THE CALM AFTER ELECTIONS

Since the local elections on 31 March, financial conditions have stabilised. Markets reacted favourably to the defeat of the ruling party at local level. The result of the elections is not expected to change the economic stabilisation programme of Finance Minister Mehmet Şimşek. The Monetary Policy Committee maintained its key rate at its last meeting in April, a rate which it had raised again in March. Household consumption continues to drive growth, which will remain sustained this year unless fiscal policy becomes very restrictive, which is unlikely. The rebalancing of growth components is underway, although it is not yet sufficient to curb the non-energy current account deficit.

EASING OF FINANCIAL MARKETS AFTER THE ELECTIONS

Since the local elections on 31 March, financial conditions have eased in Türkiye. The USD to TRY rate has stabilised at around 32, while it had depreciated by 9% between January and March. The main index of the Istanbul Stock Exchange (BIST 30) has gained 9% (in local currency) since the end of March. The 5-year CDS maturity spread remained stable, at below 300 basis points, a level attesting to a stronger investor confidence in Turkish sovereign risk. Only yields on 10-year government bonds (26%) remain as high as they were before the elections. But this can be explained by an inflation still very strong (68.5% y/y in March 2024) and monetary tightening; the policy rate of the central bank (TCMB) was raised to 50% on 22 March (compared to 8.5% on 22 June 2023).

The AKP, the party of President R.T. Erdogan, is weakened after the local elections. The Kemalist CHP party, the main opposition party, won 37.7% of votes compared to 35.5% for the AKP. The major cities (Ankara, Istanbul) remained in the hands of the CHP, and the number of municipalities controlled by the AKP fell from thirty-nine to twenty-four.

The markets therefore reacted favourably to this defeat of the ruling party at local level. The result of the elections is not expected to change the economic stabilisation programme of Finance Minister Mehmet Şimşek. In addition, the BCRA's Monetary Policy Committee maintained its key rate at its last meeting in April. In this context, the rebalancing of growth components is underway, although it is not yet sufficient to curb the non-energy current account deficit.

ECONOMIC GROWTH IS DOING BETTER THAN JUST HOLDING UP

In Q4 2023, growth was still dynamic at 1.0% Q/Q (4.8% y/y), mainly thanks to sustained household consumption (3.6%) despite the acceleration in inflation. The balance of foreign trade also contributed to growth, albeit only slightly (+0.3 percentage points). Investment, on the other hand, fell (-0.8%), but after a very strong increase in Q1-Q3 2023 (+11%) and also in previous years. It should be noted that investments in machinery and capital goods (measured at constant prices) and imports of non-automotive capital goods (measured in dollars) were 80% higher at the end of 2023 compared to the end of 2019, an unparalleled performance among OECD countries.

In Q1 2024, growth held up very well. On average over January-February, manufacturing production was up 3.5% compared to Q4 2023 (after +2.5% in 2023on year average) and, over January-March, automotive production rose by nearly 6% (after +8.6% in 2023 on year average). Credit card payments, which have contributed significantly to the momentum of household purchases since mid-2021 (see Chart 1), still showed spectacular growth of 40% over a year in real terms. In addition, according to statistics for the official average hourly wage for the entire economy, the catch-up in purchasing power since 2023 has continued, with a further, very significant revision of the minimum wage.[1] At the same time, public consumption and investment may have once again contributed to growth (see below). On the other hand, exports, measured in dollars, shrank by 1% q/q, and private capital investment is expec-

FORECASTS

	2021	2022	2023e	2024e	2025e
Real GDP growth, %	11.4	5.5	4.5	3.0	3.0
Inflation, CPI, year average, %	19.6	72.3	53.9	56.2	28.7
Gen. Gov. balance / GDP, %	-2.8	-1.0	-5.2	-4.8	-3.5
Gen. Gov. debt / GDP, %	37.9	26.9	25.6	25.0	25.0
Current account balance / GDP, %	-0.9	-5.4	-4.0	-3.0	-2.0
External debt / GDP, %	53.3	50.6	45.1	42.1	41.0
Forex reserves, USD bn	72.5	83.0	93.0	98.0	103.0
Forex reserves, in months of imports	3.1	2.6	2.9	3.0	3.0

TABLE 1

e: ESTIMATES & FORECASTS
SOURCE: BNP PARIBAS ECONOMIC RESEARCH

TURKEY: HOUSEHOLD CONSUMPTION

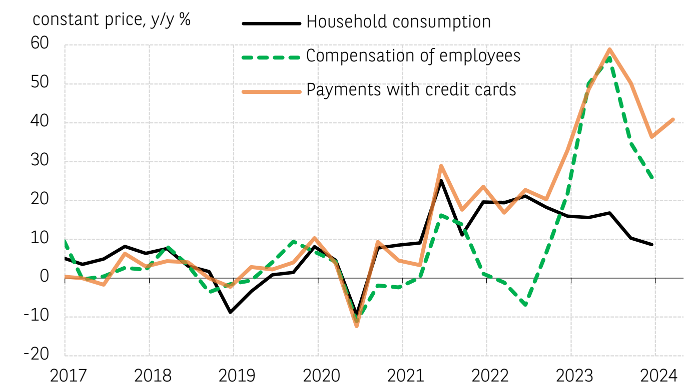

CHART 1

SOURCE: TURKSTAT, TCMB, BNP PARIBAS

1 The minimum wage was revised from 50% on 1st January 2024 (multiplied by 2 over a year) to TRY 20,002 per month, i.e., EUR 580.

ted to have contracted once again. The downward correction in capital goods imports continued over January-February and, according to the TCMB survey indicator, investment intentions continued to weaken, although they remain at a historically high level.

Ultimately, growth is likely to remain positive in Q1. Also, for the whole year, in a scenario of a decline in monthly inflation already observed (3.3% in March compared to 4.3% in January)[2] and stabilisation of the lira, allowing the central bank to ease its tightening a little, GDP growth should be at least 3%, unless fiscal policy becomes very restrictive, which is unlikely.

CONTROLLED BUDGET SLIPPAGE

The anticipated budgetary slippage throughout last year, following revision of the budget in June 2023 and publication of the Medium-Term Economic Plan (MTEP) in September, ended up happening at the very end of the year. The central government deficit stood at 5.2% of GDP in December, compared to just 2.7% in September. At the end of March 2024, in cumulative terms over twelve months, it reached 5.4%. Nevertheless, it is twice as low as a major research institute, the TEPAV, had feared a year ago. Moreover, the accounts published by the Ministry of Finance are on an accrual basis and not on a cash basis. These accounts consider expenditure commitments for 2023, whether disbursed or not. The budget implementation published by the Treasury, which is, conversely, based on actual disbursements, also shows a slippage, but from a much lower level (from 2.4% at the end of 2023 to 3% in March). In Q1 2024, expenditures excluding interest increased by 16% in real terms compared to Q1 2023. However, there is no acceleration compared to 2023 as a whole (excluding December).

For 2024, the MTEP target is 6.4% (including earthquake-related expenses). In theory, this target is quite credible. However, there are two reservations regarding changes to public finance metrics. Firstly, the weight of interests on debt has increased significantly, from 1.9% of GDP (11% of income) in March 2023 to 2.7% (respectively, 13.6%) one year later. However, this deterioration is not a matter for concern. Secondly, the central government's debt does not take into account expenditures incurred in relation to the earthquake (as these have not been disbursed).

By the end of March, debt represented just 25% of GDP. If we add the 2.4 points of GDP difference between the deficit based on commitments and the deficit based on cash and, taking into account our deficit forecast for 2024 (4.8%), an assumption of nominal GDP growth of 60% and an appreciation of the lira's real exchange rate of just over 20% (against a USD-EUR basket), the ratio will remain unchanged at 25% of GDP. For 2025, fiscal consolidation is expected to be more marked, with a primary balance sheet in equilibrium compared to -1.8% of GDP in 2024.

STABILISATION OF EXTERNAL ACCOUNTS NOT YET COMPLETED

The TCMB's foreign exchange reserves have stabilised since the local elections (see Chart 2). These reserves had been eroded over the first three months of the year, not due to a deterioration in the balance of payments, but as a result of stronger demand for dollars from residents and a reduction in the position of fx swaps of the commercial banks with the Central Bank.

2 Over a year, the peak in inflation should be reached in May (slightly above 70%), to end up at around 40% in December.

TURKEY: CENTRAL BANK (TCMB) INTERNATIONAL RESERVES

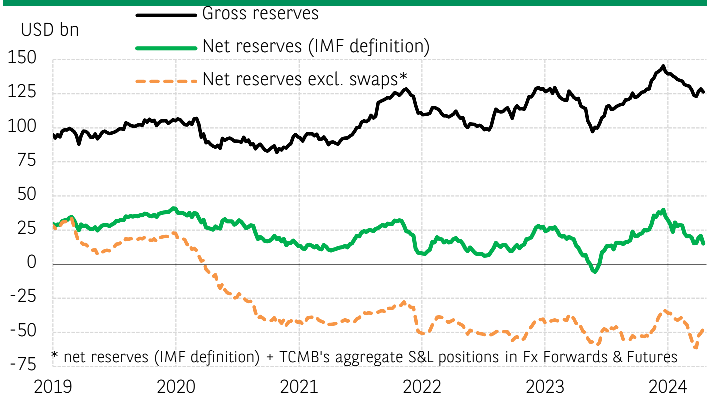

CHART 2 SOURCE: TCMB, BNP PARIBAS

In February, and in cumulative terms over 12 months, the current balance deficit fell to USD 32 billion (2.8% of GDP), a division by two compared to its peak in spring 2023. This improvement can only be explained by a lower deficit in the balance of "gold & energy" items, which shrank from 10% to 6% of GDP. However, the trade balance of other products, the trade balance of services (dominated by tourism revenues, which reached USD 40 billion over 12 months) and the trade balance of revenues, aggregated, still show a major surplus.

The expected decline in the errors & omissions item was offset by the surplus of the balance of portfolio investments. On the other hand, in Q1 2024, residents' deposits covered by the currency risk protection mechanism (KKM) were predominantly transferred to dollar deposits despite the rise in interest rates on deposits in TRY. In mid-April, the equivalent of USD 70 billion remained in deposits not yet transferred (and therefore still held in TRY). With the tourism season, it should be possible for the current account deficit to stabilise at around 2.5% of GDP. If so, this should support the recent stability of the lira and favour transfers from KKM deposits to deposits in TRY.

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