

FORTIS BANK

Macro Scope

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Weekly Economic and Strategic Review

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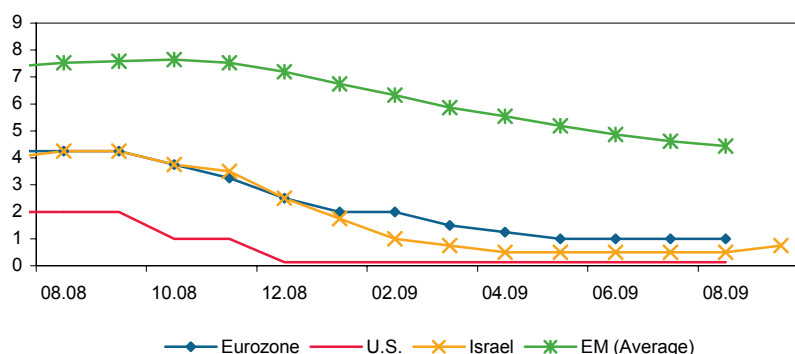
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Some Like It Hawk...

Undoubtedly, the most striking development of the last week was the Bank of Israel's unexpected interest rate hike. The Bank raised the rates by 25 bps to 0.75%. Although the scale of Israel economy is relatively small and the amount of interest rate hike is also fairly limited, markets attached very much importance to this event. The underlying reason of this is the Bank's leading role in the current monetary easing period. Indeed, Bank of Israel was the first in introducing abrupt rate cuts and entering into the quantitative easing period among the other emerging markets. The Bank started cutting the rates in September 2008 and policy rate at 4.25% was pulled down to 0.5% in April 2009. In the same period, the local liquidity was raised by purchasing sizable amount of bond and F/X assets from the banks. These measures bore fruits and Israel is now one of the least-affected countries in terms of the production loss during recession time. The cumulative decline between the peak and the bottom of seasonally adjusted industrial production was registered at 10.7% in Israel, more limited than Turkey's 18.0%. Moreover, the monthly recovery, which was posted after reaching the rock bottom up to last monthly figure, was 2.1% and this was also a more benign level vs. Turkey. Accordingly, in the environment of strengthening signs for the exit from the global recession, Israel's decision to end the loose monetary policy period seemed to be taken as an important signals. The general perception is that the other countries will also follow this suit with a specific lags depending on the strength of recovery. Recall that, CBT was one of the Central banks that started to cut the interest rates earlier (November 08). This might spur the sentiment that Turkey is one of the potential candidates which will track the decision of Israel closely. Moreover, this is an important risk in terms of the V-type recovery supporters for Turkey. In this report, we will try to determine how relevant this monetary policy change is to Turkey.

Monetary Policy Interest Rates (%)

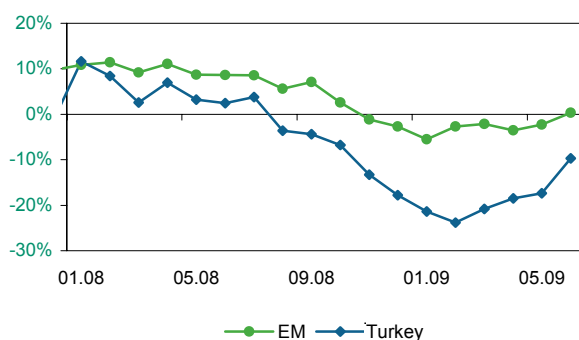


Source: Reuters, Fortis Economic Research and Strategy

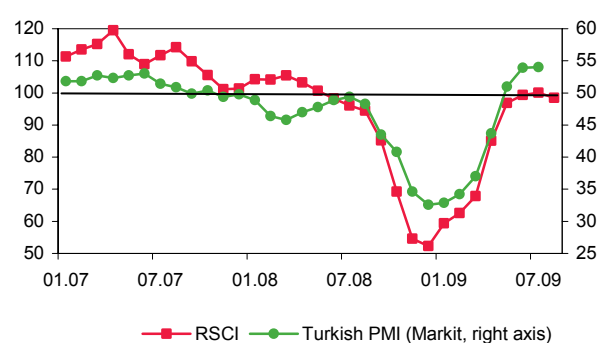
We mentioned our view about the monetary policies and interest rates in our May 19th and June 29th *MacroScope* reports. **We do not think that this low interest rate period stemming from the extremely high excess capacity and output gap in the economies will be permanent.** The scenarios that assume the interest rates will preserve their low levels for a considerable time under the context of rapid recovery do not sound realistic to us. Based on our view, current levels of the interest rates may be valid only in the lingering stagnation periods. Accordingly, there are two alternatives herein. The inflation and the interest rates may remain low on the back of more negative growth outlook or in parallel to the stronger growth performance they may stand at a level close to the long term averages.

Yet, our findings should not be taken as that we think Turkey will be one of the first countries to implement the exit strategy from the looser monetary policy. We still preserve our slow economic recovery assumption and the latest data and developments, which will be analyzed below, support our view. **Such an outlook shows that there is no need for Central Bank to hurry for implementing the exit strategy from the loose monetary policy.** While our positive growth forecast for 2010 is fairly above the market's consensus, the way we read this situation is different from the other analysts. As we mentioned in our weekly report released two week before, *“Even though we think that the upside risks to our above-consensus 4% growth forecast for 2010 have increased due to the base year effect of a deepened recession in 2009, this does not change our sight on the overall stagnation period. After all, the growth performance in 2010 would be a technical correction and would not alter the dismal outlook of the underlying growth trend.”* We highlight that monitoring nothing but the annual growth rates in the periods of strong base effect would be misleading and the levels of seasonally adjusted industrial output and GDP would be more reliable indicators for figuring out the actual strength of recovery. **As we mentioned in the first page of this report, if the compensation of output loss at 18% is delayed further, the growth would not be felt in a wide range even though annual growth rates reach elevated levels.**

Industrial Production (Annual Change)



Real Sector Confidence Index (RSCI) and Turkish PMI (*)



(*) The critical threshold that separates the expansion and contraction periods is taken as 100 and 50 for RSCI and Turkish PMI, in the same order.

Source: Reuters, CBRT, Markit, Fortis Economic Research and Strategy

In the statement of August MPC meeting, the Bank said that recent data releases indicate that the **ongoing recovery in economic activity will be gradual and protracted**. External demand remains weak, domestic investment demand continues to contract and labor market conditions do not display a significant improvement. **Moreover, recent developments have increased the uncertainty regarding the strength of the consumption recovery.** This last phrase confirms the weak domestic demand cycle to be seen after the termination of tax cuts (which we warned about the preceding weeks) and it is broadly in line with our slow recovery scenario. **The Real Sector Confidence Index, the first and the most important data of August, also showed that the recovery in the production front lost its momentum.** The index, which July figure at 100.1 hit the critical 100-threshold that separates the expansion-

contraction period, regressed to 98.5 in August. While this decline came after an uninterrupted 7-month increase, the deteriorated assessments regarding the current situation of overall orders and worsening expectations for the orders in the upcoming period played a big role on this decline. **This development was in line with our view for the continuation of the weak tendency of economy in parallel to the fading impact of tax cuts started in 2Q09.**

All in all, while Israel became the first country that ended the monetary and quantitative easing period, it also rekindled the interrogations about the low interest rate period foreseen to be a long-lasting trend by some. Meanwhile, Turkey may become the subject of the interest rate hike speculations as it started to ease the monetary policy earlier than other EM countries. Yet, Turkey is in a slow and gradual recovery period which is also supported by the recent data flow. Therefore, the Central Bank does not have to be in hurry for starting the rate hikes.

Economic and Political Agenda

- At home, critical data disclosures such as foreign trade statistics and inflation will top the agenda this week. Separately, the Treasury will publish its borrowing program for September. Coming to the external arena, while PMIs will be important both in Eurozone and U.S., the labor market developments will be on the forefront in the U.S. The markets will closely eye ADP Employment Report, non-farm payrolls and unemployment rate. Meanwhile, minutes of August 12th FOMC meeting will be released on Wednesday.

Data issuances at Home

Importance	Indicator	Unit	Date of issuance	Fortis (Consensus)
Medium	Treas. Borrow. Prog., Sep.	-	Aug. 31 st	-
High	Imports & Exports, July	US\$ bn	Aug. 31 st , 14:00 GMT	13.1 & 9.1 (13.0 & 9.0)
Medium	TEA's Preliminary Exports, Aug.	US\$ bn	Sep. 1 st	7.5
Medium	CBNC-e Cons. Conf. Ind., Aug.	-	Sep. 1 st , 6:00 GMT	-
High	ICC Price Index, Aug.	% m/m	Sep. 1 st , 9:00 GMT	-
High	CPI, Aug.	%m/m	Sep. 3 rd , 14:00 GMT	0.1 (0.21)
High	PPI, Aug.	%m/m	Sep. 3 rd , 14:00 GMT	(0.21)

Importance	Country	Indicator	Unit	Date of Issuance	Consensus
High	Eurozone	Manufacturing PMI, Aug.	-	Sep. 1 st , 7:58 GMT	47.9
High	U.S.	Manufacturing ISM, Aug.	-	Sep. 1 st , 14:00 GMT	50.3
Medium	U.S.	Pending Home Sales, July	% m/m	Sep. 1 st , 14:00 GMT	0.0
Medium	Eurozone	GDP (1 st revision), 2Q	% q/q	Sep. 2 nd , 9:00 GMT	-0.1
Medium	U.S.	ADP Employment, Aug.	K	Sep. 3 rd , 13:15 GMT	-263
Weak	U.S.	Unit Lab. Cost & Prod., 2Q	% q/q	Sep. 2 nd , 12:30 GMT	-5.3 & 5.9
High	Eurozone	Services PMI, Aug.	-	Sep. 3 rd , 7:58 GMT	49.5
High	Eurozone	ECB Rate Decision	bps	Sep. 3 rd , 11:45 GMT	no chg.
High	U.S.	Non-manufacturing ISM, Aug.	-	Sep. 3 rd , 14:00 GMT	48.0
High	U.S.	Non-farm Payrolls, Aug.	K	Sep. 4 th , 12:30 GMT	-223
Medium	U.S.	Unemployment Rate, Aug.	%	Sep. 4 th , 12:30 GMT	9.5

Macro-Economic and Financial Forecasts

Macro Economic Outlook of 2007-2010

	2008	2009f	2010f	2011f
GDP (TRY - mn)	950.1	928.7	1,018.5	1,126.2
GDP (US\$ - bn)	734.9	599.2	648.7	691.8
GDP Growth (y/y % chg)	1.1	-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	-37.8	-61.2	-66.1
Exports (FOB, excl. luggage trade)	132.0	102.4	102.7	106.1
Imports (CIF, incl. gold)	201.7	140.2	163.9	172.2
Current Account Balance (US\$ - bn)	-41.3	-11.5	-32.1	-34.3
Current Account Balance / GDP (%)	-5.6	-1.9	-5.0	-5.0

Financial Indicators Forecasts

	August 28 th	1M	3M	6M	12M	2009	2010
US\$/TRY	1.4955	1.5000	1.5000	1.5600	1.5800	1.5000	1.5800
EUR/TRY	2.1319	2.1000	2.1000	2.1500	2.0500	2.1000	2.0500
FX Basket	3.6274	3.6000	3.6000	3.7100	3.6300	3.6000	3.6300
EUR/US\$	1.4255	1.4000	1.4000	1.3800	1.3000	1.4000	1.3000
O/N	7.75%	7.00%	7.00%	7.00%	8.50%	7.00%	10.00%
Benchmark Bond	9.50%	9.50%	10.50%	11.50%	12.00%	10.50%	12.50%

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