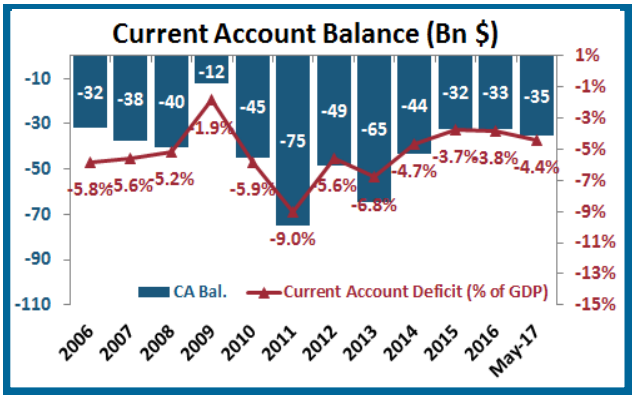
CBT kept all rates and its communication unchanged at July meeting...

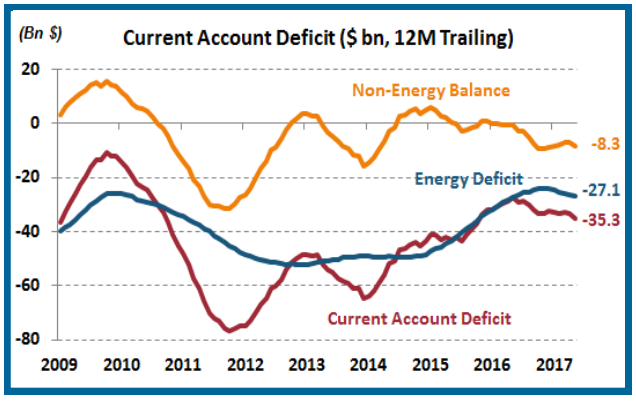
● In its July meeting CBT kept weekly repo, O/N lending and borrowing rates and late liquidity funding lending rate unchanged at 8.0%, 9.25%, 7.25% and 12.25% respectively. Monetary Policy Committee will convene on September 14th.

● The decision text was the same as previous month's expect for one sentence. Regarding economic activity, the bank now expects the economy to "maintain its strength", instead of "further accelerate due to the supportive measures and incentives provided recently." The text also revealed that a seat at the committee that was vacated in April was filled.

● Aside from minor tweaks and new assignments, July policy rate decision and the following text clearly states that CBT will continue to maintain its current tight monetary stance until inflation developments and expectations improve significantly. As annual inflation will likely hover around levels twice CBT's official target for the remainder of the year, average funding rate and structure may remain unchanged as well.

External Sector





Energy and gold imports push current account deficit wider..

● Current account deficit (CAD) in May came in above expectations at $5.24 bn. 12 month cumulative CAD increased to $35.3 bn from $33.2 bn in April (May 2016: $27.5 bn).

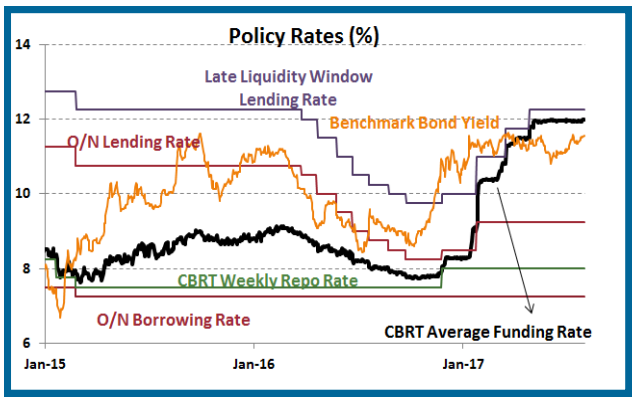
● Portfolio inflows have been the main source in financing the deficit. Net portfolio inflow in May has reached $5.5 bn, highest level in last 3 years. There has been an FDI inflow of $0.4 bn. Reserve assets increased by $2.5 bn and net errors and omissions by $1.7bn. 12 month cumulative energy deficit went up to $27.1 bn from $26.4 bn a month ago. Annualized tourism revenues increased slightly to $14.4bn from $ 14.3bn.

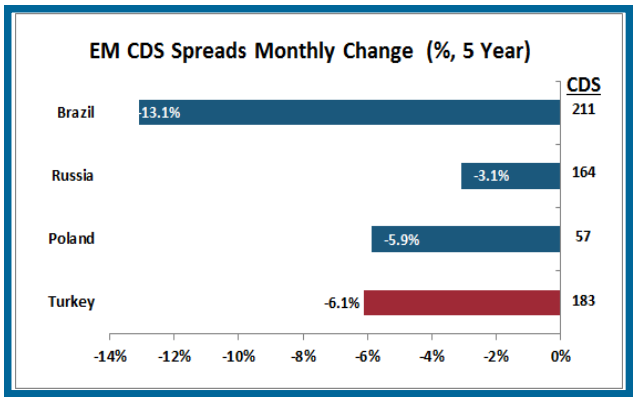
● Stripped from energy and gold imports, current account deficit has remained almost unchanged compared to end of 2016 at a period of high loan growth and solid domestic consumption. As energy prices continue to remain weak, CAD to GDP level can be expected to stay at manageable levels, namely below 5.0%.

DenizBank Economic Update

Financial Markets

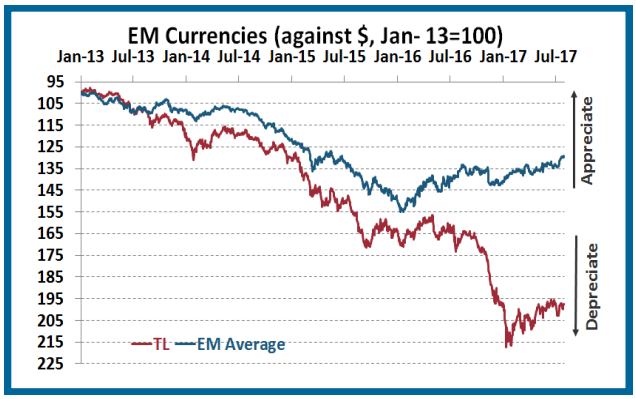
Debt Market

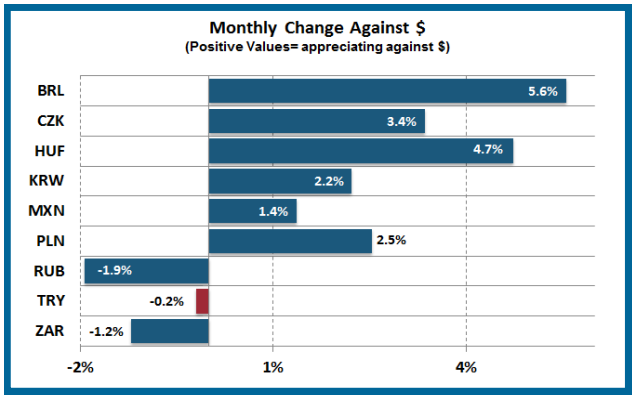




2-year benchmark bond yield is at 11.55%.

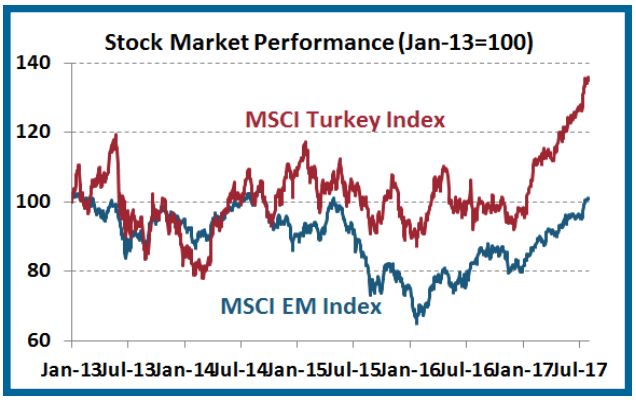
Currency Market

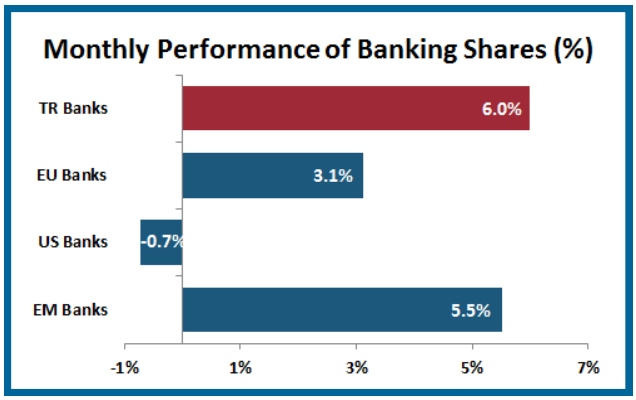




EM currencies, on average, appreciated against USD.

Stock Market



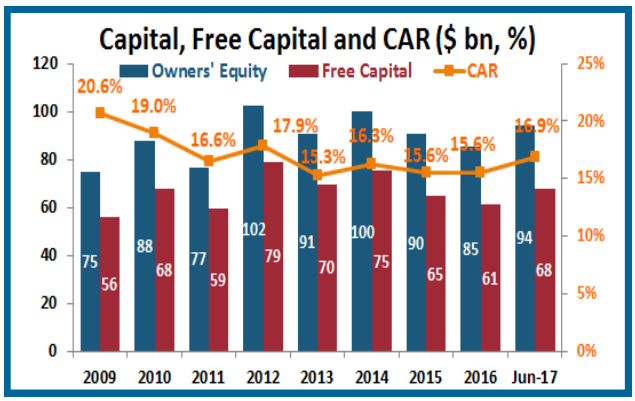


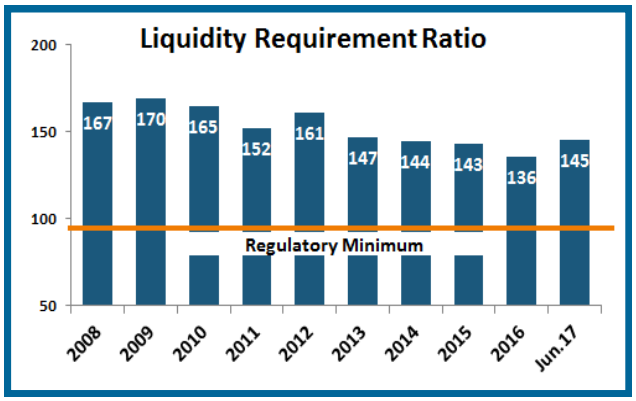
EM equity markets continued to perform well in July with Turkey outperforming its peers.

DenizBank Economic Update

Banking Sector (I)

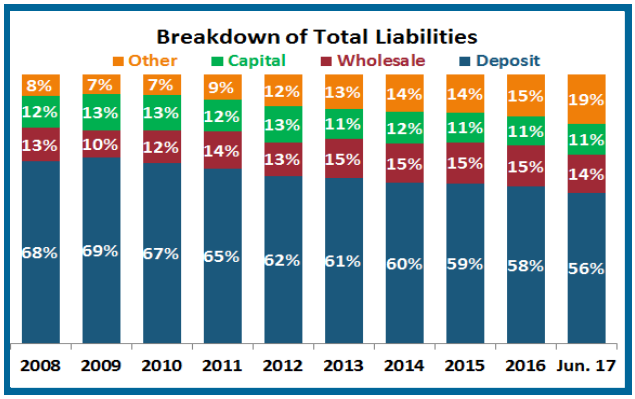
Capital

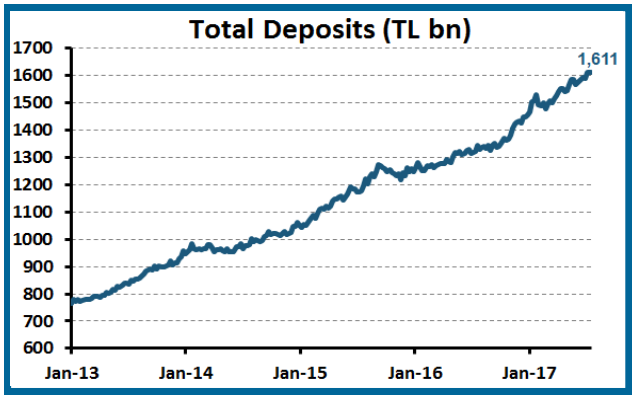




CAR increased to 16.9% in Jun 17.

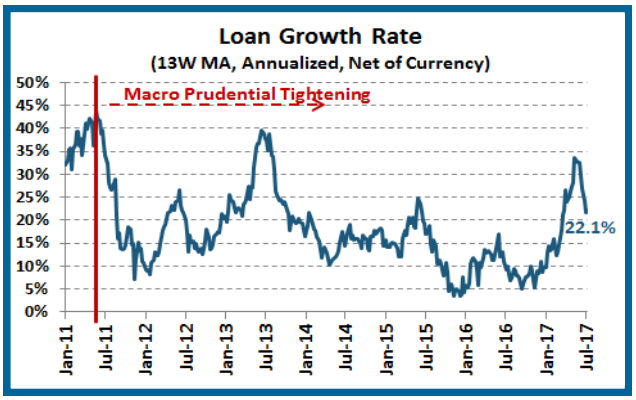
Funding

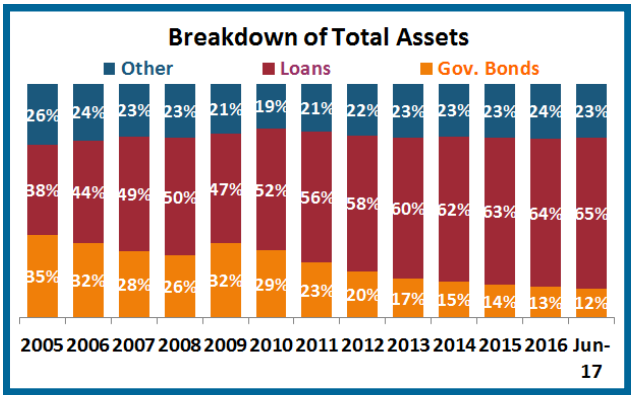




Share of deposits in funding was at 56% as of Jun 17.

Lending



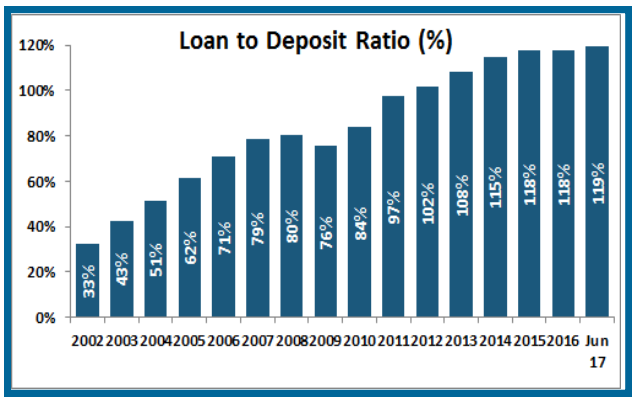


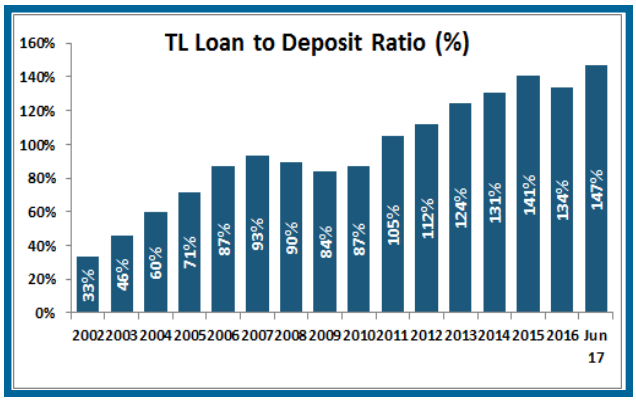
Annualized loan growth is at 22.1% as of Jul 21st.

DenizBank Economic Update

Banking Sector (II)

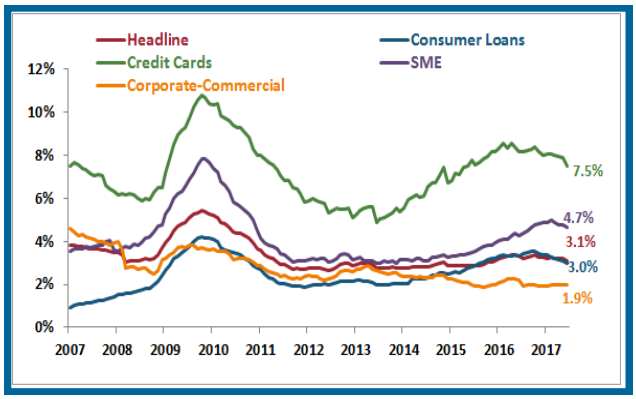
Loan to Deposit Ratios

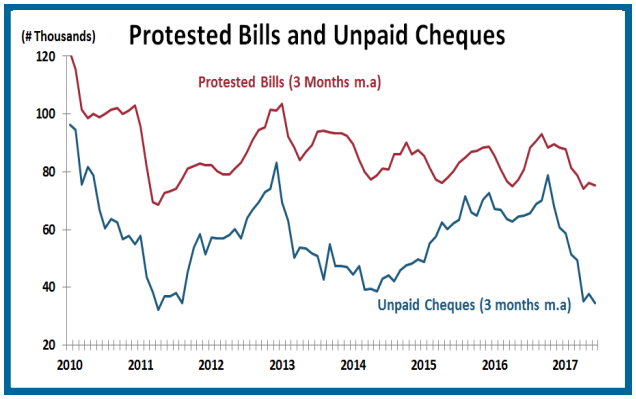




Loan to deposit ratio is 119% in June.

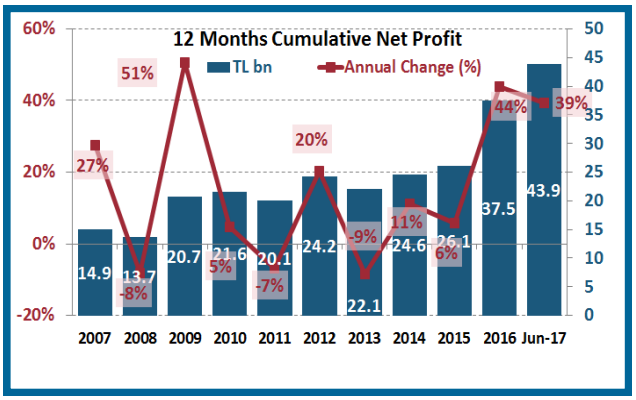
Loan Quality

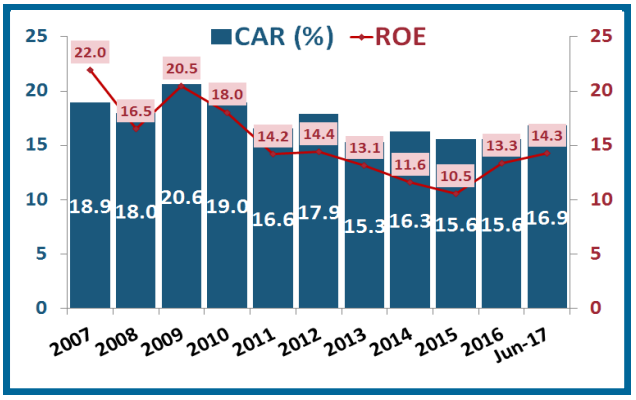




Headline NPL ratio for the sector is at 3.1% as of Jun 17.

P & L





In Jun 17, banking sector's annual profit increased YoY by 39% while ROE is 14.3%.