BBVA Research

Türkiye Economic Outlook

Garanti BBVA Research

July 2024

Creating Opportunities

Key Messages

- US activity cools further and inflation moderates. EZ headline inflation moderated in June but core inflation remained stable with sticky services prices. The Fed left rates unchanged with a dovish hint and signaled future cuts, while the ECB cut rates by 25bps, emphasizing data dependency.

- On Türkiye, we maintain our expectation of a soft landing (3.5% GDP growth forecast in 2024 & 2025). The targeted rebalancing in the economy has been slowly taking place due to the counter effects over the monetary transmission mechanism and still supportive fiscal stance.

- The Government aims to keep the budget deficit to GDP ratio below 5% in 2024 and 3% in 2025. Inadequate savings in the short run lead the Ministry to find new revenue sources as presented in the draft bill.

- We forecast consumer inflation to come down to 47-48% by Sep on strong favorable base effects and finish the year at 43% (with 38 USDTRY by year end).

- If an effective policy mix lacks in fight against inflation, the CBRT would remain restrictive longer than we expect in our baseline. This is why we have an upward bias on our CBRT funding rate forecasts, which would have a downward impact on our GDP forecasts for 2025.

- The pace of reserves accumulation has lost momentum compared to early May due to mostly weakening foreigner capital inflow, which reduces the need to sterilize TL liquidity in the market.

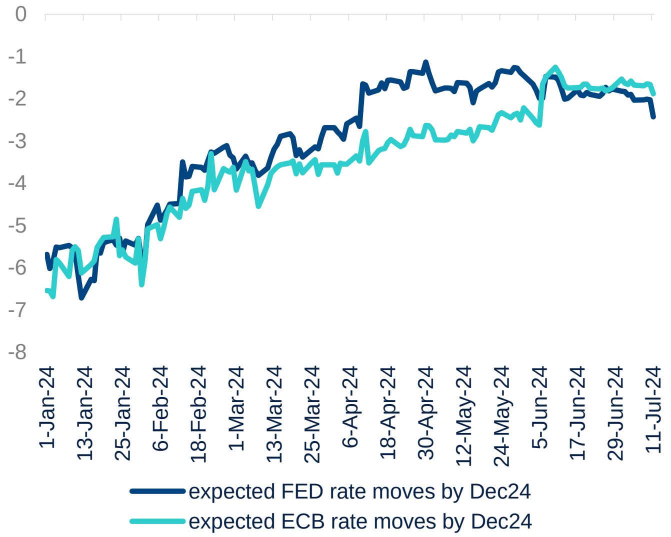
Research

01

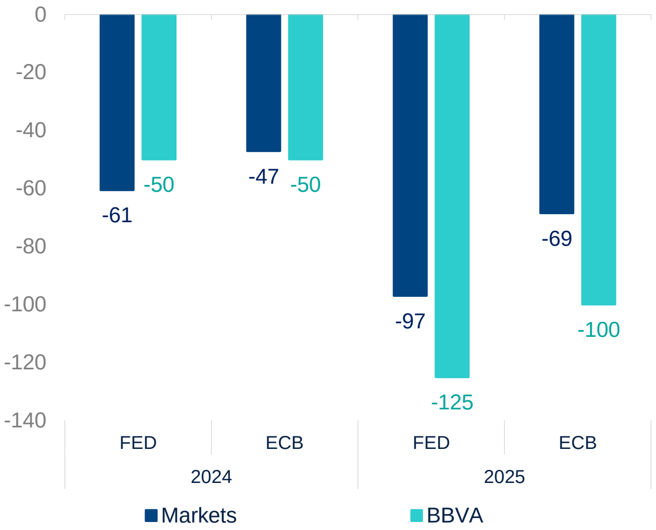
Global Economic Outlook

Markets' implied yields fully price in two 25bp Fed interest cuts in 2024. On ECB, implied yields price in one additional cut in 2024 and 60% odds for an additional one

NUMBER OF FED'S AND ECB'S INTEREST RATE CUT (x25bps) IN 2024 (NUMBER)



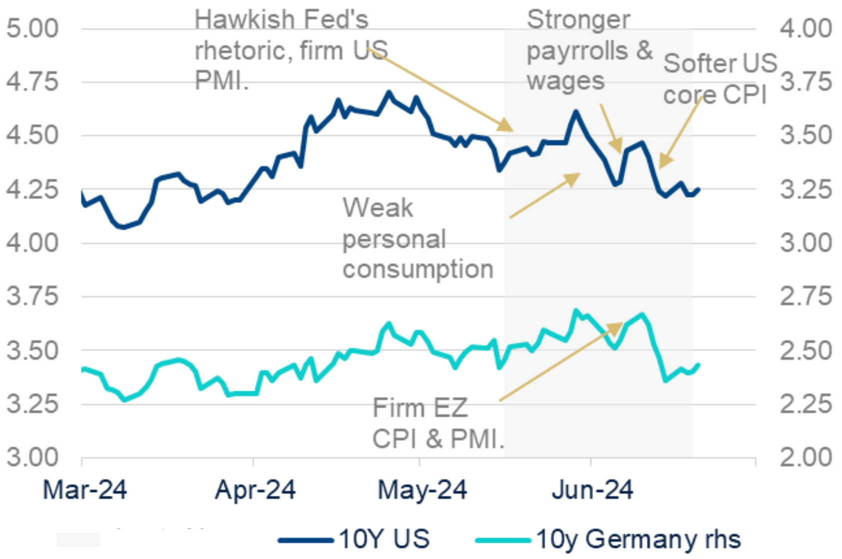
TOTAL IMPLIED INTEREST RATE CUT IN FED AND ECB INTEREST RATES IN 2024 (BPS; LAST DAY JULY 11)



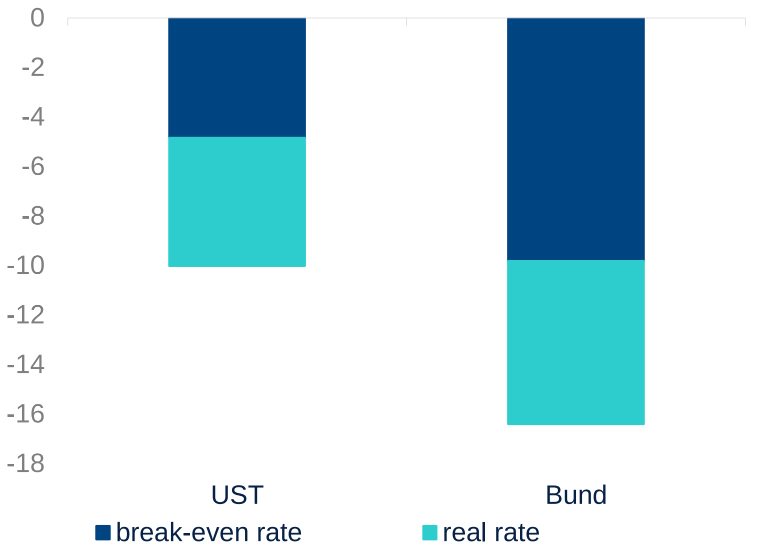
Source: Bloomberg and BBVA Research

Sovereign yields were volatile but recently slid back on softer US core CPI and safe haven flows underpinned by the French turmoil

US AND GERMANY 10Y SOVEREIGN YIELD
(%)



US AND GERMANY 10Y YIELDS DECOMPOSITION
(bps change in June)

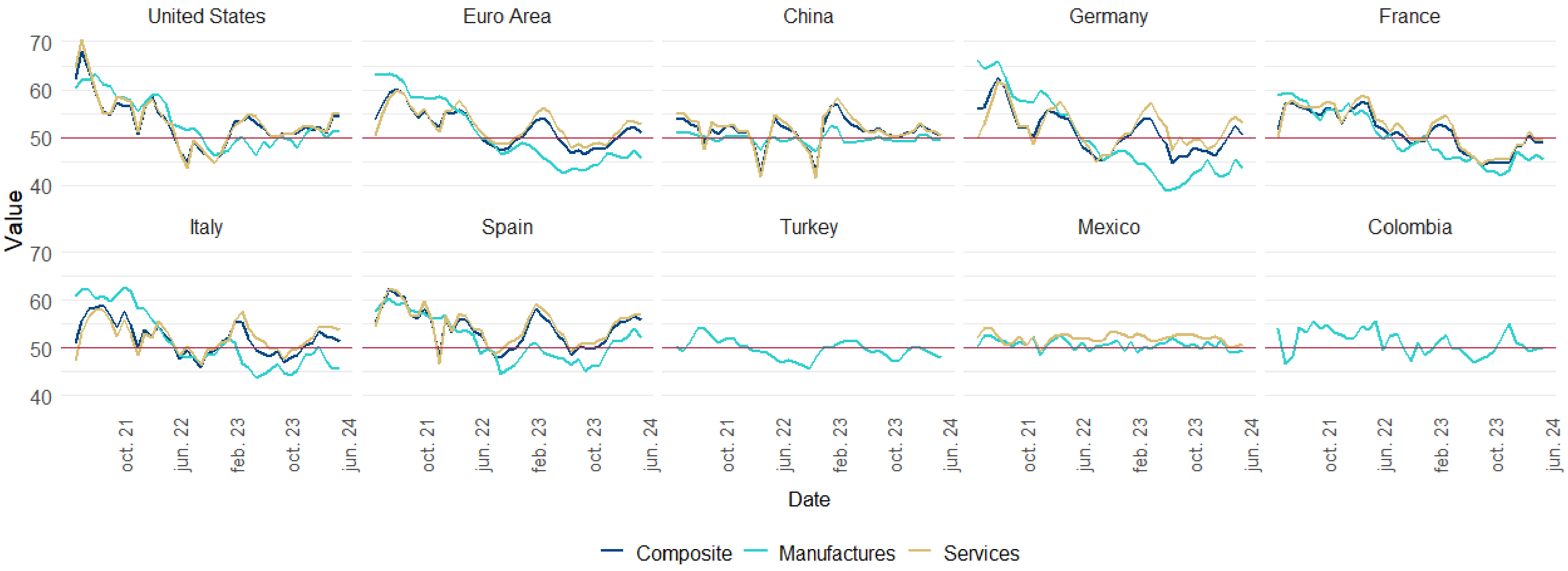


Source: Bloomberg and BBVA Research

Activity: US PMIs stabilized; EZ worsened with manufacturing surprising to the downside; China's remain near 50

PMI INDICATORS

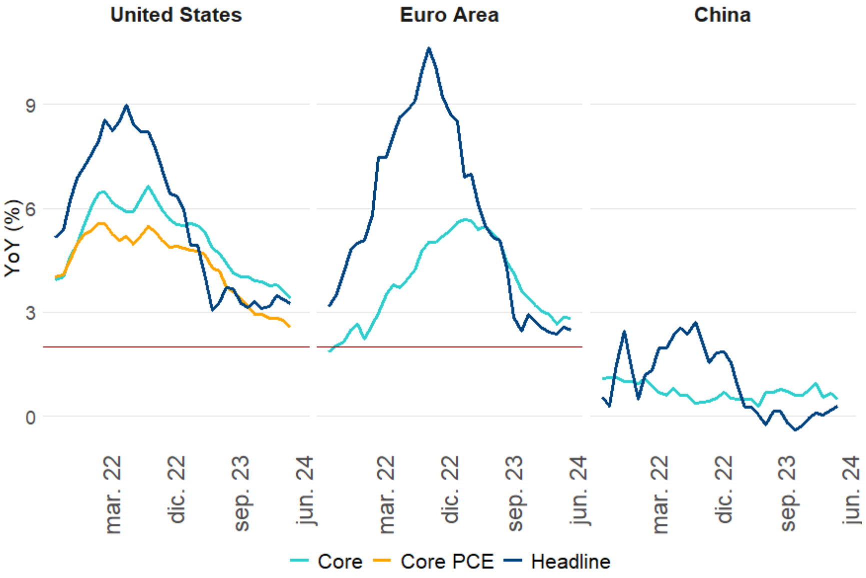
(HIGHER THAN 50: EXPANSION; LOWER THAN 50: CONTRACTION)



Source: BBVA Research based on data by Haver

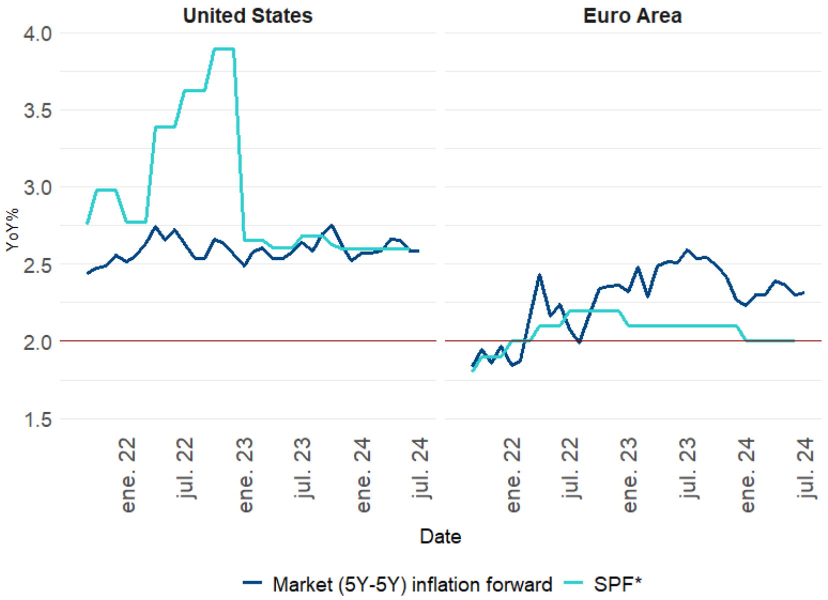
Inflation: US June data showed a clearer moderation; in the EZ, inflation slowed slightly in June in line with expectations. Services inflation remains sticky

CORE AND HEADLINE INFLATION
(% YOY)



Source: Haver and BBVA Research

INFLATION EXPECTATIONS
(% YOY)

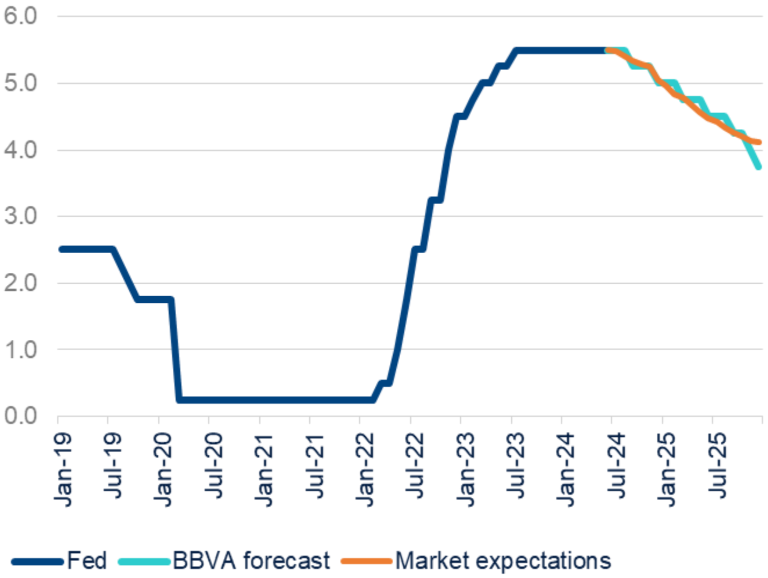


SPF for US: 5-Y annual-average rate of headline CPI inflation, for EA; refers to 2028.
5Y5Y Last data as 9th of July 2024

Source: SPF: Philadelphia Fed and ECB

Fed: We continue to expect the start of the easing cycle in September with two rate cuts this year. The slowdown in QT has begun in June

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



Source: BBVA Research based on Bloomberg

FOMC June meeting: The Fed held the policy rate unchanged at 5.25-5.50% and offered a slight dovish wink following the better-than-expected core CPI print in May.

- Broadly unchanged projections for GDP growth and the UR point to the continued confidence in a scenario in which the economy grows around potential in 2024-26
- The Fed signaled just one rate cut this year as priced in by financial markets. Powell said that either one or two rate cuts were a “plausible” outcome

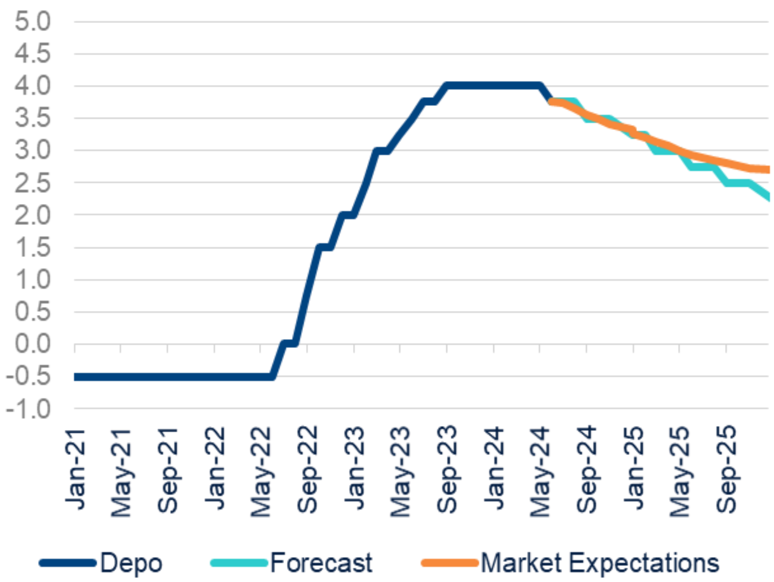
Baseline scenario (no changes)

We expect the first rate cut in Sep. and another cut in Dec. to take it down to 5.00% by year-end and 3.75% by end ‘25.

- QT: The reduction of the monthly pace of Treasuries runoff to a $25bn cap (vs $60bn) has begun this month

EZ: The ECB delivered a hawkish cut. We continue to expect two more cuts this year, with a bias toward just one more

ECB: DEPO RATE FORECASTS (%)



Source: BBVA Research based on Bloomberg

June meeting:

- The ECB delivered a well-advertised 25bp rate cut. Lagarde repeatedly stressed that they remain data-dependent, with no commitment to further steps.
- Growth and inflation forecasts were revised upwards, reflecting data surprises, making the move a "hawkish cut"; the medium term outlook remains broadly unchanged.

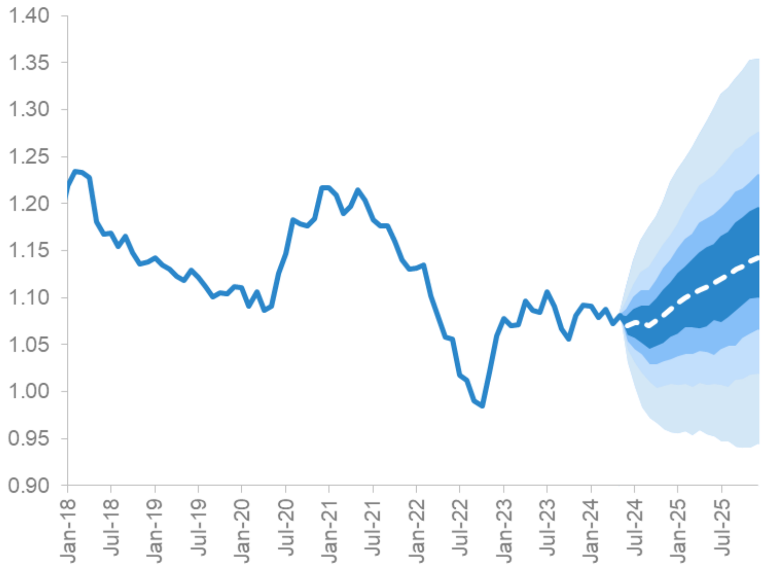
Most ECB officials have said that the June rate cut was appropriate, but they urge caution on subsequent action

Baseline scenario (NO CHANGES):

- Rates: 2x25 bps of rate cuts in 2024 if there are no major surprises in inflation outlook during the rest of the year. Additional four rate cuts in 2025. Bias to less cuts.
- Gradual QT: for APP to continue, and for PEPP to start the 50% roll-off in 2H24, with reinvestment until Dec/24.

EURUSD: No changes in forecasts. The risk continues to be tilted to a weaker Euro

EURUSD: PROJECTION



	Probability						
	-70%	-50%	-25%	Base	25%	50%	70%
Dec-24	1.01	1.03	1.06	1.09	1.12	1.14	1.17
Dec-25	1.02	1.07	1.10	1.14	1.20	1.23	1.28

Source: BBVA Research and Bloomberg

- The euro continues to face important risks ahead:
  - ✓ European political uncertainty
  - ✓ US elections (dollar positive initially if Trump wins)
  - ✓ bias of Fed rate cut cycle even more gradual than expected
  - ✓ slower EZ and global growth
  - ✓ geopolitics (the EZ and the US stand at the opposite ends of energy independence)

- Our medium-term baseline scenario continues to support a very gradual appreciation: narrowing rate spreads, contained volatility, EUR's undervaluation (current estimation of equilibrium around 1.20)

BBVA Research baseline scenario: inflation and interest rates are likely to decline, but will remain relatively high, favoring subdued activity growth

Scenario drivers

Interest rates will gradually fall, also in the US, where cuts were postponed amid large uncertainty, but will remain at contractionary levels

Fiscal policy will scarcely contribute to ease inflation pressures, mainly in the US; some consolidation is likely in Europe from 2025, given new fiscal rules

Supply conditions: geopolitical context makes negative shocks more likely than in the past, but no particular shock is assumed in baseline scenario

Macro trends: prospects

Global growth to be weak in 2H24 and recover somewhat in 2025; China's structural deceleration will weigh down

Inflation will ease further, but is set to remain higher than in recent decades on demand (fiscal policy, etc.) and supply (geopolitics, protectionism, etc.) issues

Volatility on geopolitics and US elections, likely offsetting the positive effects triggered by lower Fed rates

Interest rates and FX forecasts

Interest rates: Official interest rates (%)

	2022		2023		2024		2025	
	eop	average	eop	average	eop	average	eop	average
US	4.50	2.02	5.50	5.23	5.00	5.40	3.75	4.50
EMU	2.00	0.23	4.00	3.40	3.25	3.75	2.25	2.79
Mexico	10.50	7.88	11.25	11.17	10.50	10.94	8.50	9.50
Argentina	75.00	58.71	100.00	101.00	30.00	51.42	24.00	26.63
Colombia	12.00	7.88	13.00	13.13	8.50	10.92	6.00	6.60
Peru	7.50	5.54	6.75	7.54	5.00	5.69	4.50	4.65
Türkiye (One-Week Repo)	9.00	12.63	42.50	20.67	45.00	48.54	30.00	37.42
Türkiye (Avg. Funding Rate)	9.04	12.66	42.50	20.46	45.00	48.75	30.00	37.42

*EMU: Depo rate

Long-term interest rates: 10 yr rates (%)

	2022		2023		2024		2025	
	eop	average	eop	average	eop	average	eop	average
US	3.62	2.94	4.01	3.95	4.37	4.37	4.07	4.21
EMU	2.13	1.19	2.11	2.46	2.30	2.38	2.20	2.25

Exchange rates (vs USD)

	2022		2023		2024		2025	
	eop	average	eop	average	eop	average	eop	average
EURUSD	1.06	1.05	1.09	1.08	1.09	1.08	1.14	1.12
USDMXN	19.60	20.11	17.18	17.74	19.06		18.69	
USDARS	172.89	130.70	641.85	296.50	1177.00	953.88	1600.00	1399.58
USDCOP	4789	4260	3948	4319	4155	3986	4190	4176
USDPEN	3.83	3.83	3.73	3.74	3.80	3.77	3.75	3.80
USDTRY	18.66	16.56	29.10	23.80	38.00	33.47	45.50	42.06

Macroeconomic forecasts

GROSS DOMESTIC PRODUCT
(ANNUAL AVERAGE, YOY)

	2022	2023	2024	2025
United States	1.9	2.5	2.2	1.9
Eurozone	3.5	0.5	0.7	1.4
Spain	5.8	2.5	2.5	2.1
Latam*	3.8	1.9	1.5	2.7
Argentina	5.0	-1.6	-4.0	6.0
Colombia	7.3	0.6	1.8	2.8
Mexico	3.7	3.2	2.5	2.4
Peru	2.7	-0.6	2.9	2.7
Türkiye	5.5	4.5	3.5	3.5
China	3.0	5.2	4.6	4.2
World	3.5	3.2	3.1	3.3

(*) Argentina, Brazil, Chile, Colombia, Mexico and Peru

INFLATION
(ANNUAL AVERAGE, EOP INDICATED, YOY)

	2022	2023	2024	2025
United States	8.0	4.1	3.2	2.6
Eurozone	8.4	5.4	2.5	2.0
Spain	8.4	3.5	3.3	2.4
Latam				
Argentina (eop)	94.8	211.4	140.0	45.0
Colombia (eop)	13.1	9.3	5.4	3.8
Mexico (eop)	7.8	4.7	4.2	3.5
Peru (eop)	8.5	3.2	2.6	2.4
Türkiye (eop)	64.3	64.8	43.0	25.0
China	2.0	0.2	0.5	1.5
World	9.3	7.6	7.2	4.7

(*) Argentina, Brazil, Chile, Colombia, Mexico y Peru

BBVA Research

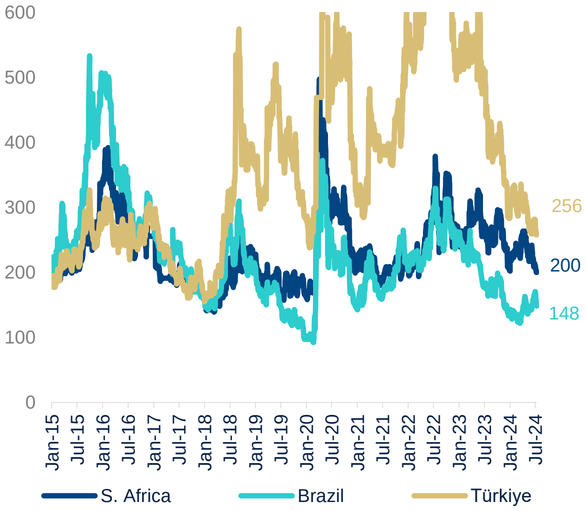
02

Türkiye Economic Outlook

Creating Opportunities

Türkiye was removed from the FATF's grey list. Moody's rating decision to be announced on July 19th. Further upgrades will be key to reinforce more capital inflows

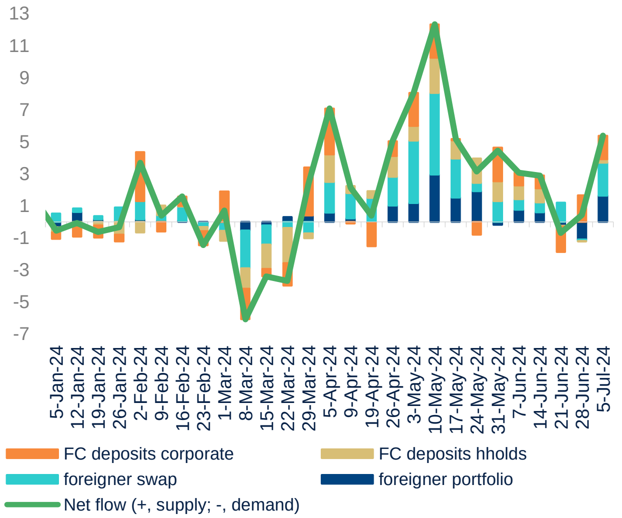
TÜRKİYE'S 5-YEAR CDS WRT PEERS
BPS



SOVEREIGN RATINGS

	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
Brazil	12	BB	Ba2	BB	
S. Africa	13	BB-	Ba3	BB-	
Türkiye	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

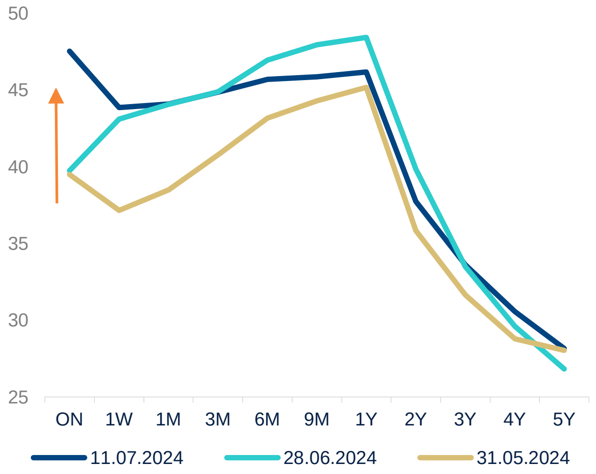
FC FLOWS OF SUPPLY & DEMAND
US$BN, WEEKLY, ADJ. FROM PRICE EFFECTS



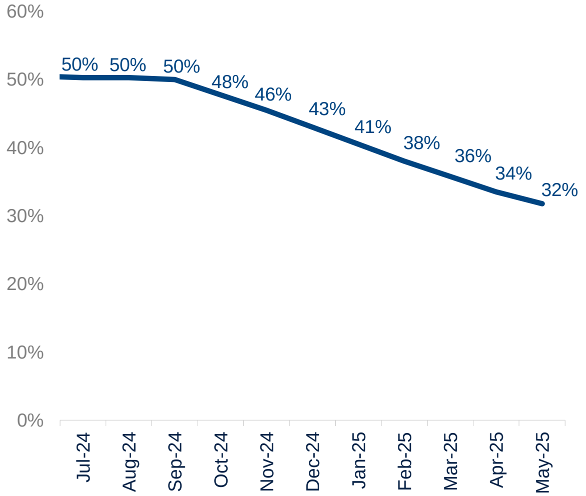
Source: Bloomberg, CBRT & Garanti BBVA Research

Short term carry trade swaps have started to materialize some profit. Markets price 43% policy rate of the CBRT by end 2024

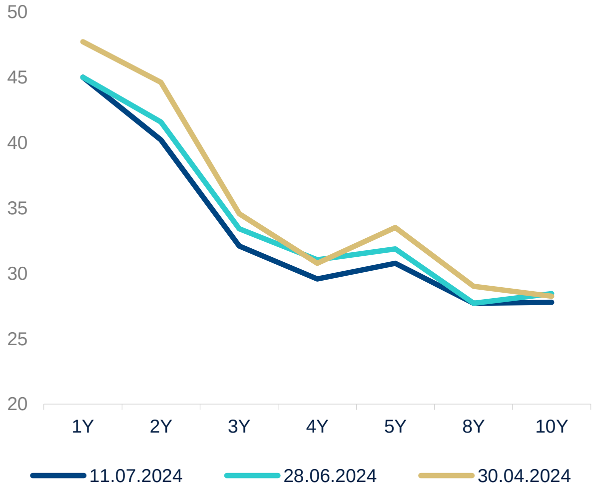
USDTRY FORWARD IMPLIED YIELD CURVE, %



TL REF IMPLIED CBRT FUNDING RATE EXPECTATIONS, %



TRY YIELD CURVE, %

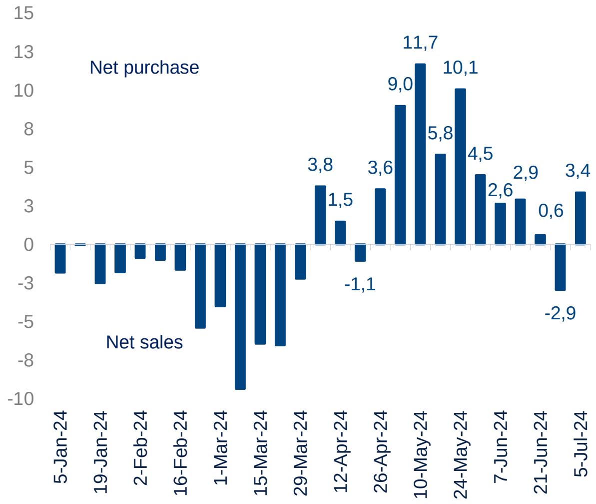


Current swap restrictions as a share of banks' regulatory capital (US$92 billion as of July 5th): 5% for 7 days or less, 10% for 30 days or less and 30% for 1 year or less.

Source: Bloomberg & Garanti BBVA Research

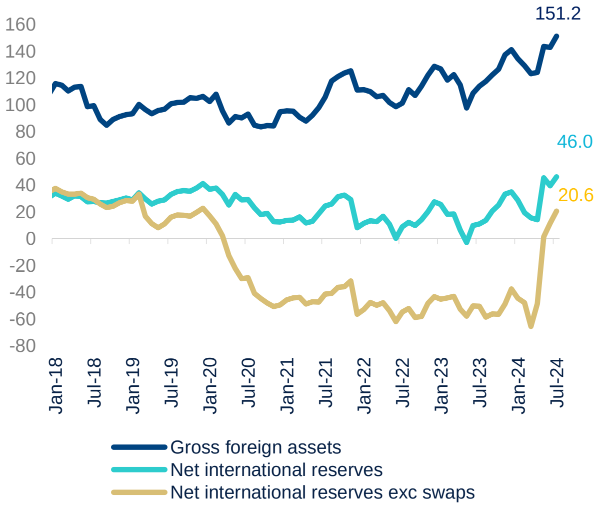
The pace of reserve accumulation has started to gain pace again after the FATF decision at the end of June

CBRT INDIRECT RESERVES FLOWS*
US$BN, weekly flow

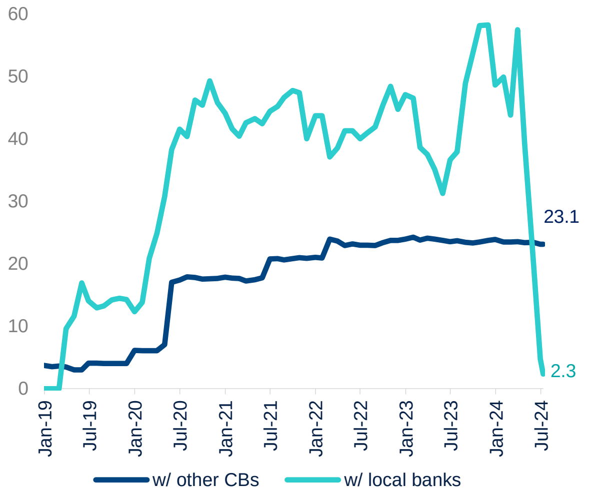


** Including the assumption from 30% of exports and services income inflows as of June 10th, and rediscount loans. CBRT payments due from KKM are assumed to have a similar ratio in Garanti BBVA since March 29th.*

CBRT INTERNATIONAL RESERVES
US$BN as of July 10th



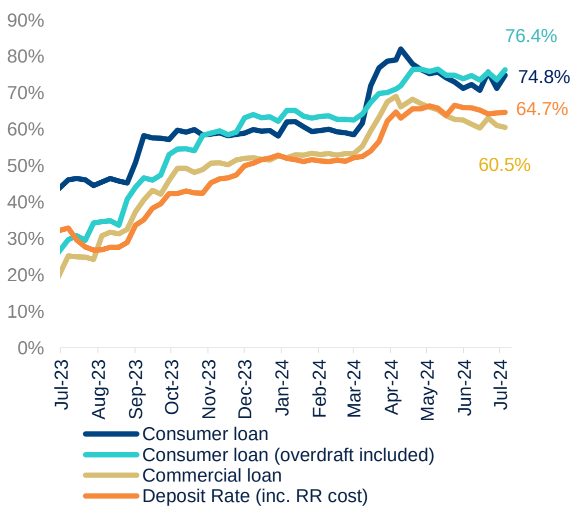
BILATERAL SWAPS OF THE CBRT
US$BN as of July 10th



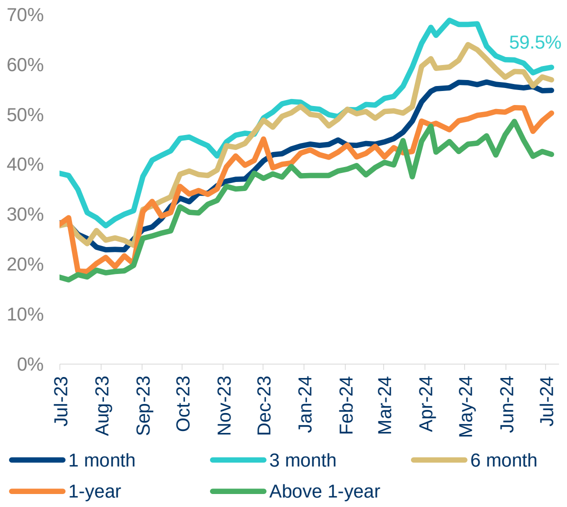
Source: CBRT & Garanti BBVA Research

Demand remains decisive on the TL lending rates, resulting in a counter pressure on TL deposit rates. TL commercial lending rate getting far below the TL cost of funding in the sector. FC lending stays competitive

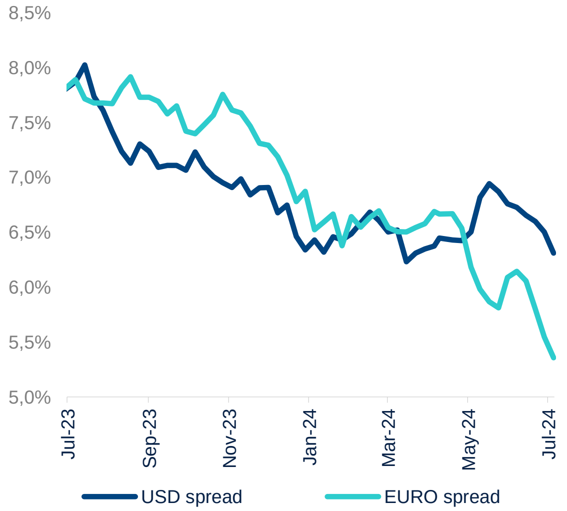
CONSUMER & TL COMMERCIAL RATES
%, flow, sector



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



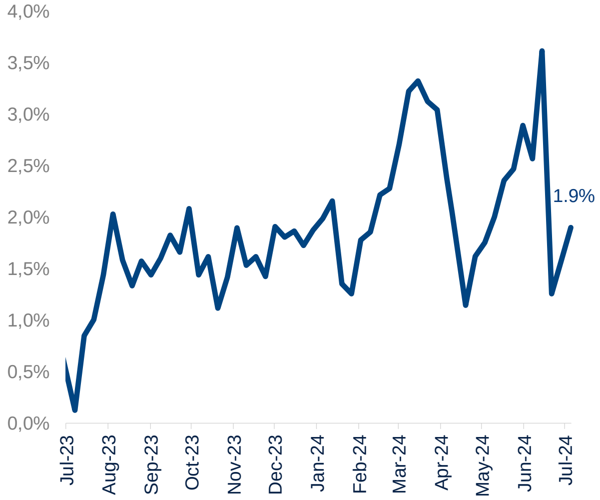
FC LENDING SPREAD
%, flow, sector



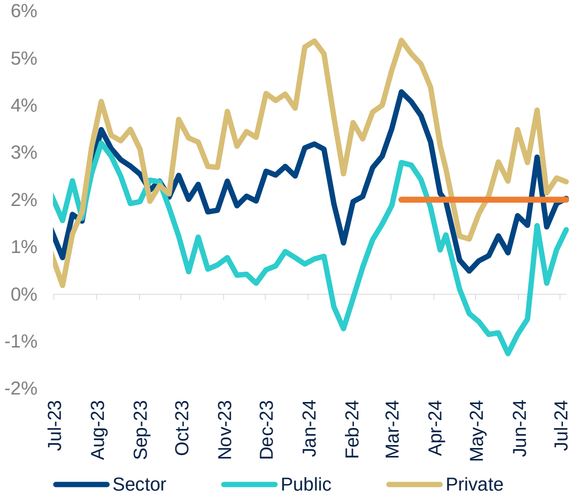
Source: CBRT & Garanti BBVA Research

Credit conditions squeeze further. Still, credit growth continues to be closer to the monthly growth caps of 2%

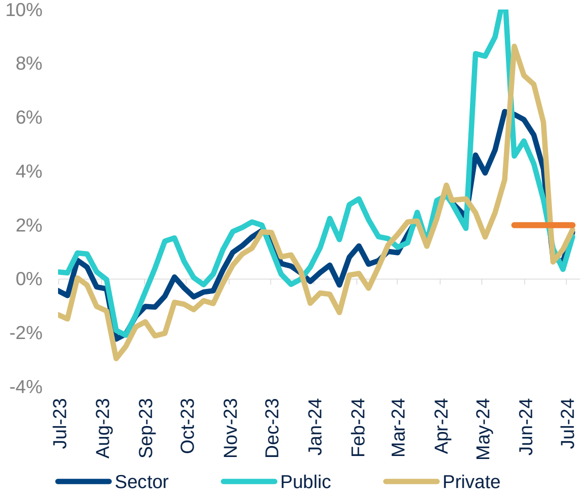
TOTAL CREDIT GROWTH*
4-week rolling, FX adjusted, sector



TL CREDIT GROWTH
4-week rolling, deposit banks



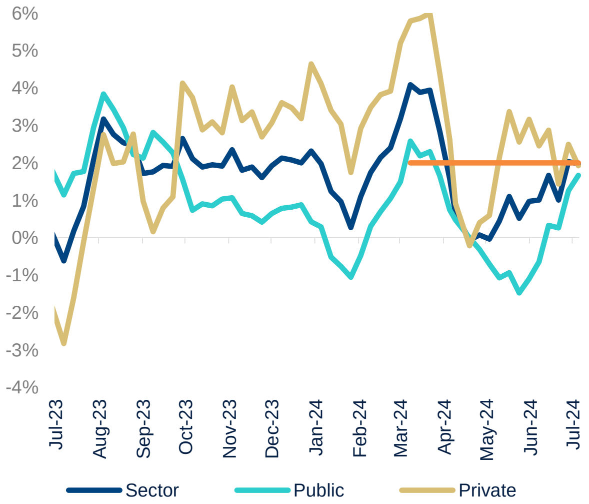
FC CREDIT GROWTH
USD, 4-week rolling, deposit banks



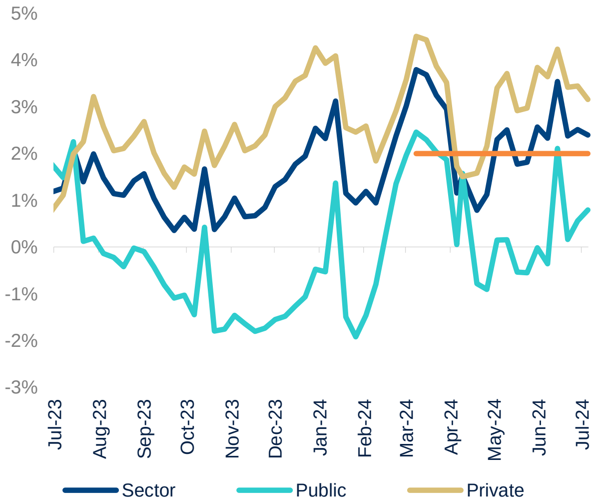
Source: BRSA, CBRT & Garanti BBVA Research

The credit composition is not favorable for inflation. Retailer lending remains much stronger than commercial lending

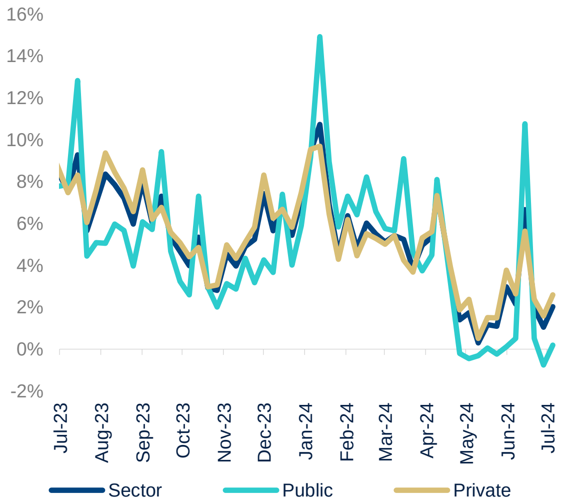
TL COMMERCIAL LENDING
4-week rolling, deposit banks



CONSUMER LOANS GROWTH
4-week rolling, deposit banks



RETAILER CREDIT CARD SPENDING
4-week rolling, deposit banks

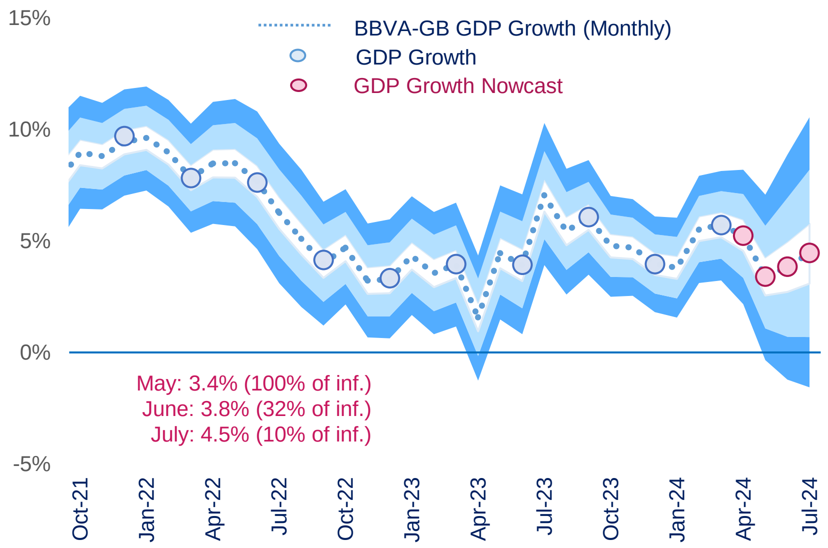


Source: BRSA, CBRT & Garanti BBVA Research

We nowcast nearly 4% y/y and 0% q/q GDP growth for 2Q24. We nowcast a mild negative quarterly growth as of early July, while calendar day effects support the annual figure. Stronger aggregate demand than supply still signals depletion from inventories

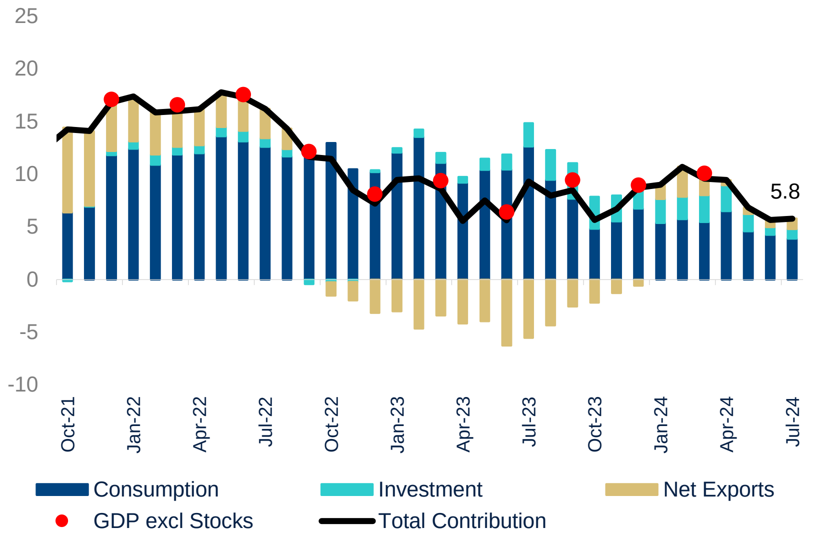
GARANTI BBVA MONTHLY GDP INDICATOR

YOY, 3M MOVING AVERAGE



GARANTI BBVA MONTHLY GDP CONTRIBUTION

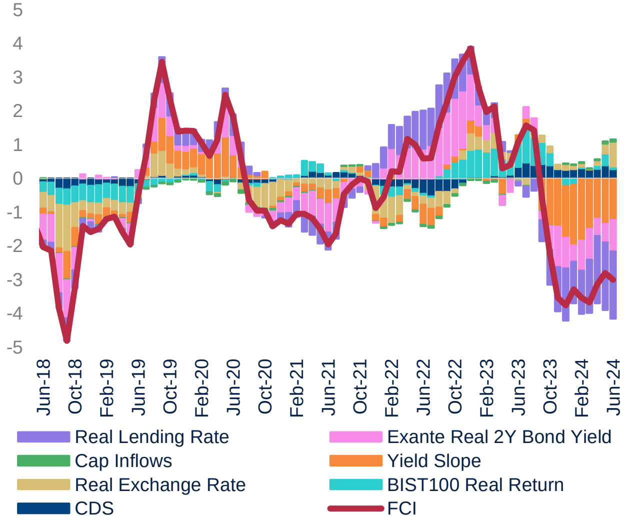
ANNUAL, PP, EXC GOV CONSUMPTION



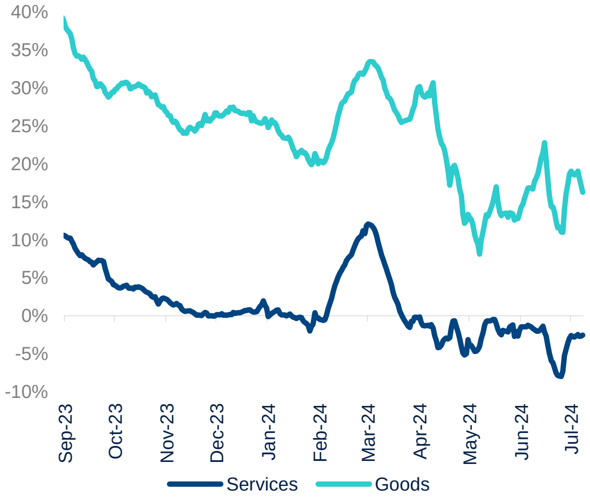
Source: TURKSTAT, CBRT & Garanti BBVA Research

Households’ spending availability maintains somewhat a resistance against a clearer deceleration in consumption, particularly on goods

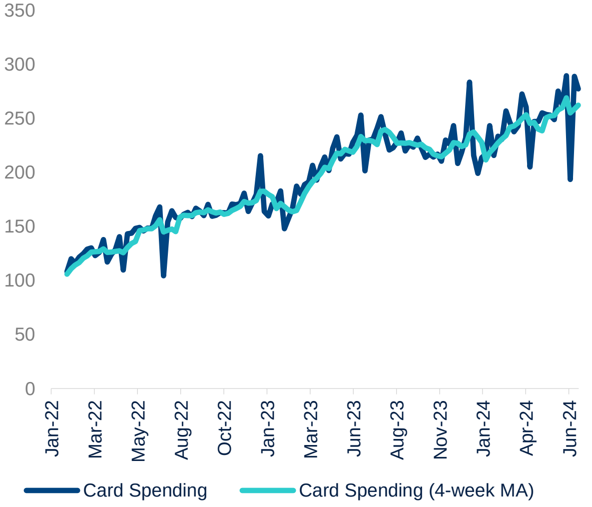
GARANTI BBVA FINANCIAL CONDITIONS INDEX
monthly, standardized, + easing, - tightening



GARANTI BBVA BIG DATA CONSUMPTION
REAL, 28-DAY SUM, YOY



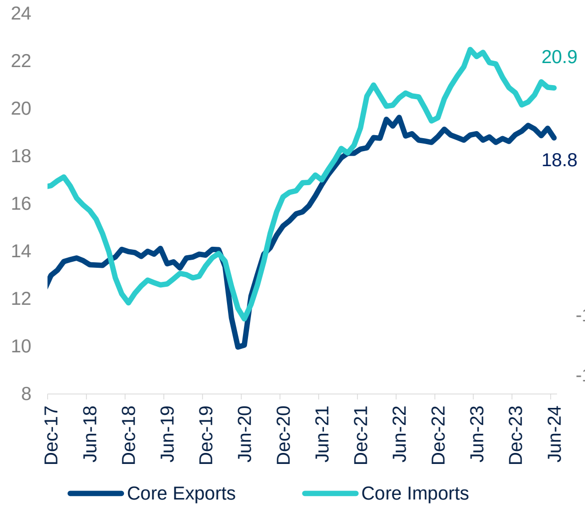
CARD SPENDING RELEASED BY THE CBRT
REAL, JAN22=100



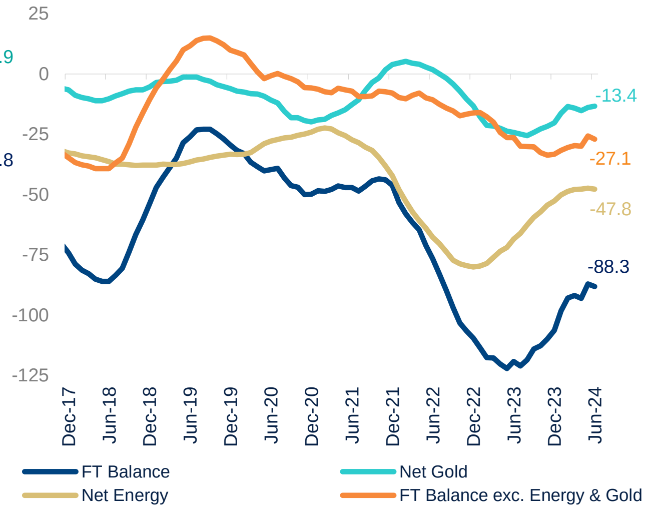
Source: TURKSTAT, CBRT & Garanti BBVA Research

Core imports decelerate only gradually. We expect a clearer deceleration of imports together with some improvement in exports in 2H24

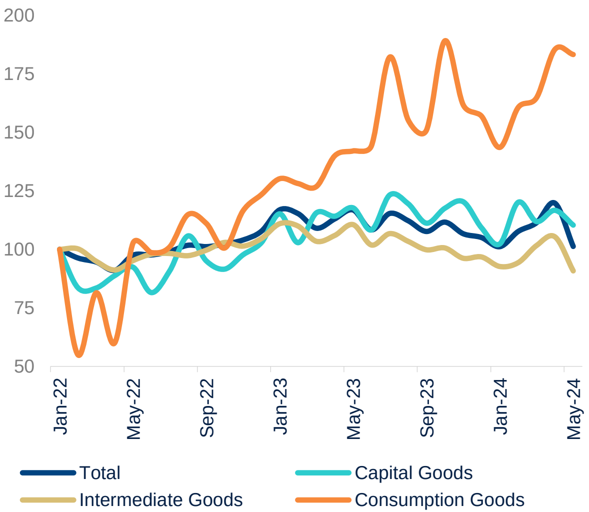
GOODS EXPORTS & IMPORTS
EXC ENERGY & GOLD, SA 3M AVG, US$BN



GOODS FOREIGN TRADE BALANCE
12-MONTH, US$BN



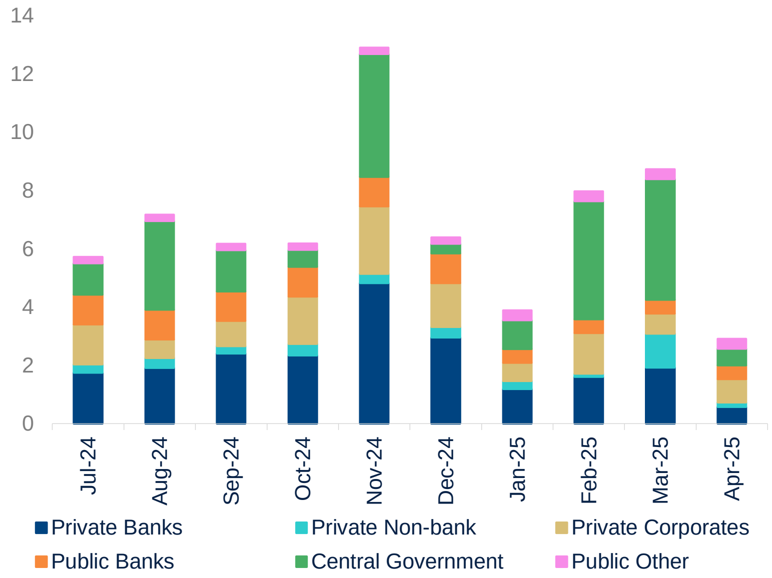
IMPORT VOLUME BY SEGMENT
2022 JAN=100, SEAS CAL ADJ



Source: TURKSTAT, CBRT & Garanti BBVA Research

External loan redemptions will hover 6-7bn$ on average in one year horizon. Yet, roll-over ratios continue to be promising

EXTERNAL LOANS ON A REMAINING MATURITY BASIS FOR THE NEXT 12 MONTHS (BN USD, AS OF APRIL 2024)

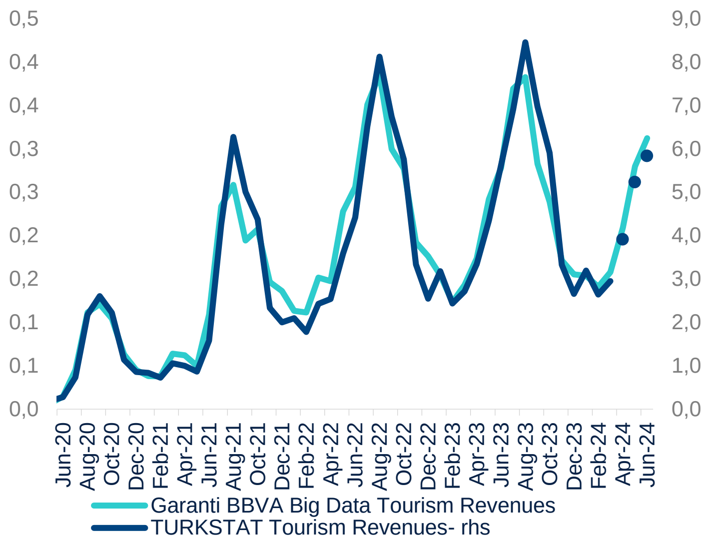


LT EXTERNAL LOANS ROLL-OVER RATIO OF BANKS & REAL SECTOR (12 MONTH ROLLING, %)

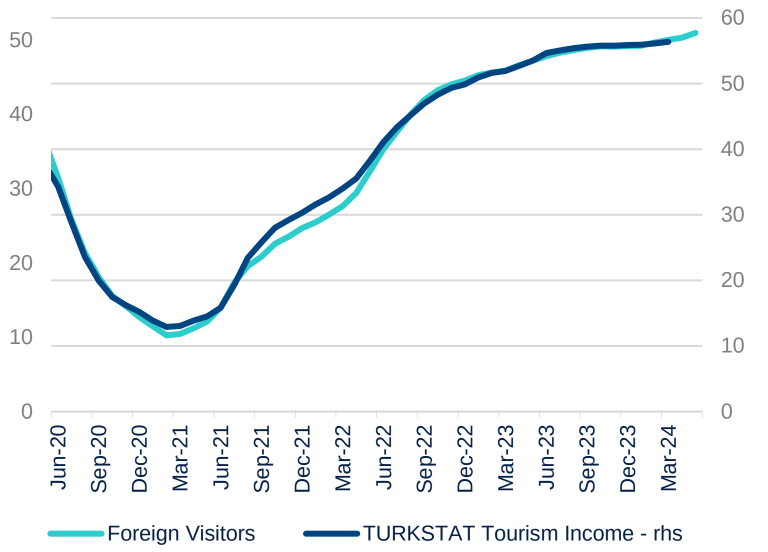
Source: CBRT and Garanti BBVA Research

Our big data tourism revenues signal around 58bn$ whole year revenue, given the performance in 2Q24. We assess the Government’s 60bn$ tourism revenue target for 2024 is achievable

GARANTI BBVA BIG DATA TOURISM REVENUES
(bn$)



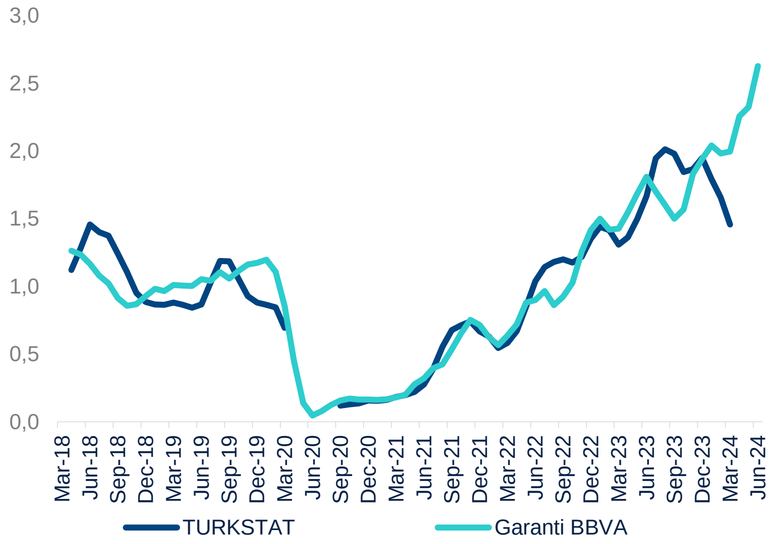
TOURISM REVENUES & FOREIGN VISITORS
(12M sum mn people, bn$)



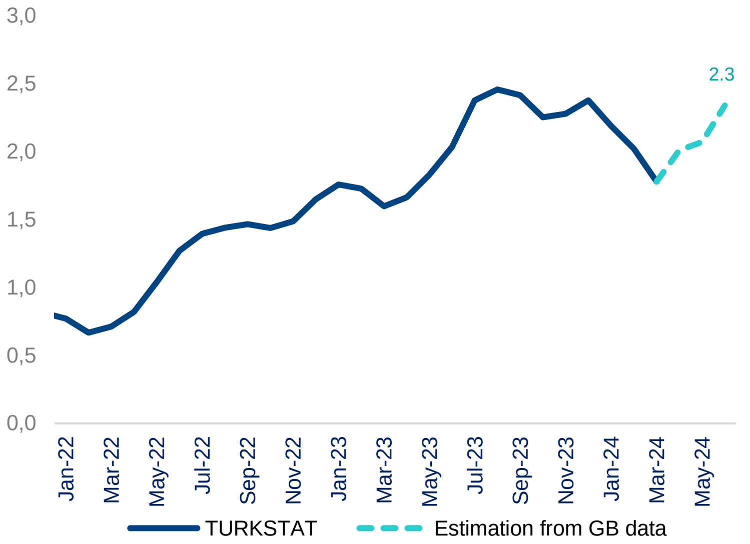
Source: TURKSTAT, Ministry of Tourism & Garanti BBVA Research

Garanti BBVA big data tourism expenditures track official data (TURKSTAT) well and signal a clear acceleration since the start of the year, implying at least 8.5bn$ full year tourism expenditures

TOURISM EXPENDITURES: TURKSTAT VS. GARANTI BBVA
(mean adjusted, 3 month moving sum, US$bn)



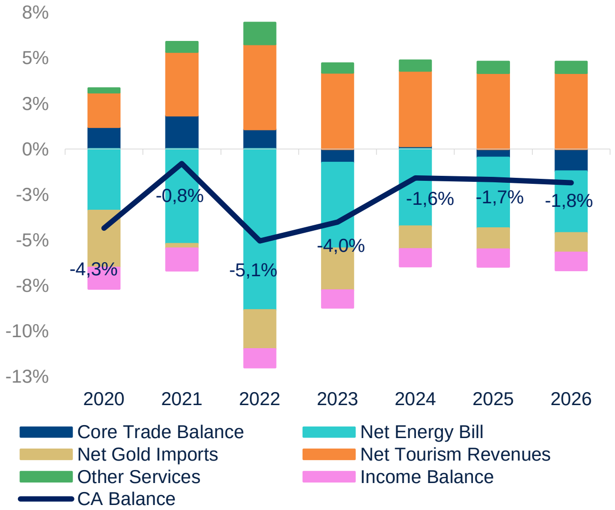
TOURISM EXPENDITURES WITH ESTIMATED LEVELS FROM GB DATA (nominal 3 month moving sum, US$bn)



Source: TURKSTAT & Garanti BBVA Research

Overall, our big data tourism flows show that the revenues would be parallel to what we had assumed for 2024, whereas the expenditures would be slightly higher

CURRENT ACCOUNT DEFICIT FORECASTS
% GDP



bn$	Core Trade Balance	Net Energy Bill	Net Gold Imports	Tourism Revenues	Tourism Expenditures	Net Tourism Revenues	Other Services	Income Balance	CA Balance
2022	9.9	-80.1	-19.4	46.5	4.3	42.2	10.7	-9.1	-45.8
2023	-8.5	-52.7	-25.7	54.6	7.6	47.0	5.6	-10.6	-44.9
2024	2.1	-53.9	-15.8	61.0	8.5	52.4	7.1	-12.1	-20.0
2025	-6.4	-52.9	-15.8	65.8	9.2	56.6	8.5	-12.9	-22.9
2026	-18.0	-49.0	-15.8	70.3	9.8	60.5	9.1	-13.8	-27.0

- On the revenues side, if we mimic 2Q performance of Garanti and assume the same 2H23 revenue for 2H24, we reach 58bn$ full year revenue. Given Garanti BBVA's %12 annual growth in 1H24, 2H24 performance would be much better than last year, implying closer or slightly above 60bn$ revenue in 2024 (61bn$ assumption).
- On the expenditures side, given the clear acceleration so far implied by Garanti BBVA, there would be slight upside risk on our tourism expenditures assumption of 8.5bn$ for 2024 which we attain by replicating the same exercise above on revenues.
- Overall, there would still be around 5-8bn$ current account surplus during 3Q24 (vs. 17bn$ deficit in 1H24)

Source: TURKSTAT, CBRT & Garanti BBVA Research

On BoP math (swaps are not included), the CBRT will accumulate reserves, supported by foreigners' increasing exposure

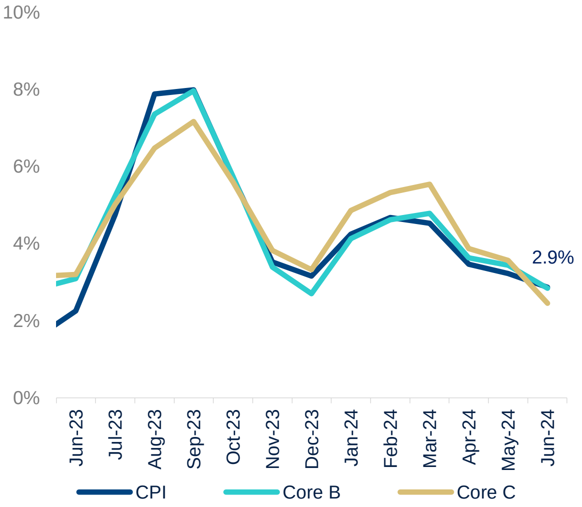
US$BN											Baseline	
	2015	2016	2017	2018	2019	2020	2021	2022	2023	May'24	2024	2025	2026
External Financing Needs	**58**	**82**	**99**	**75**	**44**	**82**	**58**	**89**	**91**	**68**	**101**	**88**	**92**
Current Account Balance	**-21**	**-22**	**-35**	**-15**	**15**	**-31**	**-6**	**-46**	**-45**	**-25**	**-20**	**-23**	**-27**
Long-Term Credit Redemptions	**31**	**54**	**56**	**54**	**52**	**44**	**44**	**35**	**39**	**36**	**71**	**55**	**55**
Banks	11	34	37	37	31	26	26	23	22	21	44	30	30
Other	19	20	20	17	22	18	18	12	17	15	27	25	25
Government	6	5	8	6	7	7	8	8	8	6	**10**	**10**	**10**
Total Financing Sources	**46**	**82**	**91**	**64**	**50**	**50**	**81**	**101**	**89**	**96**	**141**	**105**	**105**
Net FDI	**14**	**11**	**8**	**9**	**6**	**4**	**6**	**9**	**5**	**4**	**7**	**8**	**8**
Government Eurobonds	**3**	**6**	**10**	**8**	**11**	**9**	**10**	**11**	**11**	**8**	**10**	**10**	**10**
Other Portfolio Inflows	**-15**	**5**	**18**	**-5**	**-10**	**-12**	**1**	**-18**	**5**	**21**	**20**	**10**	**10**
Long-Term Credit Renewals	**67**	**66**	**60**	**53**	**42**	**36**	**51**	**40**	**44**	**45**	**84**	**57**	**57**
Government	2	2	2	2	1	1	2	3	3	3	2	2	2
Banks	38	37	37	28	23	21	24	17	25	27	**55**	**30**	**30**
Other	28	28	21	23	18	13	25	20	16	15	**27**	**25**	**25**
Short-Term Borrowing	**-23**	**-7**	**4**	**-8**	**-4**	**3**	**-2**	**0**	**6**	**8**	**5**	**5**	**5**
Trade Credits	**-2**	**-2**	**7**	**-8**	**9**	**-2**	**5**	**1**	**5**	**2**	**5**	**5**	**5**
Net Deposits	**-2**	**-1**	**-1**	**0**	**4**	**19**	**9**	**36**	**23**	**14**	**10**	**10**	**10**
Net Error and Omissions	**3**	**5**	**-15**	**16**	**-10**	**-8**	**1**	**23**	**-9**	**-6**	**0**	**0**	**0**
Reserve Assets (Sources-Needs)	**-12**	**1**	**-8**	**-10**	**6**	**-32**	**23**	**12**	**-2**	**28**	**40**	**17**	**13**
Rollover Ratios (renewals/redemptions)													
Banks	332%	108%	101%	76%	74%	81%	94%	76%	116%	128%	125%	100%	100%
Other	143%	139%	105%	139%	85%	75%	138%	164%	99%	100%	100%	100%	100%

** May'24 corresponds to previous 12-month sum*

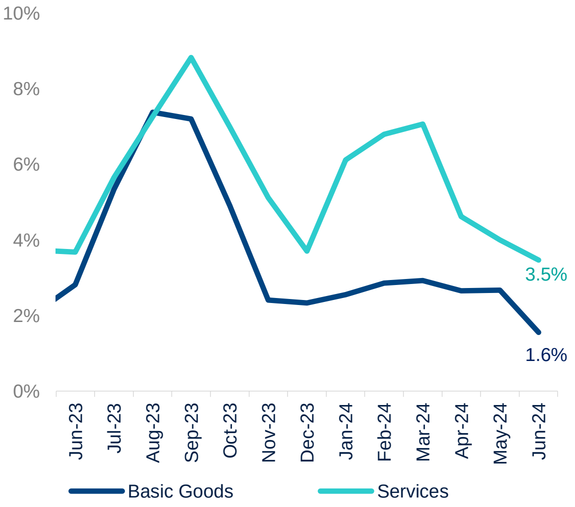
Source: TURKSTAT, CBRT & Garanti BBVA Research

According to our calculations, 3-month sa inflation trend at 2.9% in June (vs. 1.5% target of the CBRT in 4Q24), implying an annualized trend of near 40%

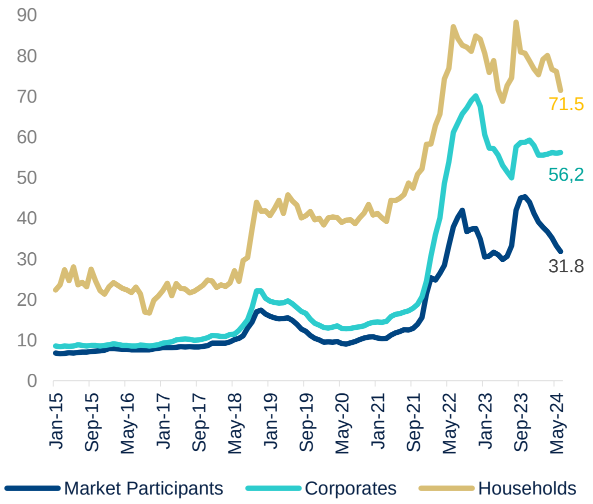
TREND CPI INDICATORS
SA MoM, 3M AVG



TREND CPI INDICATORS
SA MoM, 3M AVG



CBRT SURVEY ONE-YEAR AHEAD INFLATION EXPECTATIONS, %



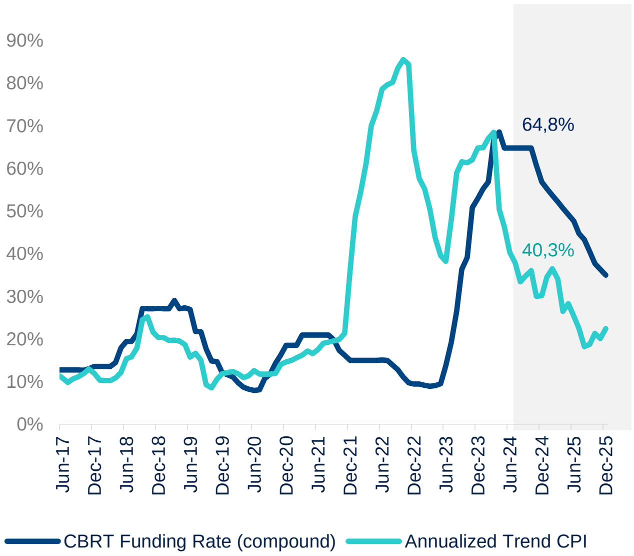
TWO KPIs of the CBRT

- Monthly inflation trend of 1-1.5% by the end of 2024 (vs. 3% in May)
- Inflation expectations converging to the projected inflation range (34-42% for 2024 and 7-21% for 2025)

Source: TURKSTAT, CBRT & Garanti BBVA Research

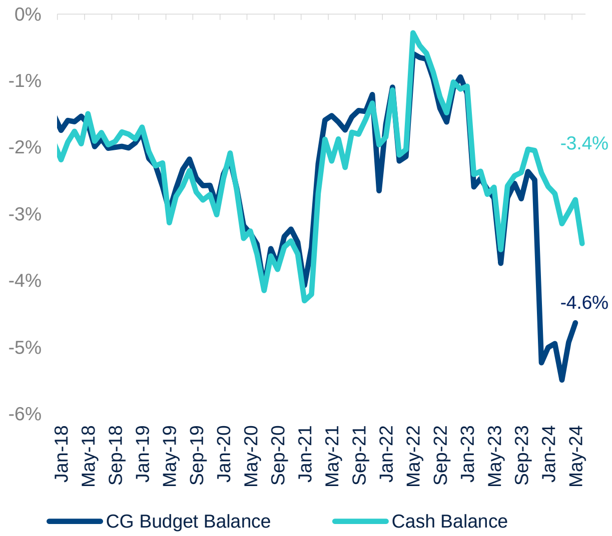
Monetary stance is historically much tighter. We expect the gap between cash and accrual basis budget deficit to be closed this year with delayed quake expenditures

CBRT FUNDING RATE & CPI UNDERLYING TREND, %



We maintain our view on the start of a gradual rate cutting cycle as of Nov24 (45% by 2024 end), following the removal of commercial credit growth caps in Sep-Oct24

CENTRAL GOVERNMENT BUDGET & TREASURY CASH BALANCE, % GDP

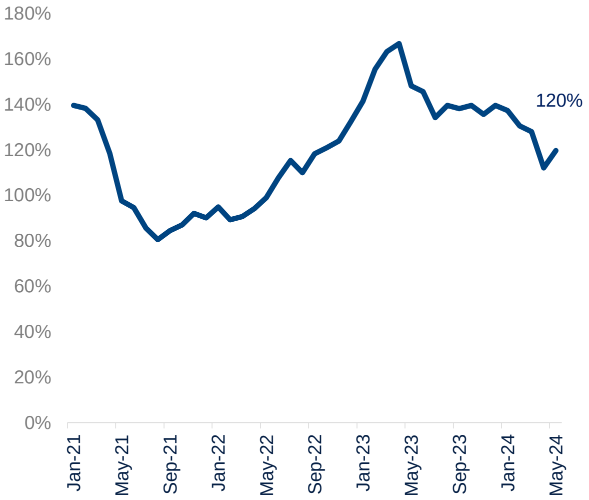


We expect the gap between cash and accrual basis deficit to be closed this year with delayed quake expenditures and finally have 5% GDP both cash & budget deficit by end 2024

Source: Treasury, CBRT & Garanti BBVA Research

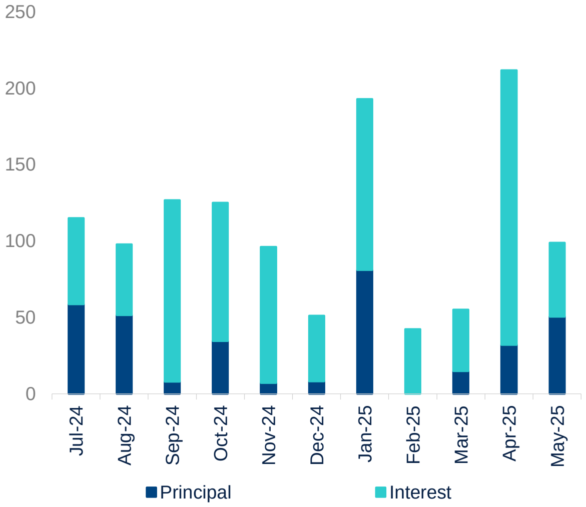
The Treasury might help the CBRT sterilize potential excess TL liquidity during the summer. Nevertheless, the need has cooled down due to a slower reserves accumulation in the last weeks

TREASURY DOMESTIC DEBT ROLL-OVER RATIO, %



2024 target of 136.5% will require much higher debt roll-over ratio levels in the next months

TREASURY DOMESTIC DEBT CALENDAR
BN TL



- Fiscal savings package implied a very limited effect of 0.2-0.3% of GDP this year, which would increase in the medium run.
- Inadequate saving in the short run leads the Ministry to find new revenue sources.
- Leaked draft bill signals an impact analysis of 639bn TL (1% of GDP) for 2025.
- The Government aims to keep budget deficit to GDP ratio below 5% in 2024 and 3% in 2025.

Source: Treasury & Garanti BBVA Research

We keep our prudence for the baseline with a smooth transition, paving the way towards LT FDI inflows

Orderly & smooth transition to a rule-based approach

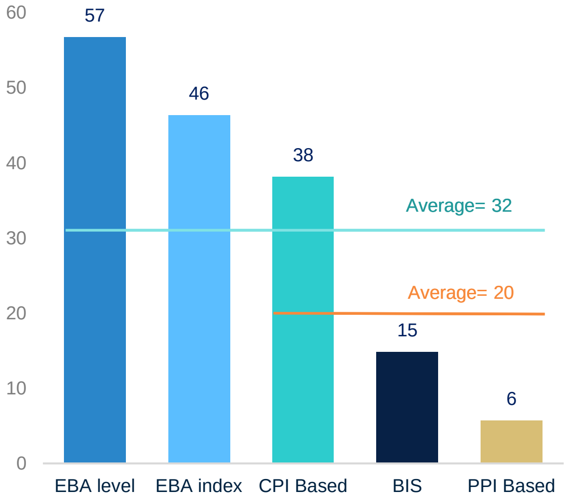
- Soft-landing assumption kept with fiscal impulse on quake recovery and support from foreign capital inflow
- 50% policy rate maintained until 4Q24 and we introduce 2 rate cuts in Nov and Dec, following some ease in credit growth caps initially
- Domestic demand decelerates (capped credit growth, below inflation wage hikes and lower subsidies)
- More or less a stable lira during summer (CBRT is assumed to maintainbpurchases) with a steady nominal depreciation thereafter (38 USDTRY by 2024 year end and 45.5 USDTRY by 2025 year end)
- Inflation is put under control with 43% by 2024 year end and 25% by 2025 year end. LT convergence maintained as 15%, assuming low contribution from the needed reforms

GARANTI BBVA BASELINE SCENARIO

	2023	2024	2025	2026
GDP growth (avg)	4.5%	**3.5%**	**3.5%**	**3.8%**
Unemployment Rate (avg)	9.4%	**9.3%**	**10.5%**	**10.8%**
Inflation (avg)	53.9%	**57.6%**	**30.3%**	**21.4%**
Inflation (eop)	64.8%	**43.0%**	**25.0%**	**18.5%**
CBRT Cost of Funding (avg)	20.5%	**48.7%**	**37.4%**	**25.2%**
CBRT Cost of Funding (eop)	42.5%	**45.0%**	**30.0%**	**22.0%**
USDTRY (avg)	23.74	**33.44**	**42.06**	**49.56**
USDTRY (eop)	29.44	**38.00**	**45.50**	**53.00**
Current Account Balance (bn$)	-45.0	**-20.0**	**-22.7**	**-26.9**
Current Account Balance (% GDP)	-4.0%	**-1.6%**	**-1.7%**	**-1.9%**
Primary Balance (% GDP)	-2.7%	**-1.5%**	**0.6%**	**1.0%**
Fiscal Balance (% GDP)	-5.2%	**-5.0%**	**-3.3%**	**-3.0%**

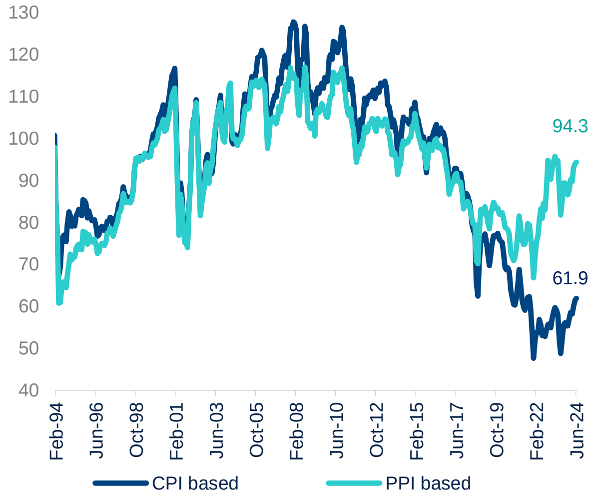
From the historical perspective, we estimate a current real exchange rate undervaluation of 20-25%

TRY REAL UNDERVALUATION*
%



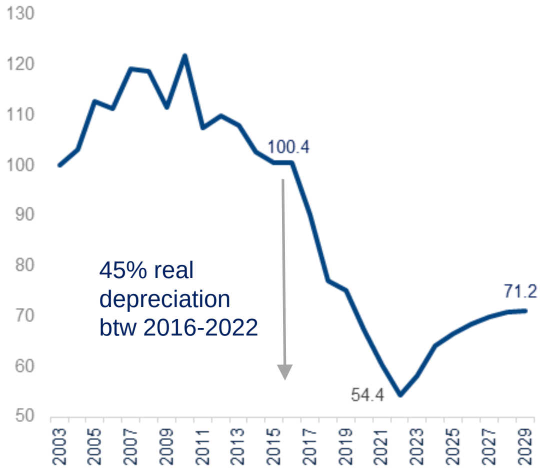
EBA analysis of IMF refers to an assessment made by 2022 end. Since CA balance has already started to adjust, we can conclude a current real undervaluation of 20-25%.

REAL EXCHANGE RATE
2003=100, monthly basis



The average of CPI based and PPI based indices is 78.1 as of June 2024, referring to 22% REER gap relative to 2003.

REAL EXCHANGE RATE WITH FORECASTS
2003=100, CPI based, annual average

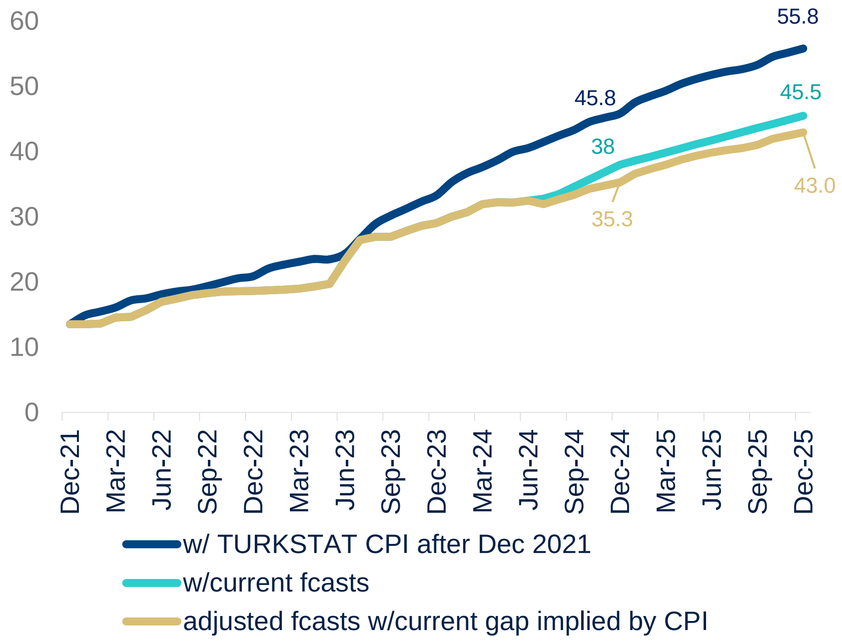


We assume REER gap will be closed in the long run. We reduce real appreciation pace in the next years (23% btw 2023-2029)

Source: IMF External Balance Assessment (EBA) by 2022 end, BIS by 2023 end, CBRT by May 2024 and Garanti BBVA Research
* The EBA methodology has provided the framework for conducting external sector assessments by IMF. EBA methodology includes three main components: (i) cross-country regression models to benchmark the current account (CA), (ii) similar regression models to benchmark the real effective exchange rate (REER), and (iii) the external sustainability (ES) approach, in cases where risks arising from a large net international debtor position can be relevant.

From the nominal FX perspective, the CBRT has allowed a 23% gap (2Q24 avg) relative to the nominal FX implied by inflation differentials

PPP BASED EXCHANGE RATE
USDTRY Level

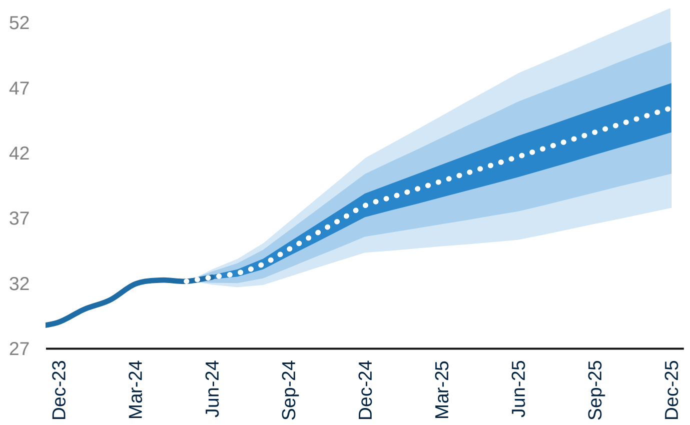


- We start our PPP analysis from end 2021 when KKM accounts have been introduced.
- Following May 2023 elections, the CBRT allowed the exchange rate to close the gap with the PPP-based exchange rate in July 2023.
- Thereafter, they attain the goal of keeping a real appreciation trend (monthly nominal depreciation lower than the monthly CPI) to speed up the disinflation process.
- The gap between the nominal exchange rate and the PPP-based exchange rate reached 23% in 2Q24 on average. If we maintain this gap with our current CPI forecasts, USDTRY might be 35.3 by 2024 end and 43.0 by 2025 end (vs. 38 and 45.5, respectively, in our forecasts).

Source: TURKSTAT, CBRT and Garanti BBVA Research

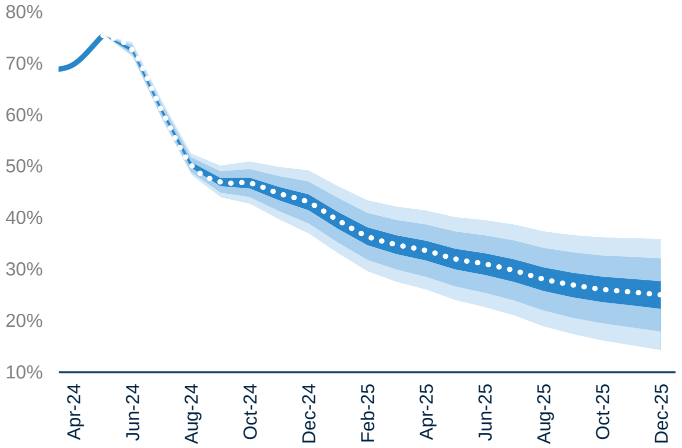
We expect USDTRY to keep a steady nominal depreciation without a major shock in 2024-2025 and a slower disinflation path compared to CBRT

USDTRY FORECASTS
Nominal level



	Probability Distribution Levels						
	-70%	-50%	-20%	Base	20%	50%	70%
Dec-24	34.29	35.59	37.09	38.00	38.91	40.41	41.71
Dec-25	37.73	40.44	43.60	45.50	47.40	50.56	53.27

CONSUMER INFLATION FORECASTS
YoY

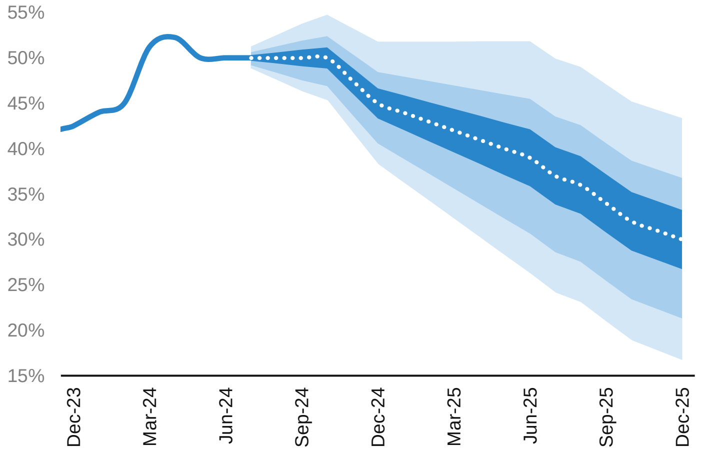


	Probability Distribution Levels						
	-70%	-50%	-20%	Base	20%	50%	70%
Dec-24	36.8%	39.0%	41.5%	43.0%	44.5%	47.0%	49.2%
Dec-25	14.1%	17.9%	22.3%	25.0%	27.7%	32.1%	35.9%

Source: Garanti BBVA Research

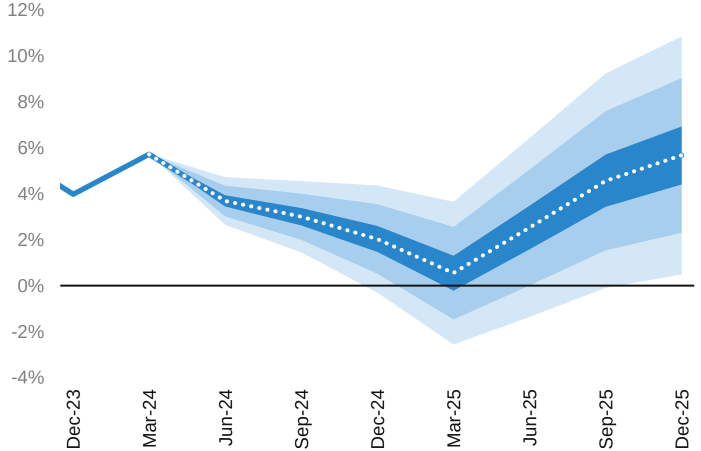
We have an upward bias on CBRT rates, which would have a downward impact on our GDP forecasts in the short term

CBRT FUNDING RATE FORECASTS
%



	Probability Distribution Levels						
	-70%	-50%	-20%	Base	20%	50%	70%
Dec-24	38.2%	40.6%	43.3%	45.0%	46.7%	48.4%	51.8%
Dec-25	16.6%	21.3%	26.7%	30.0%	33.3%	36.8%	43.4%

GDP GROWTH FORECASTS
YoY

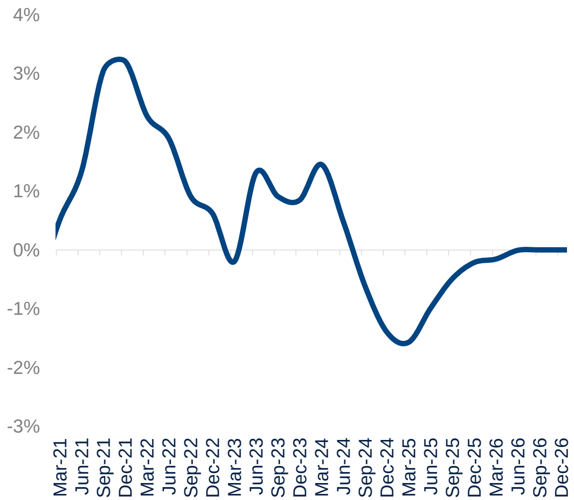


	Probability Distribution Levels						
	-70%	-50%	-20%	Base	20%	50%	70%
2024	2.4%	2.8%	3.3%	3.5%	3.7%	4.2%	4.6%
2025	-0.9%	0.6%	2.3%	3.5%	4.7%	6.4%	7.9%

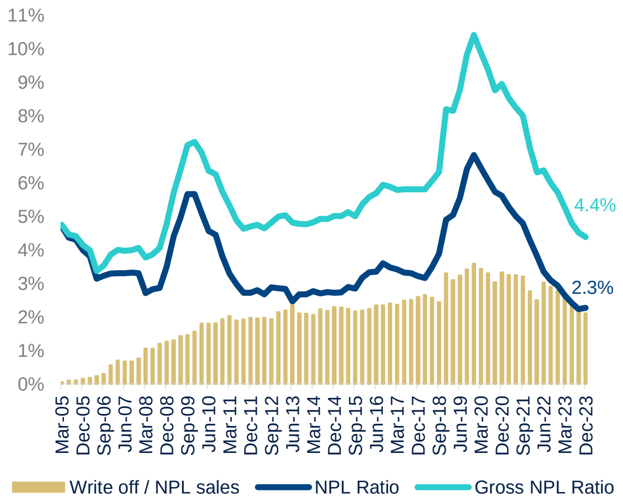
Source: Garanti BBVA Research

We expect output gap to become negative as of 3Q24 and deepen further at least until 2Q25

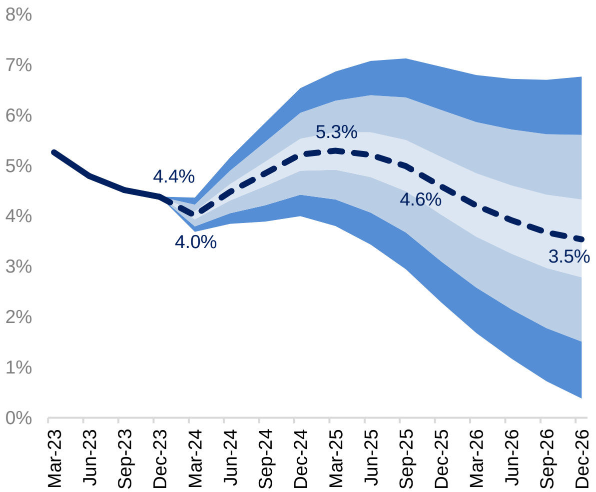
OUTPUT GAP FORECASTS
DIFF W/ POTENTIAL



GROSS NPL RATIO W/ WRITE-OFF & SALES
%, private deposit banks



GROSS NPL RATIO FORECASTS
%, private deposit banks



Delayed effects might put 2025 GDP growth under pressure. On the positive side, more favorable external demand conditions and increasing capital inflows will support the growth outlook. The pace of deceleration in 2H24 will be key for 2025 (3.5% GDP growth expected in 2024 and 2025).

In one-year horizon, NPL ratio might increase by at least 1-1.5pp in private deposit banks, according to our forecasts

Source: TURKSTAT, Turkish Banking Association and Garanti BBVA Research

Disclaimer

This report has been produced by:

Chief Economist
Seda Guler Mert
sedagul@garantibbva.com.tr

Kerem Baloglu
Economist
KeremBalo@garantibbva.com.tr

Ali Batuhan Barlas
Principal Economist
AliBarl@garantibbva.com.tr

Yigit Engin
Senior Economist
YigitE@garantibbva.com.tr

Deniz Ergun
Senior Economist
DenizErg@garantibbva.com.tr

Adem Ileri
Principal Economist
AdemIl@garantibbva.com.tr

Gul Yucel
Senior Economist
GulYu@garantibbva.com.tr

Mert Zobi
Economist
MertZ@garantibbva.com.tr

ENQUIRIES TO: Garanti BANKASI A.Ş. Nispetiye Mah. Aytar Cad. No:2 34340 Levent Beşiktaş İstanbul.
Tel.: +90 212 318 18 18 (ext 1064) - www.bbvaresearch.com

BBVA Research

Türkiye Economic Outlook

Garanti BBVA Research

July 2024

Creating Opportunities