Activity Pulse

Türkiye | Risks become tilted to downside on activity

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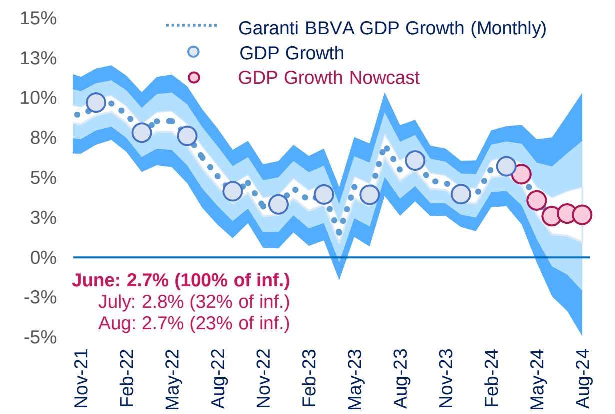
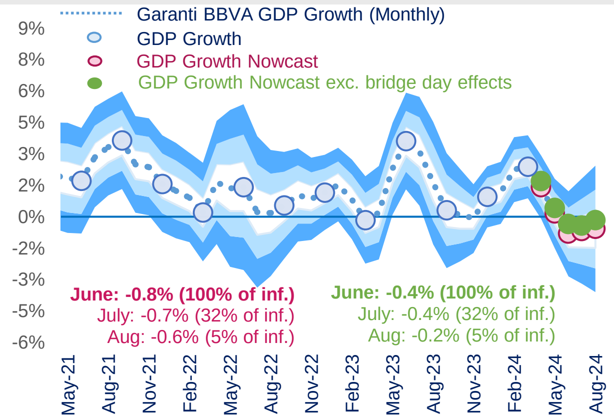
- Following the hard data realizations of June, we now assess that the bridge day effects (additional holiday days due to extended religious holidays) do matter much higher than we had previously expected on economic activity. Consequently, our monthly GDP indicators nowcast a quarterly contraction of 0.8% in 2Q which slightly improves to -0.6% in 3Q as of early August. Yet, if we exclude bridge day effects in a counterfactual analysis to understand the underlying trend, the quarterly contraction would be more modest at around 0.4% and it does not change much so far in 3Q in the absence of any hard data. Overall, the lagged effects of the monetary tightening have started to be seen more clearly but its magnitude is still not clear, given the high uncertainty due to the bridge day effects and also the adjustment after the strong quarterly growth rate of 2.4% recorded in 1Q.
- Despite the uncertainties, we observe a stronger deceleration in aggregate demand in late 2Q and expect restrictive monetary stance and tighter financial conditions to enable a deeper correction in 3Q. The positive output gap has diminished further, which will turn into negative in 3Q and reduce inflationary pressures soon.

Figure 1. **Garanti BBVA Monthly GDP Nowcast*** (3-month average YoY)



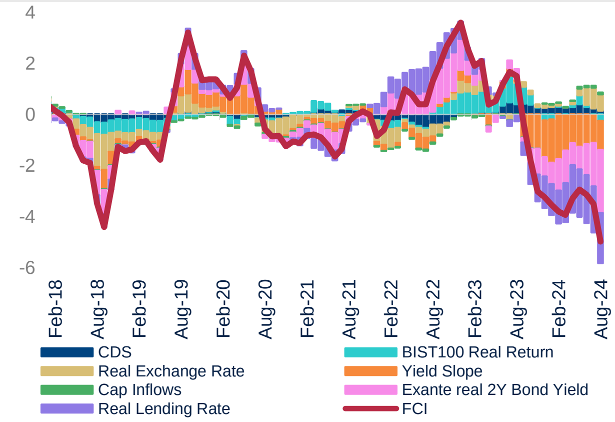
Source: Garanti BBVA Research, GBTRGDPY Index in BBG
*An average of different model results synthesizing high-frequency indicators to proxy monthly GDP

Figure 2. **Garanti BBVA Monthly GDP Nowcast** (3-month average QoQ)



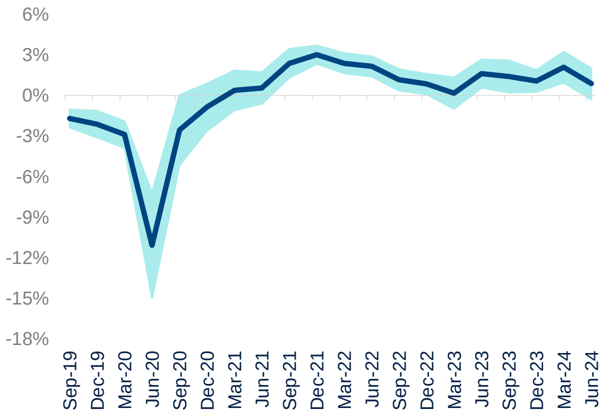
Source: TURKSTAT, Garanti BBVA Research

Figure 3. **Garanti BBVA Financial Conditions Index** (standardized, + easing, - tightening)



Source: CBRT, Bloomberg, Garanti BBVA Research

Figure 4. **Garanti BBVA Output Gap Estimation** (% deviation from Potential GDP)

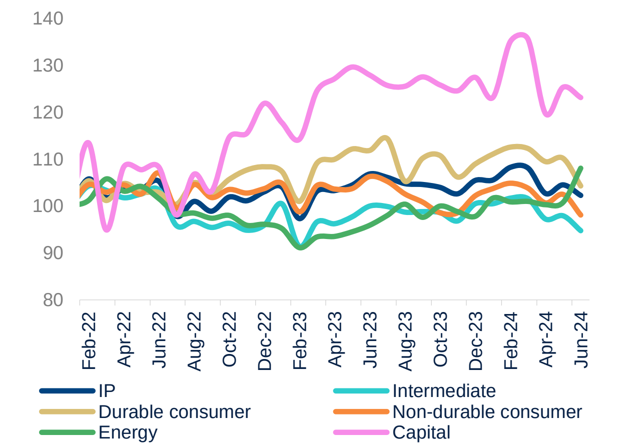


Source: TURKSTAT, Garanti BBVA Research, Output Gap with %95 Confidence Band

- We now evaluate that the risks start to be slightly to the downside on our 2024 growth forecast of 3.5%. The magnitude of the expected fiscal consolidation and the duration of tight monetary stance will be decisive on growth outlook. The CBRT's projections on output gap indicate a GDP growth of around 1.5% for 2025, following nearly 3% GDP growth in 2024. In this respect, the new Medium Term Program (MTP), to be released in early September, has gained even more importance to understand the political will on the pace of adjustment in the economy because 2025 GDP growth forecast was forecasted as 4.5% in the last MTP.

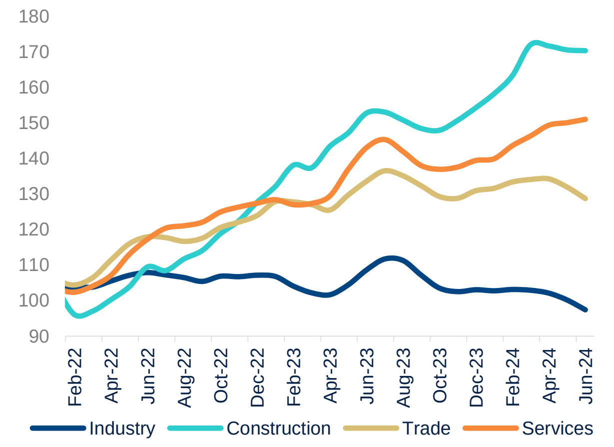
- On the supply side, industrial production (IP) declined by 2.1% m/m in June, largely due to the negative impact of the bridge effects. Together with bridge days in April, 2Q growth performance was lackluster, posting 3.9% q/q decline. However, if the negative calendar day impact (5 days less working days in 2Q) is excluded, the overall contraction in industry is much lower since the impact of each bridge day might be around 0.8pp to 1pp. Taking this impact into account, sub-sectoral details reveal a broad-based worsening across all sectors on quarterly terms in 2Q except for energy.
- Overall turnover index (industry, construction, trade and services) fell by 3.2% q/q in 2Q (vs +2.6% q/q in 1Q) especially on the back of industry and trade sectors (Figure 6). Industry turnover continued to confirm the worsening in activity, declining by 5.4% q/q in 2Q. Despite the recovery in trade volume index in June by 1% m/m, supported by all subcategories, trade sales contracted sharply by 3.6% in 2Q after the expansion of 3% in 1Q24. On the other hand, services sector could prevent further deceleration in activity in 2Q based on our calculation, since the services turnover deflated by services deflator (Figure 7) increased by 2.05% q/q (vs 3.6%).

Figure 5. **Industrial Production Index** (seasonal and cal. adj., Jan22=100)



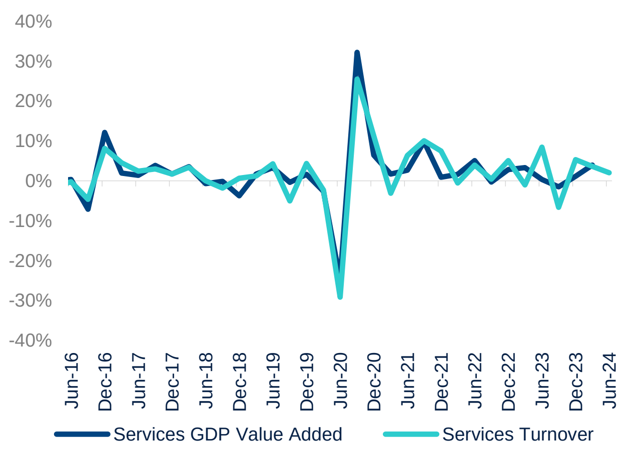
Source: TURKSTAT, Garanti BBVA Research

Figure 6. **Sectorial Turnover Indices** (real, 3MA, seasonal and cal. adj., Jan22=100)



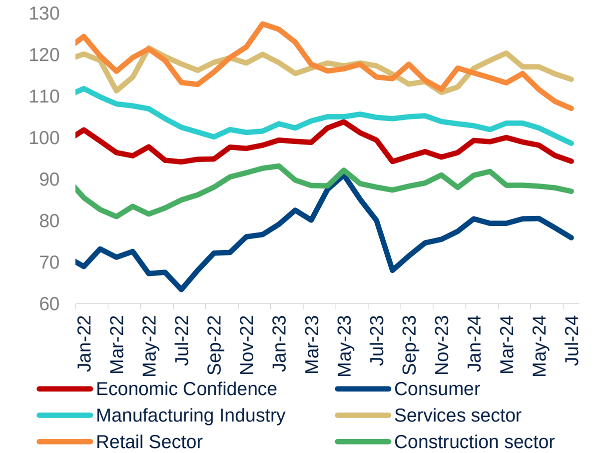
Source: TURKSTAT, Garanti BBVA Research

Figure 7. **Services GDP Value Added vs Services Turnover** (%, QoQ, seasonal and cal. adj.)



Source: TURKSTAT, Garanti BBVA Research

Figure 8. **Economic Confidence Index** (seasonal and cal. adj.)

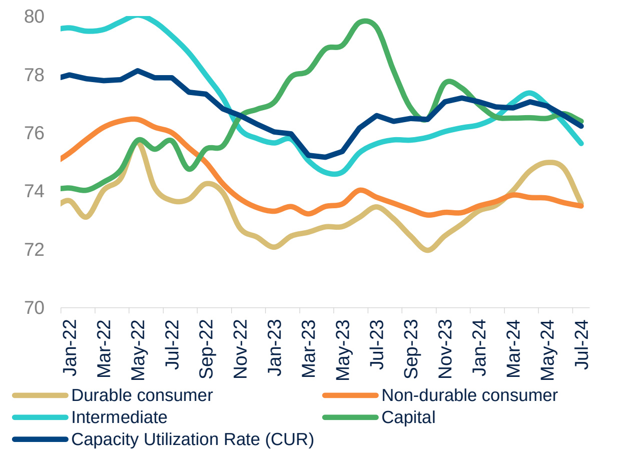


Source: TURKSTAT, Garanti BBVA Research

- Leading indicators such as manufacturing capacity utilization rate together with confidence indices and economic tendency surveys signal further deterioration in activity in 3Q.
- Economic confidence continued to deteriorate in July with 1.5% m/m decline while there was also a broad-based worsening of sectoral confidence as well, the largest loss being recorded in manufacturing (Figure 8).

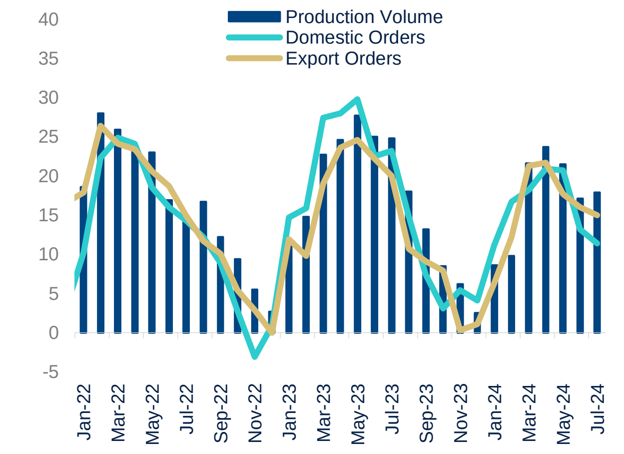
- Manufacturing capacity utilization declined for the fourth time in a row in July with 0.3pp m/m, primarily led by the declining capacity in durable consumption goods and intermediate goods (Figure 9). Manufacturing PMI showed a steep decline in July with 47.2 (47.9 in June and 48.5 in 2Q24 vs. 49.8 in 1Q24), while all sectors were below the threshold of 50, with electronic & electrical equipment sector recording the lowest level of production across all sectors. Despite the further deterioration signal, industrial production may recover in July on monthly basis stemming from the reversing impact of bridge days in 3Q.
- The economic tendency survey (Figure 10) signals very limited improvement in the production volumes of companies in the next 3 months, mainly due to the return to business-as-usual after religious holidays. On the other hand, both domestic and export orders in the next 3 months continued to decrease, indicating a much challenging demand outlook in 3Q. In line with these expectations, the intermediate goods imports excluding gold imports (Figure 11) inched downward in July along with intermediate and capital goods.
- The lagged impact of the ongoing deterioration in activity has started to be observed on employment since seasonally adjusted unemployment rate inched upward to 9.2% in June (we note that the calendar day effects still do matter), while the total underutilization rate, also described as broad-based unemployment, jumped to 29.2%, the highest level since May20 where the pandemic had hit the employment hard (Figure 12).

Figure 9. **Manufacturing Capacity Utilization Rate** (%, seasonal and cal. adj., 3MA)



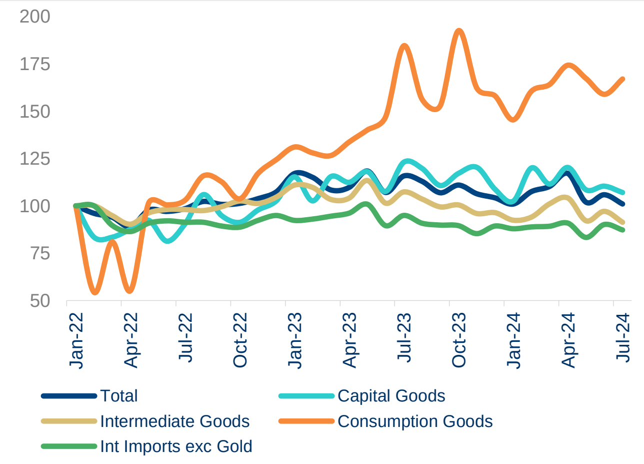
Source: CBRT, Garanti BBVA Research

Figure 10. **Production Volume, Domestic Orders and Export Orders in the Next Three Months** (Balance)



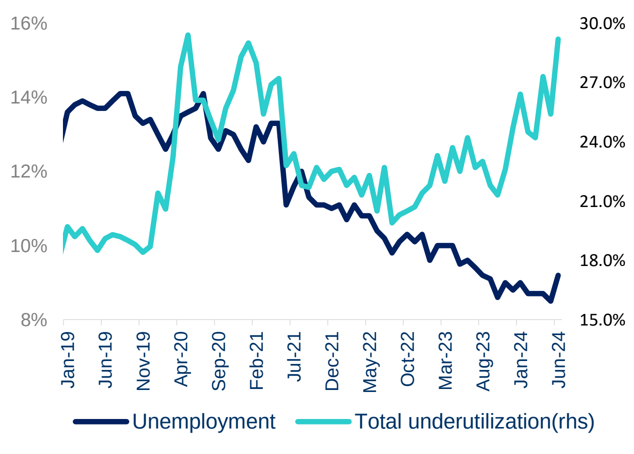
Source: TURKSTAT, Garanti BBVA Research

Figure 11. **Import Sub-Components Volume Index** (2022 Jan=100, seasonal and cal. adj.)



Source: TURKSTAT, Garanti BBVA Research

Figure 12. **Unemployment Rate** (%, seasonal adjusted)

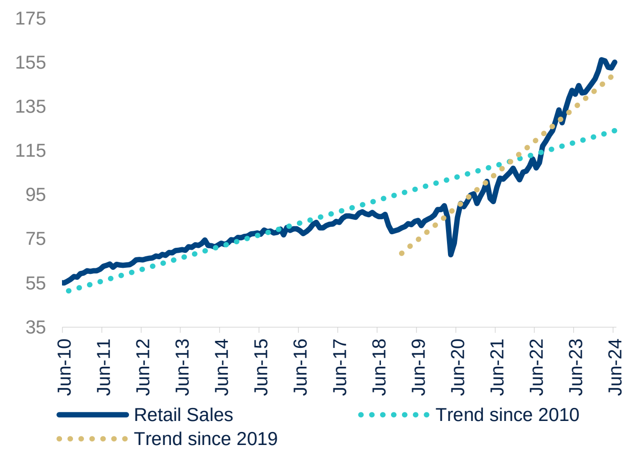


Source: TURKSTAT, Garanti BBVA Research

- Despite the recent mixed signals, the underlying trend on demand indicators displays an ongoing correction, which we expect to deepen further in 3Q considering tighter financial conditions.

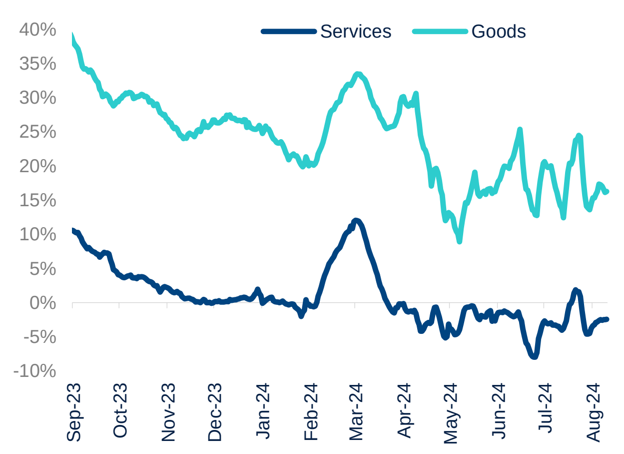
- Retail sales increased by 1.7% m/m in June, underpinned by all subcategories, though contracting by 0.5% in 2Q (prev. 6% q/q). Despite the narrowing gap in 2Q, it remains above its trend (Figure 13). Consumption goods imports rose by 2.9% m/m in July based on our calculation, after contracting in the last 2 months. Still, its 3 month moving average materialized as -1.2% q/q (vs 6.5% q/q in June). On the other hand, our big data indicators on consumption signal some stabilization in 3Q after the faster adjustment in 2Q (Figure 14).
- Capital goods production and capital goods imports also signal that the investment could be weaker in 2Q while trade data and services revenues confirm the decline in the positive contribution of net exports to aggregate demand.
- After the sharp increase in 1Q, recent hard data points out that the moderation in aggregate demand, supported by all demand components, could be stronger than our previous expectations.

Figure 13. **Retail Sales Volume Index** (level , seasonal and calendar adj.)



Source: TURKSTAT, Garanti BBVA Research

Figure 14. **Garanti BBVA Big Data Consumption Indicators** (28-day sum, YoY, adjusted by CPI)



Source: TURKSTAT, Garanti BBVA Research

BOTTOM LINE: Recent hard data demonstrates that the slow-down in economic activity has been faster than our previous expectations, but the uncertainty remains high due to the bridge day effects (2Q GDP data to be released on September 2). If the negative impact of the extended religious holidays on economic activity is excluded, the contraction in industrial production is more modest than the released data. However, leading indicators point to a continued correction in economic activity in 3Q. Tighter financial conditions and the restrictive monetary policy could sustain the rebalancing. The adverse effects of the economic slowdown on unemployment began to be observed as of June, and the unemployment rate may increase somewhat in the near future. To sum up, we assess that the risks to our 3.5% growth forecast for 2024 start to be to the downside. The magnitude of the expected fiscal consolidation and the duration of tight monetary stance will be decisive on growth outlook. We will closely monitor the upcoming MTP, which could be released in early September, to get more information on the fiscal policy and revise our growth forecasts accordingly.

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