

SLOWDOWN CONTINUED IN THE THIRD QUARTER

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Executive Summary

Following this month's data releases, Betam's economic indicators for the third quarter are now complete. In September, the industrial production index (IPI) increased by 3.9 percent, more than expected. Export volume index decreased by 9.7 percent due to the fall in gold exports and import volume index increased by 1.0 percent. The contribution of net exports to the quarterly GDP growth decreased significantly compared to the previous quarters. The Quarter on Quarter (QoQ) increase in the IPI reduced by half and fell to 0.9 percent in the third quarter from 1.9 percent in the second quarter. Our indicators imply that the QoQ GDP growth in the third quarter decreased compared to 1.8 percent growth in the second quarter. In this respect, Betam's QoQ growth forecast for the third quarter of 2012 is 0.7 percent. We estimate the corresponding year on year (YoY) growth rate to be 2.8 percent.

In September, the trade deficit decreased by \$3.6 billion compared to the same month of the last year. The decline in the trade deficit continues to reduce the current account deficit. We estimate

Table 1. Betam's quarterly and annual growth rate forecasts

	2012 3 rd Quarter Forecast
Real GDP growth, % (quarter on quarter, sa*)	0.7
Real GDP growth, % (year on year, ca**)	2.8
Current account deficit (% of GDP, annual)	7.2

Source: Betam

*sa: seasonally and calendar day adjusted

**ca: calendar day adjusted

that the ratio of current account deficit to GDP has fallen down to 7.2 percent at the end of the third quarter from 8.3 percent in the second quarter of 2012.

Growth is lower than the second quarter

In September, IPI increased by 3.9 percent from August and increased by 6.2 percent from the same month of the previous year. Due to this increase, which is above expectations, the IPI rose 0.9 percent, QoQ, in the third quarter. However, it was 1.9 percent in the second quarter. In this respect, QoQ IPI increase is reduced by half, implying further slowdown.

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In the third quarter, we observe a decline in net exports which had contributed significantly to the GDP growth since the last quarter of 2011. In the second quarter, export volume index had increased by 11.5 percent but the increase in exports dropped to 3.8 percent in the third quarter. Moreover, 2.8 increase in imports in the second quarter turned into a 0.3 percent decline in the third quarter. The figures excluding gold imports and exports also show a similar trend. According to Betam's calculations, 1.8 percent increase in real exports excluding gold in the second quarter turned into 0.6 percent decline in the third quarter and 1.3 percent decline in real imports excluding gold in the second quarter dropped to 0.8 percent decline in the third quarter (Table 2). Both our calculations and Turkstat data imply that the contribution of net exports to the GDP growth was lower in the third quarter than the second quarter.

Besides the slowdown in IPI and the decrease in contribution of net exports, consumer and real sector confidence index continued to deteriorate in the third quarter. Following these indicators we believe that the GDP growth in the third quarter will be lower than the 1.8 percent growth in the second quarter. Betam's forecast for the QoQ GDP growth in the third quarter is 0.7 percent. We estimate the corresponding year on year (YoY) growth rate to be 2.8 percent. Due to the base effect, our YoY growth rate estimate for the third quarter is very close to 2.9 percent GDP growth in the second quarter, but slowdown is apparent in the quarterly figures.

The future of economic growth

To reach the 3.2 percent annual growth that is projected in the medium term programme, the QoQ real GDP growth should be more than 1 percent and YoY growth should be more than 4 percent in the fourth quarter according to our calculations. In present conditions, it's not hard to reach medium term programme projections. Lately, the CBRT narrowed the interest rate corridor from above and reduced the weighted average cost of the funding below 6 percent. Consequently the interest rates on bank deposits and loans have been falling (Figure 4). The rating upgrade of Turkey to investment grade by Fitch is expected to further reduce interest rates. A similar rating upgrade from other rating agencies may foster capital inflows. In this case, we believe that the CRBT will take steps to slow down the flow in order to maintain financial stability. We expect that these developments will have a positive impact on growth both in the fourth quarter and throughout 2013. On the other hand, the slowdown in industrial production in Europe and especially in Germany and no immediate solution for the ongoing conflict in Syria increases concerns for the Turkish economy.

Consumption expenditure increases in the 3rd quarter

The economic indicators we use in forecasting private consumption expenditures indicate that the private consumption expenditure increased in the third quarter from the second quarter. In the third quarter, durable and non-durable consumer goods productions increased by 1.9 percent and 2.8

percent, respectively, from the last quarter. Also in the same period, special consumption tax revenue increased by 1.5 percent, mostly because of new tax hikes by the government. However, imports of consumption goods and consumer confidence index decreased by 0.6 percent and 0.5 percent in the third quarter.¹

Investment expenditure continues to fall

The economic indicators we use in forecasting private investment expenditures were mainly positive in July, August and September, but overall they didn't increase enough to offset the slump in the second quarter. Therefore, the level of the economic indicators in the third quarter is mostly lower than the previous quarter. Real sector confidence index, investment goods index and automobile production decreased by 3.7 percent, 7.8 percent and 1.1 percent, respectively, in the third quarter compared to the previous quarter. Also in the same period, capacity utilization rate fell by 1.8 percentage points. The only indicator for investment that increased in the third quarter is the IPI, but the increase was at a slower pace than that in the second quarter. In conclusion, we expect the private consumption expenditure to decrease in the third quarter compared to the previous quarter.

Contribution of net exports is smaller

Figure 2 shows monthly changes of seasonally adjusted import and export volume indices. In the third quarter, export volume index increased by 3.8 percent whereas import volume index decreased by 0.3 percent from the second quarter. When we adjust the trade data for gold trade (i.e., excluding gold imports and exports), we see that the exports and imports in real terms decreased by 0.6 and 0.8 percent, respectively. We believe that the contribution of net exports to real GDP growth will continue being positive in the third quarter, however, when gold trade is excluded, the net contribution could be very close to zero.

Current account deficit is close to 7 percent

The 12-month current account deficit had fallen to \$59 billion at the end of August. In September, the trade deficit decreased further by \$3.6 billion compared to the same month of the last year. The decline in the trade deficit continued to reduce the current account deficit and the 12-month current account deficit ended up at \$56 billion at the end of the third quarter. Therefore, we expect the 12-month current account deficit to the GDP ratio, which was 8.3 at the end of the second quarter, to decline to 7.2 percent at the end of the third quarter. We expect the decline in the current account deficit to slowdown in the fourth quarter as base effect from the previous year slowly disappears.

¹ We'd like to note that Betam forecasts consumption mostly using data on production and imports. An increase in our indicators might reflect an increase in stocks of consumption goods, instead of consumption itself.

Table 2. Monthly and quarterly changes of Betam's selected indicators (real and sa)

Indicators	July	August	September	October	2012 2 nd Quarter	2012 3 rd Quarter
Exports	-1.3	8.7	-9.7	**	11.5	3.8
Imports	0.1	-2.0	1.0	**	2.8	-0.3
Intermediate goods import	0.9	-3.6	-2.7	**	5.2	-0.6
Consumer goods import	6.1	-7.4	0.4	**	1.8	-0.6
Investment goods import	11.7	0.4	1.7	**	-8.4	-7.8
Exports without gold***	-4,2	4,4	-0,5	**	1,8	-0,6
Imports without gold***	-0,1	0,2	3,1	**	-1,3	-0,8
Industrial Production Index (IPI)	1.4	-2.0	3.9	**	1.9	0.9
Nondurable consumer goods	5.6	-2.2	1.9	**	1.8	1.9
Durable consumer goods	4.3	-1.3	9.9	**	1.4	2.8
Intermediate goods	1.0	-1.6	1.9	**	2.0	0.3
Investment goods	4.5	-7.6	6.0	**	1.6	-2.9
Capacity Utilization Rate (CUR)	0.1	-0.2	0.0	0.3	-2.4	-1.8
Nondurable consumer goods	0.1	-0.6	0.1	0.1	-0.2	-0.5
Durable consumer goods	0.2	-0.4	0.4	-0.4	-0.6	-1.4
Intermediate goods	0.3	-0.6	-0.4	0.5	-2.0	-0.9
Investment goods	-0.6	0.6	-1.2	0.3	-1.5	-2.4
Manufacturing Order Index	-8.2	4.9	**	**	3.2	-3.8
Domestic Orders	0.9	-2.0	**	**	1.6	-3.0
Foreign Orders	-2.8	0.7	**	**	4.9	-5.4
Soft Data						
Consumer confidence index (Turkstat)	1.2	-1.6	-2.4	**	-2.2	-0.5
Reel sector confidence index	-0.4	-1.2	0.8	3.9	-0.3	-3.7
Financial Data						
IMKB 100 (Stock Exchange)	3.2	3.5	1.3	0.2	-1.5	8.6
Other						
Special consumer tax* (SCT)	0.0	2.1	-0.7	**	4.7	1.5
Automobile production	-2.7	7.9	0.1	3.6	-2.9	-3.1

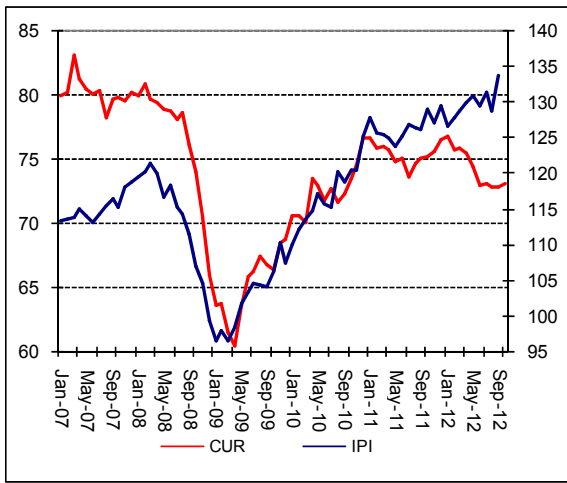
Source: TurkStat. TCMB. Treasury. IMKB. Betam. All series are real (or inflation adjusted) wherever necessary and seasonally adjusted.

*This tax is collected on sales of goods such as gas, fuel oils, alcohol, tobacco products and automobiles.

**Data not yet released

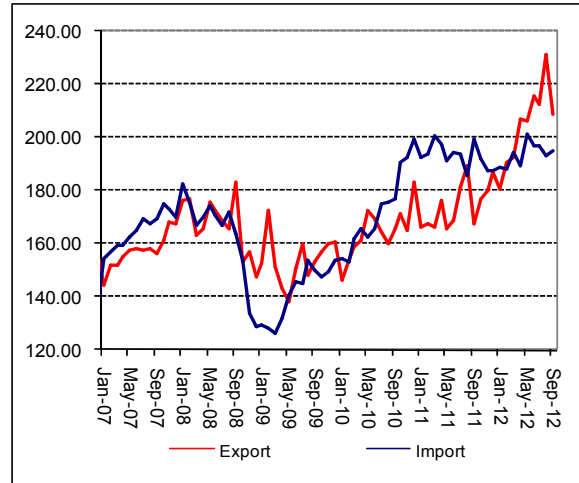
*** Betam's calculations: Nominal exports (imports) minus non-monetary gold, deflated by the export (import) unit value index.

Figure 1: Capacity utilization rate and industrial production index (sa. left axis for CUR and right axis for IPI)



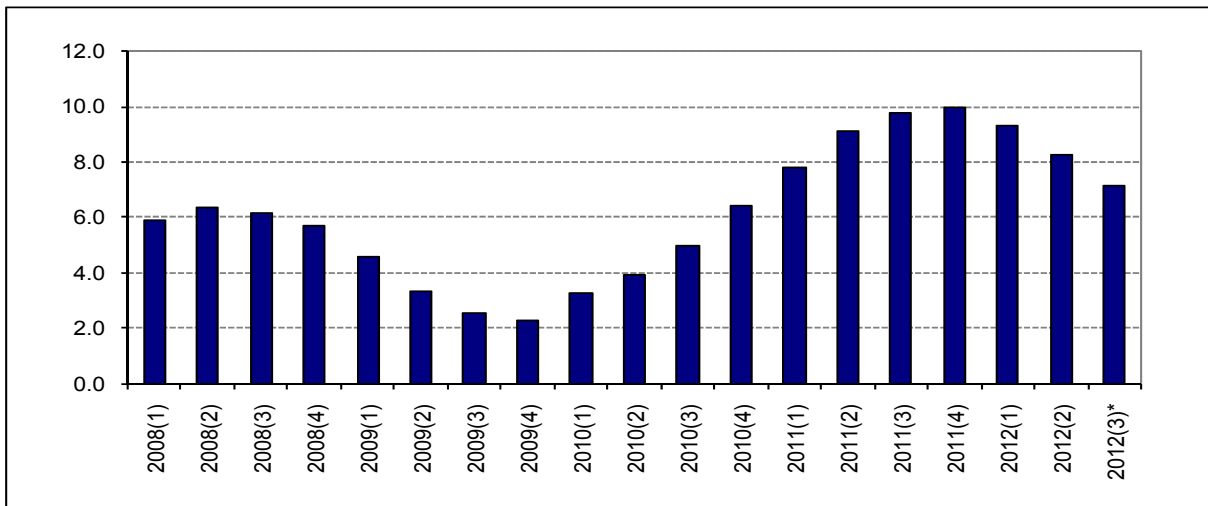
Source : TurkStat. Betam

Figure 2: Volume indices of exports and imports (sa.)



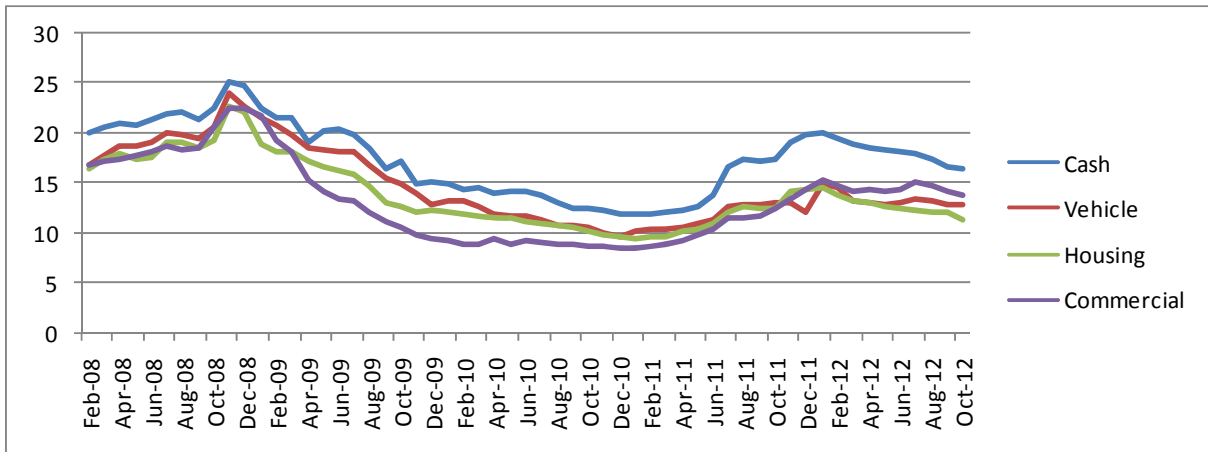
Source : TurkStat. Betam

Figure 3: Ratio of current account deficit to GDP (12-month)



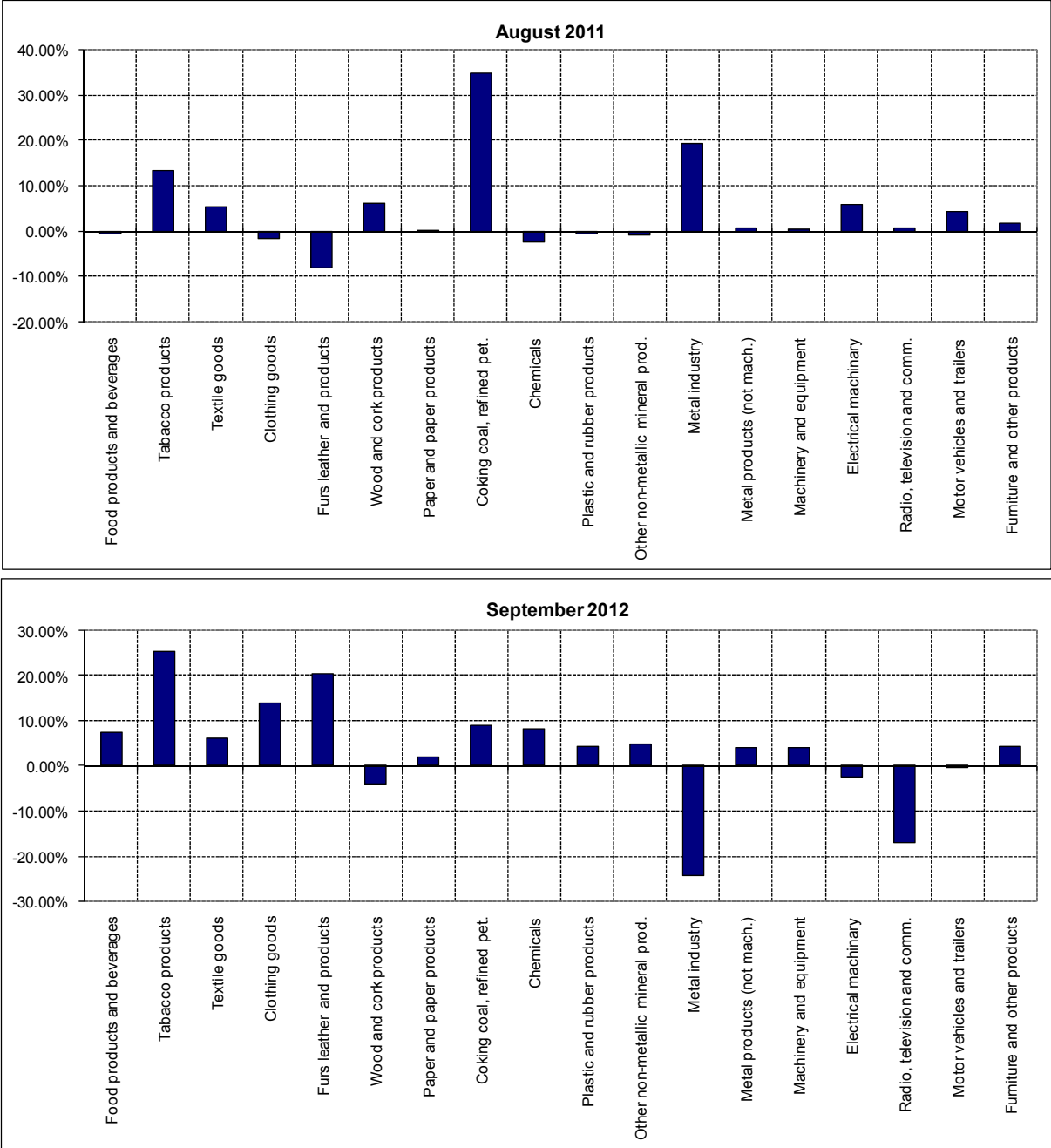
Source: TCMB. TurkStat. Betam

Figure 4: Weighted Average Interest Rates For Turkish Lira Banks' Loans (%)



Source: TCMB

Figure 5: Monthly changes of manufacturing industry exports (sa)



Source: TurkStat. Betam