



Bakış

**Macro Trends in the Turkish and
World Economy**



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General Outlook



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From the aspects of both world and Turkish economy, we've left a distressful summer behind us. Even though summer season is now remained in the past, question marks on the course of economy are unfortunately still standing.

In July's "Bakış" we wrote that trade wars erupted between the USA and China have not caused any negative consequences for global trade yet but the case that other countries starting to raise their customs walls is a source of concern for world's economy.

By adopting protectionism trends in global trade in the third quarter of 2018, some slowdowns in the growth rates of some countries started to be observed. Concerns are rising for especially developing country economies like Argentina and Turkey as well as Italy.

FED's decision to continue to increase interest rates and ECB's decision to continue to its asset purchase program are pointing out a more negative view in the near future for developing countries. Annual growth rate of global trade volume decreased to 12.5% in the second quarter of 2018 which was 14.5% in the first quarter. In July, the same trend has continued and growth rate decreased to 12.1%.

On the other hand, IMF and OECD foresee that world's economy will grow by 3.7% in 2018. Growth prospects for 2019 are also positive. But both two organizations highlight that fragility of global financial markets still stands at the end of a decade after the last global crisis.

Turkish economy is going through a period that it feels these fragilities deeply.

of political tension with the US in the middle of July set a record by testing 7 TRY levels in August. Inflation rate also pushed 25% in September, reaching out to the highest of last 15 years.

Turkish economy maintained its momentum of strong growth with 7.3% in the first quarter of 2018 but slowed down a bit with 5.2% growth rate in the second quarter just like many other developing countries. Nevertheless, growth prospects for the third and fourth quarters are grossly disrupted due to higher exchange and inflation rates.

While a number of companies which have debts in foreign currency in the last decade are announcing concordatum to avoid bankruptcy, New Economic Programme announced by the Government suggests actions to be taken for strict money and public finance policies. In government's programme, 2018 growth is foreseen as 3.8%, where 2019's growth prospect is 2.3%. The overall economic performance in the first quarter of 2019 would mainly show whether actions taken worked or not.

Size of deceleration in growth rate and direction of economic policies would be the key for capital flows. Therefore, it is crucial to adopt economic policies to ensure that this fluctuation we are experiencing would remain limited.

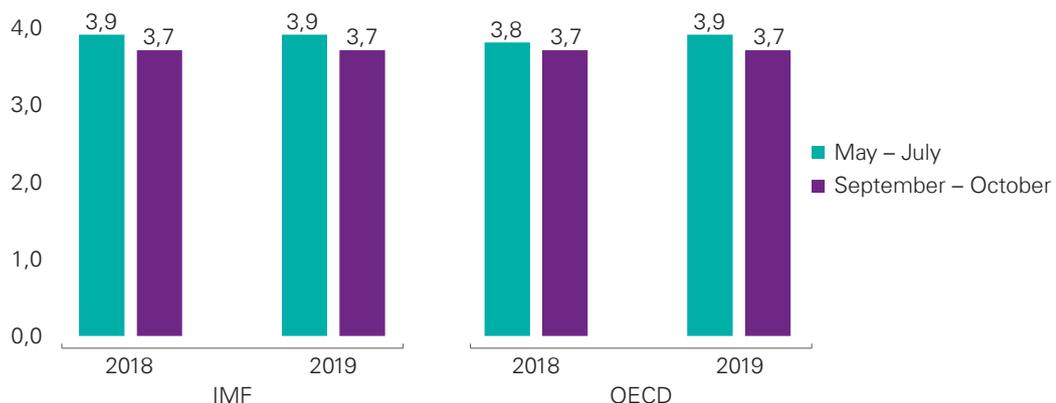
I hope you enjoy reading the report!

Increasing USD exchange rate as a result

Overview of the global economy

- In third quarter, geopolitical tensions remained in the background while slowdowns in growth rates of some countries are becoming more apparent once protectionism actions were taken in global trade. Concerns about some of the developing economies such as Argentina and Turkey are holding appetite for risk down.
- Although figures from USA economy confirm a strong growth in the country, deceleration continues under the leadership of European exporter industries and countries. FED fortified the expectations well that it would make another increase in interest rates in December by continuing gradually increasing interest rates in such environment. It also gave the signal that it would go on with a similar momentum in 2019. In Europe, as the reliability indexes point out deceleration in economic growth, ECB confirms that it would adopt termination plan for asset purchase programme by year-end.
- Due to persistence of geopolitical tensions, crude oil prices continue to rise. As with the recovery of USD, upward trend continues in production costs in world-wide. Crude oil prices upward trend backs oil exporter countries but also has a negative impact on developing economies as a whole.
- In this environment, international organizations recently made downward updates in their forecasts regarding global economy. IMF and OECD foresee that world's economy would grow at a nearly constant rate slightly above pre-crisis averages in 2019 after maintained 3.7% growth in 2018. In a decade after global crisis, it should be noted that fragility in the world's financial markets still stands and also paid attention that tensions in global trade are fundamental risks before growth prospects.

Global Growth Prospects



Source: Bloomberg, investing.com

Overview of the Turkish economy

✎ Maintaining its momentum for strong growth in 2018, Turkish economy slowed down like many other developing economies in the second quarter. Uncertainties in financial markets, diplomatic tension with USA caused a dramatic rise in mobility in Turkish financial markets in the third quarter.

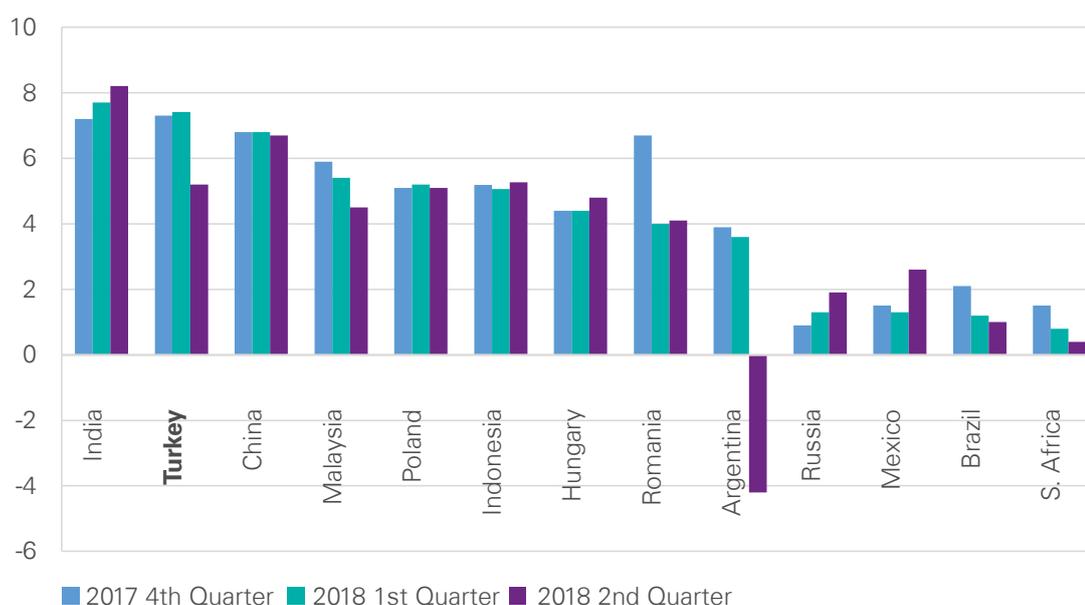
✎ Turkish Lira was losing value rapidly both in real and nominal aspects while interest rates were rising so quickly. With increase in exchange rates and disruption in pricing behavior, inflation gained speed. Hence, Turkish Central Bank (TCMB) increased political interest aggressively as a result of 625-base point interest rate increase at September's meeting even though it kept interest rate stable after July's meeting.

✎ This tightening in financial conditions slowed down national demand while stability in the strength of foreign demand was limiting deceleration in growth. Some of the preliminary data for the third quarter point out that such deceleration in growth might not be such harsh as being concerned despite the

sharp fall experienced in reliability indexes. On the other hand, inflation keeps worsening while a considerable improvement process is beginning for Turkey's foreign deficit. Course of oil prices and exchange rates current level point out a challenging period for inflation which might cause a slowdown for such improvement process of foreign deficit.

✎ After recent developments, 'New Economic Programme' declared by the Government also suggested a set of reasonable projections as being aware of this view. With this new programme, Government foresees that growth – which was calculated as 3.8% for 2018 – would decelerate to 2.3% in 2019. It is estimated that inflation would be 20.8% by year-end under the coordination of strict money and public finance policies and decrease to 15.9% by the end of 2019. However, announcing that some public investments shall be set aside and giving messages that banking sector's financial structure may be strengthen if required are prominent elements in details of this programme.

GDP annual growth rates (%)



Source: The Economist

Conclusion

 2018 second quarter data points out the dramatic deceleration in the momentum caught during second quarter of 2017. However, data announced on monthly basis gives complicated signals on the severity of deceleration in the economic activities. Data on industrial production, retail sales and turnover showed that the economy still made a strong start on the third quarter. But confidence indexes had a sharp fall with the effect of turmoil in financial markets and thus pointed out that economic activity might become stationary in the upcoming period.

 Pressure of increasing costs with the increase in exchange rates and global commodity prices accelerates inflation's rise. In this environment, economic units pricing behavior was getting disrupted while inflation was breaking records. The gap between producer prices and consumer prices points out that inflation keeps increasing in the next days. However, it is believed that Turkish Central Bank has to keep increasing interest rates to make government's set of micro measures taken to take inflation under control be effective.

 As foreign deficit was narrowing down with deceleration in national demand, tourism's support in summer season allowed Turkish economy have current accounts surplus. Although this trend may continue in the upcoming period, recent increases in oil prices may put partial limit on the improvement of current deficit in the upcoming period.

 For banking sector, credit growth momentum continued to decelerate. In return, due to Turkish Central Bank's decisions to increase interest rates and jam in liquidity conditions sector's credit and deposit interest rates kept increasing rapidly. These factors might affect profitability and growth rate of the sector in short term. It is however estimated that in medium term, the size of disruption in the quality of assets will depend on overall economic growth performance.

 Since it is considered that geopolitical tensions and non-economic uncertainties would have influence from time to time in the upcoming period, it is foreseen that Turkish financial markets fluctuations would continue depending on the global appetite for risk. For capital flows perspective, size of deceleration in growth and course of economic policies will be definitive. It is therefore believed that economic policies to ensure that mobility would remain limited should be adopted immediately.

Expectations for 2018

Growth



Even though Turkish economy achieved a growth above its potential in the first half of 2018, it started to slow down notably during the second half. Therefore, it is considered that annual growth might remain under 4%. It is also considered for the next year that global growth and appetite for risk would be the key for the trend of growth.

Inflation



As a result of disruption in pricing behavior in addition to mobility in exchange rates and increase in energy prices, inflation's tendency to increase may continue to the end of this year. Next year's potential improvement is expected to be determined by the trend in exchange rates.

Foreign Trade



As Turkish Lira's weakness is balancing negative effects of geopolitical uncertainties, it is foreseen that annual export may reach to 175 billion USD with a 10% growth rate. Import may also reach to about 260 billion USD depending on the trend in commodity prices and deceleration in national demand. In the upcoming year, effect of protectionist actions on global trade would be more apparent.

Tourism



For 2018 it is foreseen that revenues from tourism would reach to 27 billion USD, which was 22.5 billion USD in 2017. It is also estimated that moderate increase in the number of tourists and revenues from tourism might continue in 2019.

Growth expectation for 2018

3,9%

2018 GDP expectation

740
billion USD

2018 foreign trade expectations

Exports: **175** billion USD
Imports: **260** billion USD

Markets (year average)



USD/ TRY : **5.12**
Euro/ TRY : **6.09**
Euro/ USD : **1.19**
Oil : **75 USD**

Unemployment

11.3%
(year average)

Inflation

20%
(year average)

Current Deficit

45
(billion USD)

*Data given above is based on market data as of 15th October 2018.

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