DenizBank Economic Update

November 2014

- Economy
- Financial Markets
- Banking Sector

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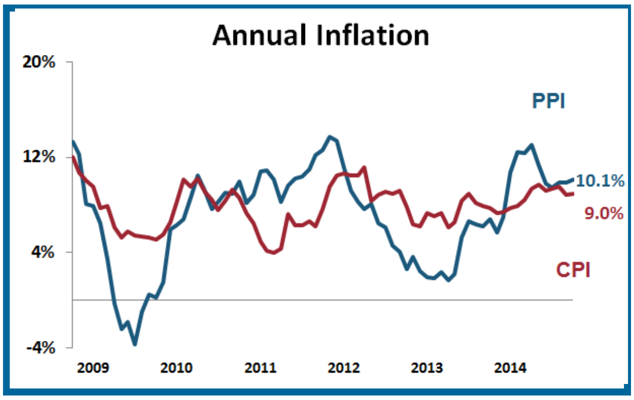
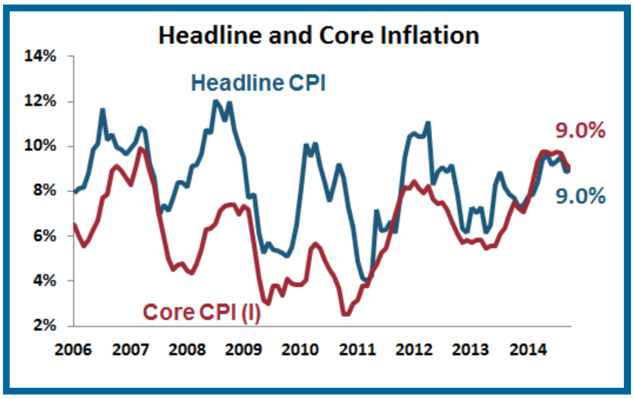
DenizBank Economic Update

Economy (I)

Inflation





Annual inflation remains well above Central Bank's target...

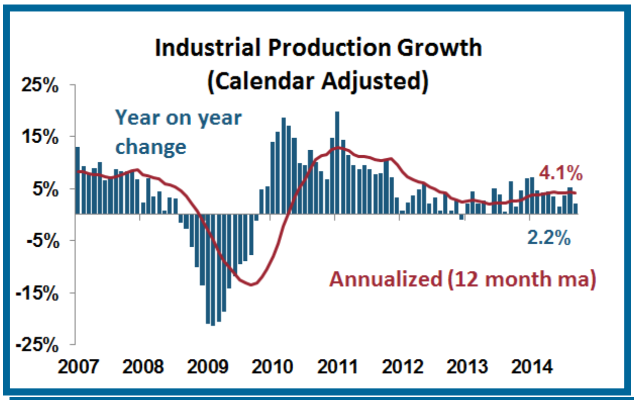
● Inflation rose 1.9% in October in line with expectations. Administrative price hikes and seasonal increase in clothing and food groups' prices pushed up the monthly inflation in October. Annual inflation slightly increased from 8.9% to 9.0%, which is substantially higher than the Central Bank's (CB) 5% (±2%) inflation target.

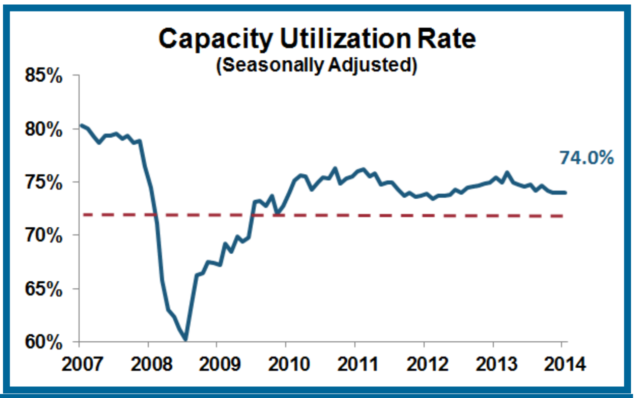
● Yearly core inflation, an important indicator of inflationary pressures, continued to improve in October. Annual Core I indicator went down from 9.3% to 9.0%, lowest level since the first quarter 2014.

● We expect inflation to increase to 9.2% by the year-end 2014 and fall sharply in the first half of 2015 and to be 7.2% by the end of 2015. Stable TL, falling energy prices and expected fall in food prices will help inflation to fall gradually.

● Our forecasts are above CB's revised forecasts of 8.9% and 6.1% for 2014 and 2015, respectively.

Growth





Manufacturing activity remains subdued

● The calendar adjusted industrial production index (IP) increased YoY by 5.2% in September slightly below the market consensus of 5.7%. Seasonally adjusted IP index posted 1.7% compared to the previous month,

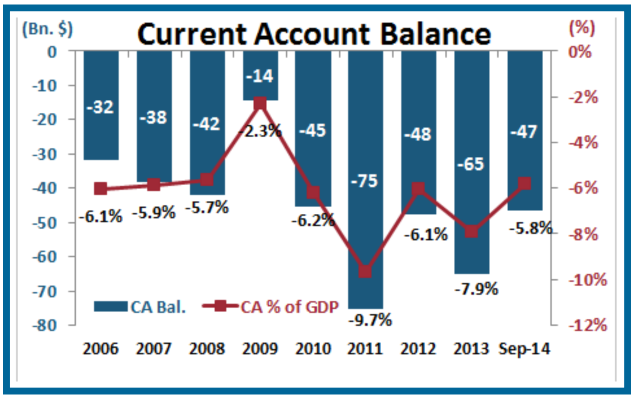
● Annualized increase in manufacturing activity declined to 4.1% in September. Leading indicators such as PMI manufacturing index increased for a third month in a row to 51.5 in October, which is the highest level since the end of 1Q14. On the other hand, capacity utilization in October stayed constant at 74%, which does not point a strong recovery in economic activity in the last quarter.

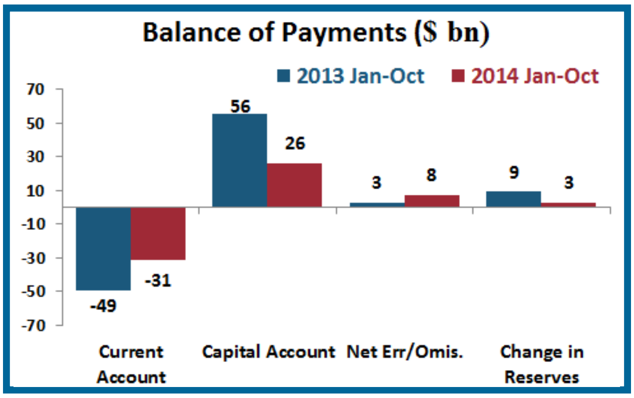
● Turkish economy is expected to grow 3.3% and 3.5% in 2014 and 2015, respectively. This slightly below long term average GDP growth of c. 5%, yet still good figures when compared with anemic growth rates all over the world.

DenizBank Economic Update

Economy (II)

External Sector





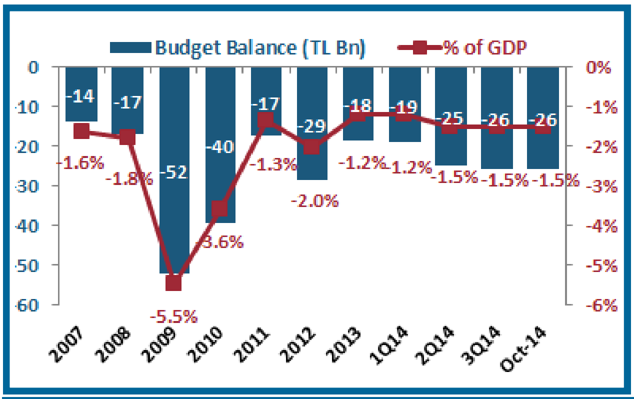
Current account continues narrowing in September.

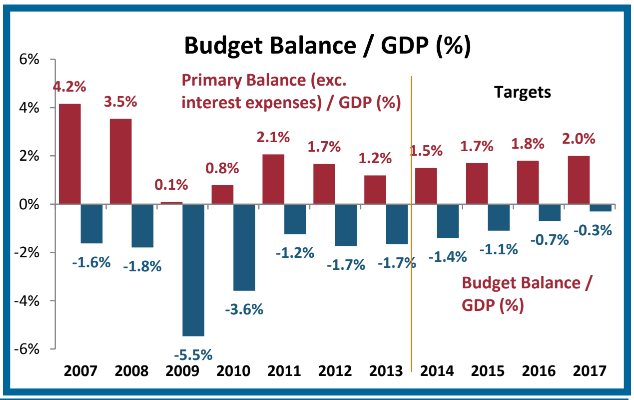
● Current account deficit came at $2.2 bn in September, below the consensus expectation of $2.6 bn. 12 month cumulative current account deficit narrowed down from $65 bn (7.9% of GDP) in 2013 to $46.7 bn (5.8% of GDP).

● Despite the risks in export markets on the back of geopolitical risks, we expect current account deficit to be at 5.5% of GDP at the year-end. Further decline in oil prices poses downside risks to our forecast.

● Recent sharp fall in energy prices will help to improve CA deficit As a rule of thumb each 10% decrease in oil prices will improve CAD/GDP by 0.5. In line with this, the CAD/GDP may fall below 5% in 2015...

Public Sector





Budget discipline maintained.

● As the end of October, 2014 the central government budget posted deficit of TL14.9 bn, while primary surplus reached to TL30.3 bn. Both YTD budget deficit and primary surplus figures are worse than the previous year due to the moderate growth in tax revenues, compatible with year-end targets.

● YTD increase in non-tax revenues was strong (up YoY by 14%) driven by one-off privatization revenues and new items classified under other revenues. On the other hand, YTD tax revenues are relatively weak (up YoY by 9%) due to moderating domestic demand. Overall, total revenues almost balanced the deterioration on the expenditure side which is up YoY by 11% with rising non-interest expenditures.

● New Medium Term Plan (MTP) for the years 2015-17 set more challenging budget targets for 2014 and the following years, such that Budget Deficit / GDP target for 2015 was reduced to 1.1%, corresponding to best performance since 2006, if succeeded of course...

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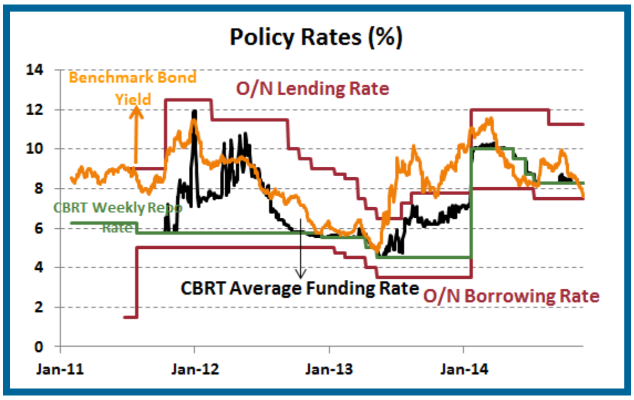
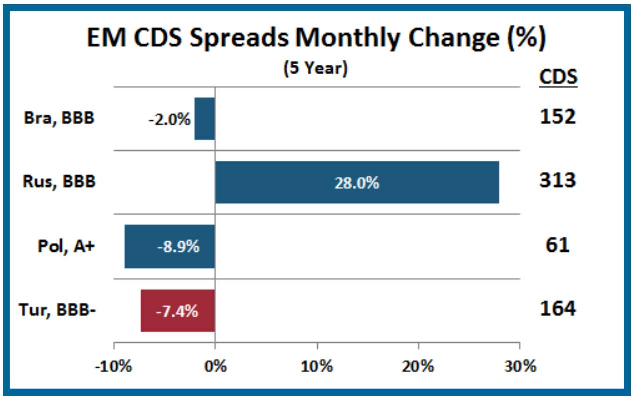
Financial Markets

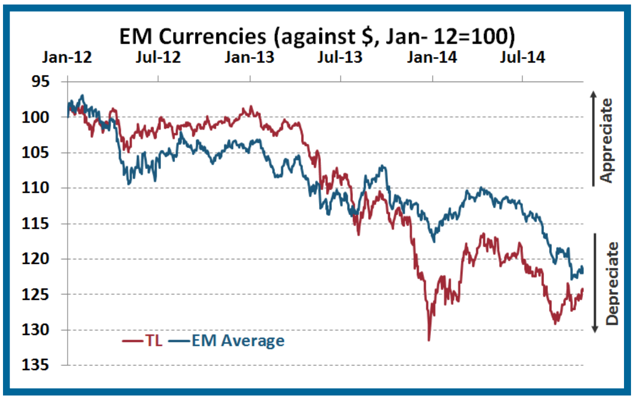
Debt Market

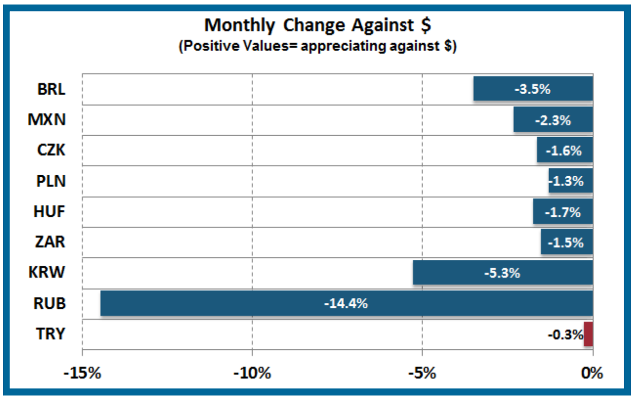




Thanks to rising risk appetite and rate cut expectation from CB, benchmark bond yield came down sharply to 7.6% from double digits in September.

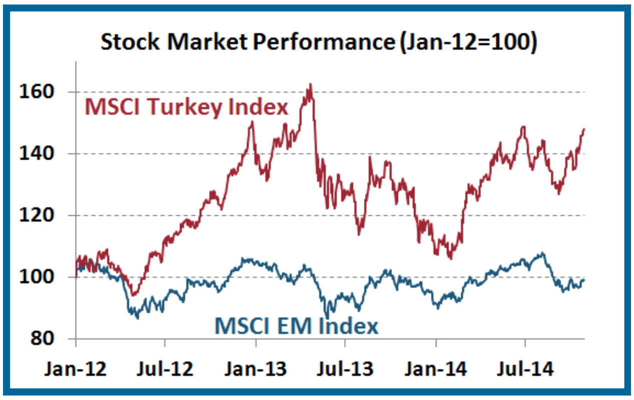
Currency Market

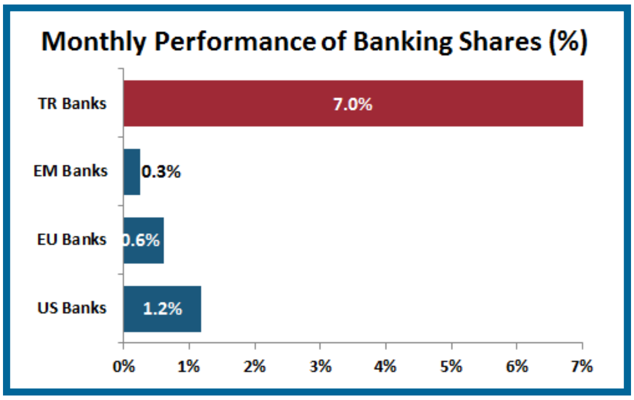




The TL was flat against the USD while EM currencies depreciated in November...

Stock Market





On the back of falling oil prices creating a positive outlook for Turkish economy, Borsa Istanbul is outperforming its EM peers...

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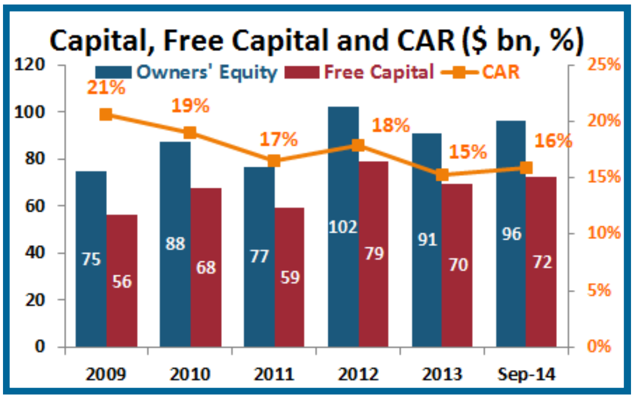
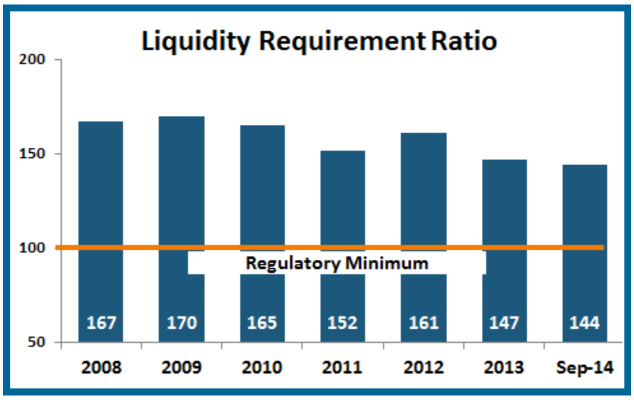
DenizBank Economic Update

Banking Sector (I)

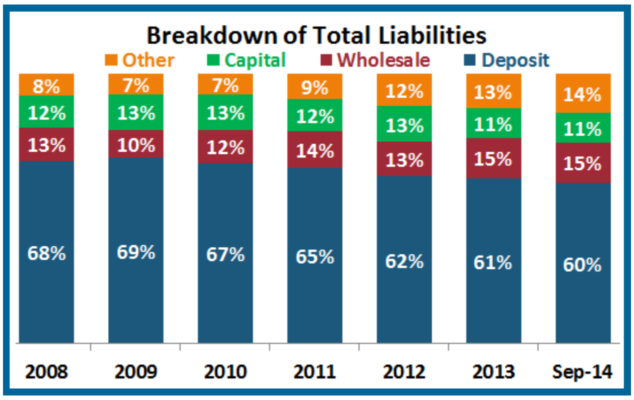
Capital

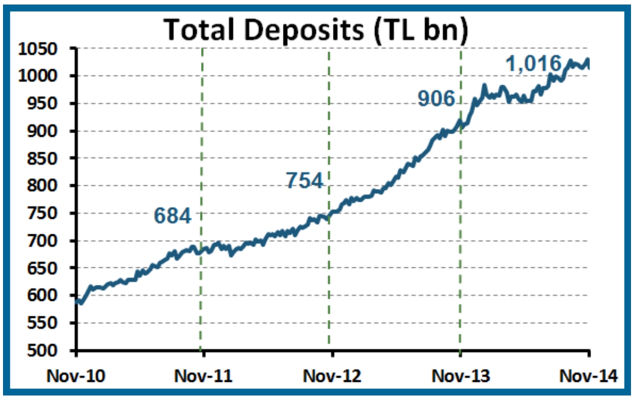




Despite declining profitability, banks are able to keep their CAR ratio at around 16%, thanks mainly due to slower loan growth.

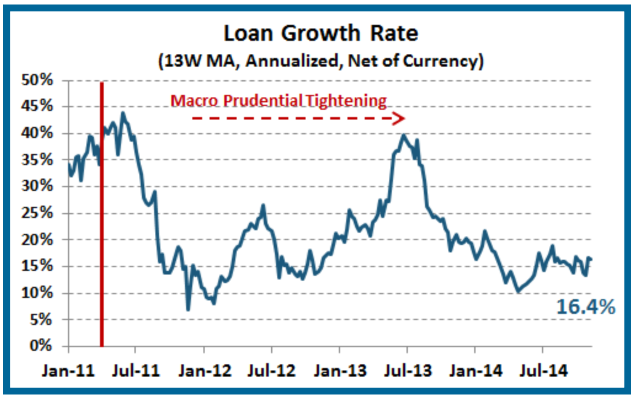
Funding

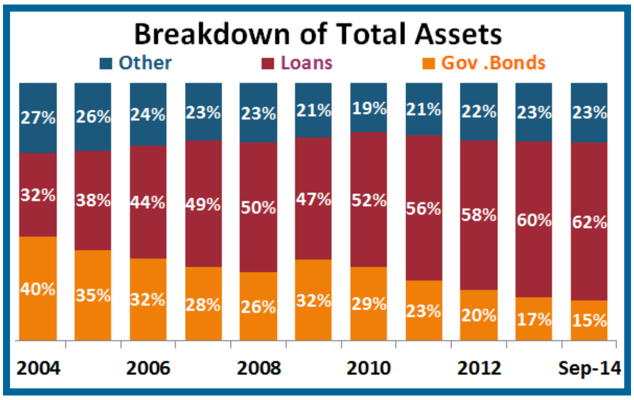




Share of deposits is slightly down to 60% in September from 61% last year...

Lending



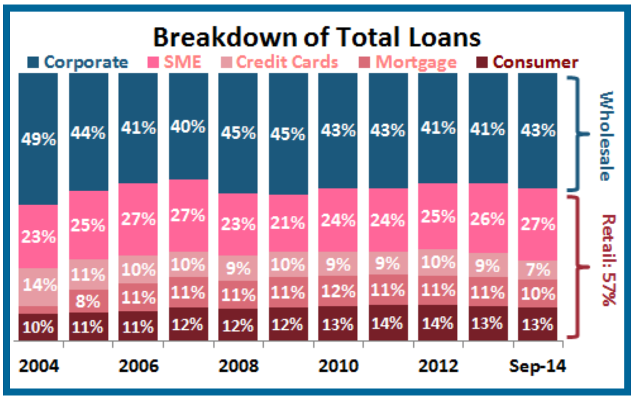


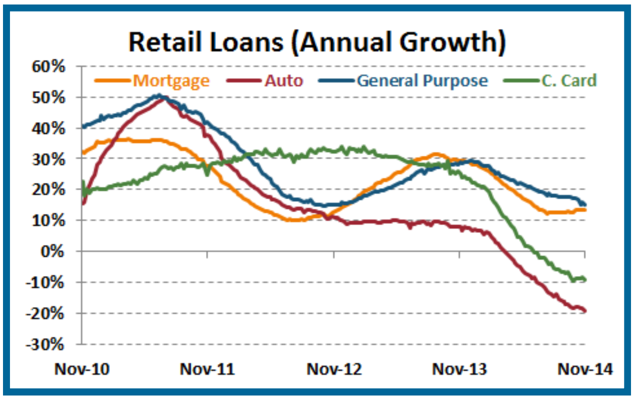
Annualized loan growth is at around 15%, which is in line with Central Bank's long term targets...

DenizBank Economic Update

Banking Sector (II)

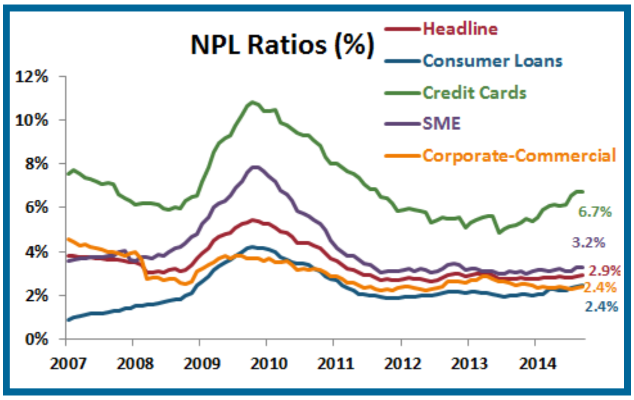
Loan Breakdown

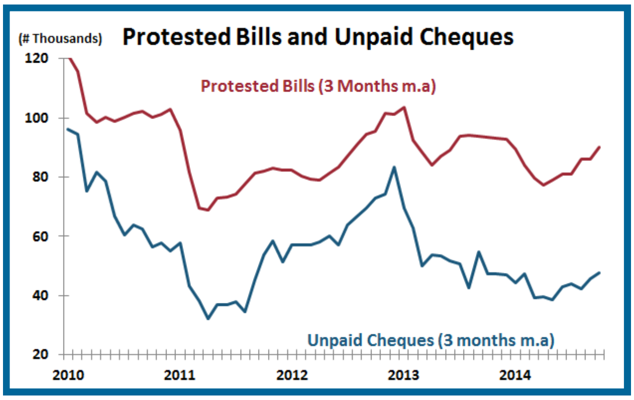




The deceleration in retail loans is more visible due to the macro-prudential measures taken by the authorities (both Central Bank and the BRSA)

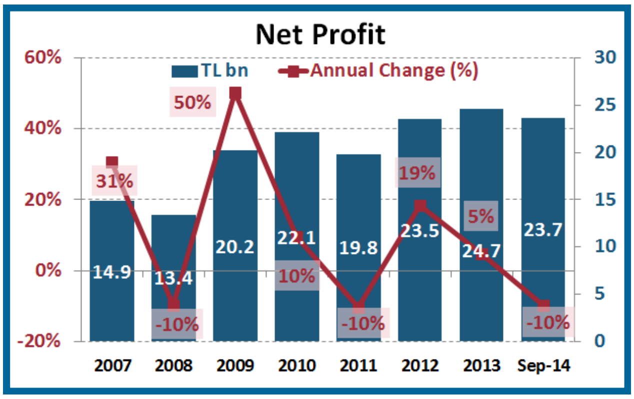
Loan Quality

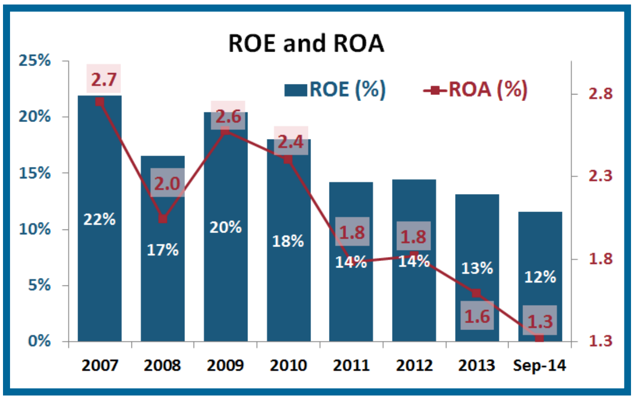




As expected, NPL ratio slightly increased due top slowing loan growth...

P & L





Profitability of the Sector is declining gradually mainly due to lower lending volumes and declining NIMs...The ROE for the year end, accordingly, is expected to ease below 12%...