Bakış

Macro Trends in Turkish and Global Economy

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General Outlook

The year 2017 started with positive expectations on a global scale after the economic challenges of 2016 and went on to renew hopes for stronger performances in advanced and emerging economies during the first half. While growth trends in the global economy are expected to continue for the remainder of the year, international institutions, such as the IMF and the OECD, have raised their growth expectations for 2017 to 3.5%.

Although growth in the US economy remained below expectations at 1.2%, the US Federal Reserve (Fed) raised its interest rates by 25 points at a meeting held in June, signaling that the slowdown in the economy would be a temporary one. Following an intense election marathon in Europe, the worries that political uncertainties in the region would escalate were put at ease after Emmanuel Macron won the French presidential elections and the central parties in Germany held onto power.

While uncertainties surrounding the Chinese economy remained on the agenda during the first half of the year, the Indian economy, which grew 6.1% in the first quarter, is expected to achieve a growth rate of more than 7% by the end of the year. On the other hand, Brazil, which grew by 1% compared to the previous quarter, is in the black once again for the first time in two years.

Following the April 16 referendum in Turkey, an increase in domestic demand was observed. Short term risks facing the Turkish economy appear to have tapered off to a stable level in the referendum's wake. While a 5% growth was achieved during the first quarter, the annual growth rate of total loans reached 21.8% as of June, thanks to the acceleration in commercial loans.

In short, the first half of 2017 met expectations in terms of both the resilience of the global and the Turkish economy. The upswing trend in global economies is expected to continue during the remainder of the year.

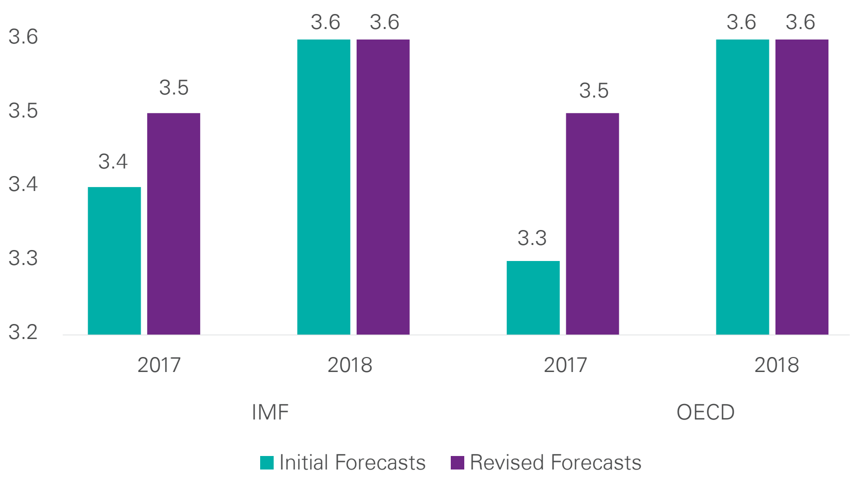
I hope you enjoy reading the report,

Murat Alsan
Chairman, KPMG Turkey

Overview of the global economy

- Entering the year 2017 with cautious growth prospects due to high political risks and geopolitical tensions, the global economy rounded off the first quarter with surprisingly strong economic results. When we look at data released in the second quarter, it is clear that advanced and emerging economies will have positive growth trends.
- In the light of the incoming data, many international organizations adjusted their forecasts for the remainder of 2017. The International Monetary Fund (IMF) revised its 2017 forecasts for growth from 3.4% to 3.5%, while the OECD raised its 2017 growth estimate from 3.3% to 3.5%. Both institutions kept their 2018 forecasts at 3.6%.
- High geopolitical uncertainties tend to support the view that risks to the global economy in the medium to long term still remain relevant, while developments in factors affecting inflation confirm the periodic positive trend in growth. Nonetheless, inflation components other than food and energy indicate that the acceleration in growth may remain limited.
- Election results in strong economies including France, the UK and Germany were important. The elections in Europe showed that the political risks to the region were not as high as they were thought to be at the beginning of the year. On the other hand, domestic political debates, particularly in the US, have increased concerns over the viability of growth-friendly policies.

Global Economic Growth Forecasts

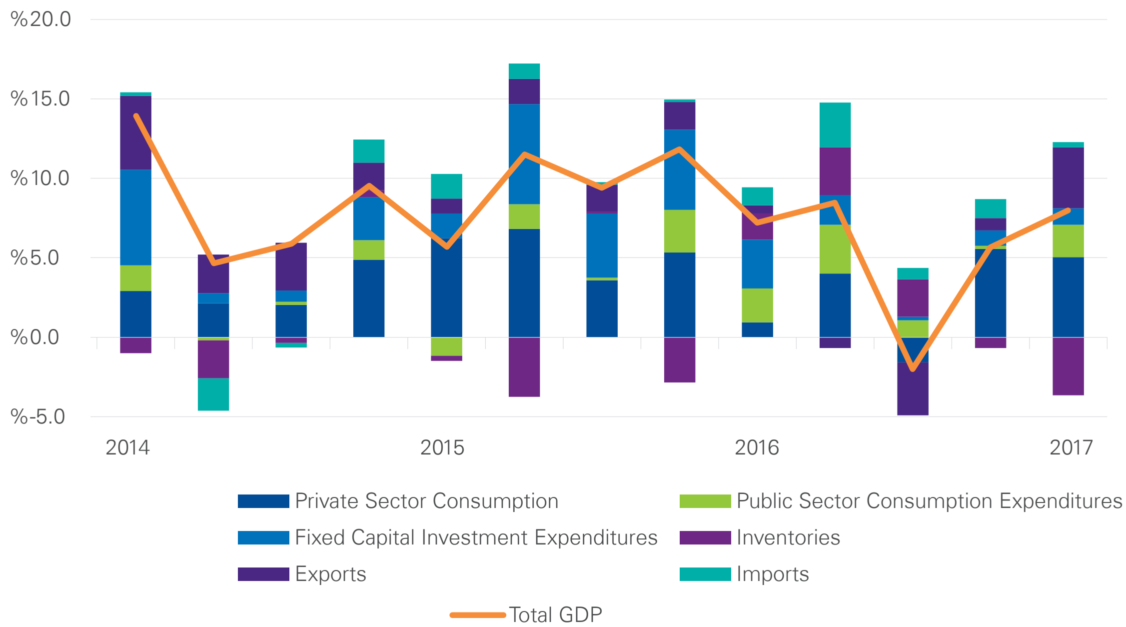


Source: IMF, OECD

Overview of the Turkish economy

- Short-term risks to the Turkish economy have been reduced following the neck-and-neck referendum results for transition to the presidential system. While the referendum results reduced the likelihood of early elections that could create a new political uncertainty, the government focused its efforts on rejuvenating the economy.
- In the first quarter, an annual growth rate of 5.0% was achieved. At the same time, while tensions with foreign political actors have been reduced in the short-term, both sides have started to adopt a more constructive language putting economic priorities above all else. While government measures taken towards the end of 2016 start to show their impact, the data flow indicates that the worst may be over in the mid-term in terms of macroeconomic fundamentals. The impact of government spending and measures to support domestic consumption were reflected in strong domestic consumption in the first quarter.
- The Credit Guarantee Fund (KGF) relieved small and medium-sized businesses in the real sector that were having difficulties finding loans. While the growth in the banking sector accelerated, profitability received a considerable boost. With the acceleration of commercial loans in the sector, the annual growth rate of total loans reached 21.8% in early June creating hopes for stronger investment and growth figures in the second and third quarters.
- Along with the supportive trend in global financial markets, the resilience of the economy has increased interest in Turkish financial assets. The Turkish lira appreciated in value by 3.8% from late March to mid-June, while equity markets rose by 10.5%, making them some of the world's best performing financial assets.

Contributions to Annual Growth



Source: TÜİK (Turkish Statistics Institute)

Conclusion

Although commercial relations with the Middle East and North African countries are still troubled by geopolitical problems, the economic activities of the EU economies and the strong results in global trade have reflected positively on the Turkish economy.

Meanwhile, the tourism sector is trying to compensate for its losses in 2016. Despite a considerable recovery in markets that suffered a severe recession last year, it is noteworthy that the number of tourists coming from the EU decreased by 20.6% in the first four months.

Credit expansion in the second quarter significantly increased the banking sector's resource needs, thus having a knock-on effect on deposit rates. This put an upward pressure on credit costs and raised serious questions in terms of growth funding.

Inflation, which peaked at 12% in the second quarter, could start falling owing to the drop in interest rates expected in the upcoming period. Keeping inflation under control to remain at stable levels is of even greater importance. Therefore, in order to support the macroeconomic framework, capital inflows to Turkey should continue to be encouraged, highlighting the need to maintain conditions that will increase investor confidence.

Expectations in 2017

Growth

While the contribution of domestic private sector consumption and public spending may decrease, the contribution from investments and net external demands may limit the slowdown in growth. Hence, it is expected that the growth rates throughout the year may fluctuate between 4-5%.

Tourism

It seems that the 2017 performance of the sector still trying to recover its losses will be determined by the number of tourists coming from the EU. With the rapid recovery in other markets, total tourism revenues could exceed $15 billion this year with an increase of around 10%.

Foreign Trade

Exports: Strong export figures to the EU despite geopolitical problems support expectations that the overall slowdown in exports will remain limited. Accordingly, exports are expected to increase by more than 10% to $160 billion this year.

Imports: In addition to continuing domestic demand, there is a significant risk that oil prices will have a smaller contribution than last year. For this reason, it is estimated that imports can exceed $225 billion with a slightly faster increase than exports.

Growth expectation for 2017

4.5%

GDP estimate

$845 billion

2017 foreign trade expectations

Exports $160 billion

Imports $225 billion

Currency markets (year average)

USD / TRY	: **3.60**
Euro / TRY	: **3.96**
EUR / USD	: **1.10**
Petrol	: **$52.5**

Unemployment

11%

(year average)

Inflation

9%

(year average)

Current Account Deficit

37

(billion USD)

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