MACRO BRIEF

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Sailing Against the Tide

2008 4th Quarter GDP decreased by 6.2% yoy-in line with our expectation (6.4%) - bringing the 2008 growth to 1.1% (Figure.1- Figure. 2). Market consensus was slightly more optimistic with a 5.8% contraction expectation. This is the first time we see a contraction in GDP since the 2001 crisis- putting a side its alarming size-, and the worst is still yet to come; leading indicators such as industrial production, capacity utilization, external demand, and to a lesser extent consumer confidence indices and credit stocks are all pointing at direr growth prospects for 2009- especially in the first half. Putting the entire blame on the global financial crisis for this contraction will be misleading; Turkey had lost its momentum long before the crisis emerged. It will be interesting to see what kind of policy actions will be in place and what their efficacy will be on growth in the upcoming period.

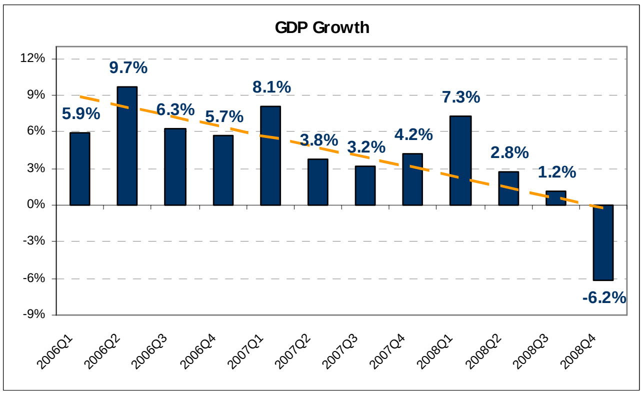

Figure.1

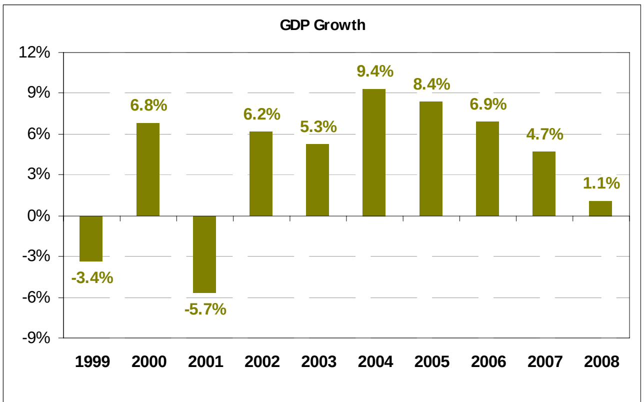

Figure.2

On the expenditures front, private consumption and private investments both displayed strong negative contributions to growth with 3.2 and 5.4 percentage points, respectively, while public expenditures continued to contribute thanks to improved debt dynamics. The Government seems to have exploited the reduction in interest expenditures to its full by compensating that by significant non-interest expenditure expansions, a state of affairs that would have been beyond contemplation as recent as three to five years ago. The breathing room provided by debt dynamics improvement is thus open to proper use but not to abuse, and the thin line had better be defined as early and as clearly as possible.

Net exports' positive contribution with 5 pp prevented a doom case scenario one might say, but the very same contribution is indeed stemming from a not so impressive economic outlook in the first place. Acceleration of the slowdown in imports is visibly stronger than the one in exports, yielding the contribution cited above, yet this is so typical of and peculiar to slowdown periods itself. Finally, the change in inventories contributed negatively to growth after 4 consecutive quarters of positive contribution.

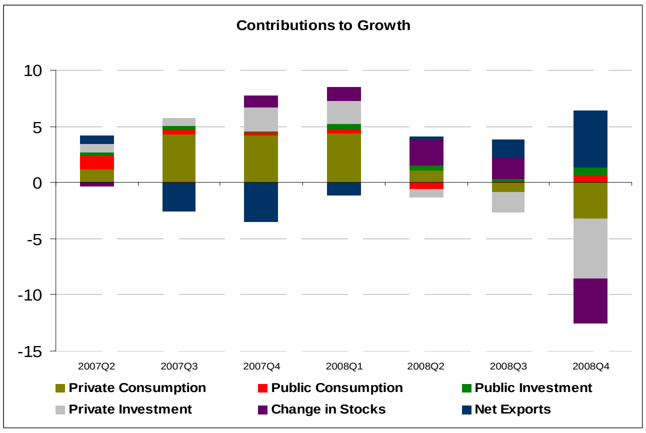

Figure.3

On the production side, Industrial Production Index signals proved to be low in noise content and Services accompanied Industry, both contributing negatively with around 2.5 pp. while agriculture contributed positively with 0.4 pp. The subsectors of Services also exhibit the Turkish Economy's overall contraction experience; Construction continued its free fall (- 0.9 pp), Trade slumped (-2 pp), and even Transportation contracted significantly (-1 pp). Only Financial Intermediation Services remains strong with a 1 pp positive contribution.

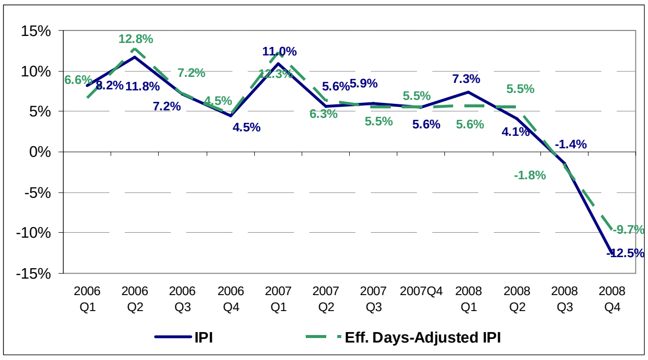

Figure.4

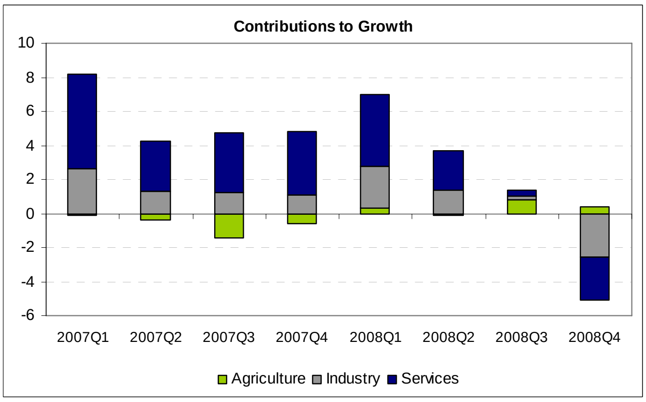

Figure.5

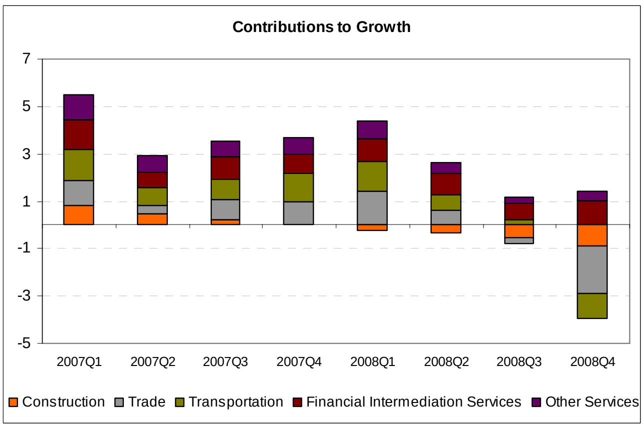

Figure.6

Market expectation for 2009 growth is -2 according to CBRT's Expectation Survey, though some are more pessimistic with forecasts declared going to levels as low as 7%.

We believe any scenario with higher than 5% GDP contraction is a major crisis scenario rather than a serious cooling down or deceleration one. It is a completely different setting and the forecasts and positioning should be done according to a period of crisis and a following period of normalization. We believe there is not clear evidence that supports such a case, the models with crisis output underestimate direct and indirect effects of Agricultural pick up in production side- effects on Trade and Private Consumption ect. - and Government spending on total consumption on the expenditure side – we believe the fiscal ease will be potent and bringing the budget deficit around 4-4.5% of GDP in 2009. In addition we also believe in the-minor but- buoyant effects of the minor revitalization packages that the government has announced recently. These factors above could not save Turkey from shrinking in 2009 but will be effective in preventing the picture from turning into one of total collapse. Our GDP forecast for 2009 is -3.2% growth, with -5.3% and -5.5% growth rates for the first 2 quarters followed by a mild pick up with -2.6% and 0.6% growth rates for the last two quarters.(Figure.7)

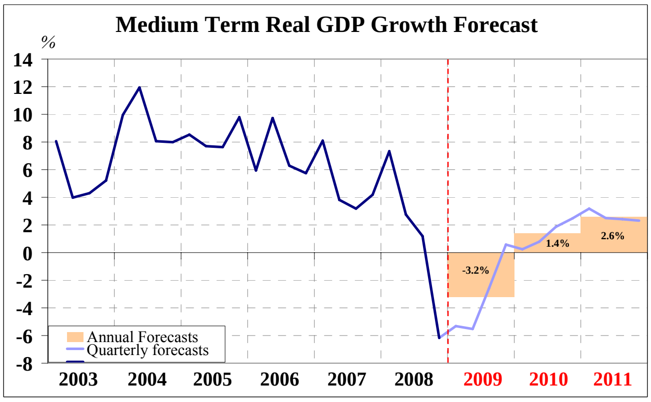

Figure.7

Since the Output Gap is so large, demand fails to serve as a threat to inflation. CBRT has tactfully taken advantage of this and moved ahead of the market, decreasing the policy rate from 16.75% to 10.5% in five months. We believe the CBRT will cease the rate cuts after a 50 bps cut this month, but we would have preferred a bolder one or a no cut instead of a mild 50 bps cut as signaling impacts will (would) be different. Another 100bps cut in total till the end of this year is our base case policy rate scenario.

Trade balance is also being affected immensely by the current environment, and the reflection is not only visible in export and import values but in quantity indices as well. Imports are slowing down much faster than exports, and that is what underlies the expectation of positive net exports contribution to growth in 2009. Current account will consequently reduce to around 3.1% of GDP.

Exchange rate dynamics is a trickier story. The prospective IMF deal will serve as a strong buffer against depreciation pressures if and when it materializes, and anticipate the opposite if it does not, and with an abrupt initial jump in exchange rates (nothing comparable to what we had seen in the past, but discernible nevertheless). If the net re-payer status of non-bank corporates is sustained with little pressure on the market and/or no sizeable effort to switch the denomination of the debt, exchange rates should remain fairly tamed. The depreciation of late has taken place in a surprisingly well-behaved fashion (low volatility). Global outlook and local disturbances could reverse that and produce a high volatility year in 2009, but we would expect 2010 to be a relatively more serene one than 2009 under all possible circumstances.

For a snapshot of our latest forecasts for 2009 and 2010, we provide the table below for the interested reader.

MACROECONOMIC SCENARIO - TURKEY

Key Indicators	**2007**	**2008**	**2009f**	**2010f**
Nominal GDP (YTL billion)	843.2	950.1	978.4	1055.0
Nominal GDP (USD billion)	645.2	730.5	586.7	669.0
Nominal GDP (EUR billion)	472.1	498.3	450.7	484.8
Nominal GDP (yoy %)	11.2	12.7	3.0	7.8
Real GDP (yoy %)	4.7	1.1	-3.2	1.4
Consumption (yoy %)	*4.6*	*0.3*	*-4.6*	*1.5*
Investment (yoy %)	*5.4*	*-4.6*	*-10.0*	*1.0*
Gov. Consumption (yoy %)	*6.5*	*1.8*	*12.0*	*4.0*
Stock Building (share in GDP %)	*-0.1*	*0.2*	*0.2*	*0.2*
Exports (yoy %)	*7.3*	*2.6*	*-10.0*	*6.0*
Imports (yoy %)	*10.7*	*-3.1*	*-13.0*	*6.5*
Inflation (CPI), eop (yoy %)	8.4	10.1	6.0	5.0
Inflation (CPI), avg. (yoy %)	8.8	10.5	6.4	6.3
Unemployment rate (%)	9.9	10.7	12.5	11.5
Exchange rate / € (eop)	1.714	2.144	2.187	2.119
Exchange rate / € (avg.)	1.786	1.907	2.171	2.176
Exchange rate / USD (eop)	1.165	1.529	1.620	1.546
Exchange rate / USD (avg.)	1.307	1.301	1.668	1.577
Parity €/USD (eop)	1.472	1.402	1.350	1.370
Parity €/USD (avg.)	1.370	1.475	1.302	1.380
Reference O/N simple, eop (%)	15.75	15.00	9.00	8.00
Reference O/N compounded, eop (%)	17.05	16.18	9.42	8.33
Benchmark (T-bill) interest rate, eop (%)	16.59	16.45	11.92	10.03
Exports (USD billion)	107.2	132.0	98.7	128.5
Imports (USD billion)	170.1	201.8	143.7	184.4
Current Account/GDP (%)	-5.9	-5.7	-3.1	-3.4
FDI/GDP (%)	3.4	2.5	2.0	2.2
Budget Balance/GDP (%)	-1.6	-1.8	-4.0	-3.0
Primary Balance/GDP (%)	4.2	3.5	1.0	1.6
Public Debt/GDP (%)	42.1	43.3	46.2	46.7
Population (thousands)	70,586	71,517	72,439	73,355

Source: Yapi Kredi Economic Research forecasts, 31-03-2009

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