

# FORTIS BANK

## Macro Scope

25 - 31 May 2009

## Weekly Economic and Strategic Review

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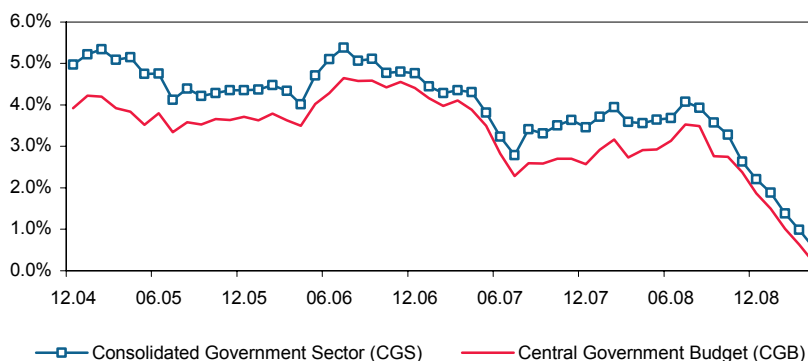
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### Live Up With Or Give Up IMF...

It has been more than one year now since Turkey finalized the last IMF program. Despite the expectations that the new economy team in the cabinet would accelerate the talks, the clarity on the deal is still lacking and the significant delay in the program is yielding doubts on whether the stand-by deal would indeed be signed at all. In our own baseline scenario, we assumed that the IMF deal would be signed. However, we have been warning that the agreement may possibly be delayed, given the substantial deterioration in the fiscal outlook, which has also been hit with the current dismal conjuncture. After all, the fiscal framework depicted by the government for a long time would have hardly allowed for a smooth progress in the IMF deal. **However, even in the absence of an IMF program, the market indicators would unlikely be adversely affected in the short term amidst the current favorable atmosphere, as the hopes that the worst of the crisis is behind, underpin the risk appetite. The key reason behind is the fact that the pessimistic scenarios once assumed for the credit flows and portfolio flows are now shelved in parallel to the growing recovery prospects for the global economy.** In essence, when sudden stop in capital flows first becomes apparent, the balance of payment problems turn to be the key risk and the IMF program turns to be vital in order to overcome this bottleneck. However, once the sentiment regarding the capital flows starts improving, this has the potential to alter the risk perceptions about the BoP (higher debt roll-over ratios, lower external financing gap). **Such a transformation in perceptions is actually an indication that the risks are shifted towards other areas.** Being aware of such risks, we had written in our April 20<sup>th</sup> *MacroScope* that the focus of the IMF program may shift to the public finance, even though the idea behind the program was initially originated to save the private sector from the adverse repercussions of balance of payment crisis.

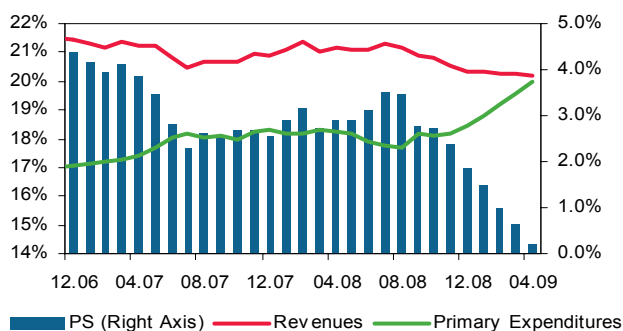
Program-Defined Primary Surplus (% of GDP)



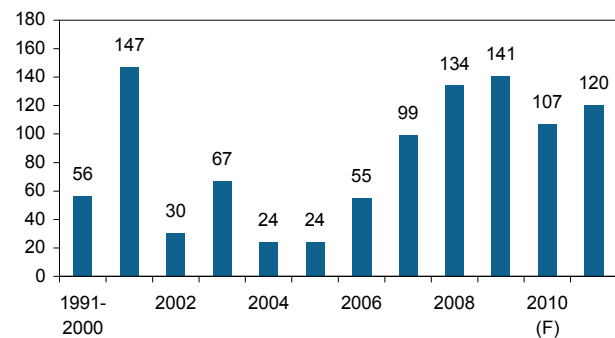
Source: Ministry of Finance, Fortis Research

Recently, various sectors are demanding the extension of the tax cuts or they are asking for similar exemptions for their own sectors, if there is not already one. Let alone these demands, even the weakness in the labor market suggested by the skyrocketing unemployment rate is by itself enough to worry us about the downside risks on the budget and primary balance. The measures launched so far (either revenue cutting or expenditure boosting) are known to add TRY19.1bn and TRY15.3bn burden on the budget in 2009 and 2010, respectively. Given the current outlook, further measures should be expected going forward. The fresh April figures on budget suggest that there is further deterioration in the primary surplus (PS) performance. The 12-month rolling PS in IMF definitions, which clean off the one-off revenues, slid to as low as 0.2% of the GDP, compared to 1.9% by the end of last year. In addition, the 12-month PS in the consolidated government sector, which also includes non-budgetary funds and SEEs, slumped to 0.6%, from 2.2% by the end of last year. Recall that in the Pre-accession Economic Program (PEP), the official forecast for the consolidated government PS was 0.6% for 2009, as compared to our forecast for 7.8% budget deficit and 1.7% primary deficit. Out of the 3.3 pp decline in the PS since July 2008, 2.2 pp is linked to the expansion in primary expenditures, while 1.1 pp is due to the decline in revenues. **It is striking to see that all of the deterioration in the PS over the last three months is solely linked to the surge in primary expenditures. That is to say, the current contractionary economic cycle cannot explain all of the weakening in the fiscal performance.** The dismal performance of GDP and the primary balance, which is sliding to the negative territory, would reverse the downtrend in the debt to GDP ratio. Above all, let alone this year's ugly picture, what most concerns us is that there is not yet any sign of intention that the government would run policies to improve the outlook in the next years. Recall that in the framework depicted in PEP, the PS was projected to remain low in the following years, as well (0.5% and 0.6% of GDP in 2010 and 2011). However, rather than weighing on the market indicators in the short term, this weakness should weigh on the medium-long term growth outlook.

Central Government Budget, Key Indicators (IMF-defined, % GDP)



The Rank of Turkey's Growth Pace Among the Developing Countries \*



(\*) The realizations and forecasts in the IMF's World Economic Outlook Report (April 2009) were used and among the 150 emerging countries take place in the report, Turkey's rank was estimated. For example, while during 2004 and 2005 Turkey's growth rate ranks as the 24<sup>th</sup> highest among 150 developing countries, Turkey's rank slides to 134<sup>th</sup> ranking in 2008. Source: Finance Ministry, IMF, Fortis Economic Research and Strategy

As we mentioned in our monthly *Glocal Strategy* published last week, Turkey has been suffering a remarkably poor growth performance since 2006. During 2004 and 2005, Turkey's growth rate ranks as the 24<sup>th</sup> highest among 150 developing countries. Yet, there has been a rapid deterioration since 2006. Coming to 2008, Turkey is ranked as the 134<sup>th</sup>. Comparing the IMF forecasts for 2009 – their estimate for Turkey overlaps with our 5% contraction forecast (we have been sticking to this figure since February) – for the developing universe, Turkey's performance slides further to 141<sup>st</sup> row. Moreover, Turkey would be benefiting less from the global economic improvement compared to other emerging universe, given the deterioration in Turkey's relative performance, which is to remain unless a comprehensive economic program is launched.

"What if there is no IMF deal?" This is a question more frequently asked in the recent term. Nevertheless, the market believes that the IMF deal will eventually

be launched, even if it is delayed and Turkey would get the expected loan. While the answer to this question would not much change the results for 2009 economic outlook, it would affect the strength of recovery in the following years. In the meantime, this issue would likely be overlooked in case the global outlook keeps improving, lowering Turkey's need for IMF loan. **Even though the worries on Turkey's external financing need settle down, lack of a comprehensive economic program would increase the risk of relative weakness in the economic performance.** Such an outlook would also be problematic for the general macro economic balances. For instance; the total debt to GDP ratio regresses below 40% in our baseline scenario which assumes 4-5% positive GDP growth rate for the upcoming years, together with a tight budget outlook under the context of IMF deal. Yet, this ratio surges over 50% in the lack of IMF deal and 3% GDP growth assumption. This may increase the risk premium of Turkey and the performance of Turkish markets may weaken vs. the other emerging peers.

## Economic and Political Agenda

- At home, on Thursday the Central Bank will publish the summary of May 14<sup>th</sup> MPC meeting. We will be looking for the hints regarding upcoming rate decision. Separately, the Bank will also release the Financial Stability Report on Thursday.
- The Treasury will unveil its borrowing program on Friday. They foresee a fairly low domestic debt service of TRY4.2bn and foreign debt service of US\$1.6bn for June. We reckon that the most important domestic redemption at TRY3.8bn will be held on June 24<sup>th</sup>. For this week, ahead of TRY693mn redemption (TRY574mn portion is being destined for the market) on Wednesday, the Treasury will issue CPI-linked bond due 21.05.2014 on Tuesday.
- Glancing at external arena, in the U.S., the durable good orders (Thursday) and the 1<sup>st</sup> revision of the growth data (Friday) will be the key developments of this week. Separately, the markets will be closed in the U.S. and U.K. on May 25<sup>th</sup>.

### Data issuances at Home

Importance	Indicator	Unit	Date of issuance	Fortis (Consensus)
High	Real Sector Confid. Index, May		May. 25 <sup>th</sup> , 14:00 GMT	-
Medium	Imports, Apr.	US\$ mn	May. 29 <sup>th</sup> , 14:00 GMT	7,900
Medium	Exports, Apr.	US\$ mn	May. 29 <sup>th</sup> , 14:00 GMT	11,100
Medium	Treasury's Borrow. Prog., June	-	May. 29 <sup>th</sup>	-

Importance	Country	Indicator	Unit	Date of Issuance	Consensus
Medium	Germany	Ifo Index, May	-	May 25 <sup>th</sup> , 8:00 GMT	85.0
Medium	U.S.	Case Shiller Hous. Price Ind., Mar.	% m/m	May 26 <sup>th</sup> , 13:00 GMT	-18.5
Medium	U.S.	Consumer Confidence Index, May	-	May 26 <sup>th</sup> , 14:00 GMT	42.0
High	U.S.	Existing Home Sales, Apr.	mn	May 27 <sup>th</sup> , 14:00 GMT	4.65
High	U.S.	Durable Orders, Apr.	% m/m	May 28 <sup>th</sup> , 12:30 GMT	-0.2
High	U.S.	New Home Sales, Apr.	Mn	May 28 <sup>th</sup> , 14:00 GMT	0.36
High	U.S.	GDP (preliminary), 1Q	% q/q	May 29 <sup>th</sup> , 12:30 GMT	-5.6
Medium	U.S.	Michigan Sentiment Ind., May	-	May 29 <sup>th</sup> , 13:55 GMT	67.9

## Macro-Economic and Financial Forecasts

### Macro Economic Outlook of 2007-2010

	2008	2009f	2010f	2011f
GDP (TRY - mn)	950.1	941.1	1,036.4	1,145.6
GDP (US\$ - bn)	734.9	595.7	638.5	690.0
GDP Growth (y/y % chg)	1.1	-5.0	4.0	5.0
PPI (y/y % chg)	8.1	6.0	5.0	4.0
CPI (y/y % chg)	10.1	5.5	6.5	5.5
Trade Balance (US\$ - mn)	-69.8	-37.9	-62.0	-67.8
Exports (FOB, excl. luggage trade)	132.0	93.4	98.7	106.4
Imports (CIF, incl. gold)	201.7	131.3	160.7	174.2
Current Account Balance (US\$ - mn)	-41.7	-11.9	-33.1	-35.9
Current Account Balance / GDP (%)	-5.7	-2.0	-5.2	-5.2

### Financial Indicators Forecasts

	May 22 <sup>th</sup>	1M	3M	6M	12M	2009	2010
US\$/TRY	1.5273	1.6000	1.5500	1.5500	1.6500	1.5500	1.6300
EUR/TRY	2.1055	2.2400	2.1200	2.0600	2.1500	2.0200	2.1200
FX Basket	3.6328	3.8400	3.6700	3.6100	3.8000	3.5700	3.7500
EUR/US\$	1.3786	1.4000	1.3700	1.3300	1.3000	1.3000	1.3000
O/N	9.25%	9.00%	9.00%	9.00%	11.00%	9.00%	12.50%
Benchmark Bond	12.30%	12.50%	12.00%	12.00%	15.00%	12.00%	14.00%

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