FORTIS

Macro Scope

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Weekly Economic and Strategic Review

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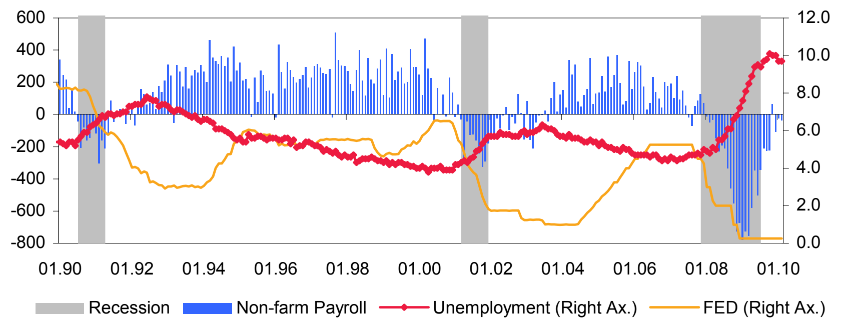
When Will The Extended Period Be Expended?

While the decoupling in the monetary policies of major economies was the recurrent theme of the markets this year, we expect the course followed by the U.S. in normalizing exceptionally low interest rates and extraordinary liquidity bailouts to remain of central importance to other countries as well – particularly through risk appetite channels. Markets took note of the Fed's renewing its pledge to "keep rates low for an extended period" following the FOMC's March 16th meeting, although the term "extended period" bought the Fed a certain amount of flexibility. An assessment of the factors affecting growth and inflation brought about minor changes in tune with these factors, compared to previous statements, but the core message was unchanged in a brief statement issued by the FOMC following a meeting held after two arduous months. This means everyone could interpret the message as they saw fit. Those expecting no rate hike this year and those foreseeing an increase in the second half both felt they were on the right track. Either scenario could reach fruition – only the evolution of indicators will tell. **But from today's vantage point, we are leaning towards the Fed's removing the phrase "extended period" from the text and increasing the rates by 25 bps in the last quarter – this of course after having drained any potential left in the ultimate liquidity pool (TALF) in June.** Yet the main driver will be confirmation of the 10.1 percent peak in the unemployment rate observed in October 2009 and onwards, while achieving a net decline trend in the months ahead. At the same time, the underperforming housing industry, duly noted in the FOMC report, should be monitored closely. In fact, the U.S. housing market has shown no discernable recovery since hitting rock bottom in the first half of 2009, which explains why the Fed in the FOMC minutes made a point of highlighting that the housing starts remained flat at a depressed level. **Barring a new deterioration in the areas mentioned the Fed can be expected to continue to gradually normalize its monetary policy.**

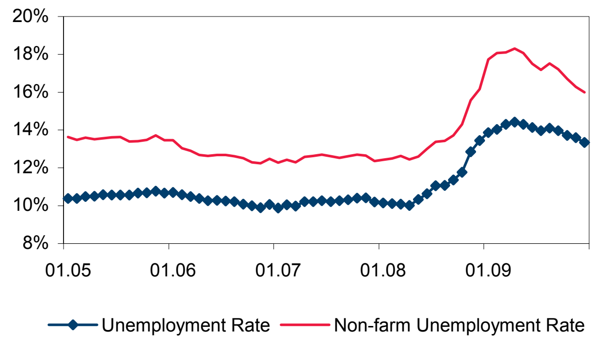
Unemployment, Non-Farm Payrolls and FED Policy Rate (1990-2010)



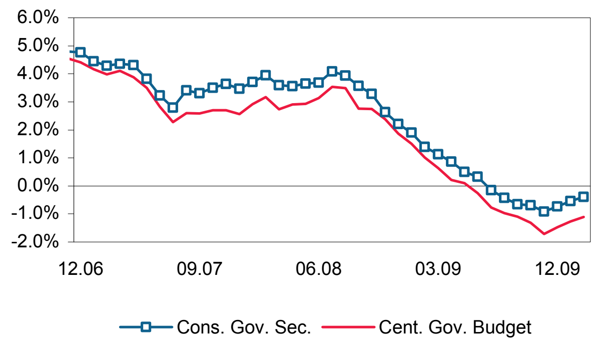
(*) Grey areas represent recession periods.
Source: FED, Reuters, Fortis Economic Research and Strategy

Also in Turkey, the struggle between pushing (accelerator) and pulling (inhibitor) factors persists with respect to normalizing monetary policies. Currently, the Fed's messages are widely perceived as pulling factor. A delay in anticipated rate hikes by the Fed balances out the upward push on the Central Bank's policy rate or long-term rates. **The other important pulling factors are the slow recovery in industrial output, low capacity utilization, and high unemployment rates.** Also on the inhibitor's side is the recent improvement in fiscal performance with its positive impact on Treasury borrowing. On the other side, **high inflation is the main pushing factor.** Negatively affected by inflation data, these pushing factors now embody inflation expectations. **Also included in the pushing factors are positive developments in the credit markets and improvements in foreign borrowing.** As for financial indicators, the **stability of the Turkish lira** exchange rate against other major currencies plays a **neutral role in the normalization** process. **Low loan rates and Treasury yields** balance the deterioration in inflation expectations to a certain degree, while **having no net effect on normalization, but it could sway the Central Bank's choice of response by pen or by sword.** In other words, in an environment where inflation expectations are inching up, which might surpass the inflation targets, a downward trend in both medium and long-term rates will not be comforting to the Central Bank and could actually highlight the need for intervention in the yield curve.

Unemployment Rate (Seasonally Adjusted)



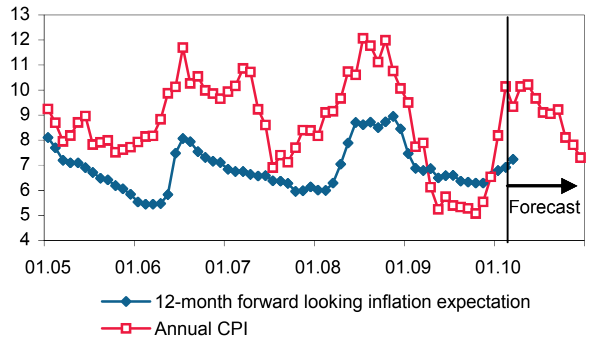
Primary Balances (% GDP)



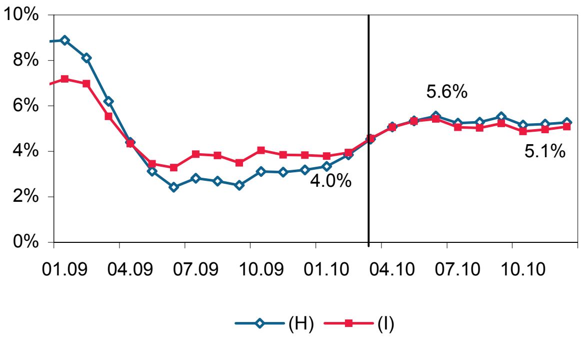
Source: Turkstat, Finance Ministry, Treasury, Fortis Economic Research and Strategy
(*) January and February figures were not available for Consolidated Government Sector. We assume that the missing data will be unchanged vs. last year

In the minutes of the March 18th meeting of the Monetary Policy Committee, the Central Bank sang its signature tune which is critical to the onset of normalization: *"the policy rate will have to be kept low for an extended period".* However, *"resource utilization in the economy will remain low for some time"* and *"there are still uncertainties regarding the strength of the global economy recovery"* sentences are omitted that shows **the CBT continued to sound more hawkish.** For the inflation outlook, however, the short note states that inflation would drop to single digits in March, yet hover significantly above the target for sometime. It would then revert back to a downward trend as the temporary factors taper off starting with the last quarter of the year, and decline to levels consistent with inflation targets by early 2011. While the Committee notes that the **core inflation indicators** would increase in the short term, especially in March and April, it would remain at levels below the target to prime the market for an anticipated increase in the core inflation rate (from 4 percent to at least 5.5 percent) – which is more important for monetary policy decisions. Given its current stance, the Central Bank also included in its policy decision **an exit clause addendum** stating that the Committee will not hesitate to tighten the stance on monetary policy sooner than originally envisioned under the baseline scenario of the Inflation Report, should any unforeseen developments lead to deterioration in general price setting behavior. **This clause gives the Central Bank an additional month to monitor pricing behavior and some latitude in its vow to stick to low rates for the long term.**

Inflation and Inflation Expectations (% y/y)



(H) and (I) Core Price Indices* (% y/y)



(*) The annual inflation rates calculated for the rest of 2010 assumes that the undelying inflation trend stays at 5% vicinity.
Source: Tukstat, Fortis Economic Research and Strategy

In summary, we expect the Fed to continue to gradually normalize its monetary policy. A rate hike by the Fed in the last quarter still remains the most feasible scenario. Set by economic indicators, the pace of normalization will continue to influence the global risk appetite. On Turkey's plate, the factors affecting the pace of normalization are in constant competition. Having considered these, the Central Bank issued a message similar to that of the Fed but strongly underlined its intention to intervene in any potential disruption in pricing behavior.

Economic and Political Agenda

- This week real sector confidence index and capacity use will be important at home. Glancing at external arena, there will be a busy agenda especially in the US, with housing data, durable goods orders and final GDP data. In Euro-zone services and manufacturing flash PMI's will be eyed.

Data issuances at Home

Importance	Indicator	Unit	Date of issuance	Fortis *(Consensus)*
Medium	Capacity Use, Mar.	%	Mar. 24th, 14:30 GMT	*(69)*
High	Real Sec. Confid. Index, Mar.		Mar. 24th, 14:30 GMT	-

Data issuances Abroad

Importance	Country	Indicator	Unit	Date of Issuance	Consensus
High	U.S.	Existing Home Sales, Feb.	mn	Mar. 23rd, 14:00 GMT	5.0
Medium	Eurozone	Services Flash PMI, Mar.	-	Mar. 24th, 8:58 GMT	52.0
Medium	Eurozone	Manufacturing Flash PMI, Mar.	-	Mar. 24th, 8:58 GMT	54.2
Medium	Germany	Ifo Index, Mar.	-	Mar. 24th, 9:00 GMT	95.8
High	U.S.	Durable Ord., Feb.	% m/m	Mar. 24th, 12:30 GMT	0.0
High	U.S.	New Home Sales, Feb.	mn	Mar. 24th, 14:00 GMT	0.32
Medium	U.S.	Core PCE, 4Q.	% q/q	Mar. 26th, 12:30 GMT	1.6
High	U.S.	GDP (final), 4Q.	% y/y	Mar. 26th, 12:30 GMT	5.7
Medium	U.S.	Michigan Sentiment Index, Mar.	-	Mar. 26th, 13:55 GMT	72.5

Macro-Economic and Financial Forecasts

Macro Economic Outlook of 2009-2012

	2009	2010f	2011f	2012f
GDP (TRY - bn) (*)	975.6	1,113.7	1,219.8	1,325.7
GDP (US$ - bn) (*)	630.6	732.7	791.2	847.9
GDP Growth (y/y % chg) (*)	-5.1	6.0	4.0	4.0
PPI (y/y % chg)	5.9	5.0	4.0	4.0
CPI (y/y % chg)	6.5	7.3	5.5	5.0
Trade Balance (US$ - bn)	-38.6	-62.8	-70.7	-70.6
Exports (FOB, excl. luggage trade)	102.2	116.0	132.6	144.4
Imports (CIF, incl. gold)	140.8	178.7	203.2	215.0
Current Account Balance (US$ - bn)	-13.9	-35.3	-39.9	-37.1
Current Account Balance / GDP (%)	-2.2	-4.8	-5.0	-4.4

(*) 2009 values are our forecasts

Financial Indicators Forecasts

	Mar. 19th	1M	3M	6M	12M	2010	2011
US$/TRY	1.5154	1.5400	1.5300	1.5200	1.5300	1.5200	1.5600
EUR/TRY	2.0723	2.1100	2.1000	2.0800	2.1400	2.1300	2.1800
FX Basket	3.5877	3.6500	3.6300	3.6000	3.6700	3.6500	3.7400
EUR/US$	1.3675	1.3700	1.3700	1.3700	1.4000	1.4000	1.4000
O/N	6.50%	6.50%	6.50%	6.50%	9.25%	8.00%	10.00%
Benchmark Bond	9.10%	9.50%	10.10%	10.60%	11.50%	11.00%	12.00%

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