Bakış

Macro Trends in the Turkish and World Economy

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General Outlook

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The global economy is about to leave behind a year in which it deeply felt the impacts of the ongoing global trade wars in which the US and China are the main actors. It appears that the impact of the trade tensions between these two giant powers that left an indelible imprint on 2019 will continue to cast a pall over the world economies for the rest of the year.

While uncertainties persist, the downside risks to the world's growth outlook will continue to be important and a loss of financial momentum will remain the main issue that should be addressed in the economies of both developed and developing countries.

The loss of momentum in EU economies which the current issue of Bakış discusses in detail, has become even more apparent now. Developments in the EU, especially in Germany, Turkey's largest trading partner, will continue to be scrutinized in Turkey even more closely in the coming period. Europe is the largest buyer of our products, and we also attract most of the foreign capital from EU countries. While most tourists come from this region, the foreign loans of our private sector are mostly provided by European financial institutions.

On the one hand, Turkey is trying to tackle its own unique problems while on the other hand, it is trying to minimize the impact of the negative developments in Europe and the global trade wars. There is also no doubt it is endeavoring to come up with sound strategies in the search for new markets and partnerships.

From this perspective, it is necessary to dedicate an extra few lines to the visit of Wilbur Ross, the US Secretary of Commerce, who stood out from his predecessors in terms of the length of his stay and the many big deals in his bag. During his 4 nights and 5 days long visit, Ross, who held intensive interviews in Istanbul and Ankara and took part in long discussions with leading figures from the business world, came off as a sincere trading partner.

In the meantime, the fact that the interest of the Turkish business world for the China International Import Expo, which took place for the second time this year from November 5-10, is even higher compared to the previous year shows another aspect of this search for new markets.

In the global markets, interest rate cuts spread in ripples in the third quarter. Interest rate cuts in advanced and emerging economies increase Turkey's appeal as a place to invest. Also, the fact that Turkish financial assets are far below long-term equilibrium values can be seen as another attraction.

In order to trigger long-term capital inflows into Turkey, it is crucial to implement the policies and measures also proposed in the New Economy Program to improve investor perceptions.

We could argue that the policies and measures proposed in the New Economy Program for 2020-2022 published at the end of last September were perceived as sound proposals to strengthen the Turkish economy.

There should be a separate column for the numerical targets set in the program. We anticipate no difficulties with a growth pace of 5 percent in the Turkish economy in the long run. Achieving the growth pace by maintaining the positive outlook in inflation and the current deficit will be the main issue.

With the improvement in inflation and the relative calm of the financial markets, CBRT rapidly lowered policy interest rates in the third quarter. It is certain that the interest rate cuts, to which public banks initially reacted positively, led to a significant relief in the markets. It can be said that the new interest rate cuts will depend on the course of inflation in the coming period. In fact, if the statements of the President of CBRT are anything to go by, the institution will be more cautious about aggressive interest rate cuts.

It is worth noting that more believe that our economy, which entered the last quarter of 2019, will perform much better in the new year on account of these new developments.

Overview of the global economy

While uncertainties remain about the course of the global trade wars, downside risks remain vital for global growth prospects. While the loss of financial momentum is making itself felt in both advanced and emerging economies, there are now almost no sectors that are not impacted by the downturn.

In the first half of 2019, global trade volume almost flatlined compared with the first half of 2018, but it showed signs of recovery in the second half of the year. The quarterly averages, however, still show a more fragile outlook and point to a decline of 0.9 percent on an annual basis.

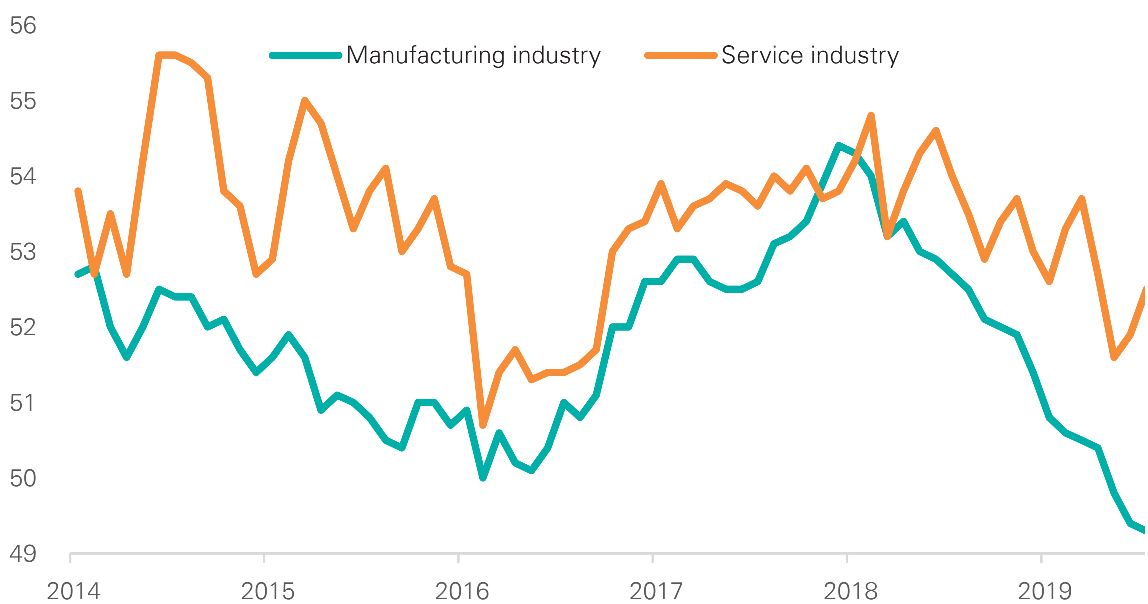
This negative trade outlook leads to a global slowdown in industrial production. Global industrial production, which rounded off the first half of the year with a growth rate of 1.3 percent, showed a slow pace and grew only by 0.3 percent in July compared with the previous month and only by 0.9 percent on an annual basis.

However, some preliminary data shows that the global slowdown is being offset by recent interest rate cuts. In this context, the global PMI Manufacturing Index was 49.3 in July, 49.5 in August and 49.7 in September. Although the index is still below 50 putting it in contraction territory, the contraction is slowing down.

On the other hand, the relatively strong PMI data for the service sector, which have been showing signs of a slowdown for some time, declined - in contrast to the manufacturing sector- in August and September after its rise in July, recalling to mind the downside risks to global growth.

Against such a backdrop, the measures taken by policy-makers have reinforced the financial positions and somewhat improved some confidence indices. While to some extent offsetting the risks to the economic outlook, it is assumed that there is no room for maneuver particularly when it comes to the monetary policy, in the event of a new shock. Further expansionary fiscal measures are therefore likely to come to the fore, especially in developed countries, in order to support growth in the coming period.

Global purchasing managers' indices (PMI)



Source: https://www.markiteconomics.com/Public/Home/Index?language=en

Overview of the Turkish economy

- The Turkish economy, which started 2019 with concerns over growth, declined slightly in the first half of the year and, contrary to expectations, remained on an even keel. On an annual basis, the Turkish economy shrank by 1.5 percent in the second quarter, and this shrinkage was observed to be in a level of 1.9 percent in the overall first half. While foreign demand has made a positive contribution to economic activity over the past six quarters, it has also significantly alleviated concerns about the current deficit.

- In light of the 0.9 percent year on year growth in the third quarter, signs of an economic recovery are pronounced more. The weak base in the last quarter of last year also increased the likelihood that GDP could change positively in the overall course of the year.

- The New Economy Program announced at the end of September contains ambitious growth targets for the coming years. Nevertheless, the program's perspective on the economic outlook was welcomed positively by the business community.

- Although the economic shrinkage is not so severe, the decline in the labor market continues. Therefore, the overall unemployment rate is around 14%, while youth unemployment is quite high at 26%.

- On the other hand, floundering budgetary performance has not yet recovered really with growth-promoting policies. While an improvement in tax revenues depends on the extent to which domestic demand can recover, expenditure savings are also important.

- The transfer of the Central Bank of the Republic of Turkey's (CBRT) reserve fund limited the deterioration in budgetary performance.

- Owing to the economic rebalancing, there was a surplus in the current account balance in the summer months with extra boost from tourism. As a result, concerns about external financing have somewhat diminished.

- Inflation has improved faster than expected due to limited volatility in exchange rates and weak course of domestic demand. As cost pressures eased, consumer inflation fell to a single-digit figure at 9.26 percent in September.

- While financial markets reacted positively to the CBRT interest rate cuts, the third quarter saw the Turkish currency rebound in real and nominal terms. Bond yields declined, while equities took their place in the "positively differentiated" side among emerging economies.

New economy program announced

- The New Economy Program for the period 2020-2022, drafted to transform the economy for sustainable growth with a focus on price stability, financial stability and productivity and efficiency, was published at the end of September.
- With the new program, consumer inflation estimated to be at 12 percent by the end of 2019 is planned to fall to 8.5 percent by 2020, and below 5 percent by the end of the program.
- The program gives the impression that there will be no tax increases that would adversely affect the fight against inflation, while there are also no signs of an aggressive fiscal tightening. It is reported that important reforms are to be implemented throughout the program for the efficient use of resources, while at the same time a set of policies are considered to broaden the tax base and ensure a just tax system.
- The economy is expected to grow by 5 percent, in a pace close to its potential, during the period the program remains in force.
- Among the steps set out in the program that should support growth are the Turkey Wealth Fund's fixed capital investments in the petrochemical, mining and energy production from domestic resources in cooperation with the private sector. It is stated that the Development Fund set up by the Development and Investment Bank of Turkey will support the production of high value-added and high technology products.
- Also, the implementations supporting the production of high value-added products will be continued through R&D, innovation, technological transformation and, in particular, the project-based investment incentive system. And, as set out in the 11th Development Plan, priority will be given to the industrial manufacturing sectors that involve chemical and pharmaceutical-medical devices, machines, electrical equipment, automobiles, electronic vehicles and railway vehicles.

Expectations for 2019

2019 GDP growth
0%

2019 GDP
700 billion USD

2019 Tourism income
25 billion USD

2019 foreign trade expectation
Export **180** Billion USD
Import **210** Billion USD

Markets

2019 year averages

USD / TL	: **5.75**
Euro / TL	: **6.40**
Euro / Dolar	: **1.11**
Brent oil	: **$68**

End of 2019

USD / TL	: **5.90**
Euro / TL	: **6.67**
Euro / USD	: **1.13**
Brent oil	: **$65**

Unemployment
13%
(2019 year average)

Inflation
13%
(year end)
16%
(year average)

Current surplus
2.5
(billion USD)

Expectations for 2020

2020 GDP growth
3.5%

2020 GDP
735 billion USD

2020 Tourism income
25 billion USD

2020 foreign trade expectation
Export **190** Billion USD
Import **250** Billion USD

Markets

2020 year averages

USD / TL	: **6.25**
Euro / TL	: **7.19**
Euro / USD	: **1.15**
Brent oil	: **$72**

End of 2020

USD / TL	: **6.50**
Euro / TL	: **7.48**
Euro / USD	: **1.15**
Brent oil	: **$75**

Unemployment
12.5%
(2020 year average)

Inflation
9%
(2020 year end)
11%
(2020 year average)

Current deficit
20
(billion USD)
deficit

*This data is based on market data dated October 14, 2019.

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