

VAKIFBANK TURKISH ECONOMY WEEKLY

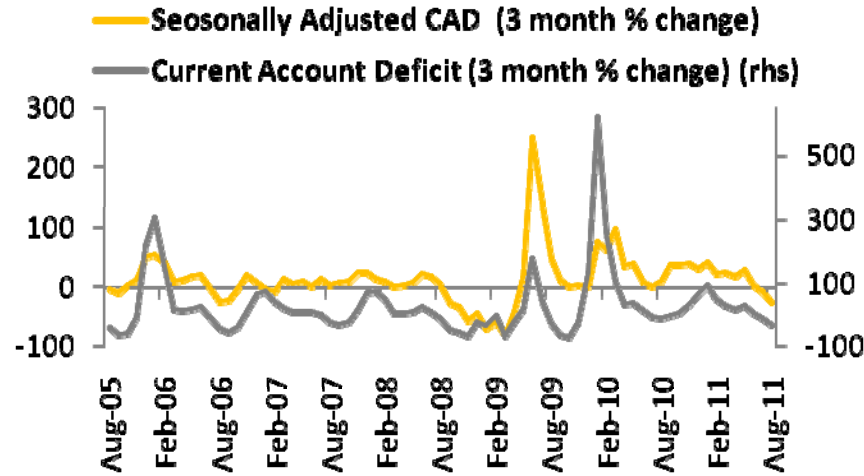
*Industrial Production and Current
Account Balance: More Visible Signs
of Slowdown*



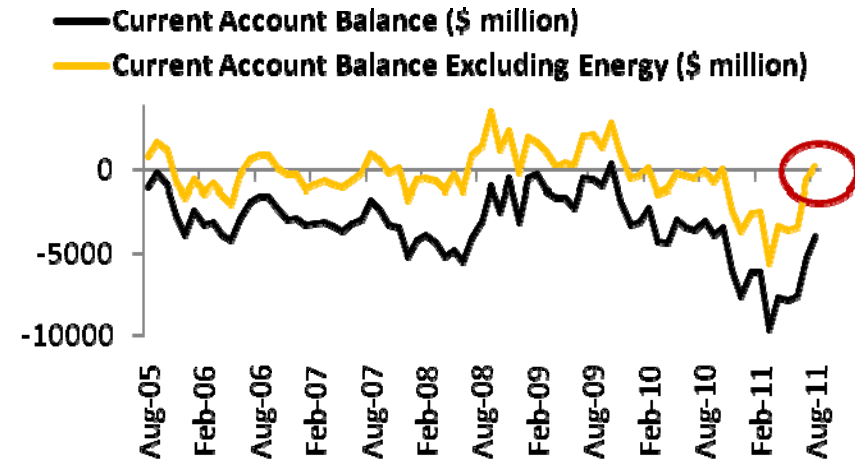
T. Vakıflar Bankası T.A.O



Current Account Deficit was \$3.96 billion in August 2011...



Source: CBRT, VakifBank

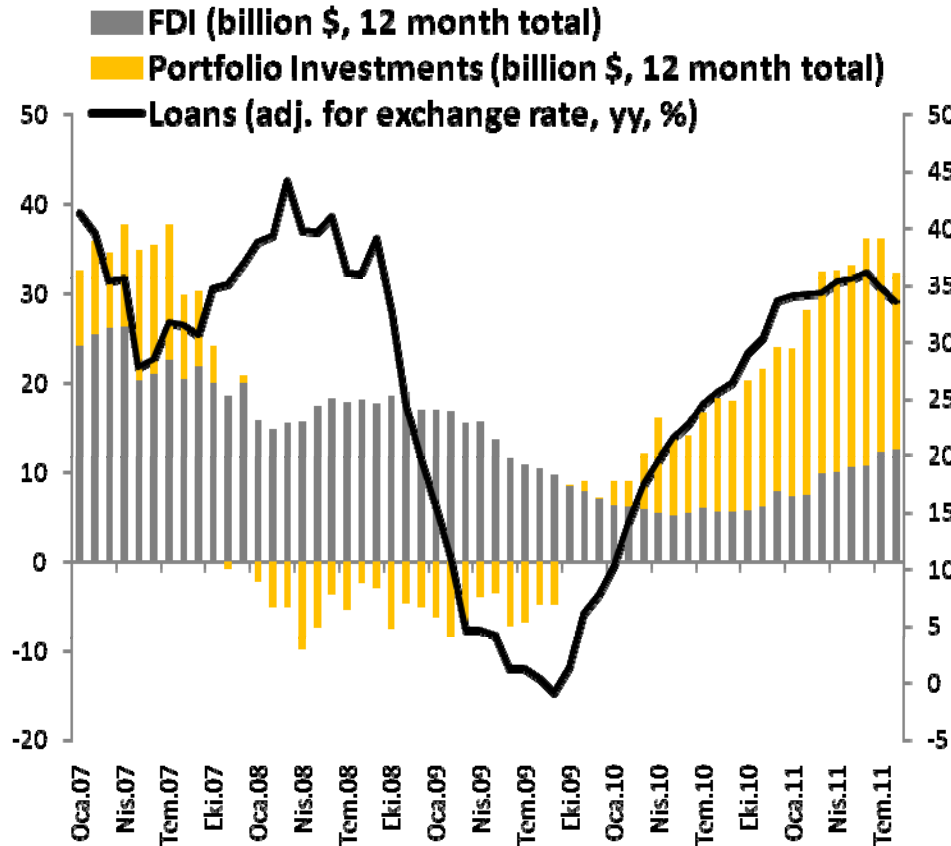


Source: CBRT, Treasury of Turkey, VakifBank

- ✔ Last 12-month trailing current account deficit (CAD) reached to \$75.1 billion in August.
- ✔ Annual increasing rate of current account deficit continued to decrease in August after July.
- ✔ The measures taken by both CBRT and BRSA and recent movements in exchange rate and oil prices contribute to the fall of increasing rate of CAD.
- ✔ Especially with the effect of tourism revenues, services positively affected the current account balance. Hence, although decline in CAD can be explained with the positive effect of tourism revenues in summer, seasonally adjusted CAD also decreased in August.

- ✔ Since energy constitutes a big part of intermediate goods import of Turkey, analyzing CAD excluding energy is more useful to see the positive movement of CAD.
- ✔ CAD excluding energy turned positive in August 2011.
- ✔ In other words, current account balance excluding energy had surplus in August for the first time after September of 2010.

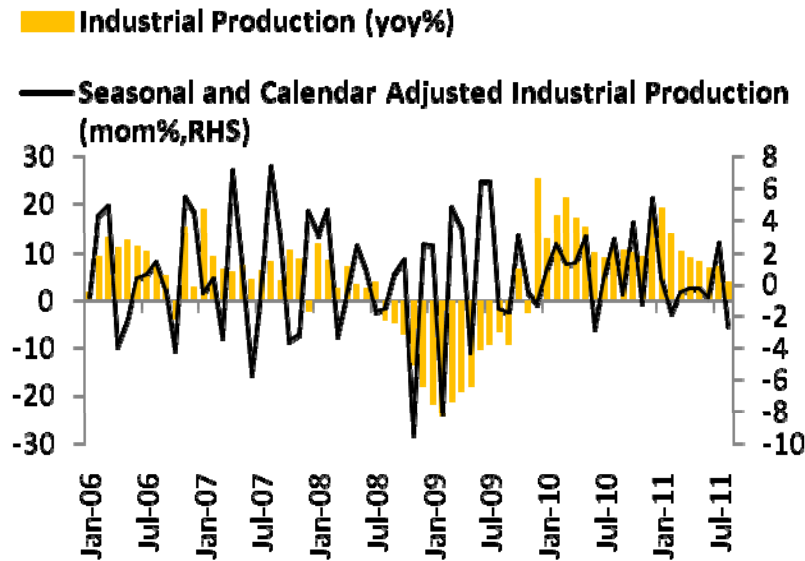
CAD financing is weakening...



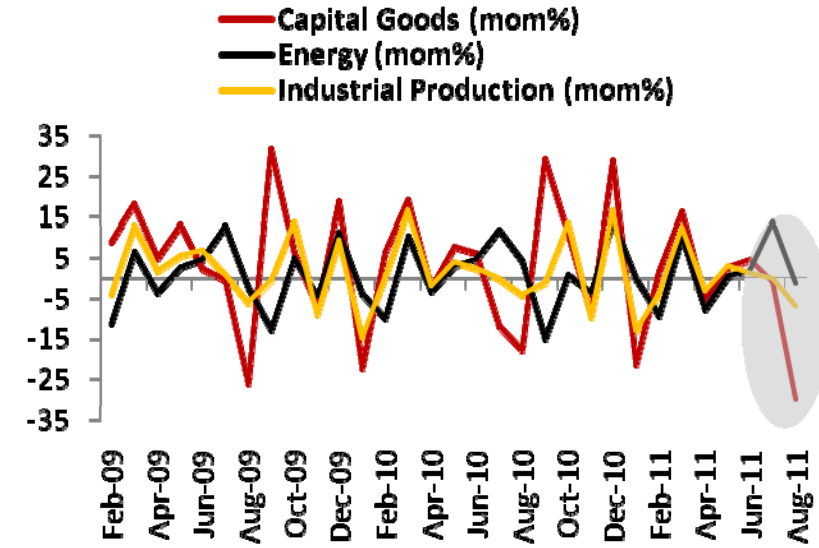
Source: CBRT, BRSA, Vakifbank

- In Jan-Aug 2011, Foreign Direct Investment (FDI) inflows reached \$8.6 billion with \$0.9 billion monthly increase in August.
- Due to \$1.5 billion outflows in August, portfolio investments decreased slightly. In the first eight months of 2011 total amount of portfolio investments were \$17.8 billion.
- Main financing source of C/A deficit was the \$4.4 billion decrease in FX reserves in August due to CBRT operations.
- The quality of C/A financing is low due to the fall in FX reserves and the high share of portfolio investments which is 33% in August.
- The fall in portfolio investments is consistent with the slightly weakening total credits, which is also explanatory for the slow down in industrial production.

Industrial production slowed down in August...



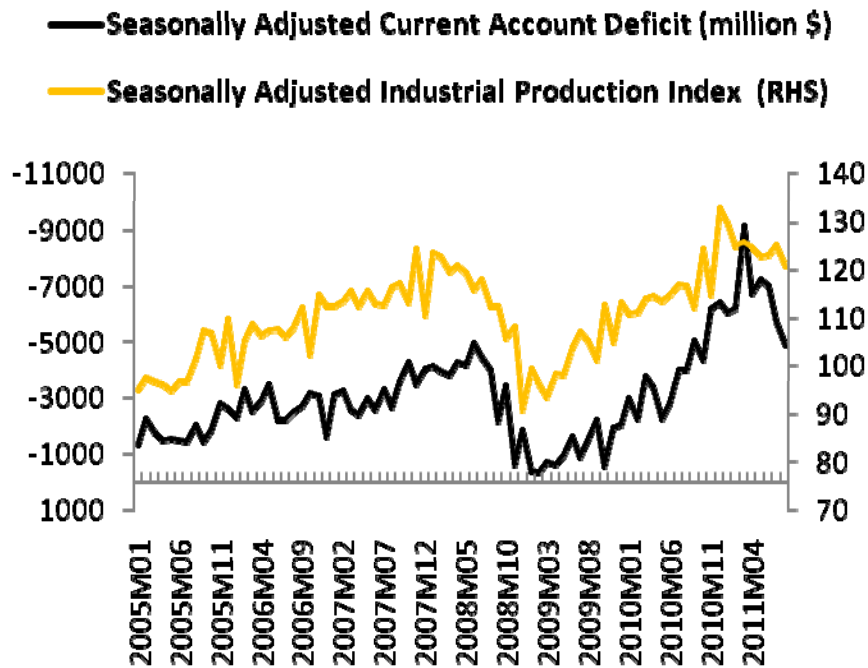
Source: Turkstat



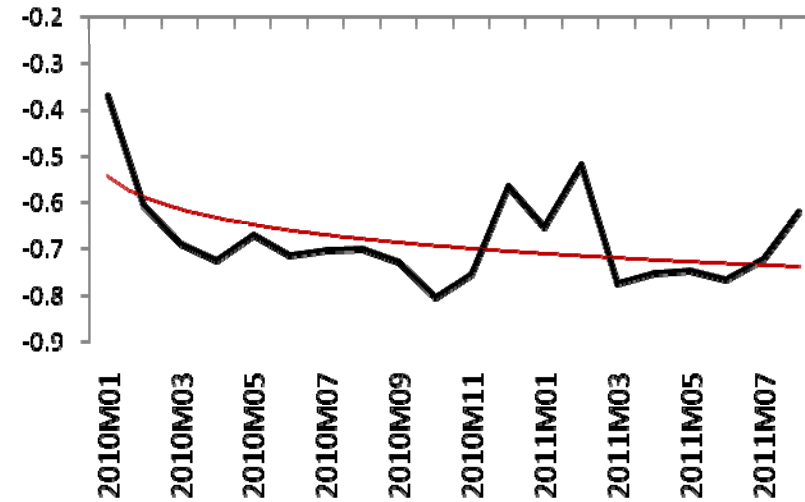
Source: Turkstat

- Industrial production rose by 3.8% in August which is the lowest level since November 2009.
- Seasonal and calendar adjusted industrial production which was negative since January, had turned to positive trend in July. Yet, it has turned to negative trend again with 2.6% fall in August.
- Industrial production in July was well above the expectations while it was under the expectations in August because production was realised one month earlier due to the Ramadan effect.
- Slowing down in seasonal and calendar adjusted production caused concerns about the further movement of industrial production. Although, with the base effect industrial production may increase in September, we expect that in Q4 2011 industrial production will continue to decline gradually. This supports our growth expectations. Moreover, decline in intermediate and capital goods production also supports this expectation.
- Besides, concerns about Eurozone exhibits a negative situation for industrial production for the coming period.

There is high correlation between current account and industrial production...



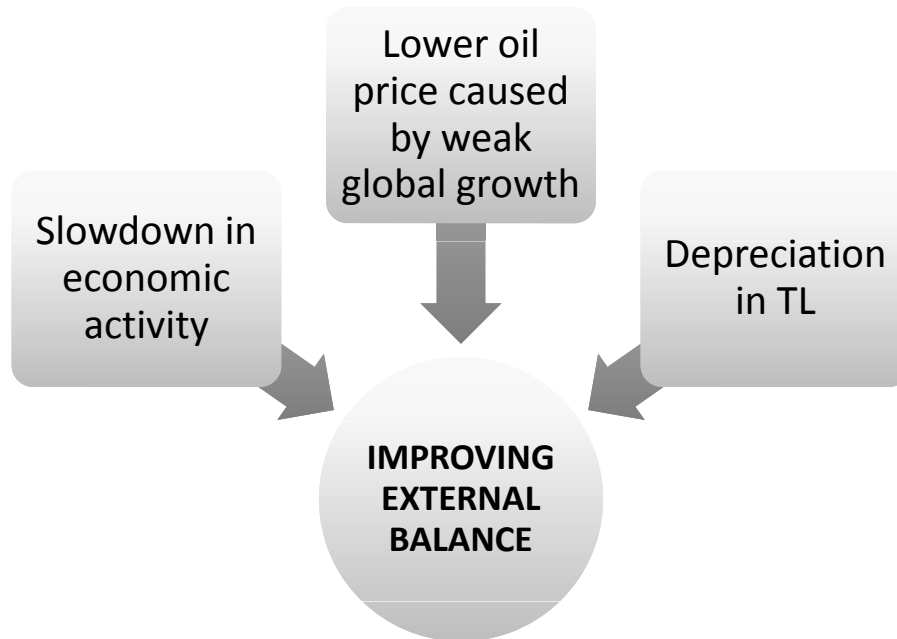
— Correlation between Current Account Deficit and Industrial Production Index
— Log. (Correlation between Current Account Deficit and Industrial Production Index)



- When we investigate the movements of both current account deficit and industrial production index together, the graph indicates a good fit between them.
- Current account deficit has followed industrial production after 3 months as seen in the Graph.
- Correlation between current account deficit and 3 months lagged of industrial production has increased since the end of the crisis. After his correlation peaked at -0.80 in the last quarter of 2010, it has fluctuated between -0.50 and -0.77.
- Recently, this correlation has slowed down a bit. It can be said that the rising prices of imported inputs depending on upward movements in exchange rate has an effect on this downward movement.

Current Account Balance Continues to Improve...

Recovery in the External Balance to Gain Momentum in Q3 and Q4



Medium-Term Economic Program, New Tax Measures and Current Account Balance.

- ✎ The government's "Medium-Term Economic Program", covering the period between 2012 and 2014 states strategy to diminish current account deficit to reasonable figures in long terms by structural reforms.
- ✎ According to the "Medium-Term Economic Program, Turkey's current account deficit is expected to be \$71.7 billions and 9.4 percent of GDP in 2011. This expectation is consistent with our forecast.
- ✎ The government increased the special consumption tax (SCT) on mobile phones and some types of motor vehicles, which are important in non-energy import. It also increased the resource utilization support fund (KKDF) for imports on credit.
- ✎ New tax measures would help reducing the current account deficit.

Serkan Özcan

Chief Economist

+ 90 312 455 7087

serkan.ozcan@vakifbank.com.tr

Cem Erođlu

Senior Economist

+ 90 212 398 1898

cem.eroglu@vakifbank.com.tr

Nazan Kılıç

Economist

+ 90 212 398 1902

nazan.kilic@vakifbank.com.tr

Ümit Ünsal

Economist

+ 90 212 398 1899

Umit.unsal@vakifbank.com.tr

Emine Özgü Özen

Researcher

+ 90 212 398 1890

emineozgu.ozen@vakifbank.com.tr

Naime Dođan

Researcher

+ 90 212 398 1892

naime.dogan@vakifbank.com.tr

Fatma Özlem Kanbur

Researcher

+ 90 212 398 1891

fatmaozlem.kanbur@vakifbank.com.tr

T. Vakıflar Bankası T.A.O

Eski Büyükdere cad. No:61 Gold Plaza

Kağıthane İstanbul, Turkey

www.vakifbank.com.tr

Vakıfbank Economic Research

ekonomik.arastirmalar@vakifbank.com.tr

The information in this report has been obtained by Türkiye Vakıflar Bankası T.A.O. from sources believed to be reliable. However, Türkiye Vakıflar Bankası T.A.O. cannot guarantee the accuracy, adequacy, or completeness of such information, and cannot be responsible for the results of investment decisions made on account of this report. This document is not a solicitation to buy or sell any of the securities mentioned. All opinions and estimates included in this report constitute our judgment as of this date and are subject to change without notice. This report is to be distributed to professional emerging markets investors only.
