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MANAGEMENT | INVESTMENT | BUSINESS DEVELOPMENT

MARKETS ECONOMY POLITICS

BI WEEKLY BULLETIN ON TÜRKİYE

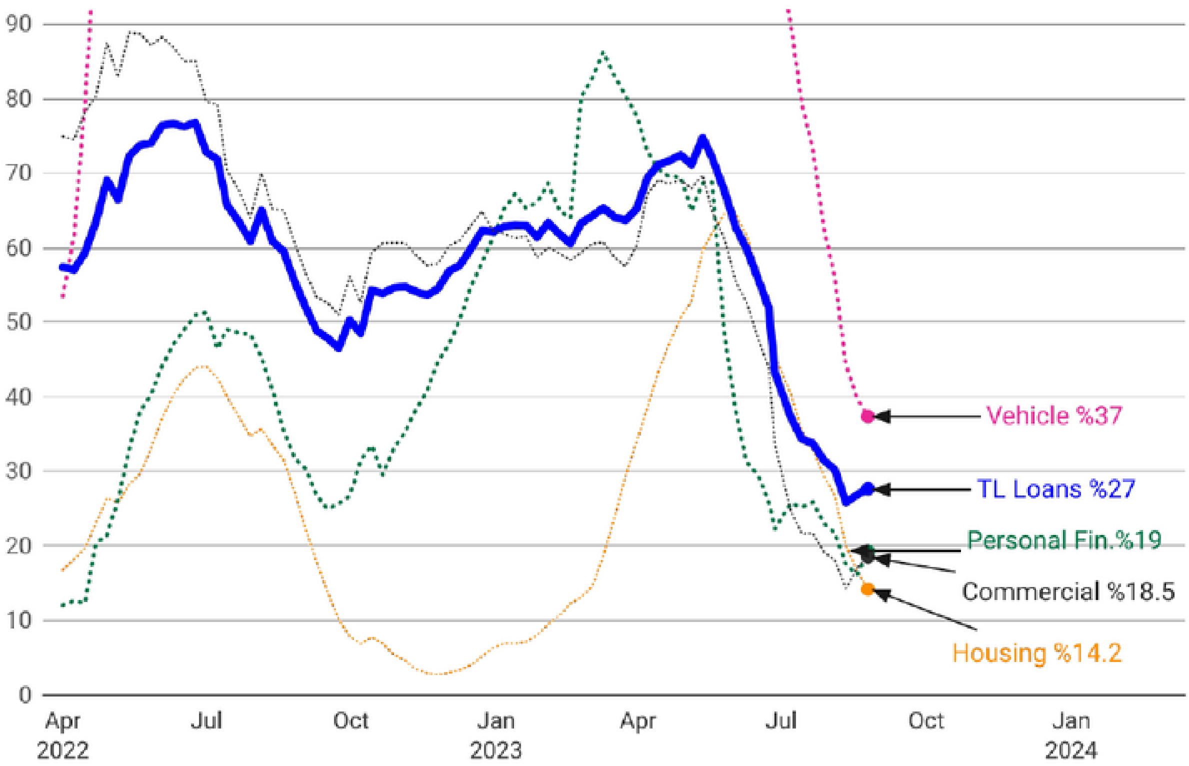
AUGUST 21 - SEPTEMBER 4 2023

CBRT Gross Reserves (September 1)

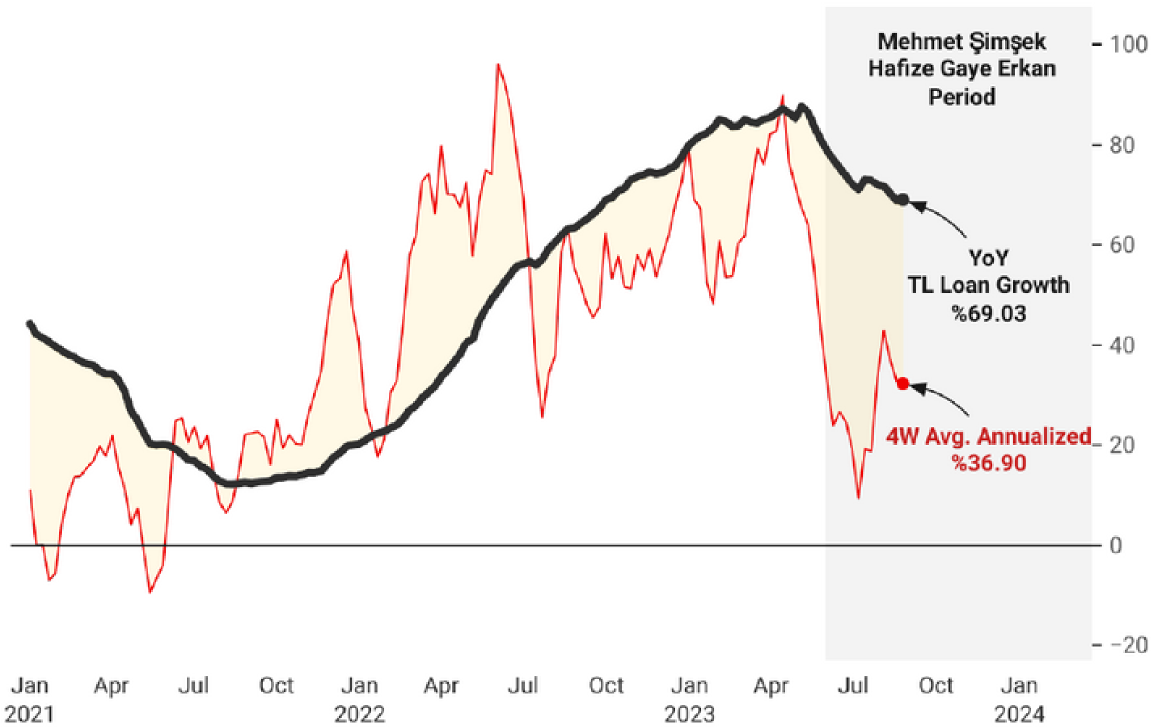
Assets (Bio USD)	30/12/22	27/08/23	YTD
Gold	45.89	42.20	-3.69
FX Banknotes	9.60	3.55	-6.05
Securities + Deposits	10.29	5.46	-4.83
Other FX Balance	62.94	68.35	5.41
TOTAL	**128.72**	**119.57**	**-9.15**

Liabilities (Bio USD)	30/12/22	27/08/23	YTD
To Turkish Banks	85.04	74.63	-10,41
To IMF & International Insti.	16.25	30.44	14,19
To Turkish Treasury	11.85	10.53	-1,32
To Turkish Banks in Swap Contract	47.41	51.44	4,03
To Foreign Central Banks	23.35	23.35	-
TOTAL	**183.90**	**190.39**	**6,49**

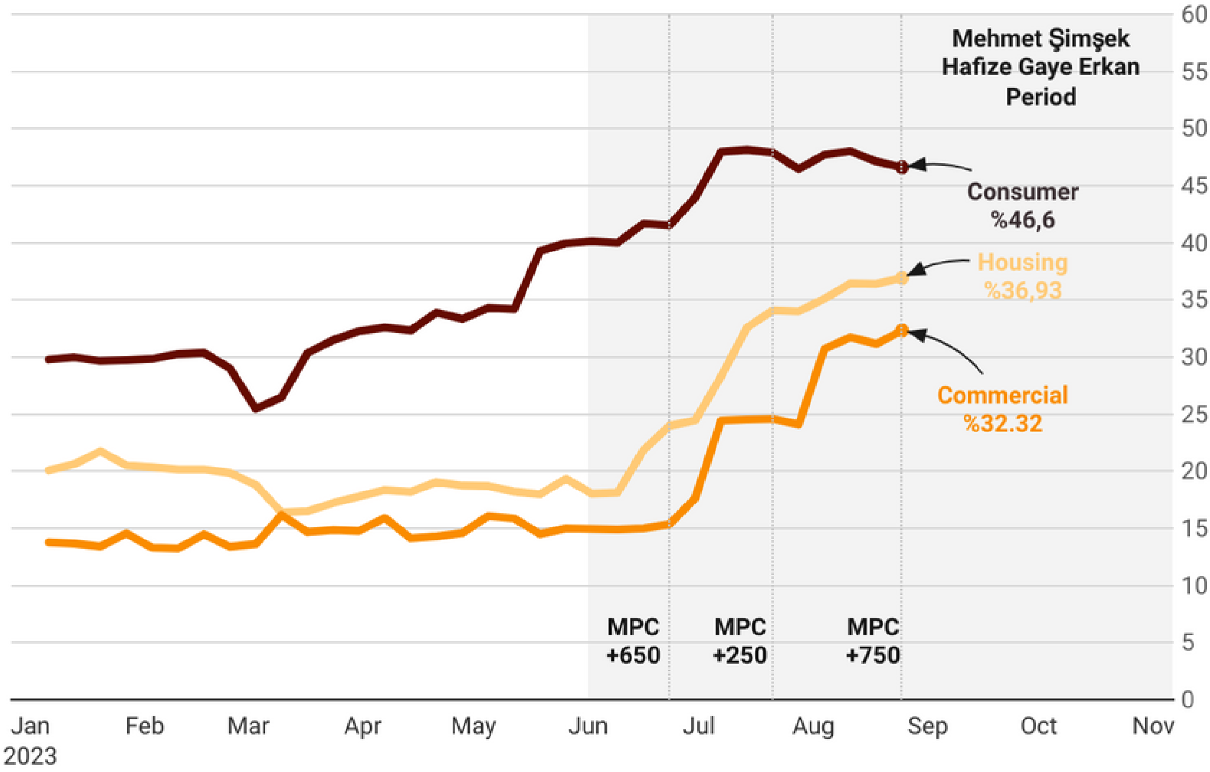
TL Loan Growth Momentum(August 25, 13 Week. Ann., %)



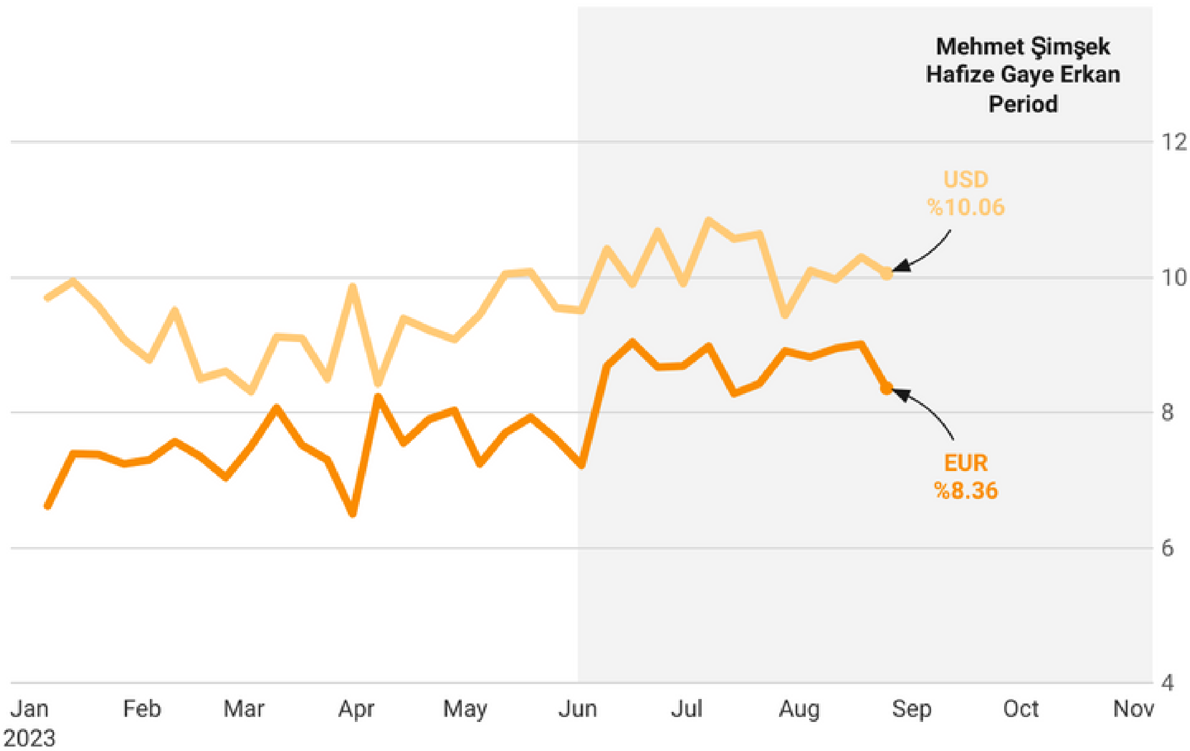
TL Loan Growth (August 25, YoY)



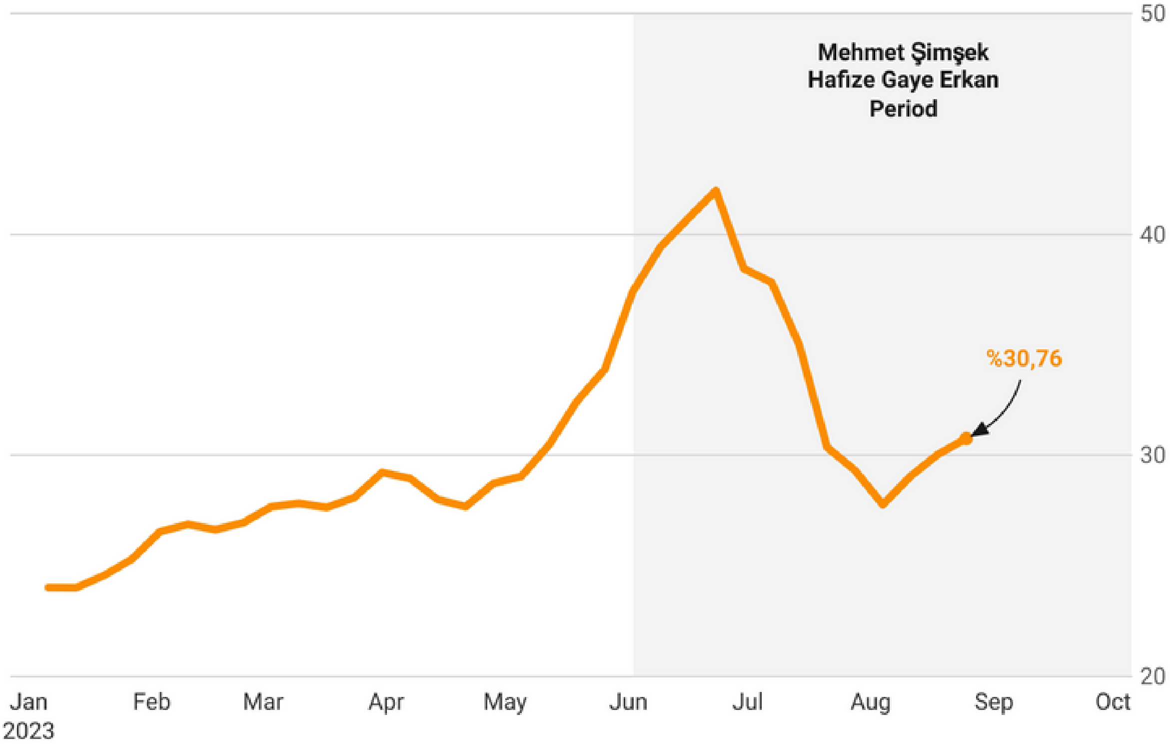
TL Loan Interest Rates (%, August 25)



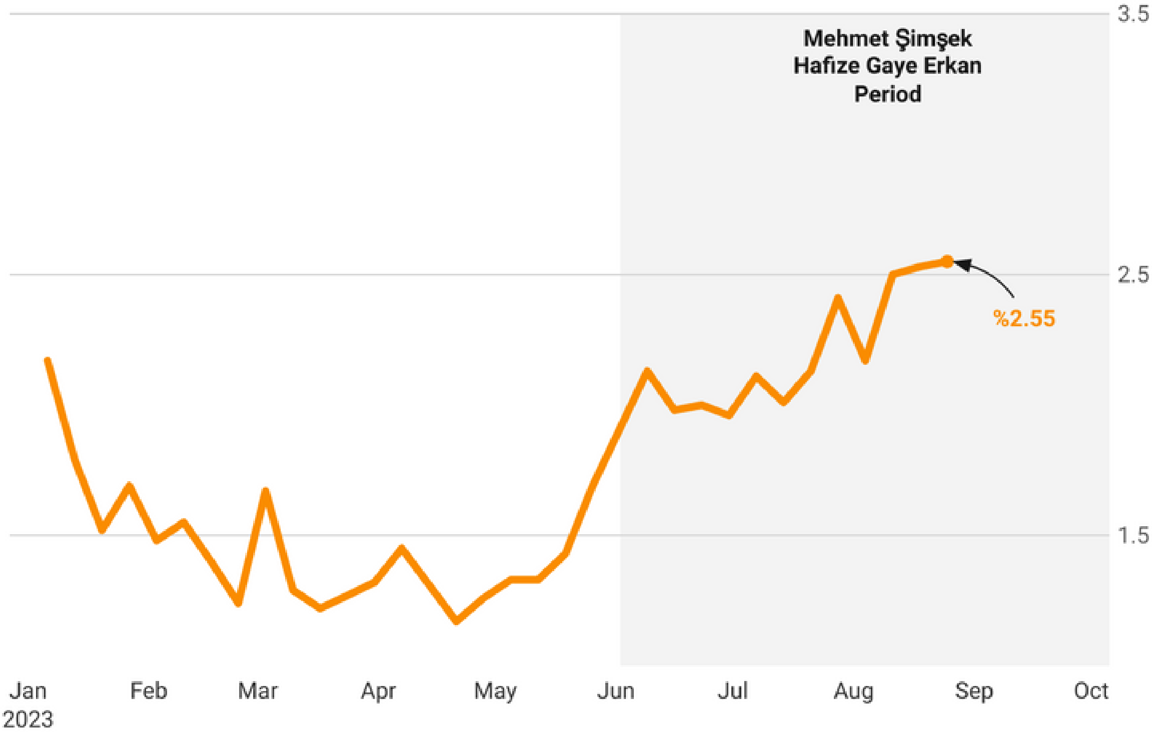
FX Loan Interest Rates (%, August 25)



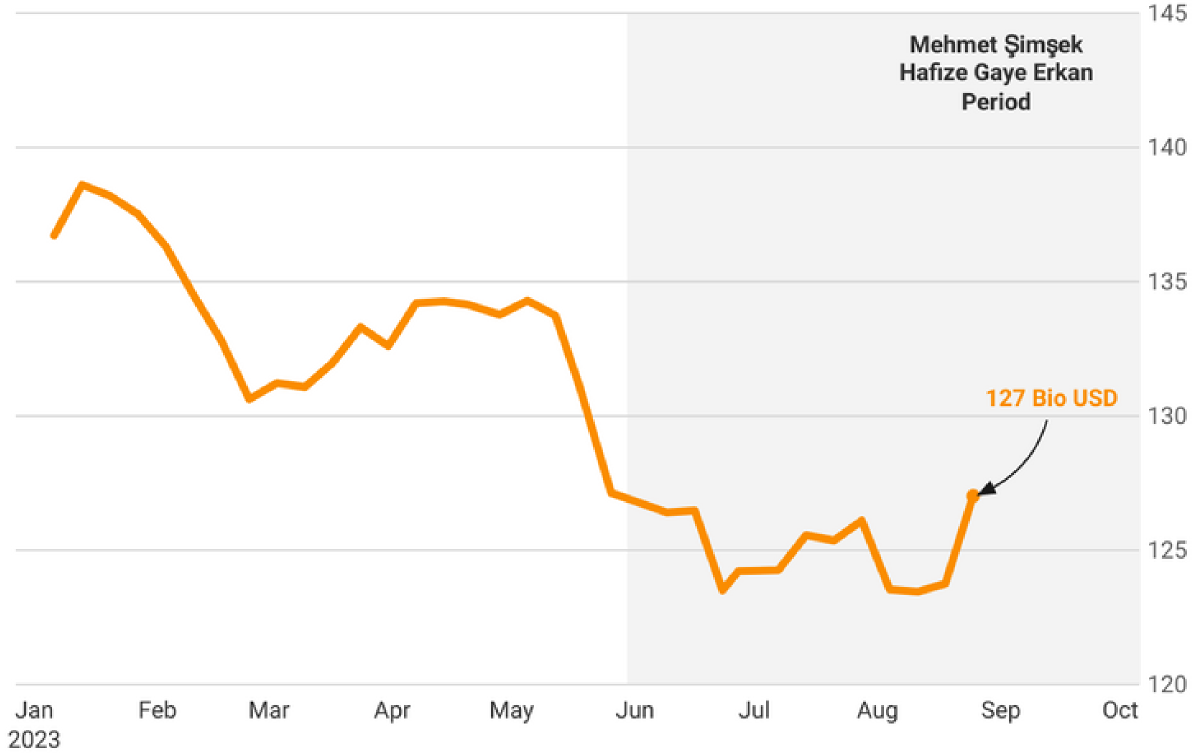
TL Deposit Interest Rates - 3M Maturity (August 25)



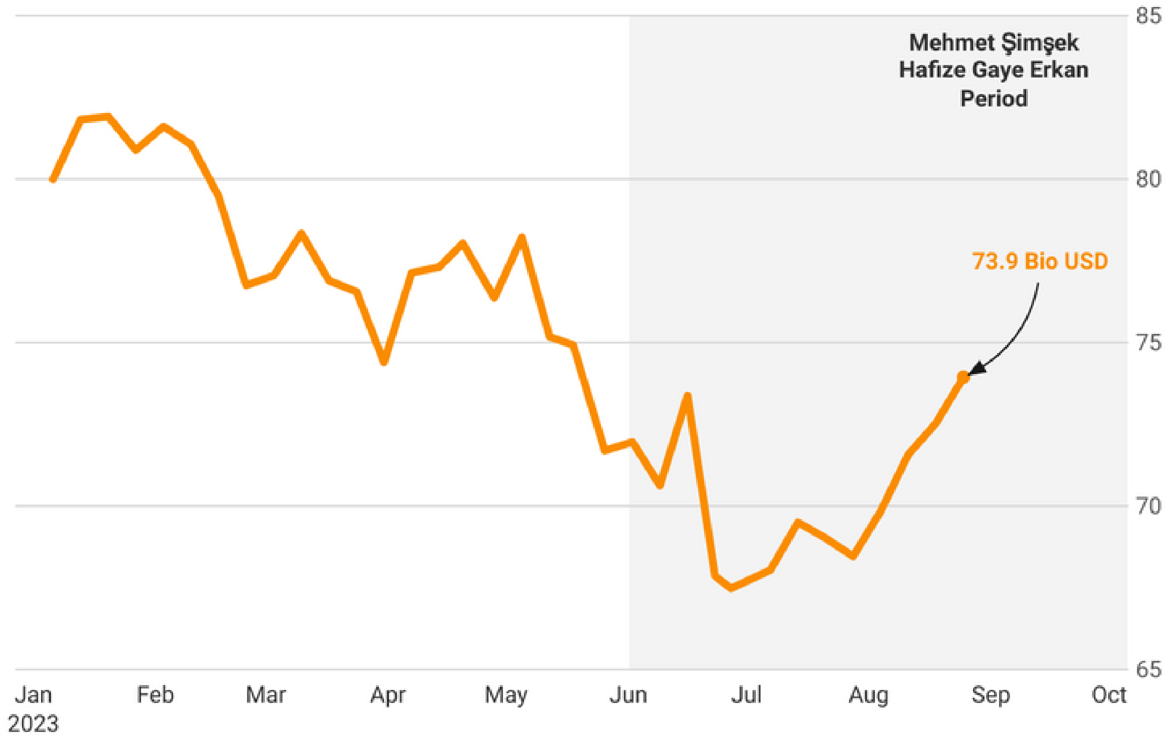
USD Deposit Interest Rates - 3M Maturity (August 25)



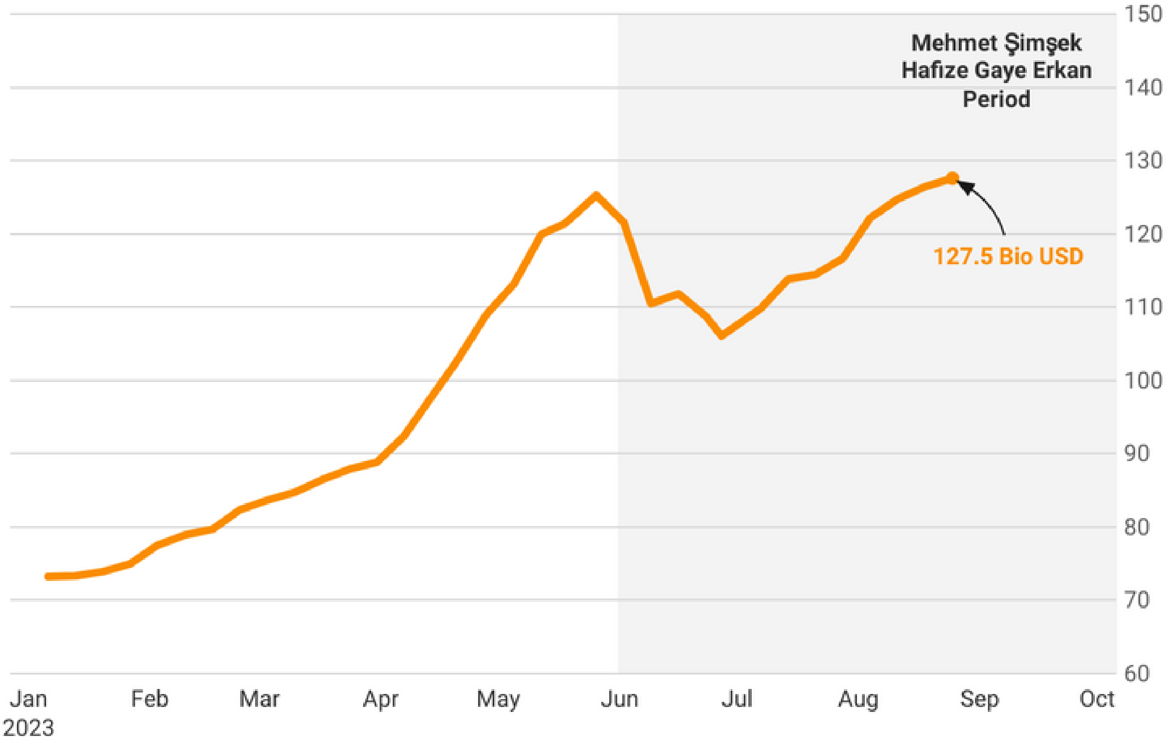
Retail FX Deposits (August 25)



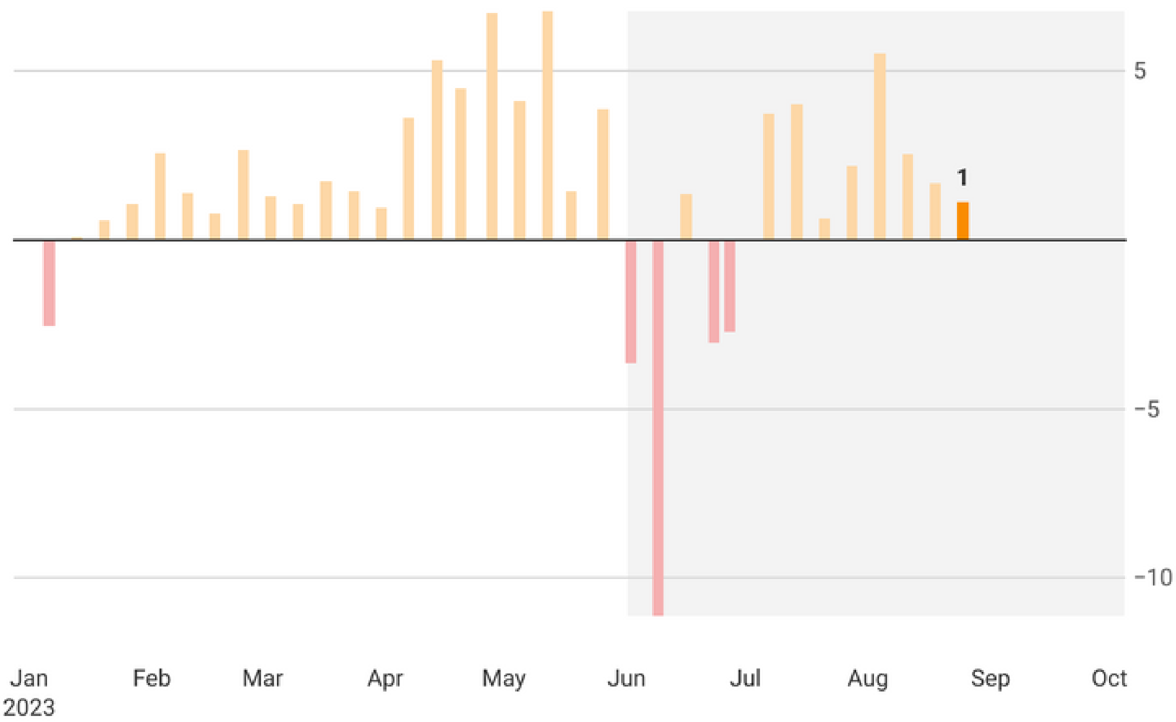
Commercial FX Deposits (August 25)



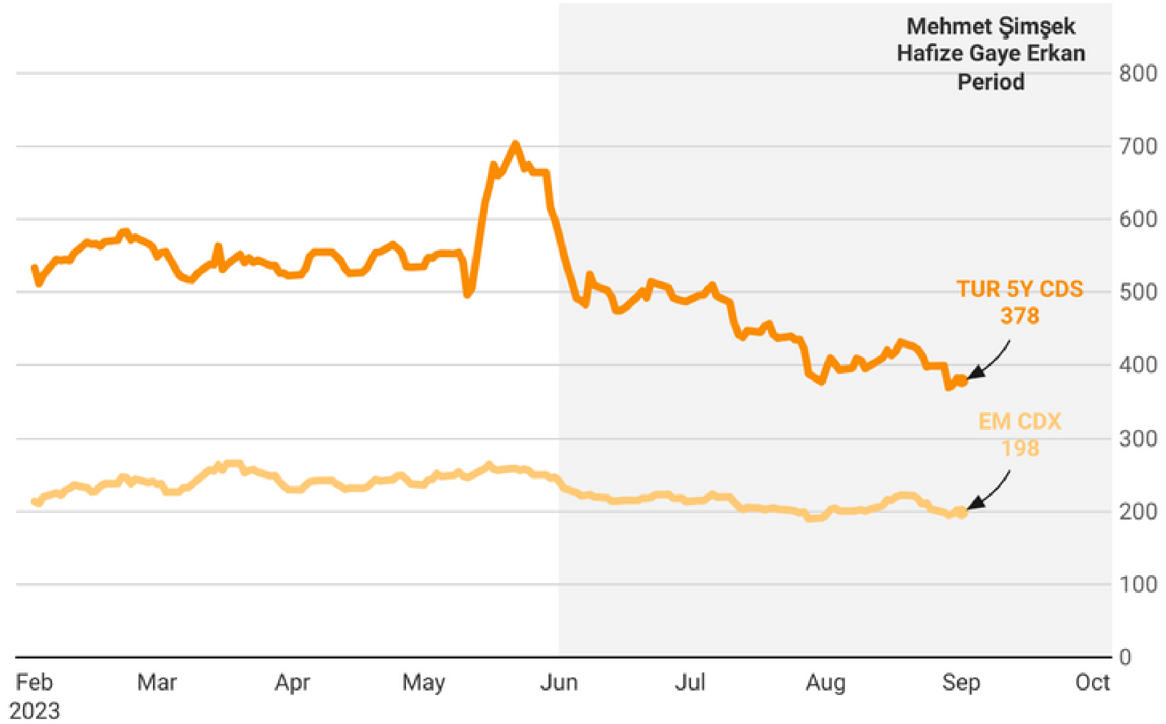
FX Protected TL Deposits (USD - as of August 25)



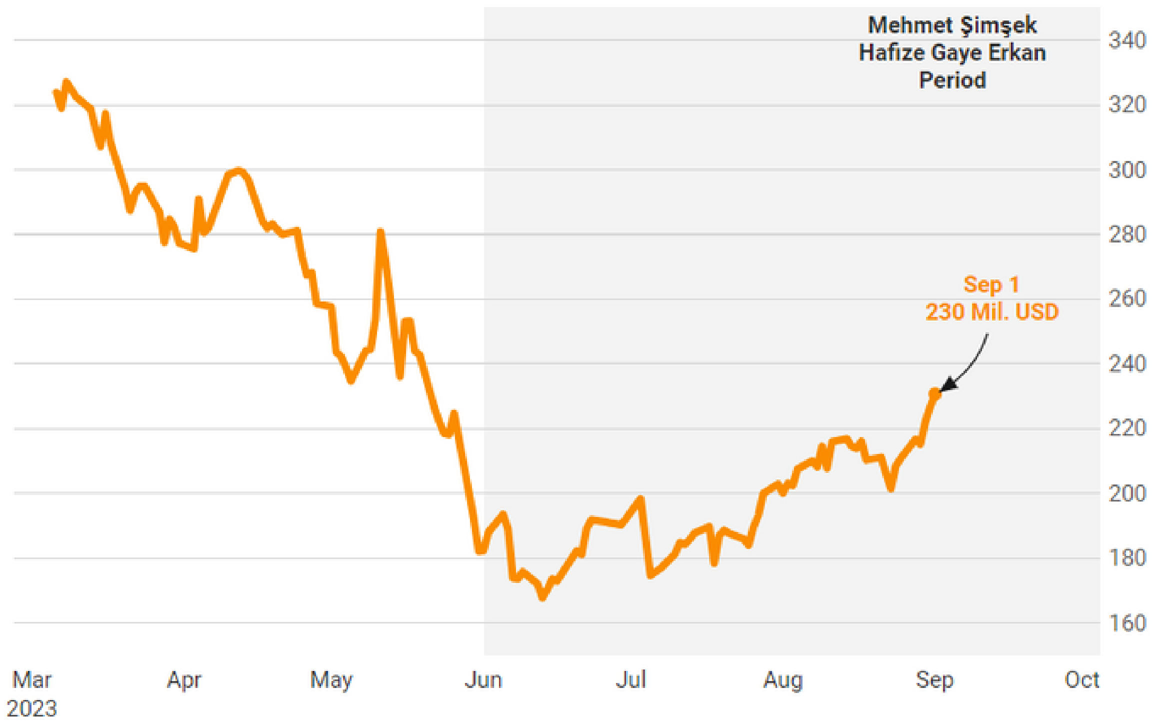
WoW Change (Bio USD)



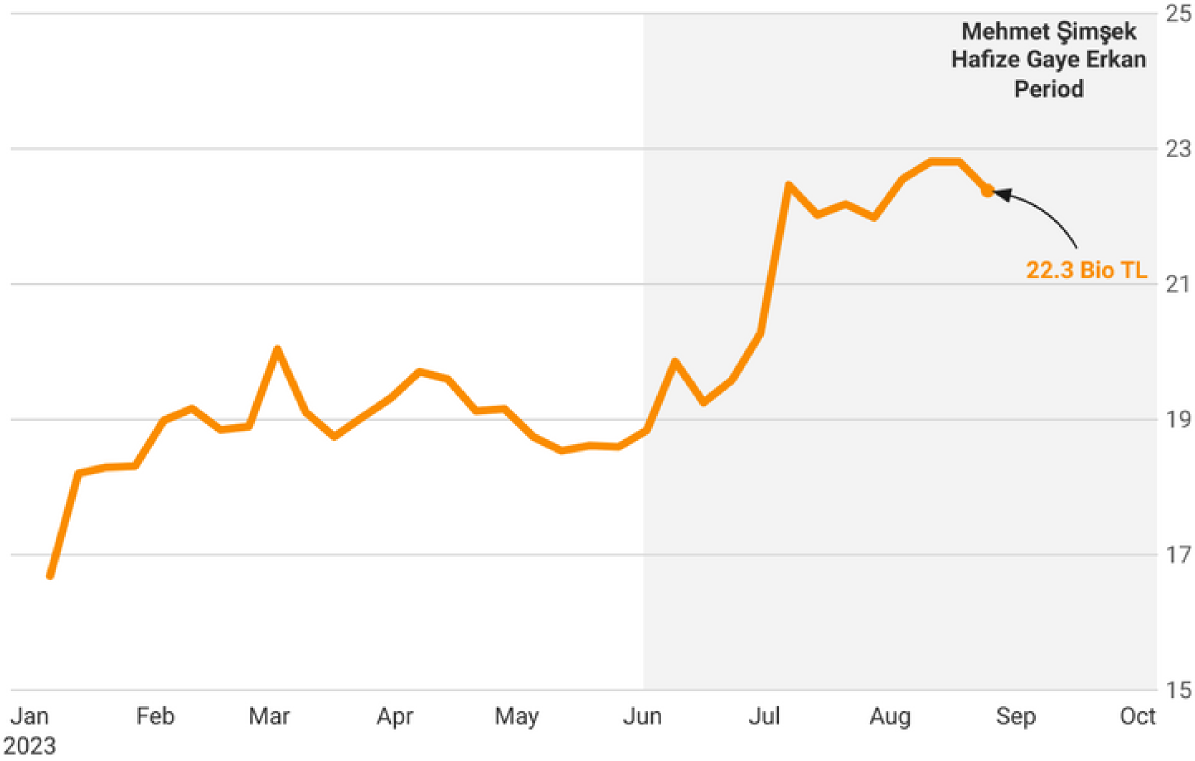
Sovereign Credit Risk (September 1)



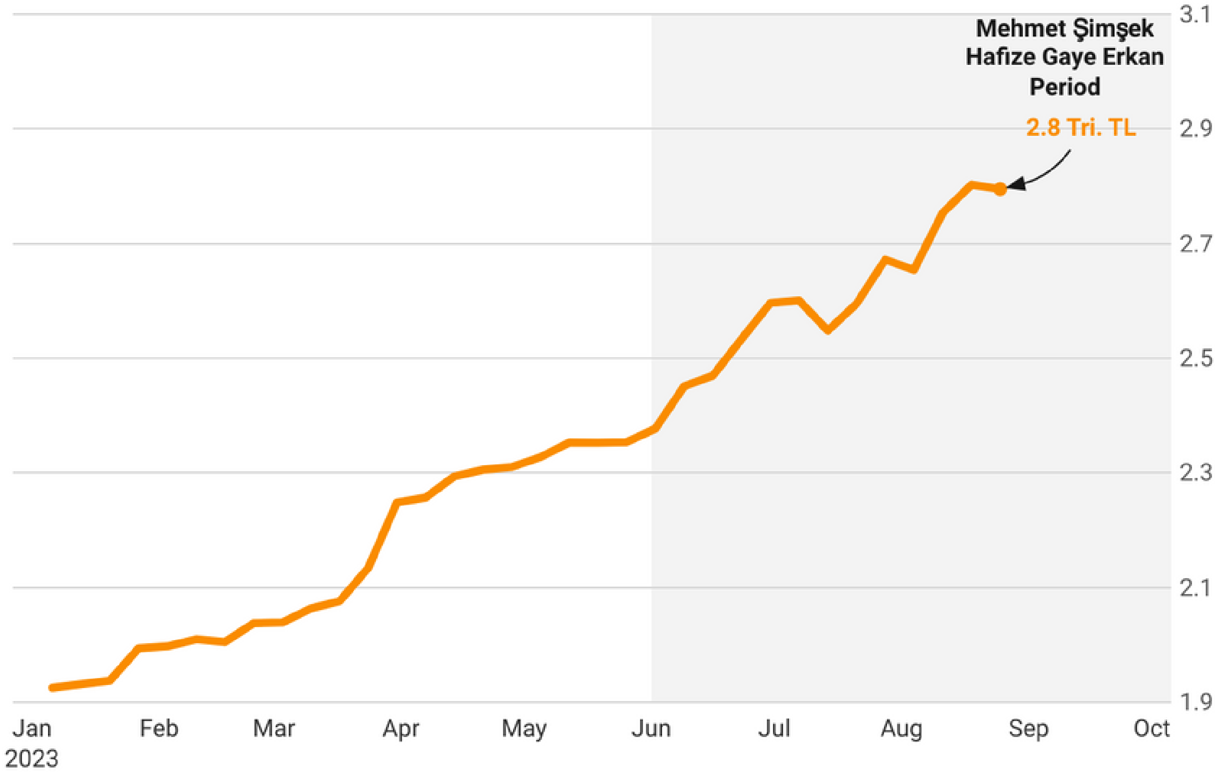
Ishares TUR ETF (AUM, Mil USD)



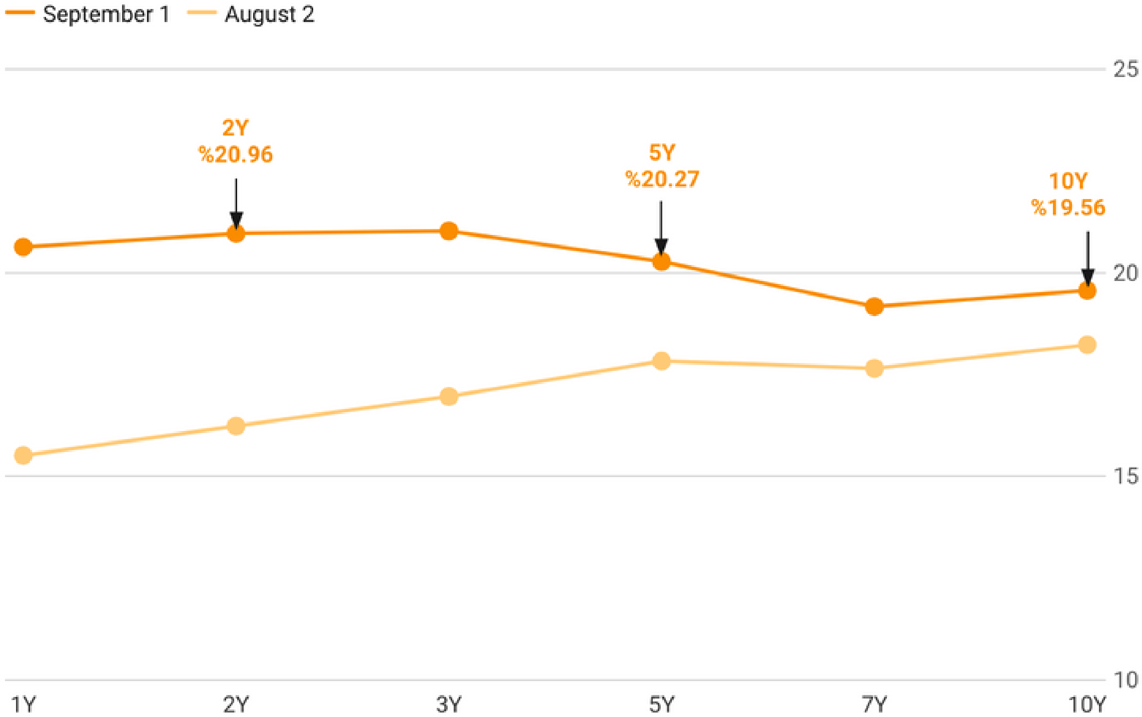
TL Treasury Bonds - Foreign Ownership (Nom, August 25)



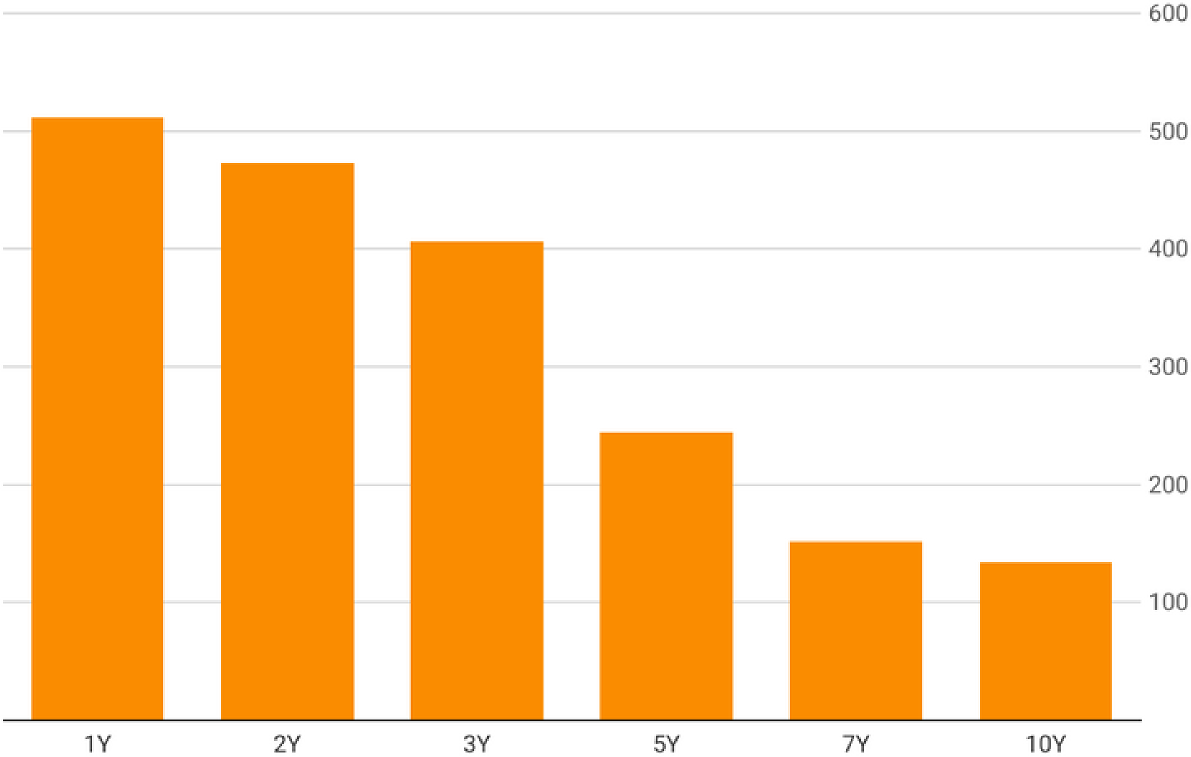
TL Treasury Bonds - Outstanding (Nom., August 25)



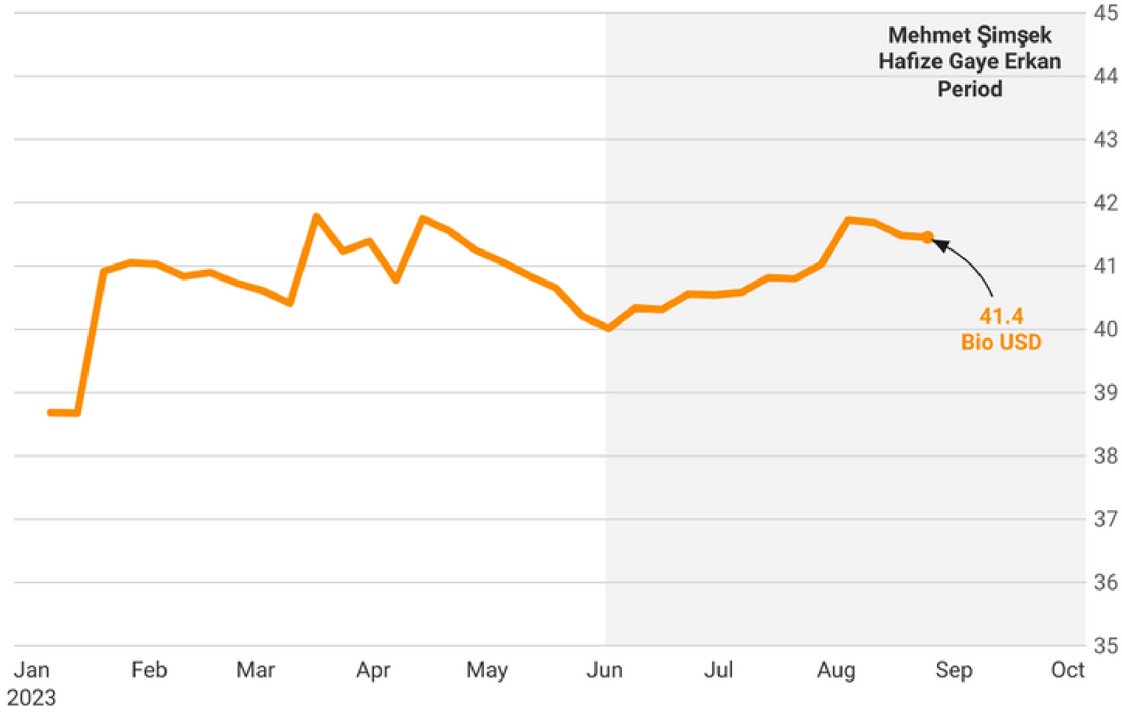
TL Sovereign Yield Curve (September 1)



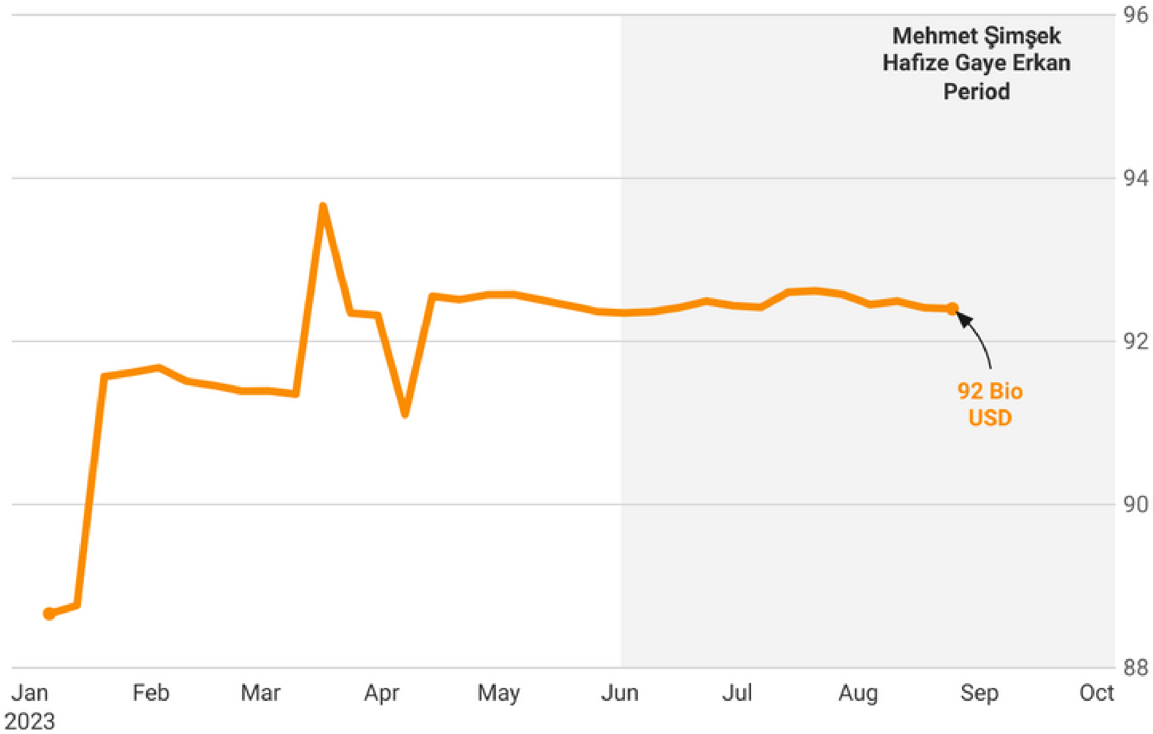
MoM Chg- basis points



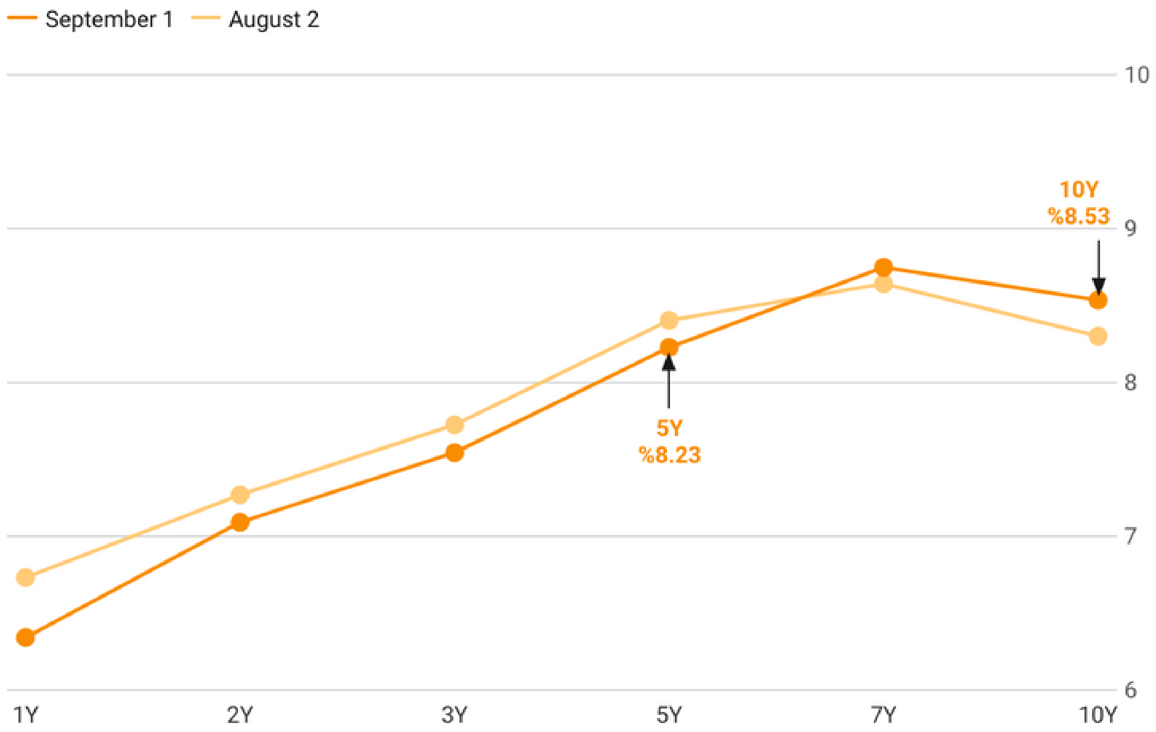
Eurobond- Foreign Ownership (Nom., August 25)



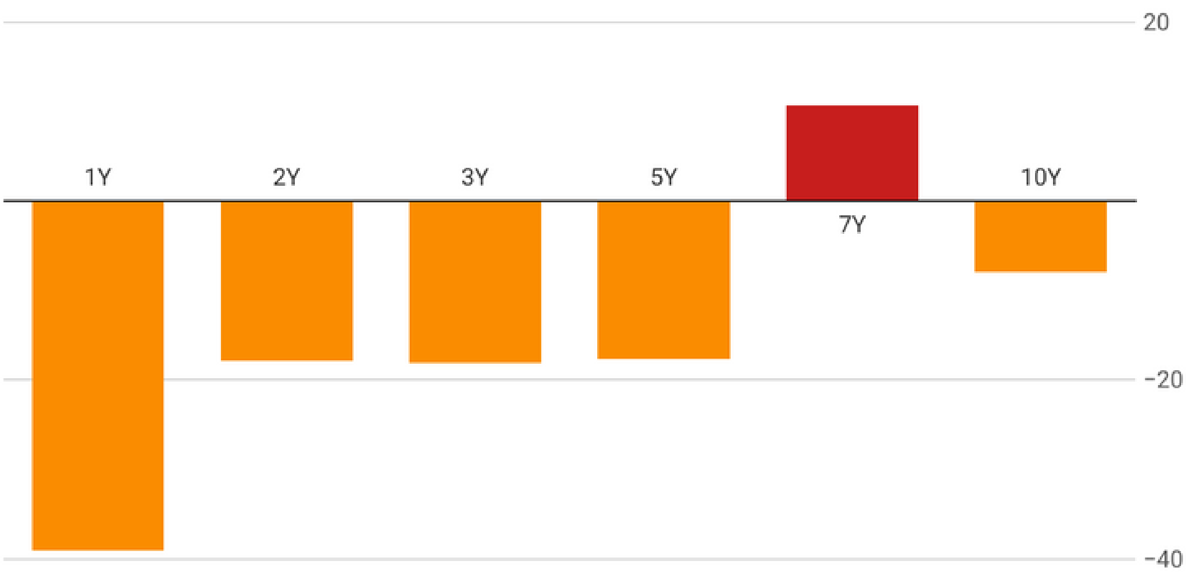
Eurobond- Outstanding (Nom., August 25)

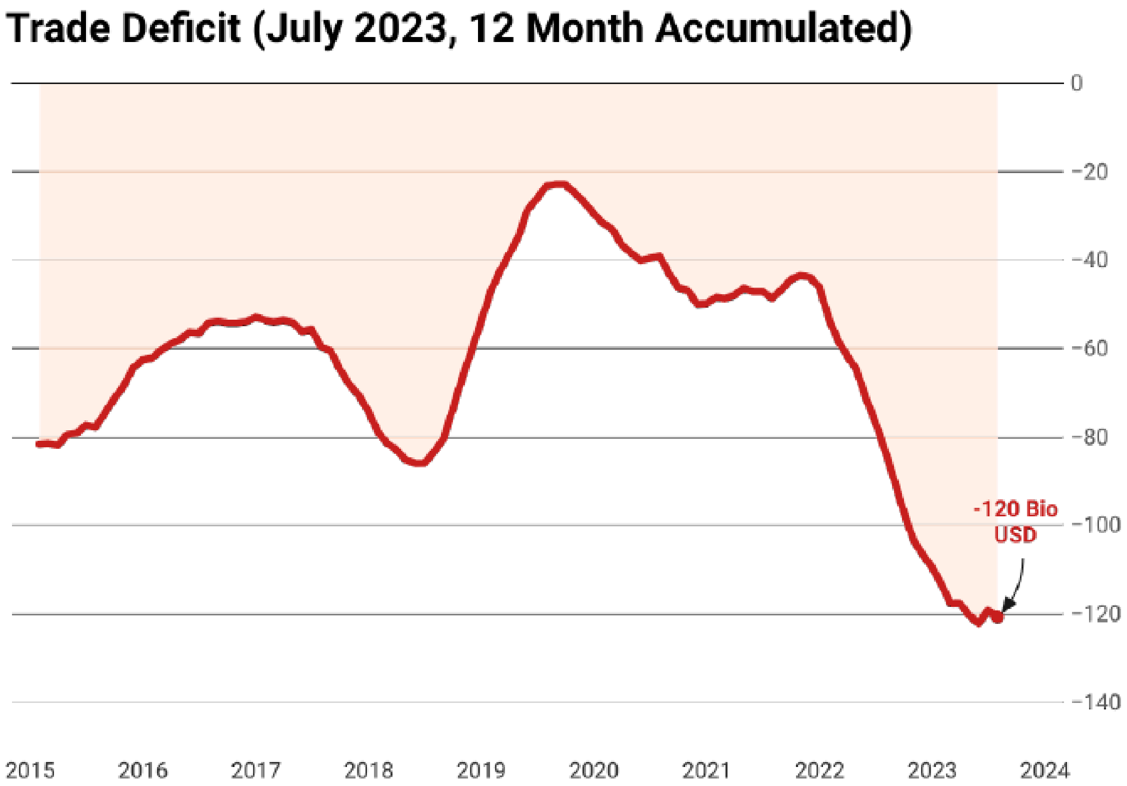


USD Sovereign Yield Curve (September 1)



MoM Chg- basis points





	July 2023	July 2022	YoY%	YTD 2023	YTD 2022	Ytd YoY%
Balance	-12.217	-10.702		-73.539		
Exports	20.078	18.537	8.3%	143.287	144.227	-0.7%
Imports	32.295	29.239	10.5%	216.827	206.505	5.0%

NOTE: Levels in USD/billion.

Supersized Rate Hike Spurs Massive Rally Across Turkish Markets

· Lira, stocks jump on much higher-than-expected rate increase

· Move seen as pivot into orthodox measures to curb inflation

By Beril Akman

Turkey's central bank's jumbo interest-rate increase triggered a major rally in the country's assets on hopes that it augurs the unwinding of policies that have sent foreign investors fleeing the $900 billion economy.

The Turkish lira, long one of the world's worst-performing currencies, surged the most in almost two years following the announcement on Thursday, to gain nearly 8% against the dollar. Local banking shares jumped, increasing by the maximum regulatory limit of 10%, as dollar bonds advanced. The cost to insure government debt against default plunged.

The Monetary Policy Committee, with newly appointed members led by Governor Hafize Gaye Erkan, surprised markets with a bigger-than-expected hike for the first time since she was appointed in June, raising the benchmark one-week repo rate to 25% from 17.5% in the sharpest increase since 2018. Most economists polled by Bloomberg predicted a hike to 20%.

“Great to see the Turkish central bank wake up the global market from its summer lull, showing it's in charge,” said Simon Quijano-Evans, chief economist at Gemcorp Capital in London. “Most central banks out there currently have negative real rates. Turkey has more, but it's getting there, one needs to think positive.”

The move is the strongest indication yet that Turkey's new administration is prepared to abandon its unorthodox policy set – most notably ultra-low borrowing costs, which even after the increase on Thursday still stand more than 20 percentage points below the latest inflation reading of almost 50%.

JPMorgan revised its estimates for benchmark interest rates and now expects a 250 basis-point hike at each meeting by the end of the year, bringing the year-end policy rate forecast to 35% from 30% previously. Meanwhile, the jump in the currency led Citigroup strategists to close a long dollar-short lira trade recommendation made just a couple of days earlier.

What Bloomberg Economics Says...

Lira Leads Emerging Market Drop After Jackson Hole Remarks

· Turkish lira weakens 2.8% as EM stocks and currencies slump

· Lira may be EM star if Erdogan supports hikes: InTouch's Matys

By Netty Ismail and Colleen Goko

Turkey's lira slumped as the euphoria surrounding Thursday's jumbo interest-rate hike subsides, with questions arising over whether the aggressive move has the blessing of President Recep Tayyip Erdogan.

The lira lost as much as 2.8% against the US dollar on Friday, the worst performance across developing markets which erased about half of the currency's gains from Thursday. Weaker global sentiment amid uncertainty over US interest rates also pushed emerging-market currencies into the red for the first time in four days.

MSCI's index of emerging market currencies slipped 0.2% after Federal Reserve Chair Jerome Powell delivered remarks at the Jackson Hole symposium in Wyoming on Friday. Powell signaled it's still too soon to declare victory over inflation, while saying the Fed "will proceed carefully" on whether to raise interest rates again.

Alejandro Cuadrado, Global Head of FX & Latam Strategy at BBVA, said the remarks reinforced "overall risk sentiment shakiness."

Concerns over China's sputtering economy also continued to weigh on emerging-marketsentiment. A short-lived rally in Chinese stocks after Beijing's latest attempt to shore up growth underscored the depth of investor pessimism toward the world's second-largest economy.

Defying the market pessimism, South Africa's rand outperformed peers, heading for its first weekly gain in four.

Expectations for investment flows are following a summit of the BRICS bloc – Brazil, Russia, India, China and South Africa – this week in Johannesburg.

Fading Rally

Turkish assets had rallied on Thursday after the Monetary Policy Committee, with newly appointed members led by Governor Hafize Gaye Erkan, surprised investors with an increase in the benchmark one-week repo rate of 7.5 percentage points to 25%.

The buying-spree proved short lived though, with investors bracing for the risk of more political meddling in monetary policy. Erdogan has chased out three central bank governors since 2019, spurring an exodus of capital that has weighed heavily on the lira.

“If in the coming days President Erdogan comments on the latest stunning decision and he strongly indicates that Governor Erkan and her team have his full support, the lira may become one of the most popular EM currencies,” said Piotr Matys, a currency analyst at InTouch Capital Markets. “At least until the Turkish president decides to reshuffle the Turkish central bank once again.”

Heavy corporate demand for dollars helped to drive the lira lower on Friday, according to traders familiar with the matter, who asked not to be identified because they weren’t authorized to speak publicly.

Companies are concerned that the currency’s rally will fade and see the current level as a dollar-buying opportunity, they said. Turkish firms with large foreign-currency positions tend to buy hard currencies when the lira rises. According to the latest central bank data, the net open FX position of non-financial companies stood at $81.5 billion in May.

Turkish Economy Slows Less Than Forecast as Rate Hikes Loom

· The $900 billion economy grew by 3.8% in second quarter

· Goldman says Turkey will probably enter recession this year

By Baris Balci

Turkish growth slowed less than predicted in the second quarter, though activity is set to be subdued for the rest of the year as officials seek to put the economy on a more sustainable footing by raising interest rates.

Gross domestic product expanded an annual 3.8% from a downwardly revised 3.9% in the first three months of the year, according to data published on Thursday. Estimates in a Bloomberg survey of analysts ranged widely, with the median forecast at 3.1%.

Consumer demand and government spending ahead of May's elections were major contributors to growth during the three-month period, the data showed.

Below are some of the highlights from the GDP report:

· Quarter-on-quarter growth quickened sharply to 3.5% in seasonally and working-day adjusted terms.

· Government spending rose by 5.3% in annual terms, down from 6.1% in the Jan.-March period. Imports were up 20.3% from a year earlier while exports were down by 9%.

· Industrial sector shrank 2.6% on an annual basis; agricultural output rose 1.2%.

Post-Election Policies

Leading indicators, including retail sales, had suggested consumption remained strong in the second quarter thanks to heavy pre-election spending by President Recep Tayyip Erdogan.

Erdogan, who won reelection to take his rule into a third decade, has since signaled a shift away from unorthodox policies – including ultra-low borrowing costs – that he championed in recent years but which caused foreign investors to flee the $900 billion economy.

The president’s new economic team, led by Finance Minister Mehmet Simsek and central bank Governor Hafize Gaye Erkan, is trying to slow inflation of almost 50%, which has inflicted a severe cost-of-living crisis on Turks.

Following Thursday’s report, Simsek said he wants to put growth on a “balanced and sustainable” path by reducing Turkey’s foreign-trade gap.

Still, Erdogan may encourage them to strike a balance and boost growth ahead of local elections in March. The president wants to recapture the mayor’s seat in Istanbul after suffering a stinging defeat there four years ago.

What Bloomberg Economics Says...

“Turkey’s 2Q GDP print carries signs of things to come: slower growth supported by domestic consumption- even as high price gains squeeze consumer spending power. It also points to a likely risk of higher fiscal stimulus before March’s local elections - countering the impact coming from tighter monetary policy.”

– Selva Bahar Baziki, economist.

Lira Options Least Bearish in 17 Months After Massive Rate Hike

By Tugce Ozsoy

Turkey's surprisingly large interest-rate increase last week so far hasn't significantly propped up embattled lira but it has cut the cost of insuring it against depreciation to the least in 17 months.

The spread in the premium on six-month options to sell the lira versus the dollar rather than buy the currency – known as the 25 Delta risk reversal – fell to 10.6%, the lowest level since March 2022.

The central bank hoisted its main rate by 750 basis points to 25%, spurring a sharp but ultimately short-lived rally in the lira. With inflation running at close to 50%, economists said hefty further tightening was needed to rebalance the economy, and it's not clear if President Recep Tayyip Erdogan – who has a track record of changing central bank governors – will back these potentially painful moves.

“This bold monetary-policy decision clearly improved market sentiment toward the lira as reflected in the costs of hedging,” said Piotr Matys, a currency analyst at InTouch Capital Markets. “That said, many traders who have a long experience of trading the lira most likely are wondering how long it may last this time.”

Global Banks Tear Up Forecasts for Turkish Rates After Huge Hike

By Beril Akman

Economists at the world's biggest lenders have a lot of catching up to do in rewriting forecasts for Turkish interest rates after the central bank blindsided the market on Thursday with an unexpectedly steep hike.

But with the lira coming under renewed selling pressure, policymakers likely won't stop a monetary tightening cycle that already delivered the biggest rate increase in years to lift Turkey's benchmark by 7.5 percentage points to 25%.

Global banks from Morgan Stanley to Barclays Plc and JPMorgan Chase & Co. now say rates will reach at least 30% by the end of the year, reflecting expectations of a massive shift from the central bank's earlier guidance of "gradual" tightening.

· Morgan Stanley revised its forecast for Turkey's terminal rate to 30%. The US bank previously forecast the key rate at 20% at year-end and then saw a cut

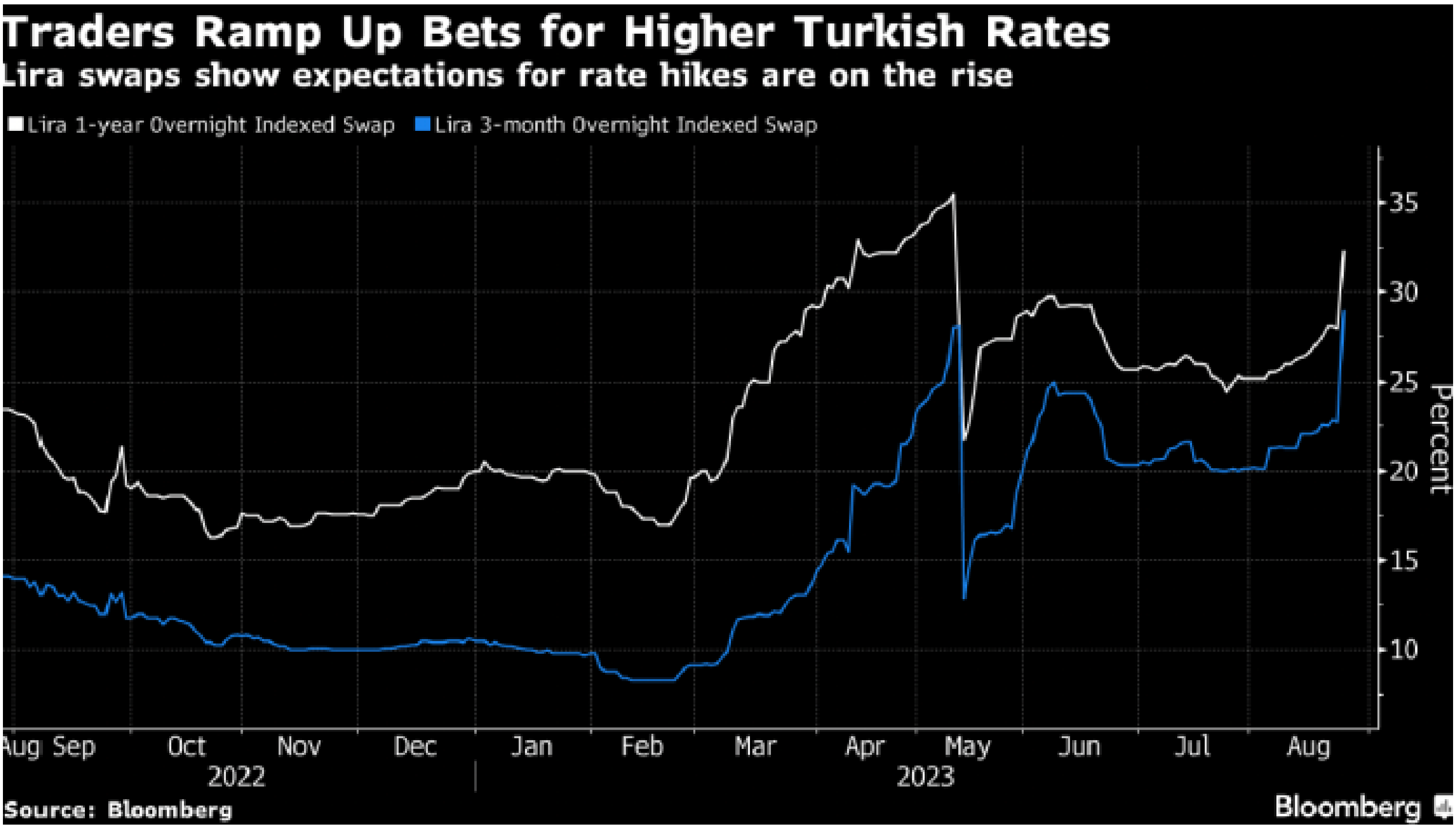
· JPMorgan now sees 250 basis-point hikes in each policy meeting by the end of 2023, moving its year-end call to 35% from 30%

· Barclays puts the year-end policy rate at 35% and 40% by the end of 2024

The Turkish central bank "delivered a major positive surprise," Barclays analysts said in a report on Friday. "This flies in the face of the commonly held analyst/market view that the policy rate is psychologically capped at 25%."

The emerging outlook is aligning with market expectations that monetary policy should be much tighter still.

The Turkish currency's overnight indexed swaps – derivatives used to bet on future borrowing costs – are showing expectations for higher rates ahead. The one-year contract spiked to 33.5%, the highest level since before elections in May, from 28% on Wednesday.



"We believe the Turkish central bank's move was important in terms of limiting the volatility in FX," said Mustafa Oner, an analyst at ICBC Turkey Investment. "It is a positive and effective action for the short-term."

The surprise decision already appeared to carry less sway with traders on Friday, with the lira weakening as much as 2.7% against the US dollar. It's the worst performance across emerging markets, erasing about half of the currency's gains from Thursday.

From BlackRock to Pimco, Bond Investors Bet Fed Hiking Is Over

• Two-year notes are a 'screaming buy': BlackRock's Rosenberg

• 'The trade to be in is steepeners,' says Rajappa at SocGen

By Ye Xie and Michael Mackenzie

For the first time since the Federal Reserve started raising interest rates almost 18 months ago, the labor market is showing enough cracks to embolden some of the world's largest bond investors to bet that the tightening cycle is finally ending.

A spate of slowing employment metrics this week, crowned by Friday's August payrolls report, has shifted market sentiment in favor of owning policy-sensitive two-year Treasuries, which BlackRock Inc.'s Jeff Rosenberg called a "screaming buy."

The prospect of the Fed wrapping up its most aggressive tightening campaign in decades also drew investors to another favorite end-of-cycle trade – a steepening yield curve. The wager is that as the focus shifts to the timing of a potential Fed pivot to easing, short-maturity notes will fare better than long-term bonds. The strategy may also be benefiting from a seasonal tendency: Companies typically rush to sell debt after the US Labor Day holiday, putting pressure on long-duration bonds.

The jobs data leaves "the bond market comfortable with the view that the Fed is on hold for now and maybe done for the cycle," said Michael Cudzil, a portfolio manager at Pacific Investment Management Co., which oversees $1.8 trillion. "If they are done for the hiking cycle, it's then about looking at the first cut that leads to steeper curves."

While inflation has been trending lower in recent months, a resilient job market has been the main stumbling block for the Fed to stop hiking after raising the borrowing costs by 525 basis points since March 2022, to a range of 5.25%-5.5%.

But now the labor backdrop appears to be cooling. A government report Friday showed that the unemployment rate jumped to 3.8%, a level last seen in February 2022, and wage growth moderated. It was the third soft labor-market release of the week, following weaker-than-expected job openings data and an ADP Research Institute report showing slowing job additions by US companies.

Bond investors cheered the data after a relentless selloff in August saw 10-year yields hit the highest since 2007.

What Bloomberg's Strategists Say...

"While it would be a little foolhardy at this juncture to completely write off the chance of another rate hike,at this point it doesn't seem like the Fed will need to go again. That may open a window of opportunity for bonds to rally in nominal terms, though it's an open question of whether real returns can go positive on the year.."

Short-term Treasuries outperformed on Friday, sending the yield curve steeper. Two-year yields dropped roughly 20 basis points on the week to below 4.9%. Meanwhile, 30-year yields were little changed on the week at around 4.30%, after rising above five-year yields for the first time in weeks.

The employment reports looked like "the beginning of the end of the robust job market and the countdown for how long can the Fed stay on hold," said George Goncalves, head of US macro strategy at MUFG. "This will favor the front-end versus the back-end," he said, adding that two-year yields could fall toward 4.5%.

Interest-rate swap traders see slightly less than a 50% chance of another hike by November. After that, they've fully priced in a quarter-point cut by June.

As wage growth cools, Rosenberg, a portfolio manager of BlacRock's $7.4 billion Systematic Multi-Strategy Fund, said the Fed has to lower borrowing costs to avoid thereal rate - or inflation-adjusted policy rate - from tightening.

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