

FORTIS BANK

Macro Scope

21 - 27 September 2009

Weekly Economic and Strategic Review

Haluk Burumcekci (Managing Director)
Tel: +212 318 34 49
Email: haluk.burumcekci@fortis.com.tr

H. Erkin Isik, CFA (Manager)
Tel: +212 318 34 05
Email: erkin.isik@fortis.com.tr

Nilufer Sezgin (Assistant Manager)
Tel: +212 318 37 90
Email: nilufer.s@fortis.com.tr

Email: research@fortis.com.tr
Tel: +212 272 79 98
Fax: +212 275 44 05

Medium Term Program Ok, Measures Lacking...

In our special report (*Macro Gets Plaudit, But Budget Is On Light Diet*) published within the week behind about the government's Medium Term Program, we said that the macroeconomic targets are realistic, yet the fiscal framework fell short of eliminating the worries about elevated debt burden and hence the pressure on Treasury's borrowing. On Wednesday's night, IMF also came up with similar remarks. In IMF website, Ms. Rachel van Elkan, Mission Chief for Turkey at the International Monetary Fund expressed their pleasure to see Turkey coming forward with a program: "*We are encouraged by the Turkish authorities' announcement of a medium-term framework that aims to gradually reverse the deterioration in the country's public finances, boost private sector activity and restore solid economic growth. Reflecting the considerable impact of the global crisis on Turkey, the authorities' plan encompasses realistic macroeconomic projections and incorporates the appropriate goal of stabilizing the public debt-to-GDP ratio by 2011 and reducing it thereafter. We also welcome the planned introduction of a fiscal rule to establish prudent budgetary targets over the longer term.*" In the remaining part of the statement, Ms. Elkan mentioned about the deficiencies of the program and their expectations that would urge IMF's involvement: "*To meet the authorities' goal of controlling the public debt burden, it will be **necessary to adopt supporting measures and structural reforms, including policies to address key spending pressures.***" Finally, she concluded "*We look forward to continuing our policy dialogue with the Turkish authorities.*" Put differently, she pointed out the necessity for the two sides work together on the measures that would back the targets of the program and turn it into an appropriate stand-by deal.

Recall that in our *Macro Scope* dated August 10th, we had mentioned about an IMF report named '*The State of Public Finances: A Cross-country Fiscal Monitor,*' where IMF summarized the preliminary strategies to ensure fiscal sustainability in G-20 countries. For Turkey, IMF set the target as stabilizing the debt-to-GDP ratio by 2011. The measures IMF found necessary to attain this target were non-renewal of fiscal stimulus, improved expenditure control, local government reform, introduction of fiscal rule and continuation of tax administration. IMF said that, these measures were the result of views of IMF staff on the intentions of the country authorities, based on discussions and announcements in addition to functioning of automatic stabilizers (recovery of revenues). **However, in the Medium Term Program, the government depends heavily on the automatic stabilizers, rather than listing a set of measures.** In that report, IMF concluded **that the level of debt-stabilizing primary balance level for the average of next 5 years is 1.7% of GDP for Turkey.** This was the most important piece of information that would shed light to today. Otherwise, IMF forecasted that debt-to-GDP rate would climb to 58% by 2014.

However, the Medium Term Program foresees that the primary balance in the consolidated government sector receding to a deficit at 2.1% of GDP this year (vs. IMF forecast of 0.2% deficit) and remaining below 0.4% surplus on average in the next 3 years. Therefore, as we had emphasized before, **we think that the fiscal framework in the program is still quite loose, similar to the outlook depicted in the Pre-Accession Program published in April.** Government foresees that the program defined consolidated public sector primary balance to GDP ratio will be -2.1% by end-2009. In the following years, this ratio will recover limitedly to 0.3% primary deficit in 2010, followed by 0.4% and 1.0% surplus in 2011 and 2012, respectively. Meanwhile, the targets for the Treasury's roll-over rates were not given in the Program. Yet, Babacan stated that this ratio would regress below 100% in the following years after reaching 112% this year. This sounds like that the roll-over ratio would remain significantly high for the next few years compared to around 70% roll-over reached in good years in the past. In parallel to the low primary balance targets suggested in the program, the debt stock is foreseen to remain elevated, as well, during 2009-2012 period. The EU-defined public debt stock to GDP ratio at 39.5% in end-2008 is foreseen to remain elevated at 47.8% as of 2012 after increasing 47.3% and 49.0% in 2009 and 2010, respectively.

Medium Term Program				
	2009	2010	2011	2012
GDP (TRY - bln)	947	1,029	1,118	1,227
GDP (US\$ - bln)	608	641	669	723
GDP per capita (US\$)	8,456	8,821	9,096	9,732
GDP Growth (y/y % chg)	-6.0	3.5	4.0	5.0
Unemployment Rate (%)	14.8	14.6	14.2	13.3
CPI (y/y % chg)	5.9	5.3	4.9	4.8
Central Government Budget Balance (TRY - bln)	-62.8	-50.0	-45.1	-39.1
Central Government Budget Balance / GDP (%)	-6.6	-4.9	-4.0	-3.2
Central Govt. Budget PS / GNP (IMF definition, TRY - bn)	-20.8	-8.4	-2.1	4.3
Central Govt. Budget PS / GNP (IMF definition)	-2.2	-0.8	-0.2	0.4
Consolidated Public Sector PS (TRY - bln)	-19.8	-3.5	4.4	11.9
Consolidated Public Sector PS / GNP (%)	-2.1	-0.3	0.4	1.0
Nominal Public Debt Stock / GDP (EU Definition)	47.3	49.0	48.8	47.8
Trade Balance (US\$ - mn)	-35.5	-45.5	-50.0	-57.0
Exports	98.5	107.5	118.0	130.0
Imports	134.0	153.0	168.0	187.0
Current Account Balance (US\$ - bn)	-11.0	-18.0	-22.0	-28.0
Current Account Balance / GDP (%)	-1.8	-2.8	-3.3	-3.9

Meanwhile, in the program, there was only a draft framework about the fiscal rule which is important in terms of establishing a fiscal discipline and setting an anchor in the medium term. It was stated that the fiscal rule will be set on the public balance and the aim will be to keep public deficit to GDP ratio aligned with a sustainable debt structure. The required legal basis for this rule is presumed to be completed in 2010 at the latest and it is planned to be put into force in 2011. Yet, even if this rule is launched and implemented with the legal framework, the important thing will be whether this rule would be bypassed with some other legal arrangement (similar to what we experienced with the limits on borrowing defined by the public internal financial control law). Economy Minister Babacan did not give any clear explanation on this issue, stating that they are still working on it. **The fiscal rule would only be strong enough if and only if it is specified by the Constitutional Law.**

All in all, launching a medium term framework is a positive to development by itself as this should eliminate the uncertainties regarding the direction intended for the economy. We also think that the government's revision in the GDP prospects towards a more realistic outlook, which is also in line with our forecasts, is a positive development regarding the program in first place. On the other hand, the framework suggested in the program is not indicating a tight fiscal discipline that can improve the risk perceptions and can have positive affect on the expectations regarding Turkey. Accordingly, the specified targets failed to meet the anticipations. It seems also hard for IMF to confirm this outlook. Yet, Babacan's statement that the negotiations are continuing with IMF prevented us from making a certain assessment about the IMF deal. On the other hand, in the lack of an IMF program, this Medium Term Program will unlikely replace its role of assuring confidence. In the long term, we will monitor the developments about the fiscal rule for a more constructive perspective on the fiscal policies.

Economic and Political Agenda

▪ This week, the Real Sector Confidence Index and Central Bank's second Expectation Survey for September will be on the agenda on Thursday at home. The rest of the week will be quiet for the domestic calendar though, with the Turkish market being closed on Monday and Tuesday due to the religious holiday. Glancing at the external arena, while the eyes will be on flash PMIs in Eurozone, Fed's rate decision will be important, as well as the housing and consumption data in the U.S.

Data issuances at Home

Importance	Indicator	Unit	Date of issuance	Fortis (Consensus)
High	Real Sector Confidence Index, Sep.		Sep. 24 th , 14:00 GMT	-
High	CB's Expectation Survey, Sep. II	-	Sep. 24 th	-

Importance	Country	Indicator	Unit	Date of Issuance	Consensus
High	Eurozone	Manufacturing Flash PMI, Sep.	-	Sep. 23 rd , 7:58 GMT	49.8
High	Eurozone	Services Flash PMI, Sep.	-	Sep. 23 rd , 7:58 GMT	50.5
High	U.S.	Fed's Rate Decision	bps	Sep. 23 rd , 18:15 GMT	no chg.
Medium	Germany	Ifo Index, Sep.	-	Sep. 24 th , 9:00 GMT	92.0
High	U.S.	Existing Home Sales, Aug.	mn	Sep. 24 th , 14:00 GMT	5.3
High	U.S.	Durable Orders, Aug.	% m/m	Sep. 25 th , 12:30 GMT	1.1
Medium	U.S.	Michigan Cons. Sent., Sep.	-	Sep. 25 th , 13:55 GMT	70.2
High	U.S.	New Home Sales, Aug.	mn	Sep. 25 th , 14:00 GMT	0.45

Macro-Economic and Financial Forecasts

Macro Economic Outlook of 2007-2010

	2008	2009f	2010f	2011f
GDP (TRY - bn)	950.1	926.1	1,016.1	1,123.5
GDP (US\$ - bn)	734.9	597.5	647.2	690.1
GDP Growth (y/y % chg)	0.9	-6.0	4.0	5.0
PPI (y/y % chg)	8.1	4.0	5.0	4.0
CPI (y/y % chg)	10.1	5.5	6.5	5.5
Trade Balance (US\$ - bn)	-69.8	-36.1	-62.2	-67.4
Exports (FOB, excl. luggage trade)	132.0	94.5	102.7	106.1
Imports (CIF, incl. gold)	201.7	130.6	164.9	173.5
Current Account Balance (US\$ - bn)	-41.3	-11.2	-31.6	-34.1
Current Account Balance / GDP (%)	-5.6	-1.9	-4.9	-4.9

Financial Indicators Forecasts

	Sep. 18 th	1M	3M	6M	12M	2009	2010
US\$/TRY	1.4626	1.5000	1.5000	1.5600	1.5800	1.5000	1.5800
EUR/TRY	2.1548	2.1900	2.1300	2.1800	2.1300	2.1300	2.0500
FX Basket	3.6174	3.6900	3.6300	3.7400	3.7100	3.6300	3.6300
EUR/US\$	1.4733	1.4600	1.4200	1.4000	1.3500	1.4200	1.3000
O/N	7.25%	7.00%	6.50%	6.50%	8.50%	6.50%	10.00%
Benchmark Bond	9.20%	9.20%	10.00%	11.50%	12.00%	10.00%	12.50%

Fortis Bank SA/NV Montagne du Parc 3 B-1000 Brussels Belgium Tel: +32 2 565 11 11	Fortis Bank Austria Euro Plaza/D Wienerbergstrasse 41 1120 Vienna Austria Tel: +43 1 81 10 43 81 85	Fortis Bank Czech Republic Myslbek Building Ovocny Trh 8 117 19 Prague 1 Czech Republic Tel: +420 225 43 60 10	Fortis Bank Denmark Gothersgade 49 3. 1123 Copenhagen Denmark Tel: +45 32 71 19 09
Fortis Bank, Succursale en France 30, quai de Dion Bouton F-92824 Puteaux Cedex France Tel: +33 1 55 67 72 00	Fortis Bank Germany Cäcilienkloster 8 50676 Cologne Germany Tel: +49 221 1611-0	Fortis Bank Greece Sygrou Ave 166 17671 Athens Greece Tel: +30 21 09 54 43 70	Fortis Bank Hong Kong 27/F, Fortis Bank Tower 77-79 Gloucester Road Hong Kong Tel: +852 28 23 04 56
Fortis Bank Hungary Deak Ferenc 15 1052 Budapest Hungary Tel: +36 14 83 81 09	Fortis Bank Italy Via Comaggia 10 I-20123 Milano Italy Tel: +39 02 57 53 24 61	BGL 50, avenue J.F. Kennedy L-2951 Luxembourg Luxembourg Tel: +352 42 421	Fortis Bank Norway Haakon VII's gate 10 0161 Oslo Norway Tel: +47 23 11 49 50
Fortis Bank Polska S.A. P.O. Box 15 02-676 Warszawa Poland Tel: +48 22 566 90 00	Fortis Bank Portugal Rua Alexandre Herculano 50-6 Andar 1250-011 Lisboa Portugal Tel: +351 213 13 93 16	Fortis Bank SA/NV, Singapore Branch 63 Market Street #21-01 Singapore 048942 Tel: +65 65 38 03 90	Fortis Bank S.A., Sucursal en España Serrano 73 28006 Madrid Spain Tel: +34 91 436 56 00
Fortis Bank Romania Tipografilor 11-15 013714 Bucharest Romania Tel: +40 21 401 17 02	Fortis Bank Sweden Birger Jarlgatan 25 10396 Stockholm Sweden Tel: +46 8 505 375 59	Fortis Bank Switzerland Rennweg 57 8021 Zurich Switzerland Tel: +41 58 322 09 70	Fortis Bank Turkey Yildiz Posta Caddesi No: 54 Gayrettepe 34353 Istanbul Turkey Tel: +90 212 274 42 80
Fortis Bank SA/NV, UK Branch 5 Aldermanbury Square EC2V 7HR London United Kingdom Tel: +44 20 32 96 80 00	Fortis Bank USA 520 Madison Avenue, 3rd Floor New York, NY 10022 United States Tel: +1 212 418 87 00		

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