BBVA Research

Türkiye Economic Outlook
January 2024

Garanti BBVA Research

Creating Opportunities

Key messages

- Rebalancing in the Turkish economy continues slowly. We expect GDP growth to materialize closer to 4.5% in 2023 and decelerate to nearly 3.5% in 2024, where the fiscal stance and the size of capital inflows will be decisive for the pace of adjustment.

- On the demand side, our big data consumption indicators signal that consumption is not decelerating much further since November, which requires tighter financial conditions to help rebalance the economy and start anchoring inflation expectations.

- We remain prudent on our inflation projections and maintain our year-end expectation of 45% with a bias slightly to the downside.

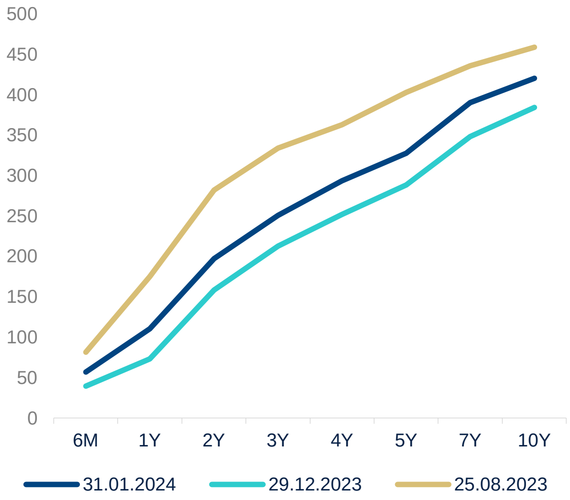
- The Central Bank (CBRT) has stopped at 45% policy rate and signaled to continue tightening via macroprudential policies and quantitative tools.

- We maintain our call of 45% policy rate throughout 2024. If inflation trend starts to decline much faster in 2H24, we also envisage that the CBRT might start the easing cycle with limited steps in 4Q24.

- On the global front, we keep our view of a soft-landing scenario with inflation easing going forward. Given recent positive inflation surprises, we brought slightly forward our forecasts of the beginning of the easing cycles to May24 from Jun24 in the US and to Jun24 from Sep24 in the EZ.

Most recently CDS curve went up slightly on concerns about inflation, off-shore TL rates converged to OIS swap rates

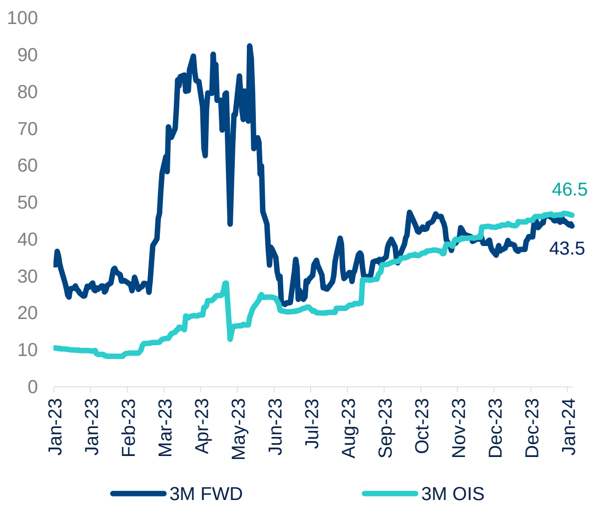
TÜRKİYE CDS CURVE
(BPS)



TÜRKİYE'S 5-YEAR CDS WRT PEERS*
(BPS)

*Chile, Colombia, Mexico, Brazil and South Africa

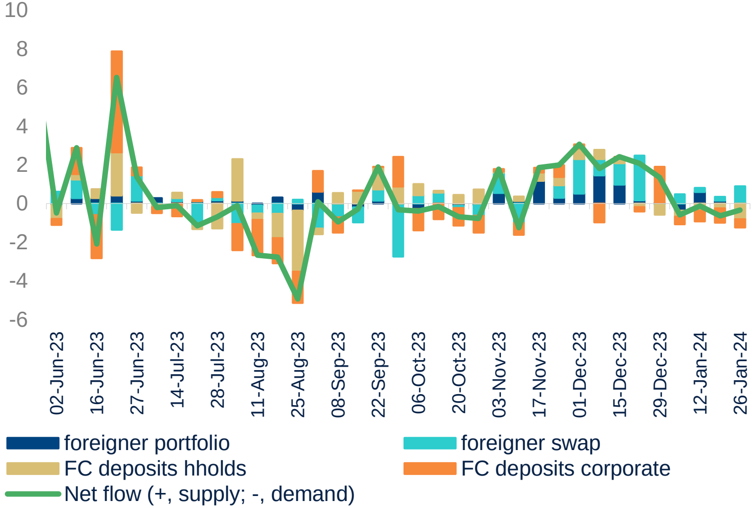
3M USDTRY FWD IMPLIED & 3M TRY OIS YIELD, %



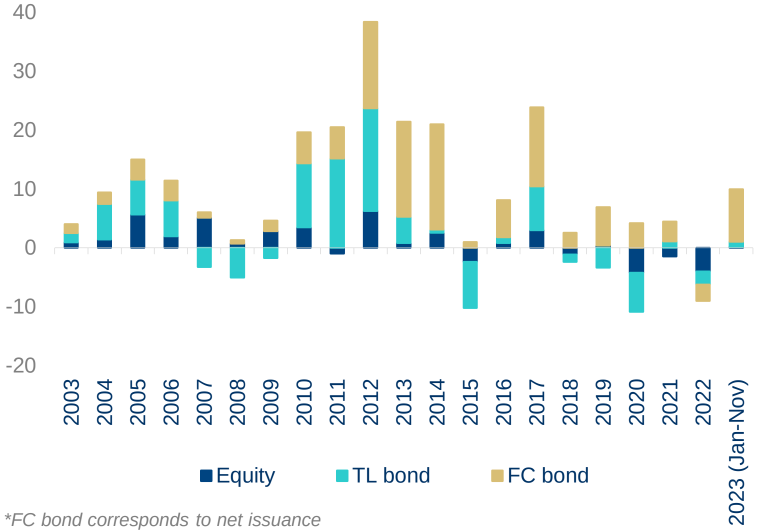
Source: Bloomberg & Garanti BBVA Research

Foreigners' portfolio inflow weakened December 22, due to holiday season and uncertainties about inflation outlook

FC FLOWS OF SUPPLY & DEMAND
US$BN, WEEKLY, ADJ. FROM PRICE EFFECTS



PORTFOLIO FLOWS* ON BOP FINANCING
US$BN



*FC bond corresponds to net issuance

Foreigners' inflow

Oct 27- Dec 22
$1.9bn equity
$3.4bn TL bond
$6.7bn swap

Dec 22 - Jan 26
$0.1bn equity
$0.4bn TL bond
$1.7bn swap

Between Jun-Nov2023:
$1.8bn equity + $0.9bn TL bond + $7.8bn FC bond

Source: CBRT & Garanti BBVA Research

Continuation of a clearer commitment against inflation will likely bring upgrades on the credit rating and further reinforce capital inflows

No	S&P	Moody's	Fitch	Meaning and Color
1	AAA	Aaa	AAA	Prime
2	AA+	Aa1	AA+	High Grade
3	AA	Aa2	AA	
4	AA-	Aa3	AA	
5	A+	A1	A+	Upper Medium Grade
6	A	A2	A	
7	A-	A3	A-	
8	BBB+	Baa1	BBB+	Lower Medium Grade
9	BBB	Baa2	BBB	
10	BBB-	Baa3	BBB-	
11	BB+	Ba1	BB+	Non Investment Grade Speculative
12	BB	Ba2	BB	
13	BB-	Ba3	BB-	
14	B+	B1	B+	Highly Speculative
15	B	B2	B	
16	B-	B3	B-	
17	CCC+	Caa1	CCC+	Substantial Risks
18	CCC	Caa2	CCC	Extremely Speculative

Moody's Positive

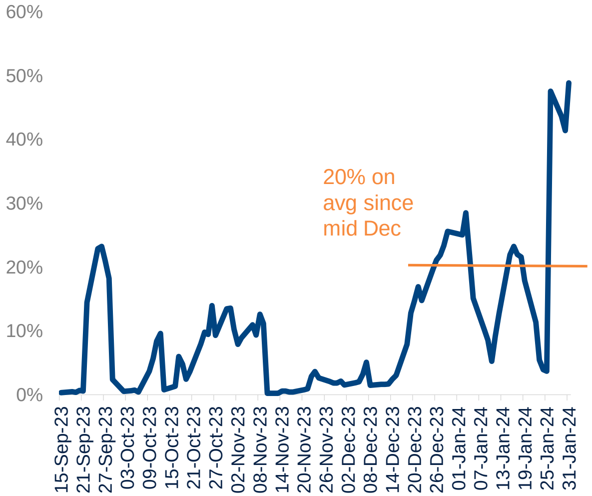
S&P Positive; Fitch Stable

- Jan-Feb CPI will be the key to understand whether inflation trend goes out of the CBRT's projected inflation range, and if so, how the CBRT will react
- If inflation trend starts to come down again as expected and reserves accumulation continues, one notch upgrade will likely happen even ahead of the election
- If a clearer commitment against inflation is seen thereafter, we might observe a few upgrades at once

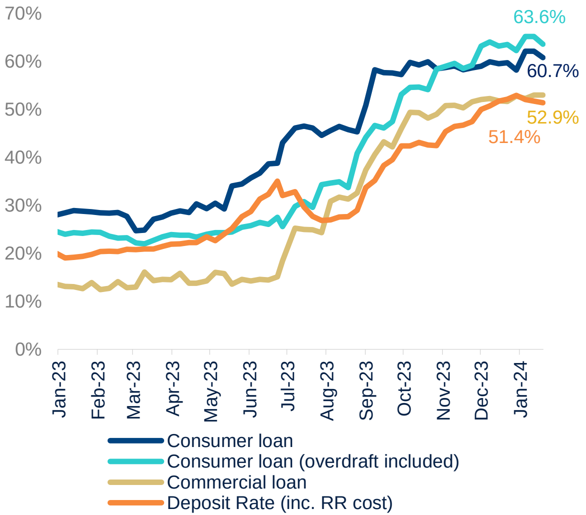
Source: Rating Agencies & Garanti BBVA Research

Competitive environment on lending activity, excess TL liquidity & renewal of ex-FC scheme deposits result in downside pressure on TL deposit rates

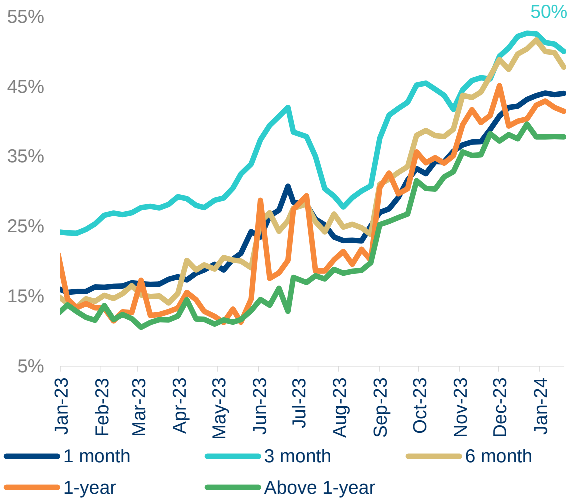
CBRT STERILIZATION / TOTAL FUNDING
%



CONSUMER & TL COMMERCIAL RATES
%, flow, sector



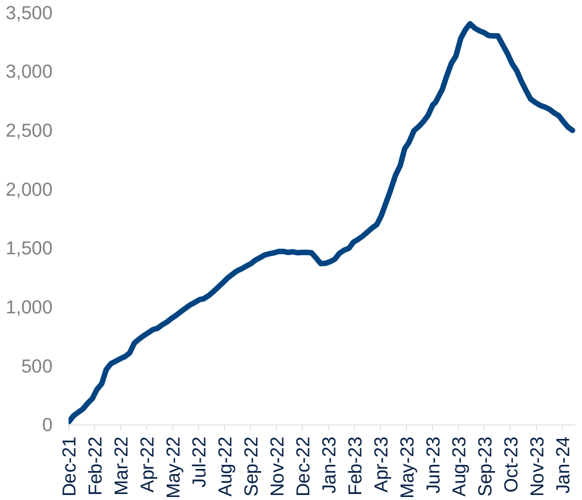
TL DEPOSIT INTEREST RATES
%, flow, sector, without RR cost



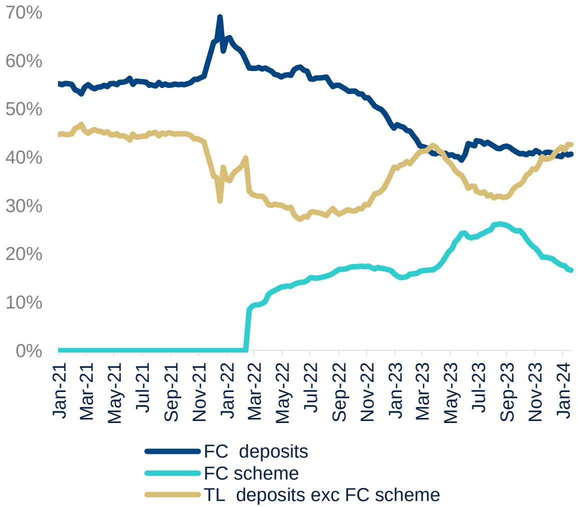
Source: CBRT & Garanti BBVA Research

More TL generation in the system, mainly flowing into TL time deposits

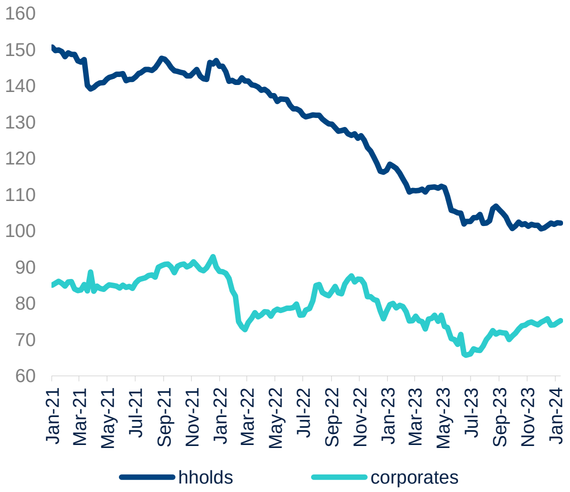
SIZE OF FC PROTECTED SCHEME
(in bnTL)



DISTRIBUTION AMONG DEPOSITS
(% share in total)



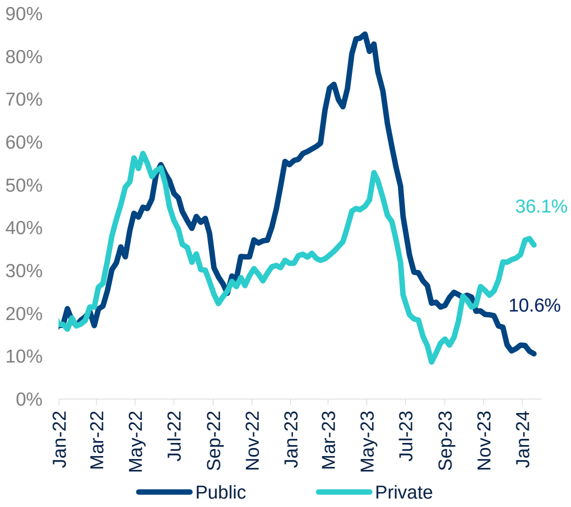
FC DEPOSITS OF RESIDENTS
(BN USD)



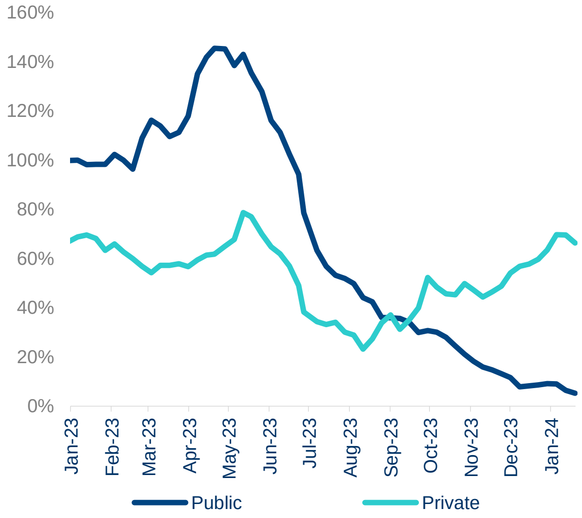
Source: Garanti BBVA Research

Private banks push for TL lending, whereas public banks are aggressive on FC lending. Overall, lending started to accelerate, though still limitedly

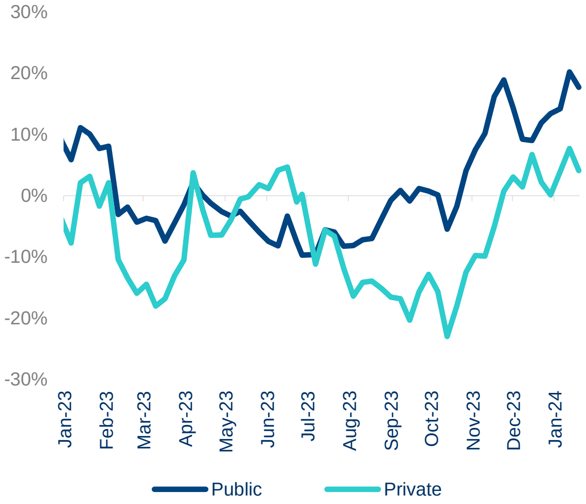
SECTOR FX ADJ. CREDIT GROWTH
13-week annualized, sector



TL CREDIT GROWTH
13-week annualized



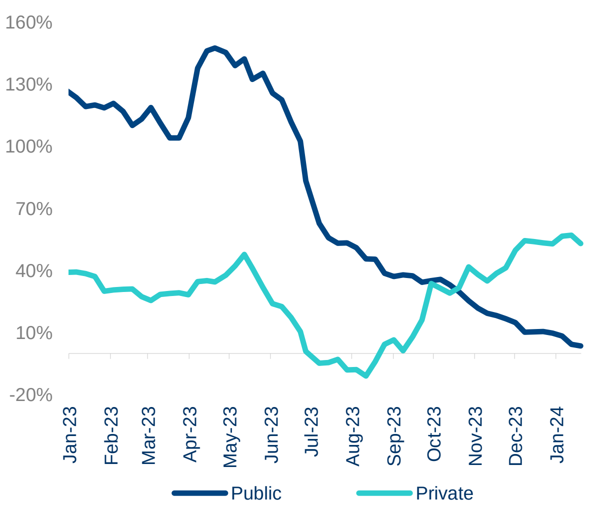
FC CREDIT GROWTH
USD, 13-week annualized



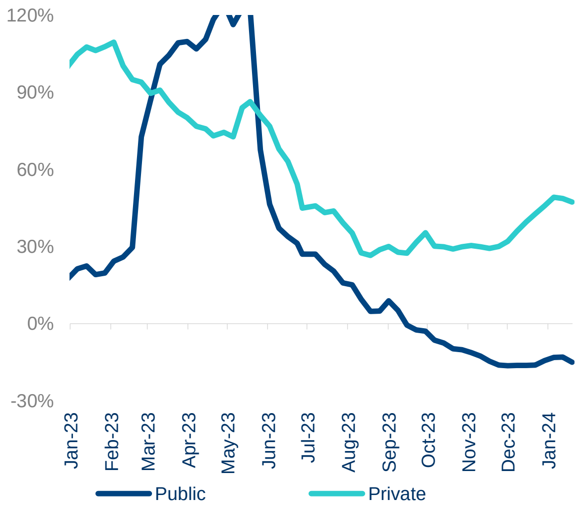
Source: BRSA, TURKSTAT, CBRT & Garanti BBVA Research

Private banks started to focus more on consumer lending (more favorable margins, continuation of strong demand, extension of card limits)

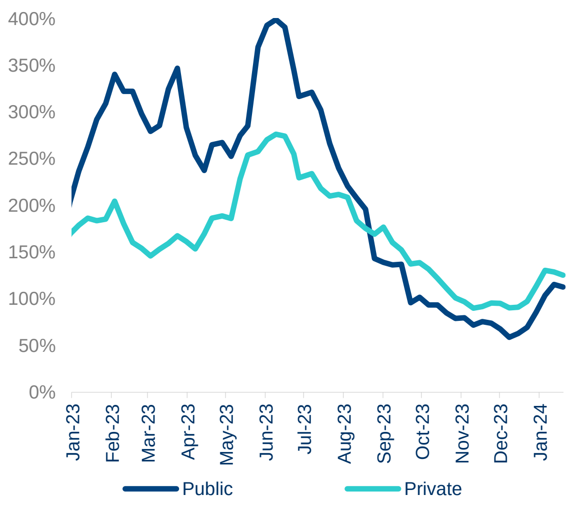
TL COMMERCIAL LENDING GROWTH
13-week annualized



CONSUMER CREDIT GROWTH
13-week annualized, without credit cards



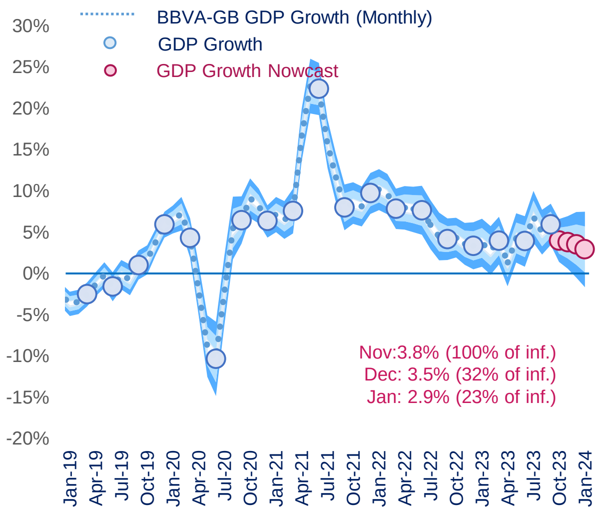
CONSUMER CREDIT CARDS GROWTH
13-week annualized



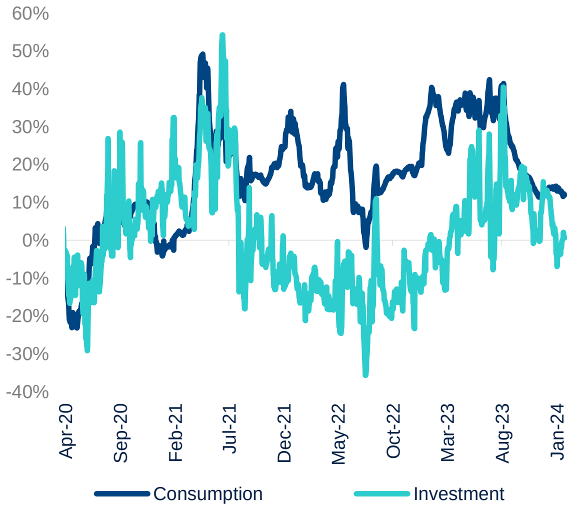
Source: BRSA, TURKSTAT, CBRT & Garanti BBVA Research

Domestic demand remains quite stronger than supply, consumption is not decelerating much further since late 4Q23

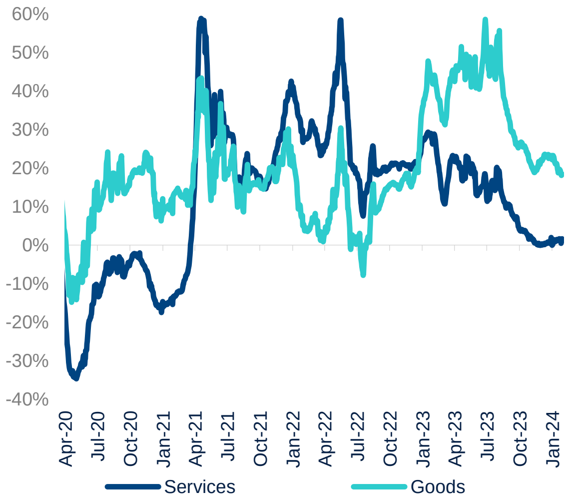
GARANTI BBVA MONTHLY GDP INDICATOR*
YOY, 3M MOVING AVG.



GB BIG DATA DOMESTIC DEMAND
(REAL, 28-DAY SUM, YOY)



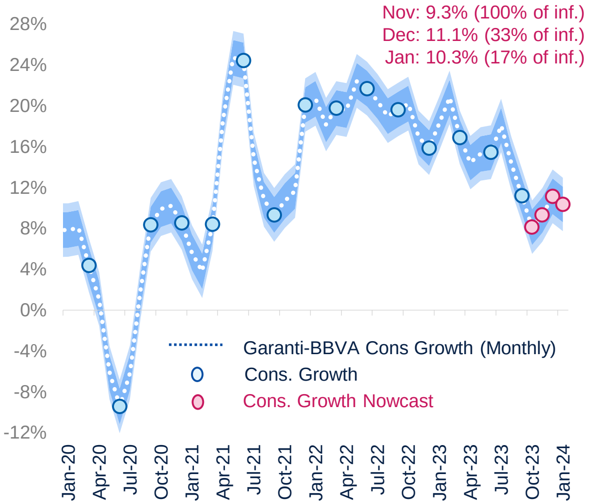
GB BIG DATA CONSUMPTION
(REAL, 28-DAY SUM, YOY)



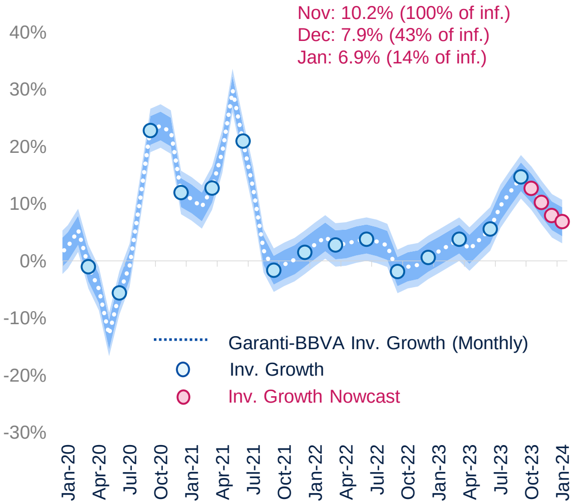
Source: TURKSTAT & Garanti BBVA Research

Consumption and investment contributed totally 9.2pp to annual GDP and the negative contribution from net exports recovered in 4Q23

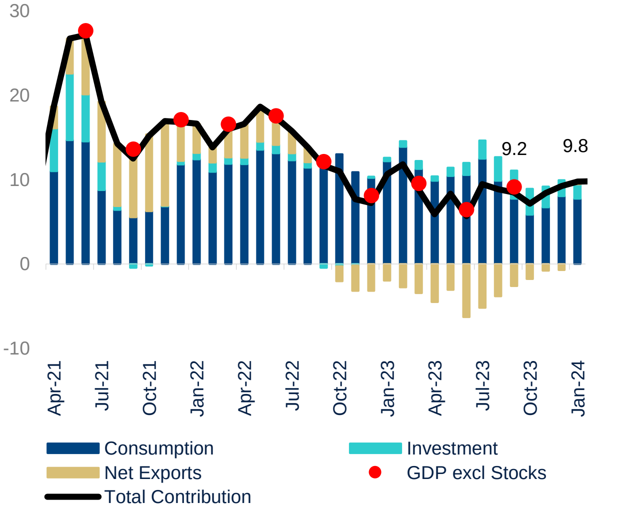
GARANTI BBVA CONSUMPTION GDP NOWCAST (YOY, 3M MOVING AVG.)



GARANTI BBVA INVESTMENT GDP NOWCAST (YOY, 3M MOVING AVG.)



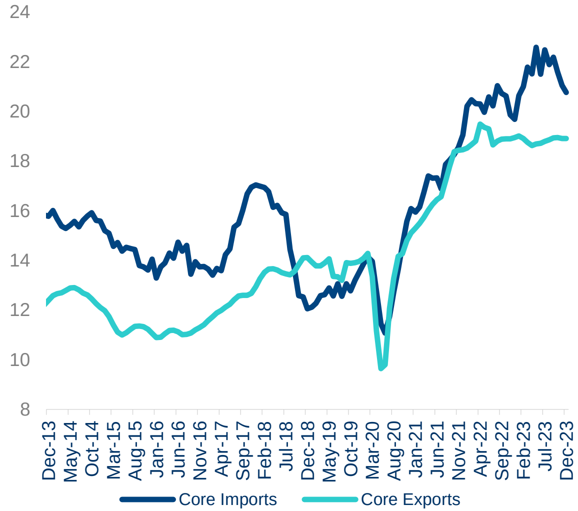
GARANTI BBVA NOWCAST CONTRIBUTION TO ANNUAL GDP (PP)



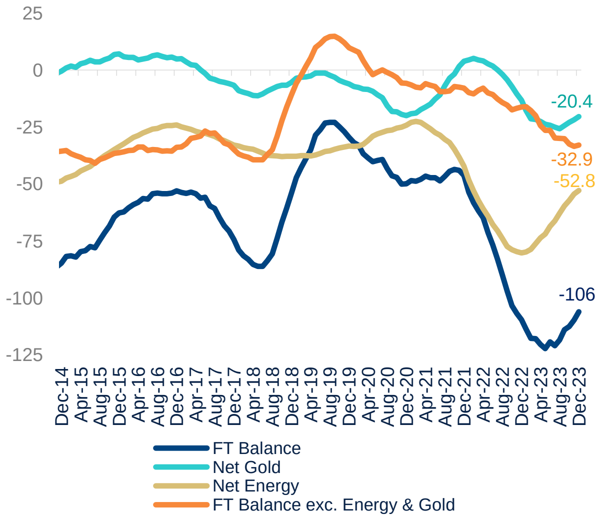
Source: TURKSTAT & Garanti BBVA Research

Core import demand declines only gradually, real appreciation contains the required adjustment on current account balance

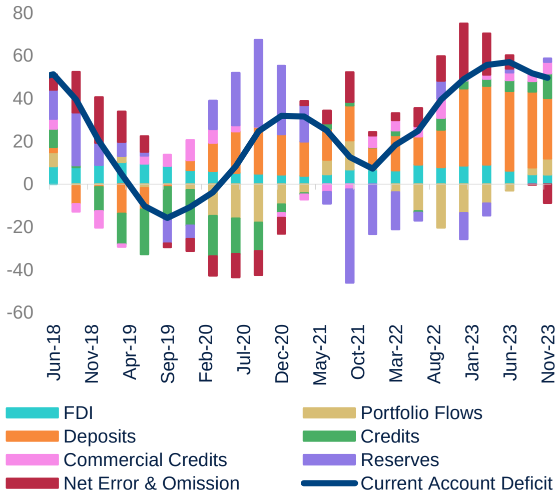
GOODS EXPORTS & IMPORTS
(EXC ENERGY & GOLD, SA 3M AVG, US$BN)



GOODS FOREIGN TRADE BALANCE
12-MONTH, US$BN



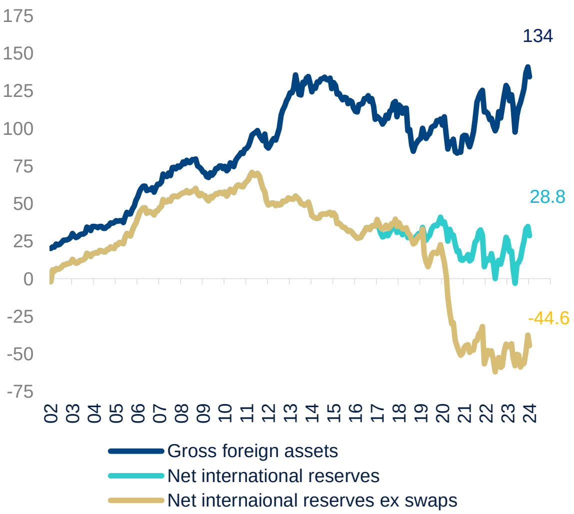
CA DEFICIT FINANCING
US$bn, 12-month cumulative



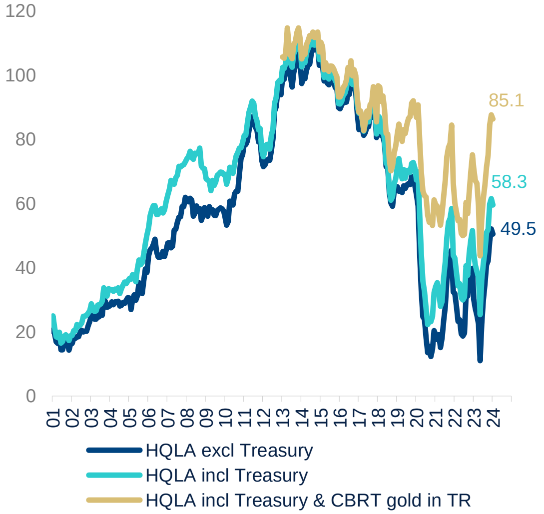
Source: TURKSTAT & Garanti BBVA Research

The CBRT reserves signal a depletion of reserves since December 22, led by weak foreign portfolio inflow and seasonal current account deficit

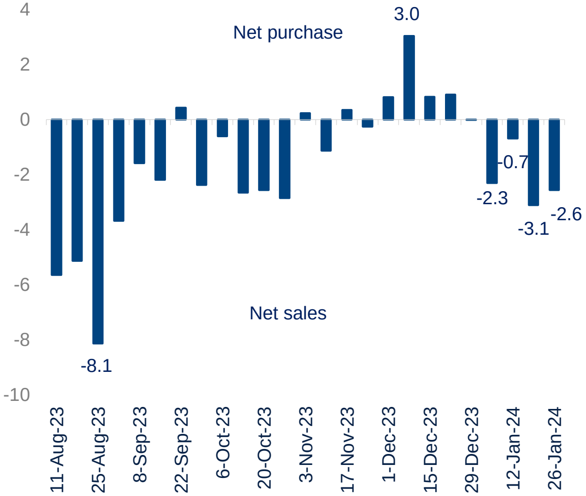
CBRT INTERNATIONAL RESERVES
US$bn as of Jan 31



CBRT HIGH QUALITY LIQUID FOREIGN ASSETS
HQLA, US$BN as of Jan 26



CBRT INDIRECT RESERVES FLOWS
US$BN, weekly flow

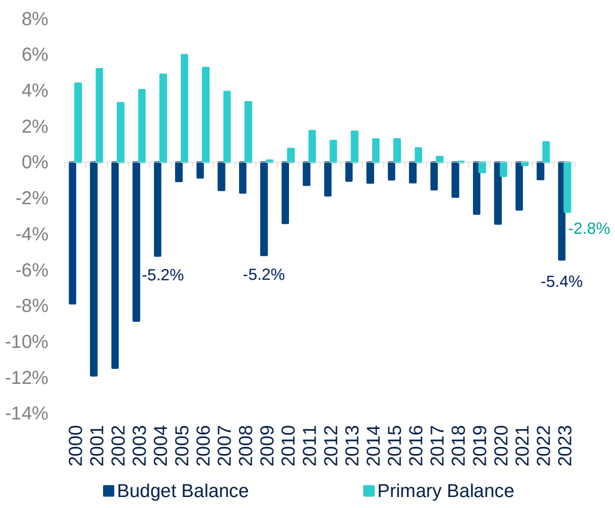


CBRT Balance Sheet US$bn	26.01.2024	29.12.2023	27.10.2023	26.05.2023	31.12.2022	31.12.2021
HQLA = FC assets - Gold - IMF SDR	81.8	85.4	75.2	49.1	75.5	64.8
HQLA - foreign CB swaps - Treasury	49.5	52.1	41.9	11.1	39.8	32.5
HQLA - foreign CB swaps	58.3	61.5	51.7	25.4	51.6	43.8
HQLA - foreign CB swaps + CBRT owned physical gold in TR	85.1	87.6	74.9	43.7	75.2	66.3

Source: CBRT and Garanti BBVA Research

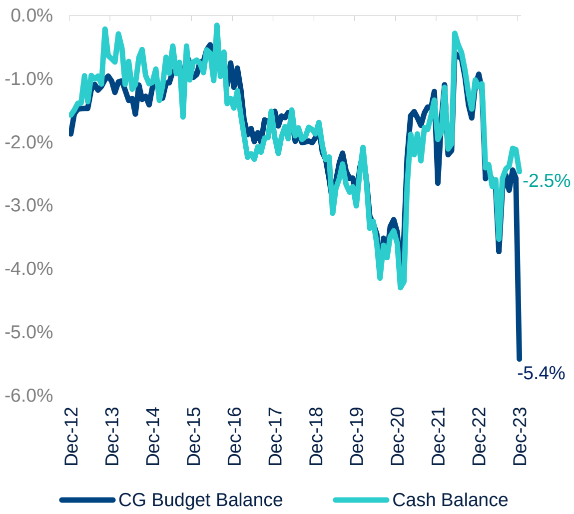
Fiscal spending will be on the radar to check for the rebalancing of the economy and achieving the targeted disinflation pattern

CG BUDGET & PRIMARY BALANCE
% GDP



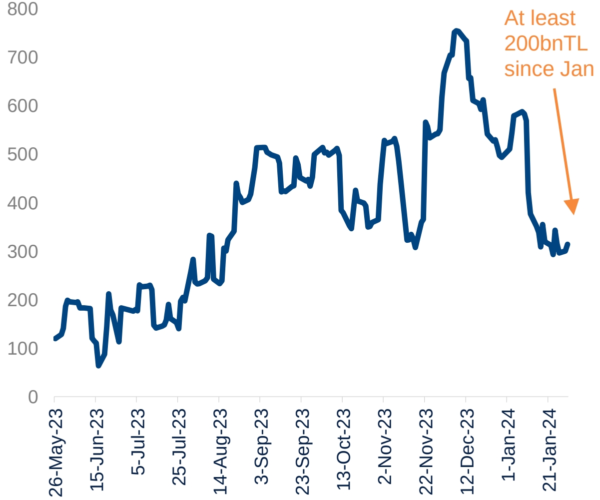
762bn TL earthquake spending forecasted > 950bn TL realized on an accrued basis (3.7% GDP)

CG BUDGET & TREASURY CASH BALANCE
% GDP



At least 700bn TL (3% of GDP) will be spent in the very short term

TREASURY TL DEPOSIT VOLUME AT CBRT
BN TL

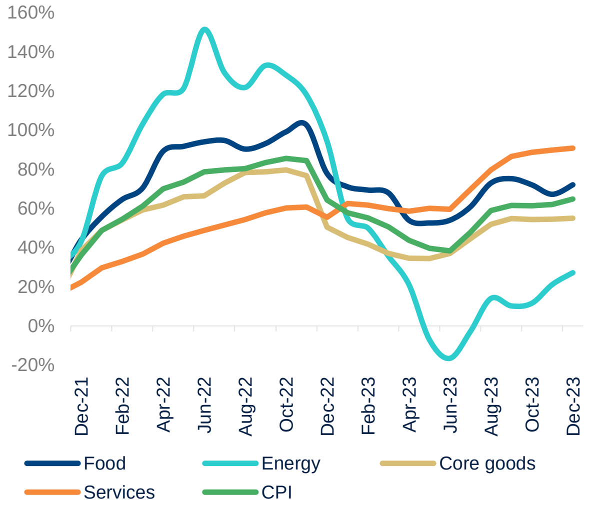


136% domestic debt roll-over target for 2024 will sterilize TL liquidity to some extent

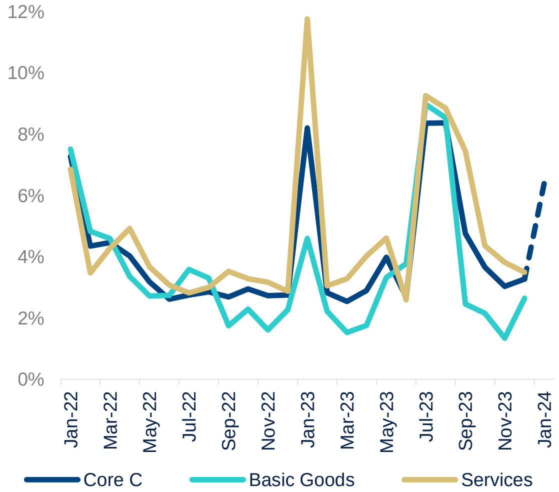
Source: Treasury and Finance Ministry & Garanti BBVA Research

Inflation trend of currently 3-3.5% m/m sa, which will accelerate in the first months of the year

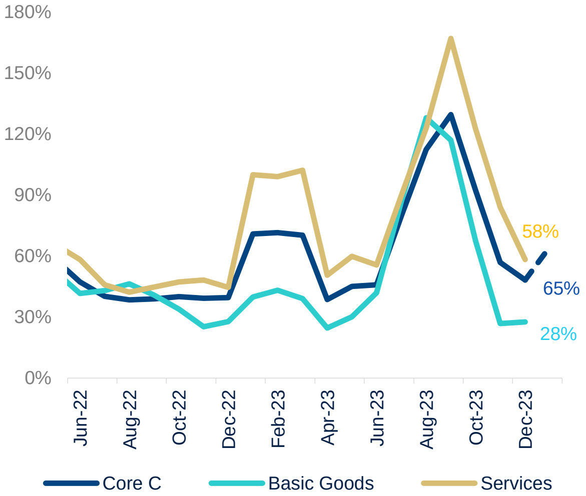
CPI SUBCOMPONENTS
YoY



TREND CPI INDICATORS
SA MoM



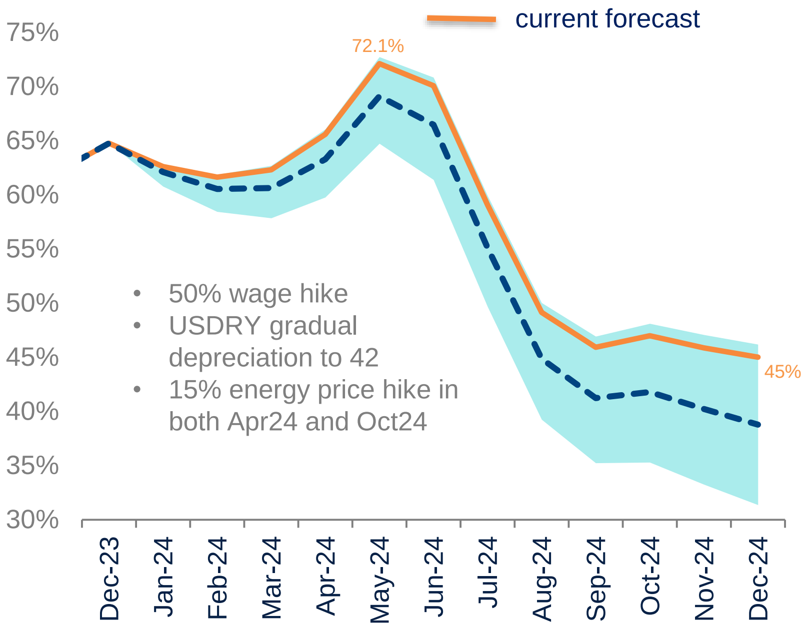
TREND CPI INDICATORS
SA 3M AVG ANNUALIZED



Source: TURKSTAT & Garanti BBVA Research

We remain prudent on our inflation projections and maintain our year-end expectation of 45% with a bias slightly to the downside

CPI FORECASTS
YoY

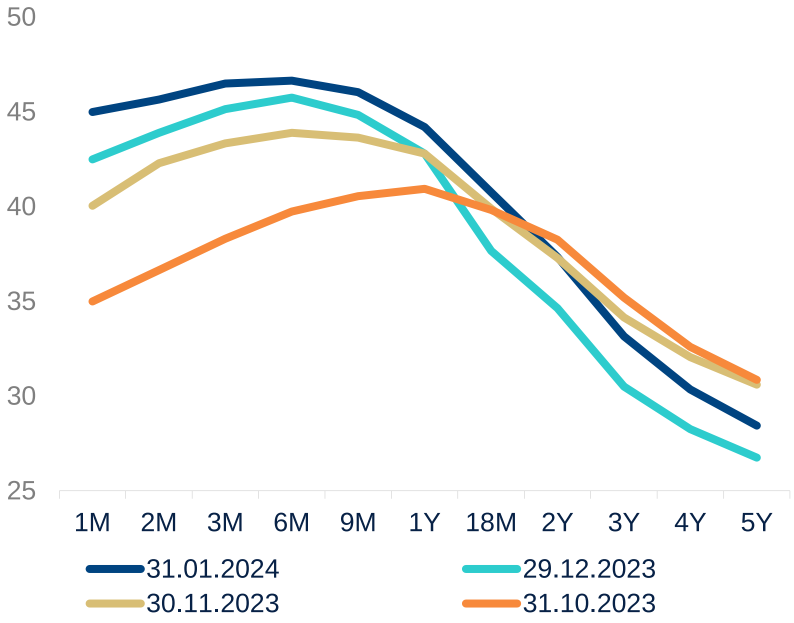


- If adjusted by seasonal factors, we calculate that the decline in the core inflation trend lost pace in December since domestic demand has not adequately slowed down yet to correct the distortions in pricing behavior
- We will watch how the monthly inflation trend will move at the start of the year and try to see whether the trend will start coming down as targeted by the CBRT

Source: TURKSTAT & Garanti BBVA Research

The CBRT stops at 45% policy rate and continues tightening via macroprudential policies and quantitative tools

TRY OIS CURVE
%



Source: TURKSTAT & Garanti BBVA Research

- The CBRT will continue to regulate the credit supply and try to keep the deposit rates as high as needed through macroprudential policies, and also maintain the quantitative tightening by extending sterilization tools at its disposal.

- On the timing to start an easing cycle, the CBRT will wait for a significant decline in the monthly inflation trend toward 1-1.5% (vs. 3-3.5% in Dec23 and most likely 6-6.5% in Jan24) given their 2025 end of the year target of 14%, and also inflation expectations converging to the projected inflation range (30-42% for 2024 and 10-18% for 2025).

- We maintain our call of keeping 45% policy rate throughout the year. If the inflation trend starts to decline much faster in 2H24, we also envisage that the CBRT might start the easing cycle with limited steps toward the end of the year.

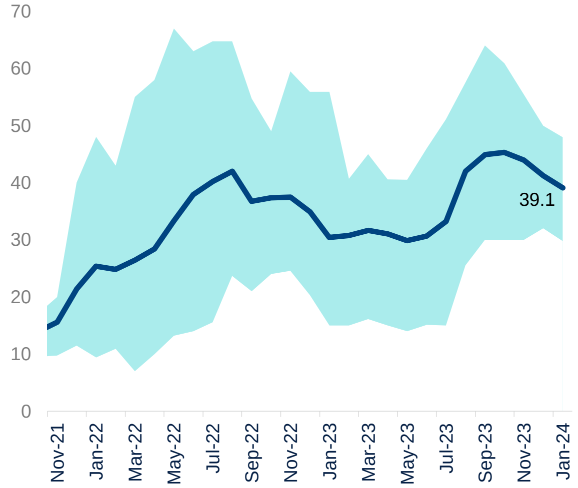
Key points from the 2024 Monetary Policy Document

- The level of monetary tightening required for the sustained price stability will be maintained as long as needed.
- The CBRT will continue to implement quantitative tightening by extending the sterilization tools at its disposal.
- The gradual reduction of securities maintenance for FX liabilities will continue. In tandem with a stronger transition from FC scheme to TL deposits, related regulations will also be simplified.
- The CBRT aims to increase the share of TL deposits to 50% in the banking system (42.7% as of Jan 19) and to sustain the fall in the FC scheme in 2024 through steps prioritizing TL deposits
- The loan composition will be shaped within a framework that is supportive of the disinflation process and macroeconomic balances. Measures may be introduced to mitigate the impact of tighter financial conditions on low income groups during this process.
- The CBRT will continue to conduct swap transactions in 2024 to support the banks' TL and FX liquidity management. A gradual reduction is also planned in swap transactions conducted by the CBRT.
- The CBRT's OMO portfolio size for 2024 was set at nominal TL 200bn (vs. nominal TL 193.5bn as of December 22, 2023), reserving the option to make additional purchases.

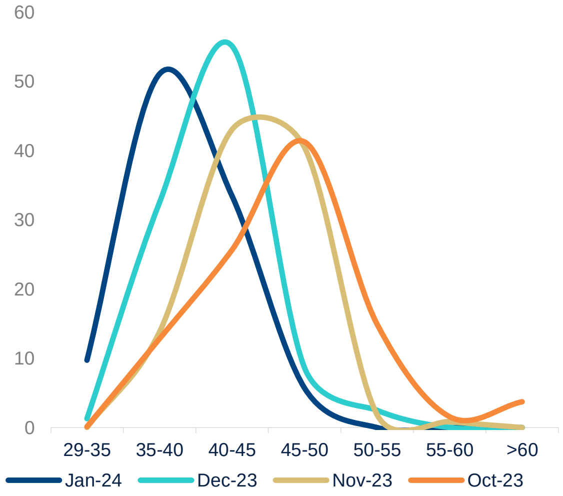
Source: CBRT & Garanti BBVA Research

Survey-based one-year ahead inflation expectations converge towards the CBRT target, whereas 2-year ahead expectations remain divergent

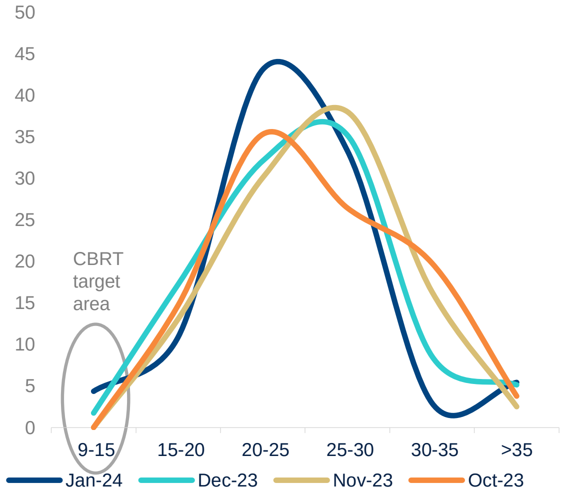
CBRT SURVEY INFLATION EXPECTATION, 12-MONTH AHEAD, %



CBRT SURVEY INFLATION EXP. PROBABILITY DISTRIBUTION, 12-MONTH AHEAD, %



CBRT SURVEY INFLATION EXP. PROBABILITY DISTRIBUTION, 24-MONTH AHEAD, %

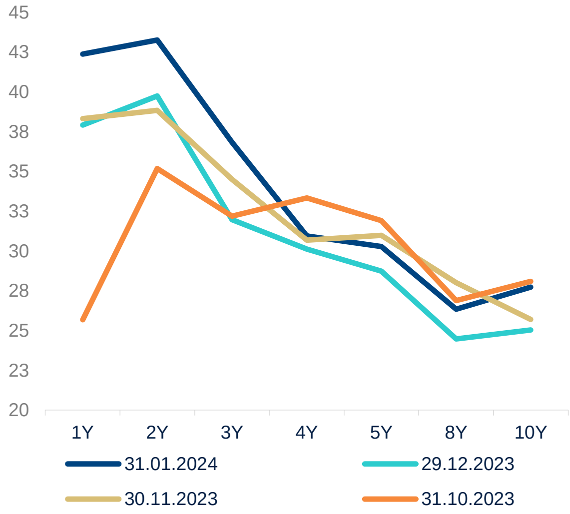


Source: CBRT, Bloomberg and Garanti BBVA Research

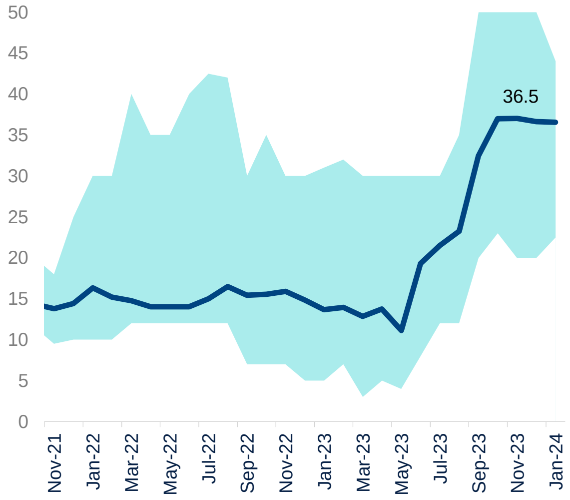
Market implied inflation expectations have started to move upward, following higher than expected minimum wage hike & potential bulk fiscal impulse

MARKET IMPLIED INFLATION EXPECTATIONS, %

TRY SOVEREIGN YIELD CURVE %



CBRT SURVEY POLICY RATE EXPECTATION, 12-MONTH AHEAD, %



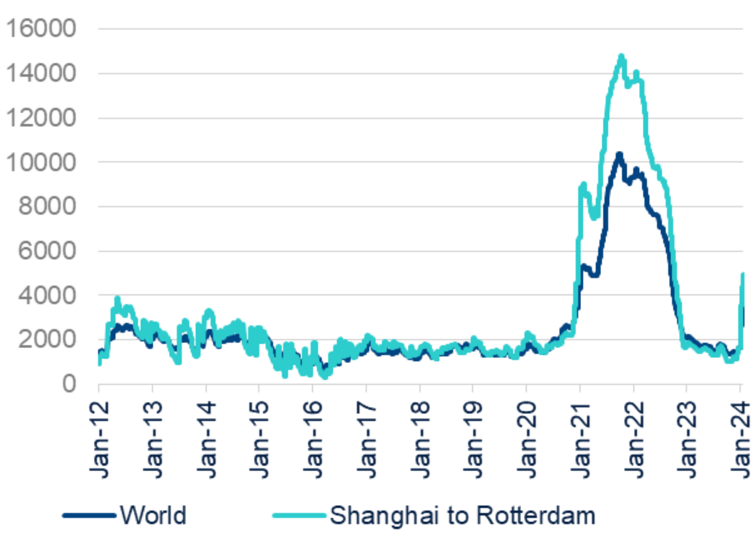
Source: CBRT, Bloomberg and Garanti BBVA Research

Baseline Scenario (Nov23): Brought-forward monetary tightening with steady depreciation

	2022	2023	2024	2025	2026	2027	2028
GDP growth (avg)	5.5%	4.5%	**3.5%**	**3.5%**	**3.8%**	**3.5%**	**3.5%**
Unemployment Rate (avg)	10.5%	9.7%	**10.3%**	**10.8%**	**11.0%**	**11.1%**	**11.2%**
Inflation (avg)	72.3%	53.9%	**55.8%**	**35.8%**	**23.3%**	**17.8%**	**15.6%**
Inflation (eop)	64.3%	64.8%	**45.0%**	**28.0%**	**20.0%**	**16.5%**	**15.0%**
CBRT Cost of Funding (avg)	12.7%	20.3%	**45.0%**	**37.4%**	**25.2%**	**19.7%**	**18.0%**
CBRT Cost of Funding (eop)	9.0%	42.5%	**45.0%**	**30.0%**	**22.0%**	**18.0%**	**18.0%**
USDTRY (avg)	16.56	23.74	**36.07**	**44.98**	**51.56**	**59.06**	**67.65**
USDTRY (eop)	18.70	29.44	**42.00**	**47.50**	**55.00**	**62.50**	**72.00**
Current Account Balance (bn$)	-49.1	-46.6	**-36.4**	**-37.4**	**-45.6**	**-49.8**	**-50.6**
Current Account Balance (% GDP)	-5.4%	-4.4%	**-3.2%**	**-3.0%**	**-3.2%**	**-3.3%**	**-3.2%**
Primary Balance (% GDP)	1.1%	-2.8%	**-2.9%**	**0.2%**	**0.7%**	**0.7%**	**0.7%**
Fiscal Balance (% GDP)	-0.9%	-5.4%	**-6.5%**	**-3.6%**	**-3.1%**	**-3.1%**	**-3.1%**

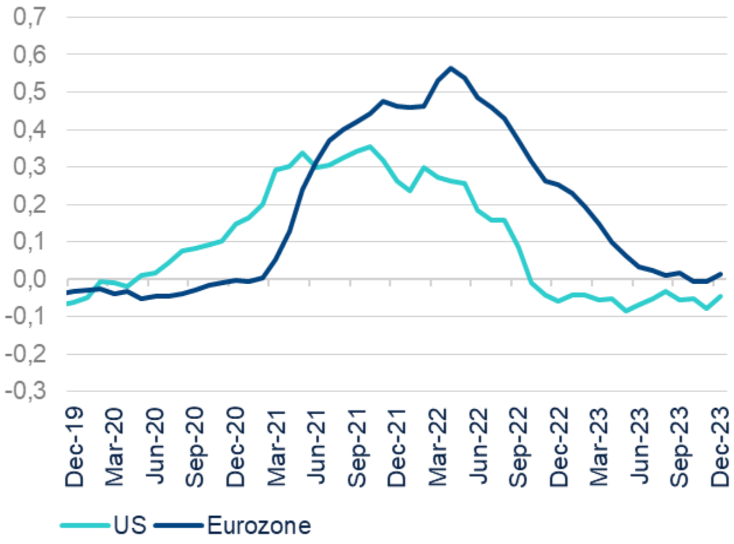
The attacks in the Red Sea have disrupted global supply chains and pushed up freight costs; mild impact on delivery times or materials shortages so far

CONTAINER FREIGHT BY SELECTED TRADE ROUTES
(USD/40 FT BOX, LAST DATA JANUARY 19TH)



Source: DREWRY WORLD CONTAINER INDEX and BBVA Research

BBVA RESEARCH BOTTLENECKS INDICATOR (*)
(INDEX)

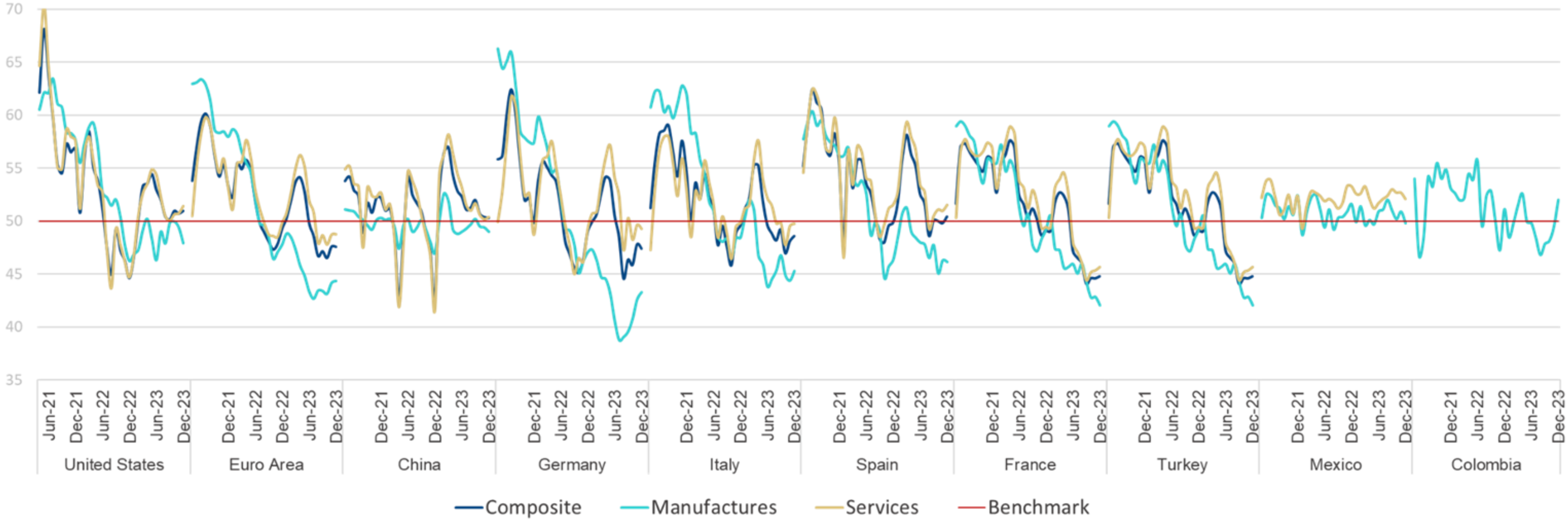


(*) Data mostly until Dec/23.
Source: BBVA Research based on data by Haver Analytics

Source: Haver Analytics and BBVA Research

PMIs remain at low levels within the contraction territory in the EZ. China and the US are around the expansion limit, but both weaker in manufacturing

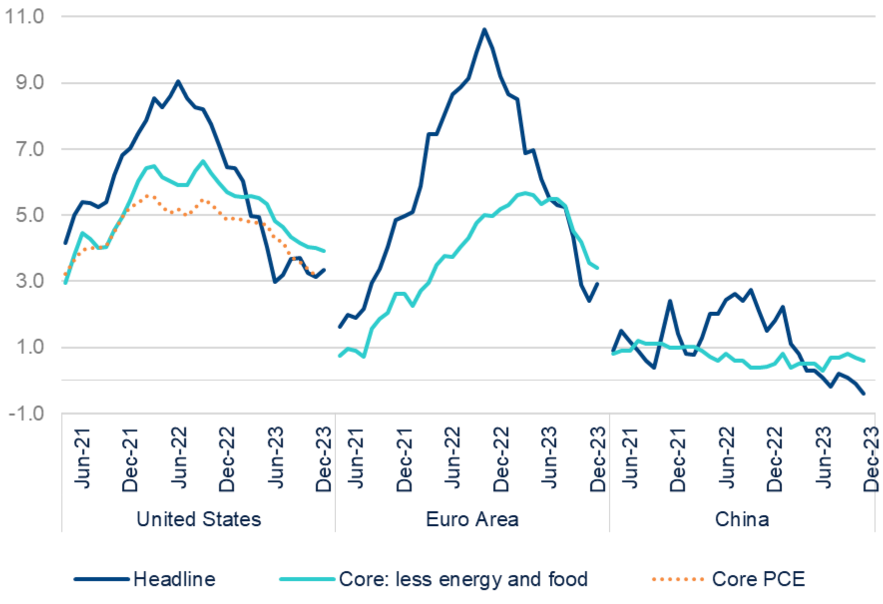
PMI INDICATORS
(HIGHER THAN 50: EXPANSION; LOWER THAN 50: CONTRACTION)



Source: BBVA Research based on data by Haver

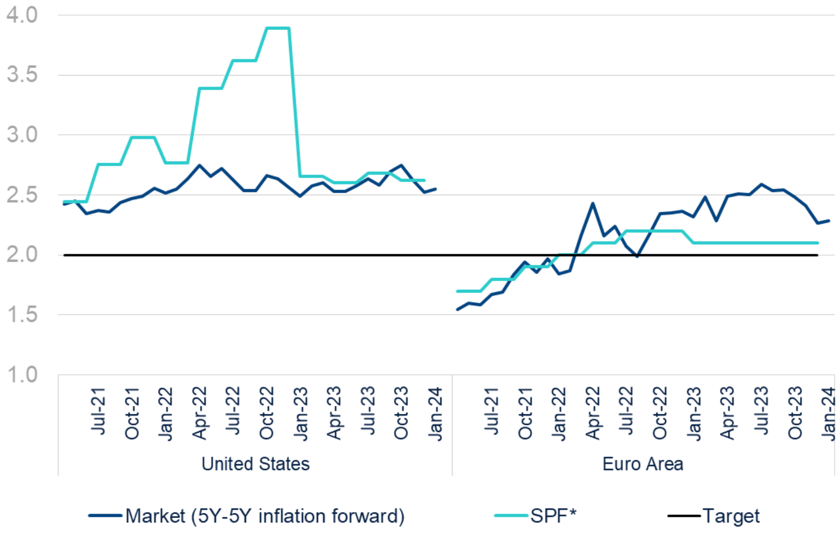
December inflation both in the US and the EZ picked up and core inflation continued to ease, but inflation surprised downwards, especially in the EZ

CORE AND HEADLINE INFLATION
(% YOY)



Source: Haver and BBVA Research

INFLATION EXPECTATIONS
(% YOY)

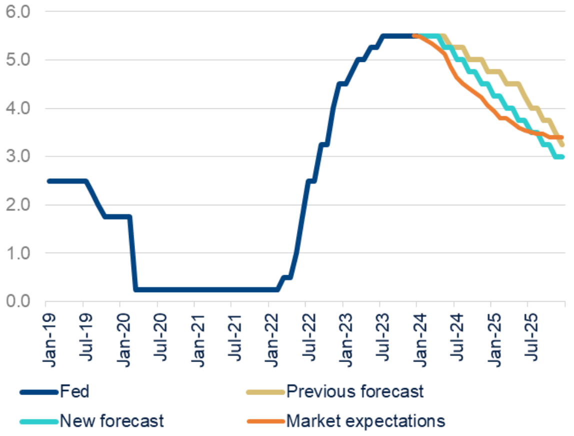


SPF for US: 5-Y annual-average rate of headline CPI inflation, for EA; refers to 2027.
5Y5Y Jan avg. up to 11th of January 2024

Source: SPF: Philadelphia Fed and ECB

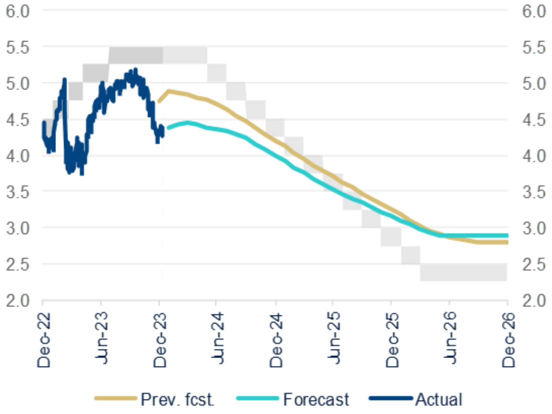
FED: We bring forward the start of the rate-cut cycle to May (four rate cuts in 2024: May, July, Sept, Dec)

FED FUNDS RATE OUTLOOK
(UPPER LIMIT OF THE RANGE, %)



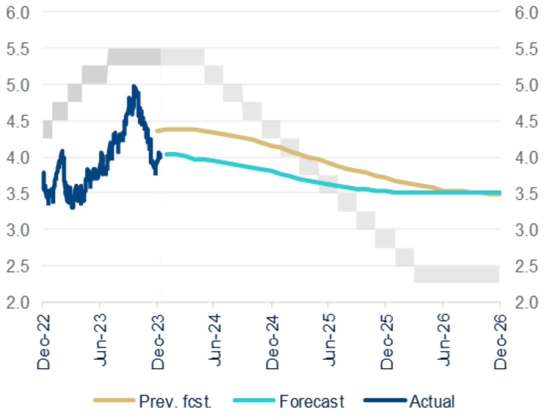
Fed funds rate (upper, eop)	23	24	25	26
New forecast	5.50	**4.50**	**3.00**	**2.50**
Previous forecast	5.50	4.75	3.25	2.50

2-YEAR TREASURY YIELD OUTLOOK
(%)



US 2y Treasury yield (eop)	23	24	25	26
New forecast	4.23	**4.0**	**3.2**	**2.9**
Previous forecast	4.8	4.2	3.3	2.8

10-YEAR TREASURY YIELD OUTLOOK
(%)

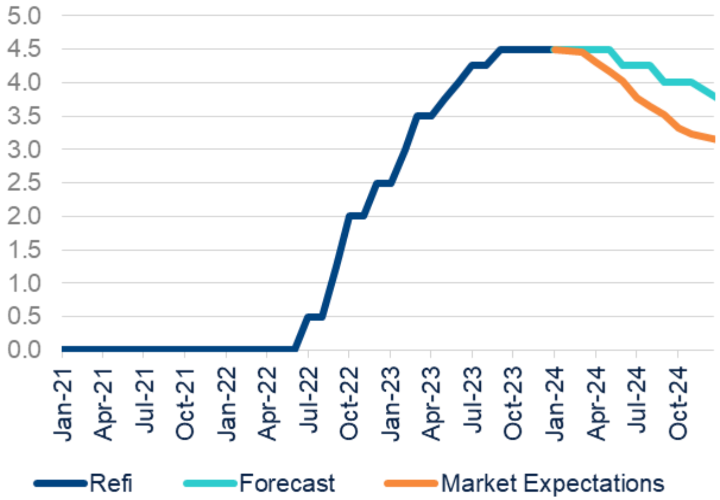


US 10y Treasury yield (eop)	23	24	25	26
New forecast	3.88	**3.8**	**3.5**	**3.5**
Previous forecast	4.4	4.2	3.7	3.5

Source: BBVA Research / Haver

ECB: No changes; we expect three rate cuts this year starting in June. New operational framework to be announced by the spring

ECB: REFI RATE FORECASTS (%)



- The ECB remains data-dependent. ECB sees monetary policy as restrictive enough to bring inflation back to the target. However, they remain concerned about still high core inflation.

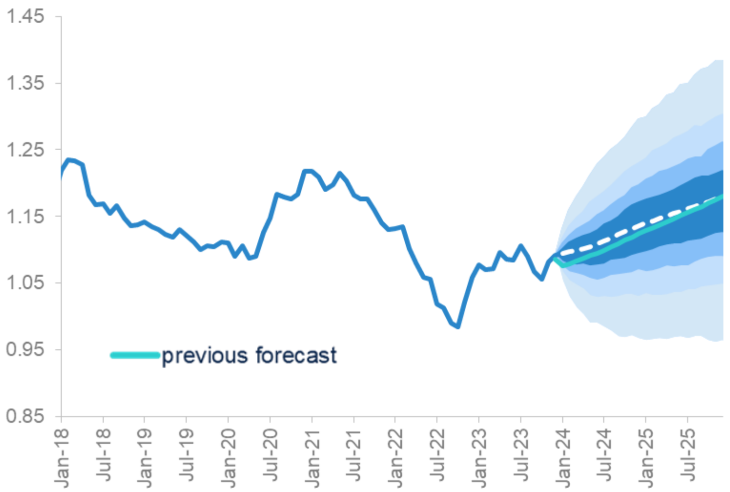
Baseline scenario:

- Rates: 3x25 bp of rate cuts (June, Sept, Dec)
- Gradual QT: PEPP no roll-off in 1H24 and 50% roll-off in 2H24. We estimate a net liquidity drainage impact of c.EUR 45bn in 2024. Reinvestments cease by end of 2024. APP roll-off in 2024 is EUR 345bn.
- New operational framework (to be announced by the Spring): more clues that the ECB is biased to a "demand-driven system"

Source: BBVA Research based on Bloomberg

EURUSD: slight upward revision as it will consolidate in higher levels in 2024

EURUSD PROJECTIONS



	Probability						
	-70%	-50%	-25%	Base	25%	50%	70%
Dec-24	1.03	1.07	1.09	1.14	1.17	1.20	1.23
Dec-25	1.05	1.09	1.12	1.18	1.22	1.26	1.30

- Upward revision of the year-end forecast based on a more favorable rate differential (**1.14 vs. 1.12 by Dec/24**)
- Short and medium term view: EUR undervaluation, narrower spreads and limited volatility should continue backing EUR
- Long-term view: gradual convergent to the equilibrium (1.20)

SHORT-TERM RISKS (WEAKER EURO) > **SHORT-TERM SUPPORT TO THE EURO**

- Geopolitics (Israel conflict)
- Reversal of speculative positions (now at high levels)
- Slow EZ and global growth

- EUR may appreciate if markets reassess aggressive rate cuts in ‘24 toward a softer rate-cut cycle

Source: BBVA Research

Disclaimer

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Türkiye Economic Outlook

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Creating Opportunities