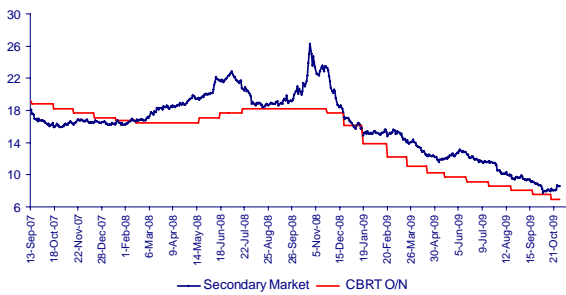


# Turkey Weekly Macro Comment

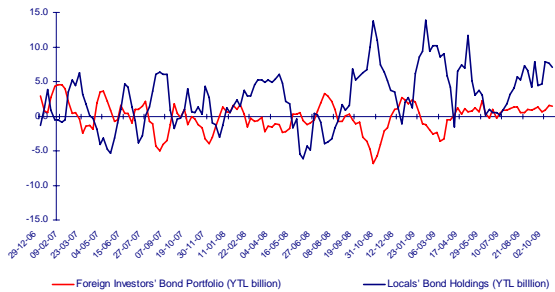
26 October 2009

## Bond Rates vs O/N



Source: Central Bank of Turkey, YK Economic Research

## Domestic & Foreign Bond Portfolios (4W change)



Source: Central Bank of Turkey, YK Economic Research

## Quo Vadis Turkey?

- The infamous question recently entails concerns regarding Turkey's "Drang Nach Osten" which is seen as a sign of gradual severance of her ties with the West. This in itself is an overly simplistic and defective perception of what indeed is taking place as we argue inside.
- Most importantly, a huge portion of the doubters pay lip service to a westernization and modernization process but miss the true essence of the process itself in a dramatic fashion.
- The perception of Westernization in style with no accompanying grasp of its essence is naturally irked by any drive towards the East and that is what you see today in Turkey once again.
- The democratic initiative in the meantime looks like having reached a stalemate due to reactions voiced by myriad circles, all domestic needless to say.
- Housing loans had another stellar showing with an increase of TL 312 million while all other credit categories slumped including credit card loans.

Cevdet Akçay

Chief Economist, Yapı Kredi Bank & Yapı Kredi Yatırım

Tel: +90 212 319 8430 cevdet.akcay@yapikredi.com.tr

## 1.1 General Outlook

This is a question that has been asked in Turkey many times and in many occasions, and the underlying question ultimately has been whether a divergence from the “targeted Western civilization” was in place. **In that sense, the question is misleading in itself in the first place as it assumes that whatever developments have led to the emergence of the question itself, the previous setting was one in which compliance with the target (read adoption of Western values and institutions) was solid and unquestionable.** Let’s leave aside the previous contexts for the sake of brevity and focus on the latest one as it is not only the most common one but is perceived to be the most threatening context of all as well.

**The infamous question recently entails concerns regarding Turkey’s “Drang Nach Osten” which is seen as a sign of gradual severance of her ties with the West. This in itself is an overly simplistic and defective perception of what indeed is taking place** as the current flirtation between Turkey and Middle East countries most presumably has the blessing of the Western world, i.e. the US and Europe. That it has the implicit and in certain cases the explicit approval of the US administration goes without saying and that is indeed one source of frustration for certain local circles here. Whatever suits the US interests in the region, it must be by default at the expense of Turkish interests they claim, and that is that. This is unequivocally a very shallow perspective and has no operational value in the today’s setting in the region or anywhere else for that purpose. As for the EU, supporters of Turkey in the EU are overwhelmingly in favor of Turkey’s enhanced power broker role in the region and those who object to Turkey’s accession do not count anyway.

Come back to our argument regarding the assumed compliance or resemblance of the setting with the “targeted western civilization” prior to the time concerns get loudly pronounced regarding the direction the country is headed towards. Doubters have been claiming for a long time that politicians with an Islamic heritage are by default not fit to pursue the “Europeanization (or Westernization) process”. Hence, all these chapter openings (and the closing of one so far) with the EU and the negotiations run by the AKP government are virtually gimmicks and thus lack sincerity and true intent. **Gauging the true intent of the AKP may be indeed difficult but the data tells us that the intent there to the extent that it exists is more than anywhere else in the political/state circles.**

**Most importantly, a huge portion of the doubters pay lip service to a westernization and modernization process but miss the true essence of the process itself in a dramatic fashion. They are fully aware of the disparity between their proposed praxis for Turkey and the Western standards and experience yet find consolation easily in justifications they produce.** For one, our society is a backward rural one and hard in its religious stance which creates a natural handicap in adopting standards shaped by an exclusively Christian culture. And secondly, the Western world pushes an agenda that serves her interests at the expense of others and is thus in conflict with our national interests, not surprisingly again by default. **These two arguments**

**should not hold water under any modest scrutiny but they have been very instrumental in generating a mind frame that is totally void of universal values and/or metrics. It is mostly the product of a mind set that totally misses the internal dynamics of the society; the same mind set which has displayed no genuine interest in discovering what the concept of “West” may indeed entail, a concept that has evolved through centuries of hard fought battles, on the fields and in minds.**

**This perception of Westernization in style with no accompanying grasp of its essence is naturally irked by any drive towards the East and that is what you see today in Turkey once again.** A short but very informative piece by Paul Salem, the Director of Carnegie Middle East Center in Beirut, in Dar Al Hayat newspaper<sup>1</sup> argues that “Turkey’s shift is, in itself, a positive development.” Salem goes on to assert that “that a functional, democratic and pragmatic country like Turkey plays a larger role in the Arab and Islamic world is a positive development.” His only reservation pertains to the Arab Israeli peace process, but the piece is otherwise quite dovish both on the overall politics of the region and on the role that Turkey is bound to play in that in particular. The title is probably as telling as any argument inside: “Could this be Turkey’s Century in the Middle East?” This is no invitation to get carried away by the prospects that the region may be offering to Turkey going forward, but merely a suggestion that Turkey’s “Drang Nach Osten” should be perceived as a prudent supplement to the normalization process taking place in Turkey who may have finally agreed to adopt universal metrics for her social restructuring.

**The democratic initiative in the meantime looks like having reached a stalemate due to reactions voiced by myriad circles, all domestic needless to say.** We do not believe the AKP Government will ultimately assign any weight to these foul cries, but their strategy seems to have shifted towards securing a stronger support from external forces, the Iraqi Government most recently. Minister of Foreign Affairs Davutoglu paid a visit to Irak last week and to all regions of the country, opening consulates in Basra and Musul. Erbil will be next, and that will serve as the official recognition of the Kurdistan Regional Government (KRG). Erbil is the capital city of Kurdistan Region as it is called in the Iraqi Constitution, and Turkey was one of the first to recognize the new Iraqi state while recognition of the KRG remained murky due to reasons not difficult to imagine. It is an autonomous region in federal Iraq and is currently the only Region in existence. According to the Iraqi Constitution, Provinces have the right to petition to become a “Region” via a referendum and with the petition drive in Basra in 2009 having failed to collect enough signatures for referendum, Kurdistan Region is the only constitutional Region in Iraq. That is quite in contrast to the Turkish John Doe perception of the situation in Iraq as the average person on the street has a natural tendency to view KRG as the most fictitious regional entity in Iraq. The truth is exactly the opposite and Turkey has taken a step forward at the state level which is bound the change the John Doe perception at some point as well. These are quite breath-taking developments and Minister Davutoglu made a very ambitious proposition in Iraq last week; to restructure the Middle East together in a way to enhance cooperation and reduce animosities.

---

<sup>1</sup> <http://international.daralhayat.com/internationalarticle/71322>

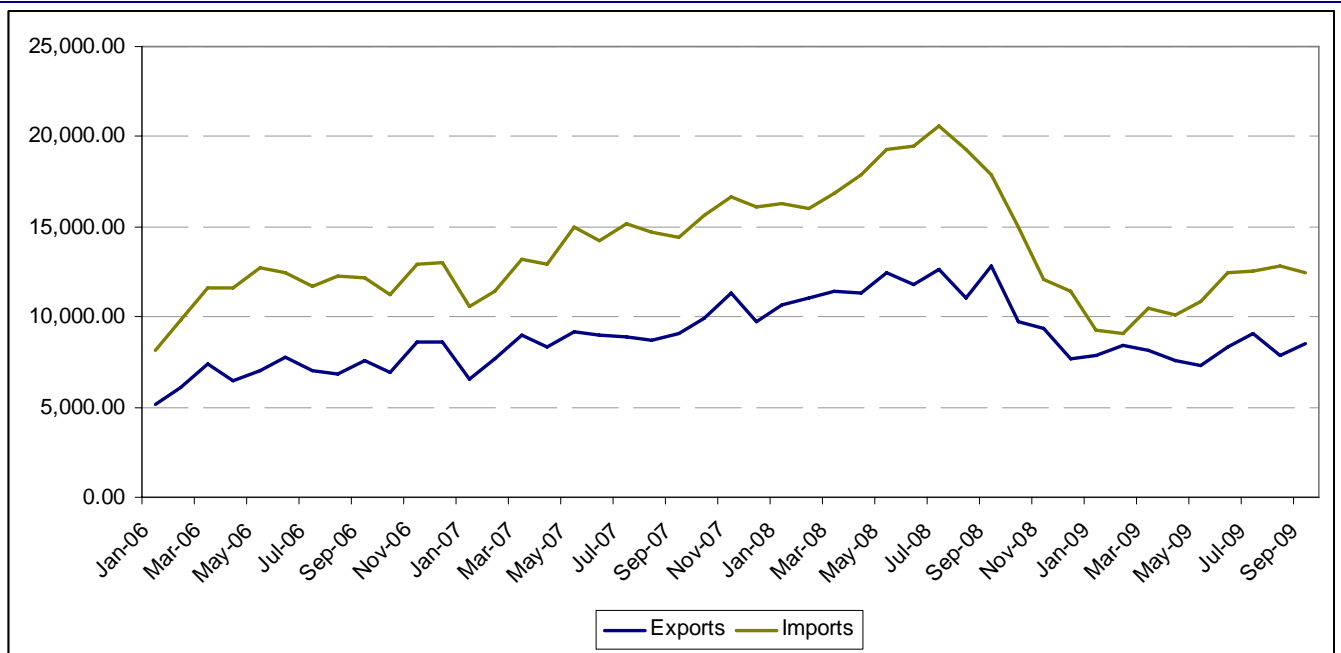
Admittedly very ambitious indeed, but beyond contemplation if the intention is not there in the first place.

What Turkey expects in return in the shortest term is the drying up of the support for the PKK in Northern Iraq, and even some help in their disarmament. Barzani does not categorically reject the idea and given jailed PKK leader Ocalan's recent criticism of the AKP Government and his overt threat that no more PKK members would return to Turkey, Barzani may seek to enhance his support within the Kurdish population in Turkey via closer ties and cooperation with the Turkish Government. Things could take daily turns for all directions here and it makes more sense to sit out these developments and see where they tend to evolve rather than speculate at will. Cautious optimism, as evasive a phrase as it is, seems to fit the situation quite well in this case.

## 1.2 Macro Data

**Foreign trade data for September were released last week and the contraction rate for exports was above that for imports for the first time in quite a while (since October 2008 to be precise when both started to contract YoY).** Yet that is no sign of economic recovery having an impact on imports demand, but is merely a reflection of the base effects coming from last year as the graph below depicts.

Figure 1. Exports vs. Imports –Monthly Level

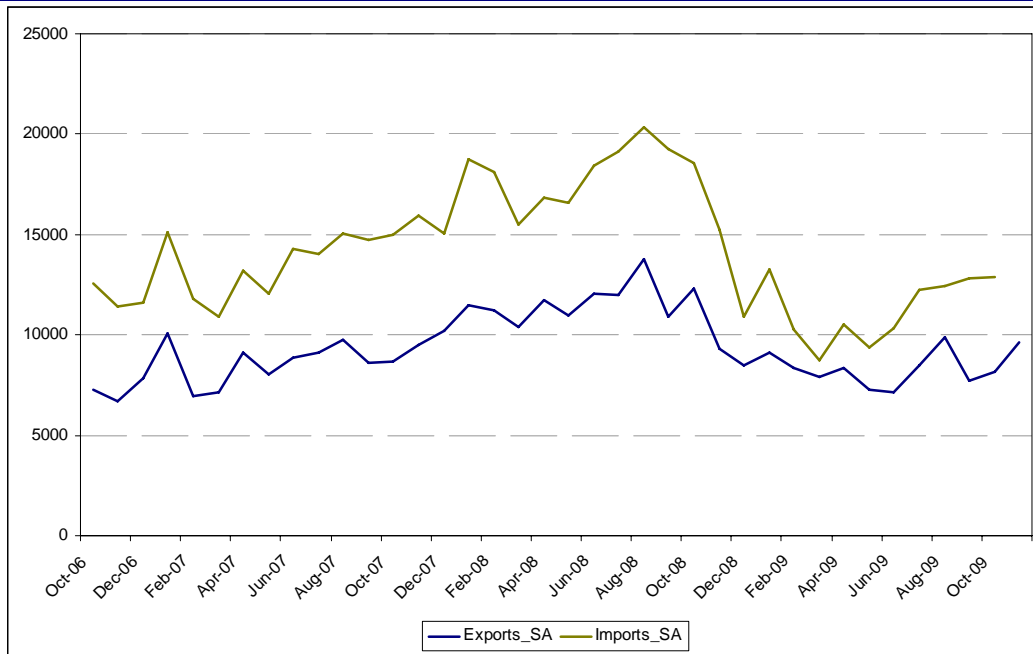


Source: Turkstat, Yapı Kredi Economic Research

Note that imports had peaked at USD 20.6 billion in July 2008 while exports kept on increasing until September where they had reached USD 12.8 billion and plunged from there on. The gap

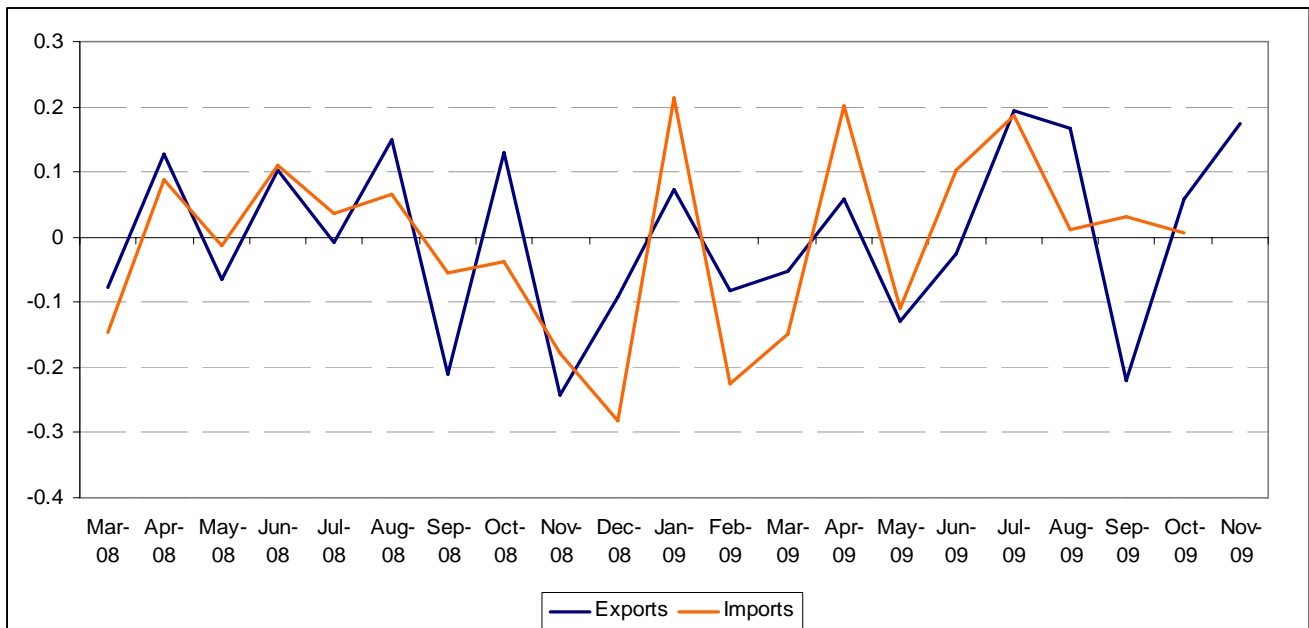
between the contraction rates of imports and exports had narrowed significantly in August and September data provides the first break in this one year long “stronger contraction in imports” period. This is yet another case where looking at rates of change on a YoY basis is misleading due to structural breaks. Looking at seasonally adjusted exports and imports and obtaining month on month rates of changes for both, we observe significant volatility in growth rates of both with that in exports particularly interesting as of late. Graphs below depict levels and MoM changes for seasonally adjusted exports and imports data and the volatility we mentioned should be obvious in the second one.

**Figure 2. Exports vs. Imports –Seasonally Adjusted Series**



Source: Turkstat, Yapı Kredi Economic Research

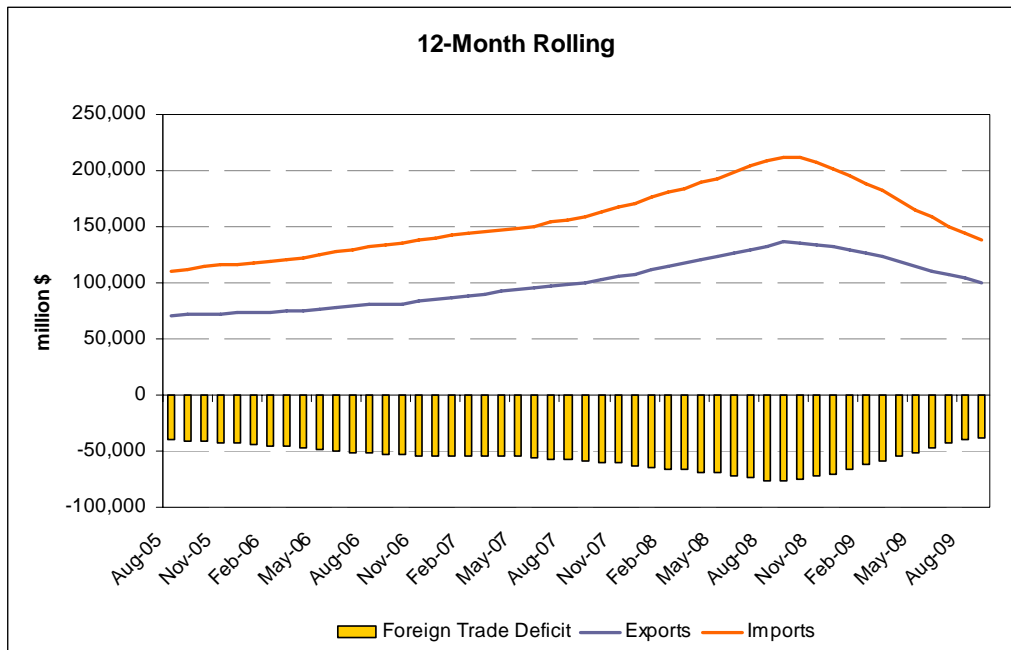
**Figure 1. Exports vs. Imports –Seasonally Adjusted Series MoM Growth**



Source: Turkstat, Yapı Kredi Economic Research

12-Month rolling trade deficit is at USD 38.6 billion, almost half the USD 75.8 billion figure in September 2008 and the lowest since August 2005 when the 12-Month rolling trade volume stood at USD 181 billion as opposed to today's crisis volume of USD 238 billion.

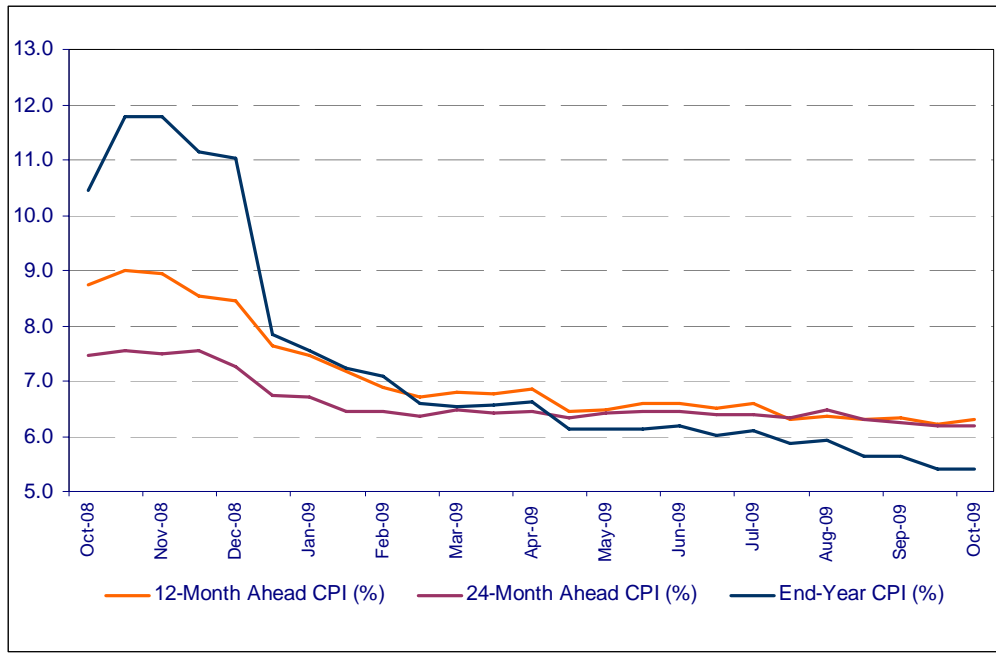
Figure 3. Exports vs. Imports



Source: Turkstat, Yapı Kredi Economic Research

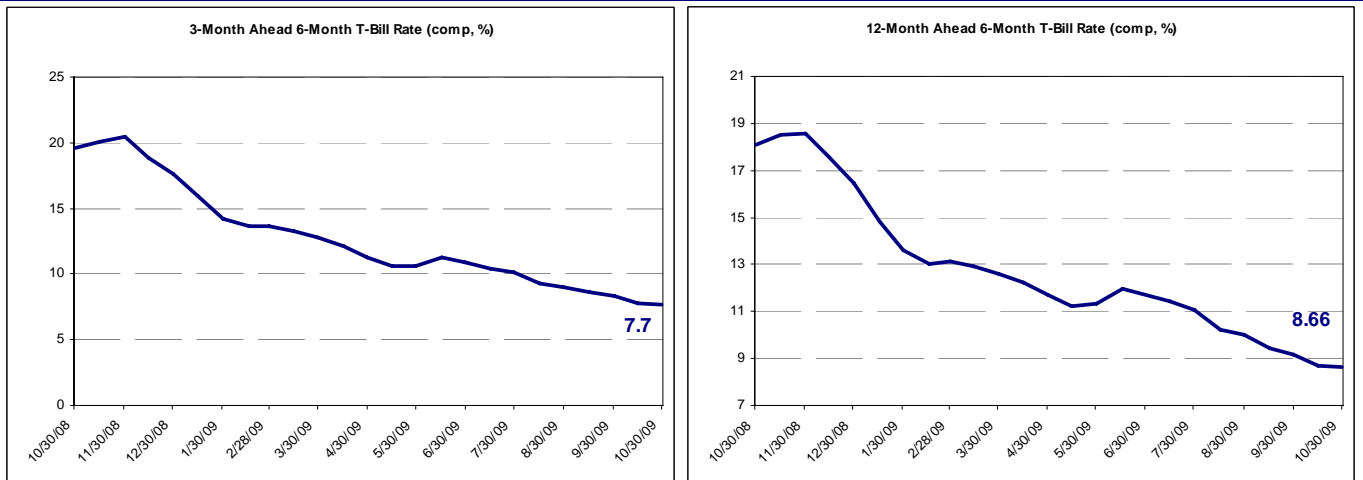
The Central Bank's second expectation survey for the month of October was released last week and there are no noteworthy changes in any of the forecasts. The only one worth mentioning for qualitative reasons could be the reduction in the next three month's O/N rate along with an increase in the 12-month ahead O/N rate while all bond rates in the 12-month horizon slightly edge down. One could come up with the explanation that the disinflationary rate hike initiation by the CBRT will be so convincing that bond rates will come down as a result of enhanced trust in disinflation but that might be stretching it a bit too much. It might be better to conclude that there is some confusion regarding the future course of inflation, bond rates, and the policy rate. The confusion is only natural as we are in uncharted waters but the information content of the series is quite limited for the decision making bodies and that is a significant deficiency in the signaling process.

Figure 4. Inflation Expectations



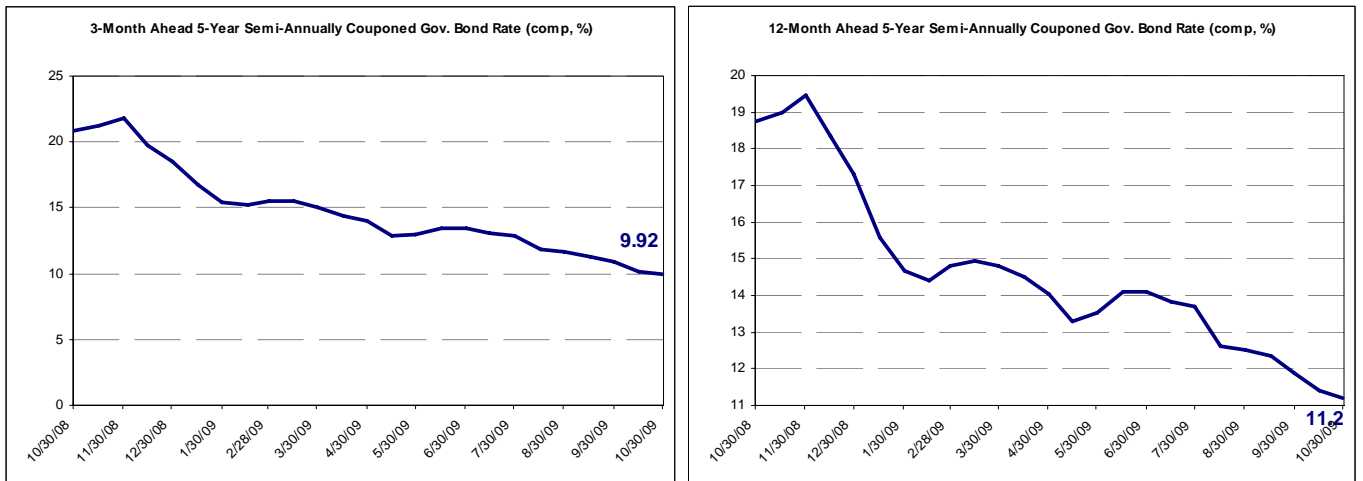
Source: Expectations Survey, Central Bank of Turkey

Figure 5. Interest Rate Expectations



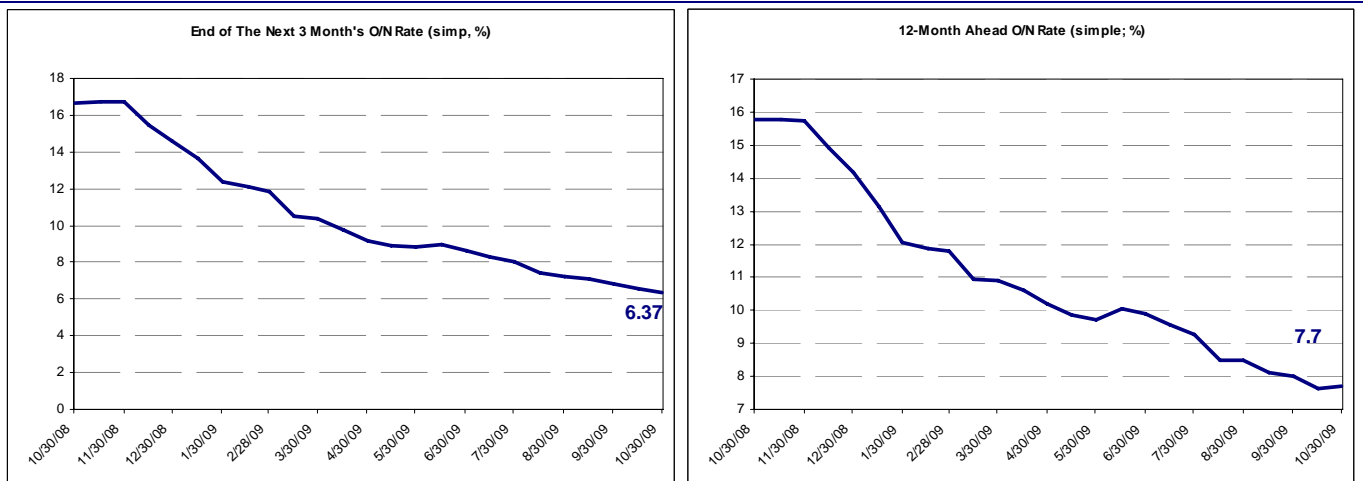
Source: Expectations Survey, Central Bank of Turkey

Figure 6. Interest Rate Expectations



Source: Expectations Survey, Central Bank of Turkey

Figure 7. O/N Expectations



Source: Expectations Survey, Central Bank of Turkey

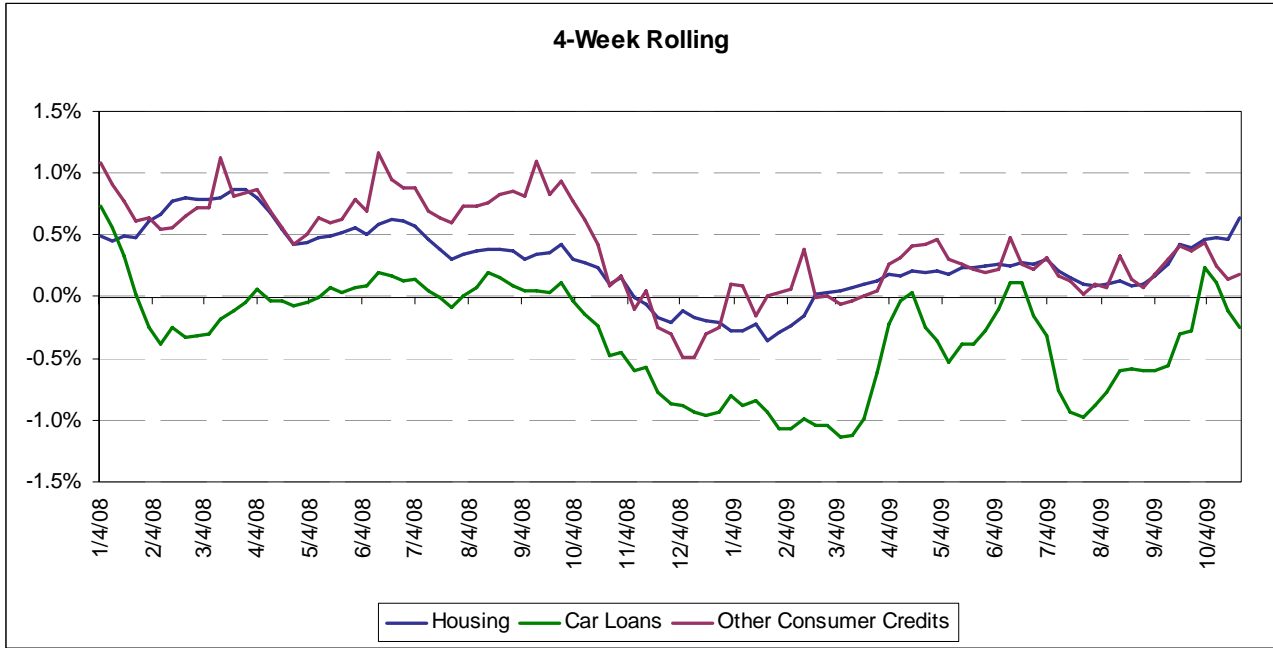
### 1.3 Weekly Data (all weekly data terminate at October 23, 2009 while consumer credits are one extra week updated)

**Housing loans had another stellar showing with an increase of TL 312 million while all other credit categories slumped including credit card loans.** This is the sixth very sizeable increase in the last seven weeks and both the cost of funding and real estate prices seem to have lured new buyers into the market. There will be limited impact on economic activity though as a huge excess supply of housing still exists.



Commercial credits maintained their erratic behavior and went up by TL 1.2 billion following a contraction of TL 2.4 billion a week ago. Even smoothed out commercial credits series are quite volatile and unless a clear trend is forming, it is very difficult to predict any discernible pattern here.

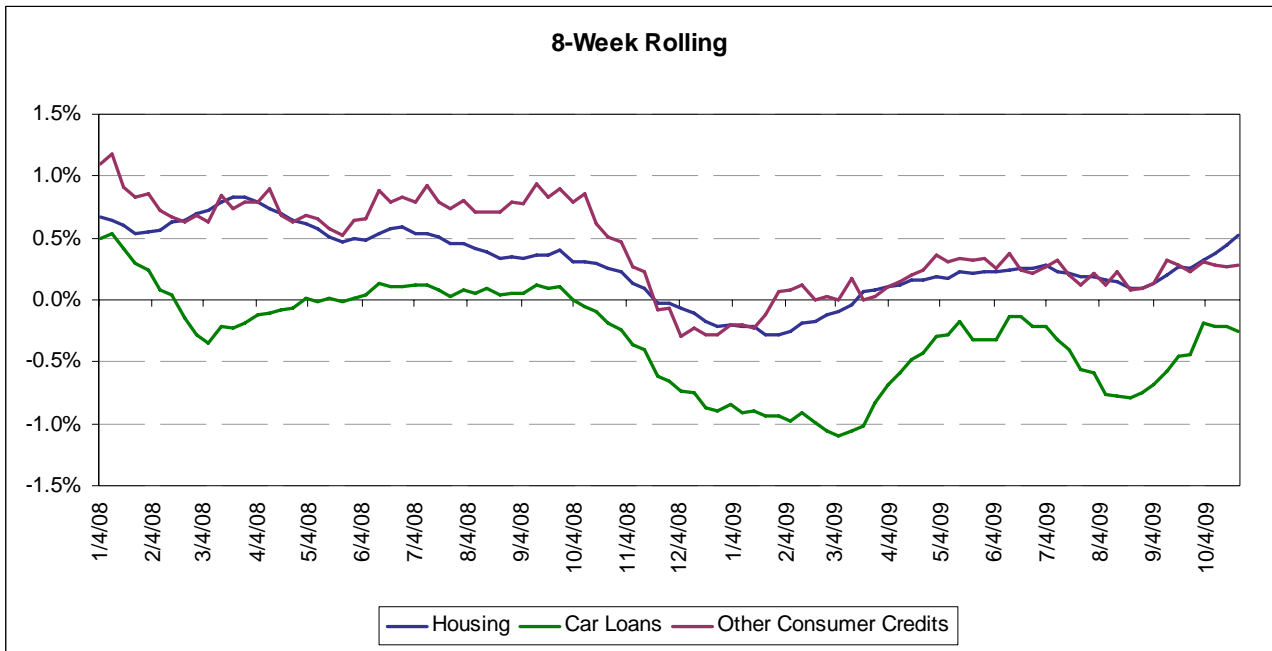
Figure 8. Consumer Credit Volume (\*)



Source: Central Bank of Turkey, Yapı Kredi Economic Research

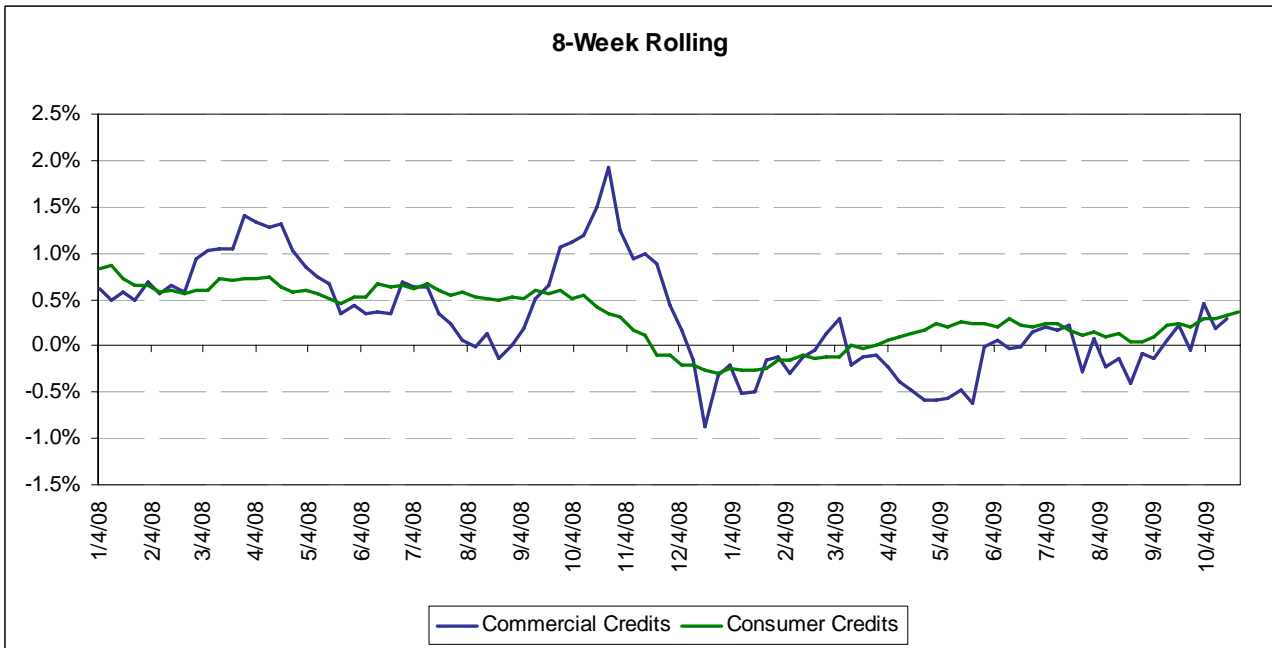
(\*)Weekly % change of 4W rolling

Figure 9. Consumer Credit Volume (\*)



Source: Central Bank of Turkey, Yapı Kredi Economic Research  
 (\*)Weekly % change of 8W rolling

Figure 10. Commercial & Consumer Credit Volume (\*)



Source: Central Bank of Turkey, Yapı Kredi Economic Research  
 (\*)Weekly % change of 8W rolling

## Markets

by Murat Berk / Economist and Investment Strategist

There was no shortage of potential catalysts for the recent decline, though it's impossible to say which were the most important.



In any case, the negative correlation between the dollar and risky assets remains well intact, at least for now. The USD found a footing this week and equities; commodities and some areas in credit (such as high yield bonds) all saw downside pressure.



There's still a lot of nervousness in the market, which is quick to react to every blip in the data and various news.



Like every bull market, this one continues to climb a “wall of worry”. Having said that, we’ve been highlighting a number of yellow flags over the past few weeks (i.e. we discussed what appeared to be rising tensions in currency markets), which typically occur as a rally gets extended. As said before, while these are no guarantees that a top is forming, they are good warnings that caution is in order.



Also, last week, we opined in this space that given the massive rally, compared to March (when we turned bullish on global markets), our expected returns now were lower and subject to more uncertainty.



The big question is whether recent market moves represent a trend change. Attempting to call a reversal is still dangerous business, and until warning flags start waving much more intensely, we should continue to give this bull market the benefit of doubt, in our view.

As discussed earlier, the combination of improving global growth and easy monetary and fiscal policy settings is typically a “sweet spot” for high beta commodity and equities (i.e. emerging markets).

A below-trend economic recovery seems already underway and policies are likely to remain supportive for asset prices as long as the recovery is sluggish and disinflationary. For example, despite “easy” monetary and fiscal policy, we note that in the US, M2 money supply continues to remain weak and business credit is still declining, suggesting any near term inflation scares may be premature in the short-term.

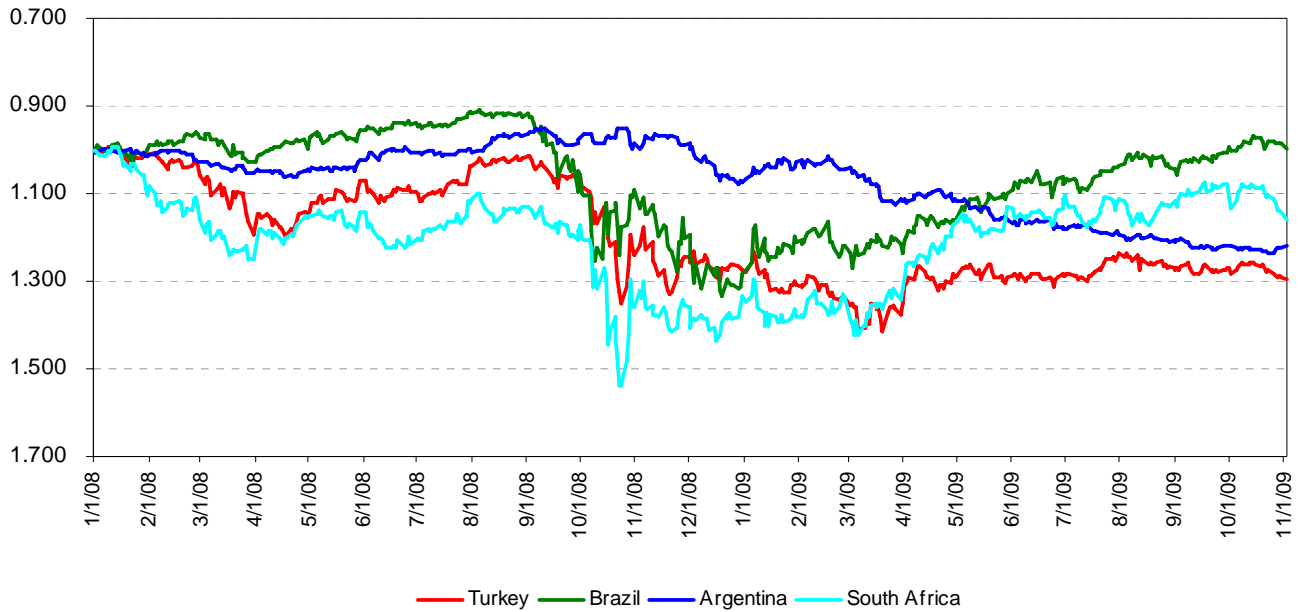
As a tangent, this week’s policy communication by the RBA, FOMC, BOE and the ECB deserve a close watch.

In the greater scheme of things the reaction to the U.S.’ attempt to reflate its way out of the deep recession and export deflation to other countries via dollar devaluation remains the big question mark, in our view.

## 1.4 Appendix

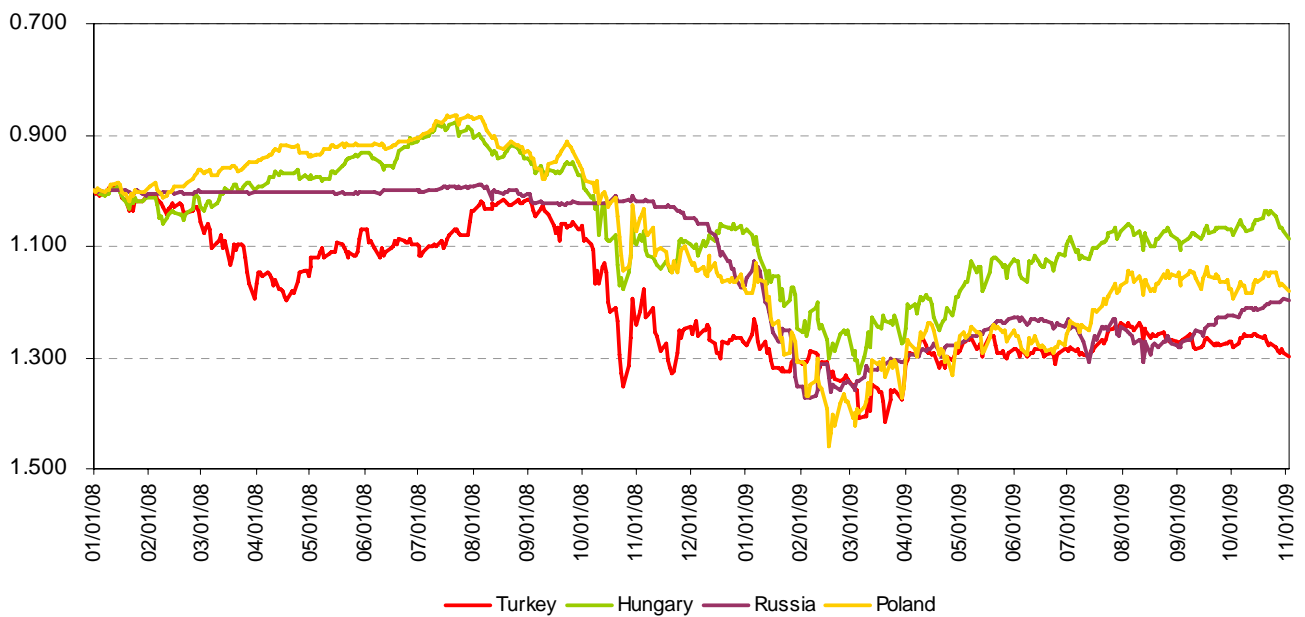
### Currency Performances

Figure 13. Turkey, South Africa, Latin America 1/Jan/2008=1.00 (\*)



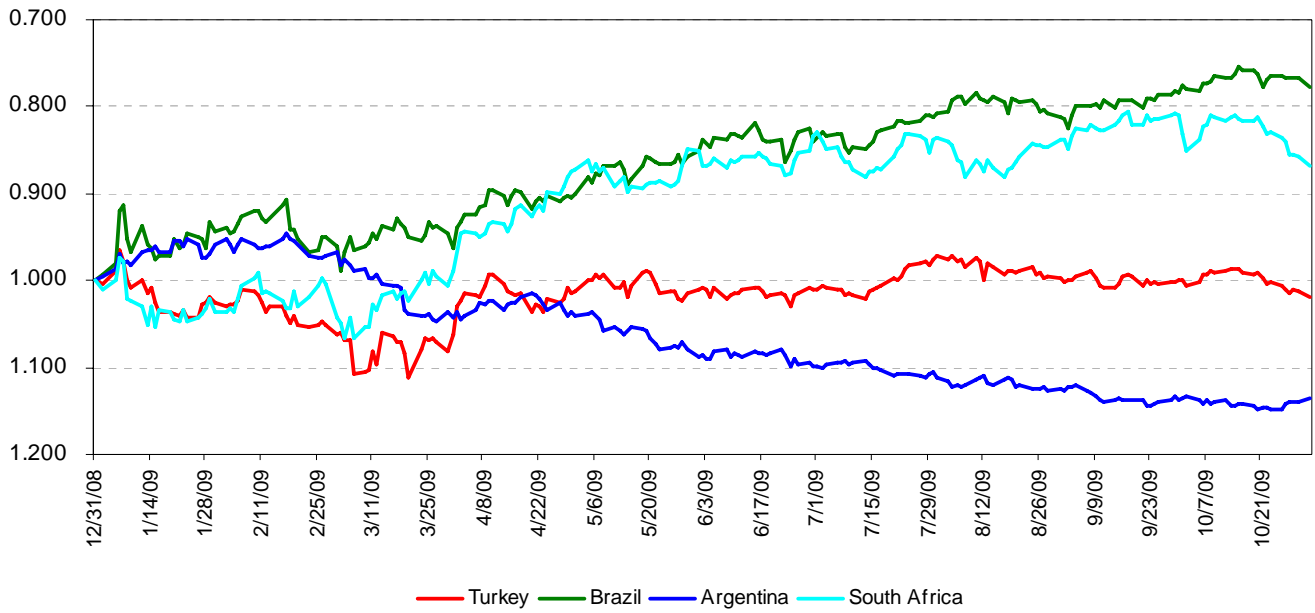
Source: Reuters, Yapı Kredi Economic Research

Figure 14. Turkey, Eastern Europe 1/Jan/2008=1.00 (\*)



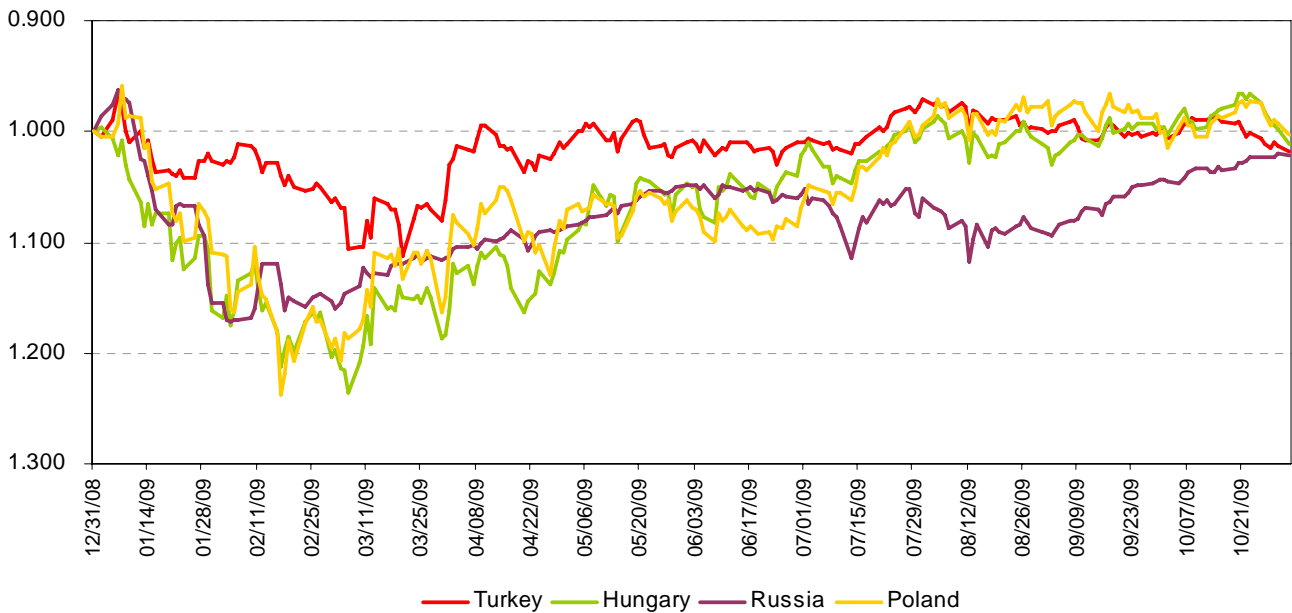
Source: Reuters, Yapı Kredi Economic Research

Figure 15. Turkey, South Africa, Latin America 1/Jan/2009=1.00 (\*)



Source: Reuters, Yapı Kredi Economic Research

Figure 16. Turkey, Eastern Europe 1/Jan/2009=1.00 (\*)

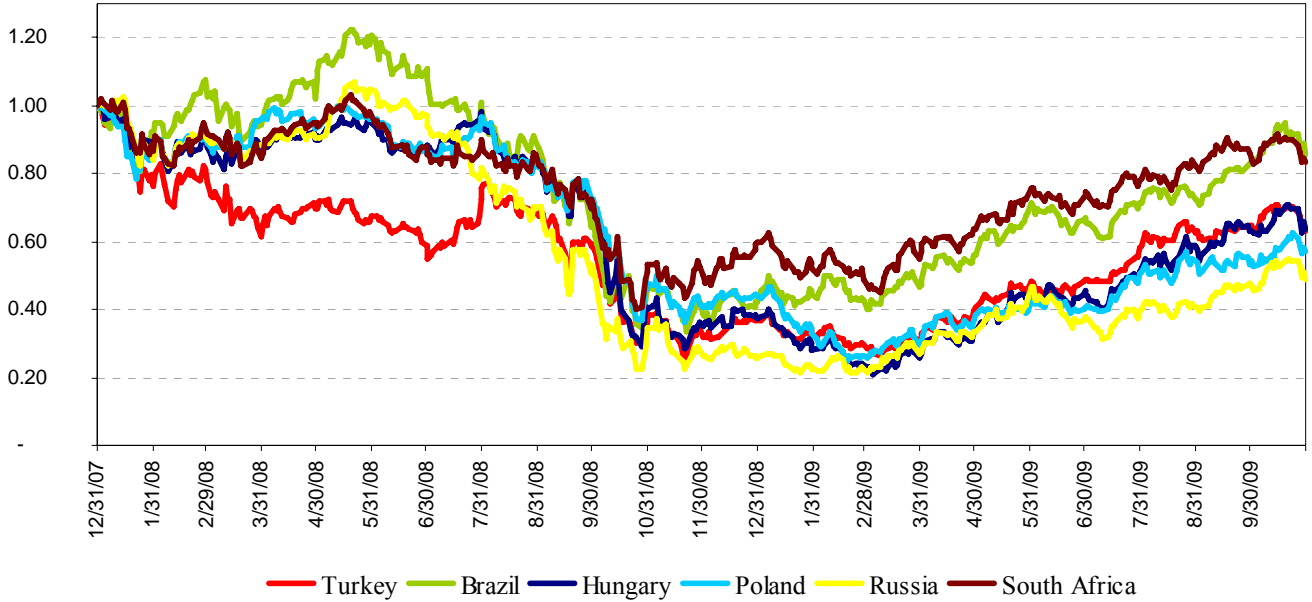


Source: Reuters, Yapı Kredi Economic Research

(\*) Currency performances are calculated against a basket consisting of 0,5 USD+0,5 EUR to neutralize movements of the USD/EUR rate. Y axes in the graphs are inverted. Hence downward move of the curve means depreciation of the currency

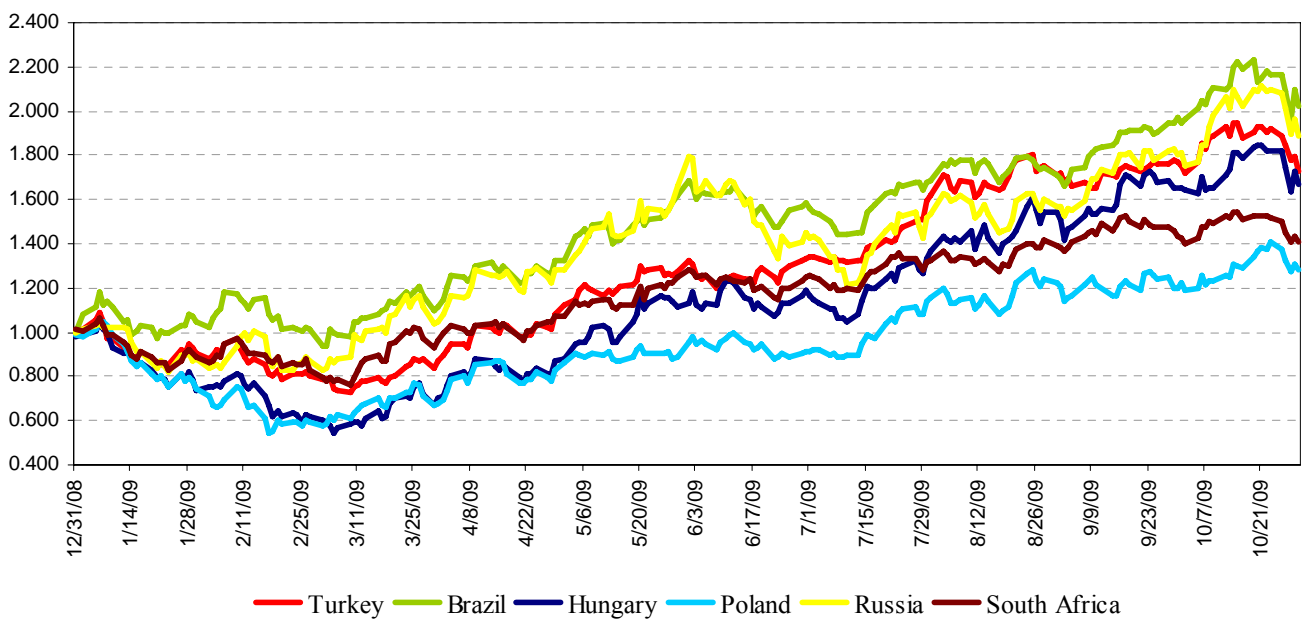
## MSCI

Figure 17. MSCI Turkey versus Other Selected Emerging Markets (12/31/2007=1.00)



Source: Reuters, Yapı Kredi Economic Research

Figure18. MSCI Turkey versus Other Selected Emerging Markets (12/31/2008=1.00)



Source: Reuters, Yapı Kredi Economic Research



## Banking Sector - Highlights of the BRSA's Weekly Data

Funding - TRY mn	2008	Aug-09	Sep-09	16-Oct-09	23-Oct-09	Change (%)			
						Chg.WoW 23-Oct / 16-Oct	Chg.MoM Sep-09 / Aug-09	Chg.QoQ 3Q09 / 2Q09	Chg.YTD 23-Oct-09 / Dec-08
1) Deposits	445,439	464,728	470,956	475,697	475,023	-0.1%	1.3%	1.7%	6.6%
- Deposit Breakdown									
i) TL Deposits	288,433	296,977	300,350	306,375	305,636	-0.2%	1.1%	0.8%	6.0%
- TL Demand Deposits	37,503	37,221	38,872	42,395	39,740	-6.3%	4.4%	-2.6%	6.0%
- TL Time Deposits	250,930	259,756	261,478	263,980	265,896	0.7%	0.7%	1.4%	6.0%
ii) FX Deposits (US\$ mn)	104,873	112,585	115,204	116,653	116,257	-0.3%	2.3%	7.0%	10.9%
- FX Demand Deposits (US\$ mn)	15,835	19,361	19,905	20,506	20,211	-1.4%	2.8%	10.6%	27.6%
- FX Time Deposits (US\$ mn)	89,038	93,223	95,299	96,147	96,046	-0.1%	2.2%	6.3%	7.9%
2) Funds from Domestic Banks	3,987	4,838	4,344	3,929	3,964	0.9%	-10.2%	-15.4%	-0.6%
3) Funds from Foreign Banks	78,153	70,965	70,493	69,880	70,071	0.3%	-0.7%	-4.1%	-10.3%
4) Shareholders Equity	85,816	100,939	101,693	103,396	103,440	0.0%	0.7%	4.9%	20.5%
<b>Total Liab. and Shrs. Equity*</b>	<b>706,949</b>	<b>739,546</b>	<b>744,609</b>	<b>750,837</b>	<b>750,373</b>	<b>-0.1%</b>	<b>0.7%</b>	<b>0.8%</b>	<b>6.1%</b>
<i>*Weekly "Total Liab. and Shrs. Equity" figures are Strategic Planning and Research estimates</i>									
Placements - TRY mn	2008	Aug-09	Sep-09	16-Oct-09	23-Oct-09	Change (%)			
						Chg.WoW 23-Oct / 16-Oct	Chg.MoM Sep-09 / Aug-09	Chg.QoQ 3Q09 / 2Q09	Chg.YTD 23-Oct-09 / Dec-08
1) Liquid Assets	41,830	38,821	38,740	38,171	36,532	-4.3%	-0.2%	-2.4%	-12.7%
2) Due from Banks	30,458	37,700	36,088	34,159	33,323	-2.4%	-4.3%	-2.6%	9.4%
3) Loans	353,120	348,933	350,991	354,231	352,561	-0.5%	0.6%	-0.5%	-0.2%
- Loan Breakdown									
TL Loans	247,671	249,750	251,131	255,988	252,881	-1.2%	0.6%	-0.3%	2.1%
FX Loans (US\$ mn)	70,436	66,566	67,432	67,684	68,415	1.1%	1.3%	2.4%	-2.9%
4) Non-Performing Loans (Net)	2,366	3,567	3,562	3,626	3,684	1.6%	-0.1%	10.1%	55.7%
5) Securities Portfolio	192,812	234,946	237,313	247,796	248,276	0.2%	1.0%	7.6%	28.8%
- TL Securities	144,876	186,154	189,075	200,536	200,564	0.0%	1.6%	10.0%	38.4%
- FX Securities (US\$ mn)	32,019	32,746	32,573	32,559	32,747	0.6%	-0.5%	2.7%	2.3%
6) Other Assets	86,363	75,579	77,915	72,854	75,997	4.3%	3.1%	-8.6%	-12.0%
<b>Total Assets*</b>	<b>706,949</b>	<b>739,546</b>	<b>744,609</b>	<b>750,837</b>	<b>750,373</b>	<b>-0.1%</b>	<b>0.7%</b>	<b>0.8%</b>	<b>6.1%</b>
<i>*Weekly "Total Assets" figures are Strategic Planning and Research estimates</i>									
Other Indicators - TRY mn	2008	Aug-09	Sep-09	16-Oct-09	23-Oct-09	Change (%)			
						Chg.WoW 23-Oct / 16-Oct	Chg.MoM Sep-09 / Aug-09	Chg.QoQ 3Q09 / 2Q09	Chg.YTD 23-Oct-09 / Dec-08
FX Pos. - Balance Sht.-(US\$ mn)	-4,153	-10,079	-11,855	-13,842	-13,595	-1.8%	17.6%	42.0%	227.4%
Foreign Exchange Net General Position (US\$ mn)	-82	915	398	-291	382	-231.3%	-56.4%	9.5%	-564.5%
Securities Held Under Custody (Nominal)	101,399	102,287	100,879	98,255	98,376	0.1%	-1.4%	-1.3%	-3.0%
- Residents (Nominal)	72,849	75,020	73,782	70,718	70,769	0.1%	-1.7%	-2.3%	-2.9%
- Non-Residents (Nominal)	28,551	27,267	27,096	27,536	27,606	0.3%	-0.6%	1.7%	-3.3%
<b>TRY/US\$ rate - (period-end)</b>	<b>1.4971</b>	<b>1.4900</b>	<b>1.4809</b>	<b>1.4515</b>	<b>1.4570</b>	<b>0.4%</b>	<b>-0.6%</b>	<b>-3.4%</b>	<b>-2.7%</b>
Ratios	2008	Aug-09	Sep-09	16-Oct-09	23-Oct-09	Change			
						Chg.WoW 23-Oct / 16-Oct	Chg.MoM Sep-09 / Aug-09	Chg.QoQ 3Q09 / 2Q09	Chg.YTD 23-Oct-09 / Dec-08
<b>Loan Structure</b>									
TL Loans/Total Loans	70.1%	71.6%	71.5%	72.3%	71.7%	-0.5	0.0	0.2	1.6
Consumer Loans/Total Loans	23.1%	24.1%	24.3%	24.3%	24.5%	0.3	0.2	0.6	1.5
Home Loans/Consumer Loans	46.3%	46.4%	46.5%	46.8%	46.9%	0.1	0.1	0.2	0.7
Auto Loans/Consumer Loans	6.6%	5.2%	5.1%	5.0%	4.9%	-0.1	-0.1	-0.5	-1.7
Personal Need Loans/Consumer Loans	47.1%	48.4%	48.5%	48.2%	48.1%	0.0	0.0	0.3	1.0
Credit Card Loans/Total Loans	9.5%	10.0%	10.0%	10.0%	9.9%	-0.1	-0.1	0.1	0.4
Commercial Installment Loans/Total Loans	10.7%	10.0%	9.9%	9.8%	9.8%	0.0	-0.1	-0.2	-0.8
Corporate & Commercial Loans/Total Loans	56.8%	55.9%	55.9%	55.9%	55.7%	-0.2	0.0	-0.5	-1.1
<b>Asset Quality</b>									
NPL Ratio	3.4%	5.1%	5.2%	5.3%	5.4%	0.1	0.1	0.6	2.0
NPL Provision Rate	80.8%	81.0%	81.7%	81.8%	81.7%	-0.2	0.6	0.6	0.8
Consumer Loan NPL Rate	2.2%	3.9%	4.0%	4.1%	4.1%	0.0	0.1	0.6	1.9
Credit Card NPL Rate	6.7%	9.7%	10.2%	10.7%	10.9%	0.2	0.5	1.2	4.2
Commercial Installment Loans NPL Rate	4.5%	7.6%	8.2%	8.4%	8.5%	0.1	0.6	1.5	4.0
Corporate / Commercial Loans NPL Rate	3.1%	4.3%	4.3%	4.3%	4.3%	0.1	0.0	0.3	1.3
<b>Other Key Ratios</b>									
Off-balance Sheet Liab./Total Assets	63.9%	66.8%	74.5%	76.3%	76.5%	0.2	7.7	9.5	12.6
FX Balan. Sheet Pos./Shrs. Equity	-7.2%	-14.9%	-17.3%	-19.4%	-19.1%	0.3	-2.4	-4.1	-11.9
Sec. Under Custody (Residents)/Sec. Under Custody (Total)	71.8%	73.3%	73.1%	72.0%	71.9%	0.0	-0.2	-0.8	0.1

## DISCLAIMER

All information enclosed in this e-mail and document has been obtained from sources believed to be reliable and accurate but which without further investigation cannot be warranted as to their accuracy or completeness. There may also appear opinions which are of non-factual nature and subject to change without notice for which Yapı Kredi Yatırım Menkul Değerler A.Ş. cannot be held responsible. This document and its contents are provided solely for the recipient(s), who is/are expected to make their own investment decisions without undue reliance on any information contained in this e-mail. In no circumstances should any information contained herein be used or considered as an offer to sell or a solicitation of any offer to buy the securities or commodities mentioned. Any of the directors, officers or employees of Yapı Kredi Yatırım Menkul Değerler A.Ş. or of their affiliates may serve as a director for companies mentioned in this document. From time to time, Yapı Kredi Yatırım Menkul Değerler A.Ş. and any of its directors, officers, employees or representatives, directly or indirectly, may have positions or otherwise be interested in any transactions, in any securities, or in any commodities mentioned. The views and opinions expressed in this document belong to the members of the Research Team of Yapı Kredi Yatırım Menkul Değerler A.Ş. and do not represent views and opinions of the Yapı Kredi Yatırım Menkul Değerler A.Ş. management. It is possible that individuals employed by Yapı Kredi Yatırım Menkul Değerler A.Ş. elsewhere or affiliates of Yapı Kredi Yatırım Menkul Değerler A.Ş. may disagree with the recommendations or opinions in this document. Yapı Kredi Yatırım Menkul Değerler A.Ş. or their affiliates may, from time to time, perform investment banking or other services for, or solicit investment banking or other business from, any company mentioned in this document. This document is for the use of addressees only. It may not be copied or distributed to any other persons without the written consent of Yapı Kredi Yatırım Menkul Değerler A.Ş.