

FORTIS BANK

Macro Scope

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Weekly Economic and Strategic Review

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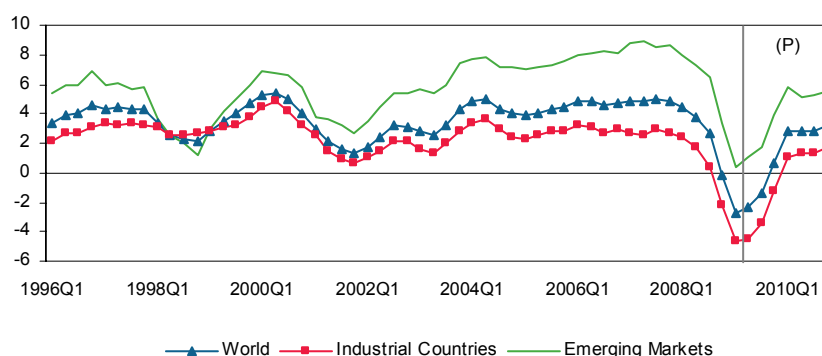
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Growth, First Minus Then Lifeless...

IMF's last World Economic Outlook (WEO) Report "Sustaining the Recovery" introduced mostly upward revisions for growth projections, as we presumed, and re-emphasized that the nascent recovery would be slow and vulnerable. Accordingly, IMF urged the countries to preserve their expansionary monetary and fiscal policies for some more time, while at the same time to be ready for exit strategies from these policies, should the recovery turns more apparent. **While giving the scenario for the global economy, IMF described the rebound to be sluggish, credit constrained and, for some time, jobless.** The global growth forecasts at 3% for 2010 and 4% for the average of 2011-2014 remained below the average performance of the previous years. More specifically, the global economy is expected to widen by 3.1% in 2010 following an estimated 1.1% contraction in 2009. The U.S. economy is foreseen to expand by 1.5% in 2009 after declining by 2.7% in 2010, while the figures are pointing to a 4.2% contraction and 0.3% positive growth for the Eurozone economy in 2009 and 2010, respectively. Turkey was one of the few countries that are now estimated to grow visibly less in 2009 than previously assumed. The Turkish economy, which was foreseen to contract by 5.1% in 2009 beforehand, is now anticipated to shrink by 6.5%. This was a deeper retrenchment than both the Medium Term Program (MTP) assumption and our projection. On the other hand, the revision in the 2010 growth forecast was much more striking. The 1.5% growth projection for 2010 is now revised markedly up to 3.7%, surpassing slightly the one suggested in MTP and coming closer to our view for 4% expansion. **While the inflation and current account deficit forecasts were not much different from the MTP, the estimates for the fiscal framework were not published in the WEO. Therefore, it remained uncertain whether the convergence in the macroeconomic framework was also valid for the fiscal front.** However, IMF Chief stated that they will continue negotiating with Turkey, giving the impression that the potential disagreements may not prevent a deal.

World Economic Outlook – Growth Forecasts (%)



Source: WEO October 2010, Fortis Economic Research and Strategy

Meanwhile, in the Financial Stability Report released a day earlier than the WEO Report, IMF revised the estimate for global writedowns on credit originated in mature markets over 2007-10 down to US\$3.4trn from US\$4trn. **While the Fund said that the stronger bank earnings are supporting capital levels, they are not expected to fully offset writedowns over the next 18 months.** Based on their revised methodology, the bank writedowns on both loans and securities reached US\$1.3trn between 2Q2007 and 2Q2009. Moreover, the Fund estimates US\$1.5trn potential additional writedowns until end-2010. Putting in percentages, **IMF says U.S. banks have recognized about 60% of anticipated writedowns, while Euro area and U.K. banks have recognized about 40%.** Systemic risks have been substantially reduced, the Fund said, yet emphasized that there are important risks regarding the monetary and fiscal policies. In the Report, the need for the financial system to provide the sufficient credit growth for sustaining the nascent economic recovery was underlined, along with the importance of an appropriate policy to withdraw the measures taken to tackle the crisis and of managing the pressure on sovereign balance sheets.

Meanwhile, in order to grasp the current pace of the global economic recovery, we now turn to the PMIs that are the most useful leading growth indicators. As of September, the PMIs in many developed and developing countries continued surfacing above the critical 50 threshold that separates the expansion and contraction periods, yet the synchronized strong gains observed in the early stage of the exit from recession have been replaced by more subdued increase or slight declines, indicating that the recovery is cutting pace. The U.S. PMI edged down vs. the previous month, yet remained above 50, similar to the Japanese PMI at 54.5. The U.K. and the Eurozone indices are a touch below the 50. In the developing universe, Chinese (54.3), Indian (55.0) and Russian (52.0) PMIs suggested that the recovery is running its course. Despite the two-month consecutive declines, the Turkish PMI at 53.3 hinted at a mild recovery. All in all, the picture gives hope that in the following months, external demand may start supporting the recovery at home that started on the revival of domestic demand. Even though exports fell by 30% y/y in September, the favorable base-year effect may trigger annual gains through the last months of the year.

In the previous weekly report we had stated that the Central Bank's view about the current outlook would be important in terms of the lower limit for the interest rates. The summary of last MPC meeting includes important information about this issue. **In brief, while CBT reiterated that the recovery will be slow and protracted, it was also stated that the consumption demand is in a weaker course in 3Q, the domestic and foreign demand continue to be weak and they are likely to remain anemic for quite some time, the moderate recovery in industrial production is likely to continue and the labor market conditions do not display a significant improvement.** This outlook has been taken as a signal for the continuation of the interest rate cuts, as we presumed. Moreover, the Central Bank said that *"Given the increased perceptions that the economy had reached a turning point, it was concluded that a slowdown in the pace of rate cuts might be considered, keeping the options open depending on incoming information"*. We read this statement as a **reduction in the amount of upcoming rate cuts to 25 bps.** This was also in line with our preceding assumptions. Our readers would remember that, we expect the policy rates coming down to 6.5% in the year-end, being slashed by 25 bps each in the following 3 meetings.

Separately, the Bank left the door open for a longer rate cut cycle, highlighting the Turkey's risk premium. Bank underlined that the country risk may be affected by two main channels. **The positive perception about the resilience of Turkish financial system** was stated as one of these channels. The other important channel that may affect the risk premium was fiscal policy in the Bank's assessments. The Bank said that *"Should the framework outlined in the Medium Term Program be supported by structural adjustments which enhance fiscal discipline, the improvements in sovereign credit risk might continue"*. The first channel would put downward pressure on the F/X rates

while the latter would put downward pressure on the interest rates. Under both circumstances, the CBT would react by extending the easing cycle more than was envisaged in the Inflation Report.

All in all, the pictures depicted by IMF for the world economy and CBT for Turkey, suggest slow and gradual recovery in the economic activity. Moreover, based on the most up-to-date leading indicators, the strong monthly increases printed in a synchronized manner in the early stage of the exit from recession, lost some momentum and started pointing to a deceleration in the economic recovery. Therefore, there still appears some more space for the monetary policy maneuvers in the countries where output is far less below their potential, such as Turkey.

Economic and Political Agenda

▪ This week, at home the industrial production due Thursday will be on the forefront. Meanwhile, IMF- WB meetings in Istanbul on October 6th – 7th will be eyed closely. Separately, the Treasury will issue discount bond and CPI-linked bond on Monday together with the new benchmark bond, fixed income bond and FRN on Tuesday ahead of Wednesday's TRY16.7bn domestic debt redemption, with TRY14.9bn portion being destined to the market. In the external arena, the services PMI will be important both in Eurozone and U.S., while BoE and ECB are expected to stay on hold.

Data issuances at Home

Importance	Indicator	Unit	Date of issuance	Fortis (Consensus)
High	Industrial Output, Aug.	% y/y	Oct. 8 th , 7:00 GMT	-4.0
Weak	Cash Based PS, Sep.	TRY bn	Oct. 8 th , 14:00 GMT	-
Medium	CB's Expectation Survey, Oct. I	-	Oct. 8 th	-

Importance	Country	Indicator	Unit	Date of Issuance	Consensus
High	Eurozone	Services PMI, Sep.	-	Oct. 5 th , 7:58 GMT	50.6
High	U.S.	Non-manufacturing ISM, Sep.	-	Oct. 5 th , 14:00 GMT	50.0
Medium	Eurozone	GDP (final), 2Q	% q/q	Oct. 7 th , 9:00 GMT	-4.7
Medium	U.K.	BoE Rate Decision	bps	Oct. 8 th , 11:00 GMT	no change
Medium	Eurozone	ECB Rate Decision	bps	Oct. 8 th , 11:45 GMT	no change
Weak	U.S.	Foreign Trade Balance, Aug.	US\$ bn	Oct. 9 th , 12:30 GMT	32.0

Macro-Economic and Financial Forecasts

Macro Economic Outlook of 2007-2010

	2008	2009f	2010f	2011f
GDP (TRY - bn)	950.1	926.2	1,016.0	1,123.4
GDP (US\$ - bn)	734.9	597.5	647.1	683.5
GDP Growth (y/y % chg)	0.9	-6.0	4.0	5.0
PPI (y/y % chg)	8.1	4.0	5.0	4.0
CPI (y/y % chg)	10.1	5.5	6.5	5.5
Trade Balance (US\$ - bn)	-69.8	-36.1	-62.6	-67.4
Exports (FOB, excl. luggage trade)	132.0	94.5	106.2	106.1
Imports (CIF, incl. gold)	201.7	130.7	168.8	173.5
Current Account Balance (US\$ - bn)	-41.5	-11.0	-31.9	-34.0
Current Account Balance / GDP (%)	-5.6	-1.8	-4.9	-5.0

Financial Indicators Forecasts

	Oct. 2 nd	1M	3M	6M	12M	2009	2010
US\$/TRY	1.4832	1.5000	1.5000	1.5600	1.5800	1.5000	1.5800
EUR/TRY	2.1616	2.1900	2.1300	2.1800	2.0500	2.1300	2.0500
FX Basket	3.6448	3.6900	3.6300	3.7400	3.6300	3.6300	3.6300
EUR/US\$	1.4574	1.4600	1.4200	1.4000	1.3000	1.4200	1.3000
O/N	7.25%	7.00%	6.50%	6.50%	7.50%	6.50%	9.00%
Benchmark Bond	8.60%	8.50%	9.50%	10.00%	11.00%	9.50%	11.00%

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