

## TURKEY MARKET REPORT

### Asia Securities Forum Annual General Meeting Tokyo November 2017

#### MACRO-ECONOMIC OVERVIEW

After a slowdown in the growth rate in 2016, when a failed coup d'état took place, the Turkish economy grew by 5.1% in the first half of 2017. In March, the government increased the size of its Credit Guarantee Fund, which guarantees loans to small and medium-sized enterprises. The increase in the Guarantee Fund backed by the Treasury supported the growth in bank loans which in turn boosted the growth rate.

On the other hand, the revival in external demand and the recovery in the tourism sector also supported the domestic economic activity as well as the external balance. The current account deficit stands at \$ 27 billion in the first eight months of 2017, which translates into around 4% of GDP in annualised terms. The current account deficit is financed mainly through portfolio investment flows (\$ 20 billion) and foreign direct investments (net \$ 5 billion), although the latter declined by 13% compared to last year.

After a rapid devaluation in the year 2016, the Turkish lira strengthened in 2017. The Central Bank of the Republic of Turkey (CBRT) maintains a tight monetary policy stance. CBRT's average funding rate was raised gradually to 12% in May, from 8% at the beginning of the year.

Still, inflation remains high, at annual rate of 11.2% as of September, while the official inflation target stands at 5% within the  $\pm 2\%$  uncertainty band. The rise in the inflation rates partly reflects the exchange rate pass through, following the rapid depreciation of the Turkish lira after the coup attempt. The year-end consumer inflation is expected to be around 10% according to the Central Bank's survey of expectations conducted among financial and real sector experts.

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Key Economic Indicators-Turkey						
	2012	2013	2014	2015	2016	2017P
<b>Population and Employment</b>						
Population (mn.)	75.6	76.7	77.7	78.7	79.8	80.1
Unemployment (average, %)	8.4	9.0	9.9	10.3	10.9	10.8
<b>National Accounts</b>						
GDP (bn. \$)	871.0	950.0	935.0	863.0	847.0	923.0-
GDP per capita (\$)	11,588	12,480	12,112	11,014	10,883	10,579
GDP, real growth (%)	4.8	8.5	5.2	6.1	3.2	5.5
<b>External Balance</b>						
Exports (FOB, bn. \$)	152.5	151.8	157.6	143.8	142.5	156.5
Imports (CIF, bn. \$)	236.5	251.7	242.2	207.2	198.6	222.0
Foreign Trade Balance (bn. \$)	-84.1	-99.9	-84.6	-63.4	-56.1	-65.5
Current Account Balance (bn. \$)	-48.0	-63.6	-43.6	-32.1	-32.6	39.2
Current Account Balance/GDP (%)	-5.5	-6.7	-4.7	-3.7	-3.8	-4.6
Foreign Direct Investment (net, bn. \$)	9.5	9.3	5.8	12.5	9.1	-
CBRT Reserves (including gold, bn. \$)	119.2	131.0	127.3	110.5	106.1	-
External Debt (bn. \$)	339.5	389.8	401.9	396.1	404.2	-
<b>Prices</b>						
CPI (y-o-y, %)	6.2	7.4	8.2	8.8	8.5	9.5
PPI (y-o-y, %)	2.5	7.0	5.4	5.7	9.9	-
<b>Fiscal Balance</b>						
Primary Balance/GDP (%)	1.2	1.7	1.3	1.3	0.8	-0.1
Budget Balance/GDP (%)	-1.9	-1.0	-1.1	-1.0	-1.1	-2.0
General Government Debt/GDP (%)	32.6	31.3	28.7	27.5	28.1	28.5
<b>Exchange Rates</b>						
USD (period-end)	1.78	2.13	2.33	2.92	3.52	-
Euro (period-end)	2.35	2.93	2.83	3.18	3.71	-

Source: CBRT, Treasury, TurkStat, Medium-Term Program

The government pursued an expansionary fiscal policy in 2017 and the budget deficit nearly tripled in the first nine months of the year as several measures, including an increase in the credit guarantee fund and a 5% reduction in the employer's insurance premia, were taken to boost growth as well as employment. The budget deficit is expected to reach 2% of the GDP by the end of the year, from 1.1% in 2016. The domestic debt rollover ratio rose significantly to 127% percent in the first nine months of 2017, compared to 91% for the whole year 2016.

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Nevertheless, the average cost of domestic borrowing rose only slightly to 11% from 10% in 2016 with the help of increased foreign investor interest.

Tax hikes were announced recently for the year 2018 to curb further growth of the budget deficit, including a 2 percentage point rise in the corporate tax rate to 22% for corporations operating in the financial industry.

The newly announced Medium-Term Program envisages an annual growth rate of 5.5% for the next three years, and a decline of the unemployment rate to 9.6% in the year 2020, from a projected 10.8% in 2017.

## **CAPITAL MARKET DEVELOPMENTS**

BIST-100 Index, Borsa Istanbul's main index, rose by 32% year-to-date 103,000 in the first nine months of 2017. FED's continued reluctance to raise interest rates along with the Turkish government's subsidies to the real economy following the events of 2016 supported the Turkish equity market.

Since 2015, IPOs have been relatively few and far in between in the Turkish Capital Markets. In the year 2017, only 3 companies successfully launched IPOs, raising TRY 1.3 billion. One of these issues constituted the bulk of the total capital raised. The primary reason behind the companies' refrain to raise capital through the public market is the proliferation of private equity firms in the last few years. Companies have in recent years chosen to seek private strategic and financial partners for their capital needs.

Turkish companies have historically relied on bank loans for financing needs however since 2012, companies started to turn to capital markets to diversify their funding portfolio. The number and volume of corporate bond issues continue to climb although a few Turkish issuers have recently defaulted on their debt obligations. Further regulatory supervision is expected by the Capital Markets Board to guide and guard the investors and capital markets.

### **TURKISH CAPITAL MARKETS ASSOCIATION**



Capital Markets Factsheet					
	2013	2014	2015	2016	2017/08
<b>Breakdown of Financial Assets (Mn TL)</b>	<b>1,369,544</b>	<b>1,856,130</b>	<b>1,994,474</b>	<b>2,327,230</b>	<b>2,640,862</b>
Residents	1,108,075	1,510,353	1,665,504	1,976,695	2,170,052
Non-Residents	261,468	345,778	328,970	350,536	470,810
<b>Market Capitalisation (Million TL)</b>	<b>586,583</b>	<b>609,493</b>	<b>554,884</b>	<b>614,069</b>	<b>845,796</b>
<b>No. of Securities on the Borsa İstanbul</b>	<b>408</b>	<b>413</b>	<b>430</b>	<b>414</b>	<b>413</b>
National Mkt, REITs and Venture Capital IT	263	254	-	-	-
2nd National, Watchlist, ECM and Free TP	145	159	-	-	-
BIST Star	-	-	117	120	128
BIST Main	-	-	184	169	164
Other	-	-	129	125	121
<b>Trading Volume (Billion TL, Cumulative)</b>					
Stock Market	1,634	864	1,022	1,012	895
Fixed Income Market (market + OTC)	1,945	673	523	661	414
Repo-Reverse Repo Market (market + OTC)	13,490	8,021	10,611	11,553	3,859
Takasbank Money Market*	831	-	257	428	377
Futures Market	-	435	566	580	501
Options Market	-	1.1	7.6	27.1	27.8
Precious Metals Market	-	-	26.4	30.4	48.0
<b>Forex Trading (Billion TL, Cumulative)</b>	<b>4,956</b>	<b>7,693</b>	<b>17,005</b>	<b>21,850</b>	<b>6,466</b>
Customer	2,970	4,353	9,546	12,245	3,519
Liquidity Provider	1,986	3,340	7,459	9,604	2,946
<b>Initial Public Offerings (Cumulative)</b>					
No. of Companies (inc. ECM)	15	12	4	1	3
IPO Size - Companies (Mn. TL)	1,052	695	44	37	1,254
No. of Inv. Trusts (inc. REITs and Vent.Cap.)	3	1	2	1	0
IPO Size - Inv. Trusts (Mn. TL)	388	19	75	306	0
No. of ETFs	1	0	0	0	0
IPO Size - ETFs (Mn. TL)	6	0	0	0	0
No. of Private Bonds/Bills	-	508	622	760	750
IPO Size - Private Bonds/Bills (Mn. TL)	-	66,358	79,618	90,148	82,492
<b>Institutional Investors (Million TL)</b>	<b>75,731</b>	<b>94,359</b>	<b>108,170</b>	<b>129,635</b>	<b>156,499</b>
Mutual Funds	30,082	33,315	37,186	43,755	54,821
Pension Funds	26,186	37,771	47,918	58,439	73,685
Investment Trusts	328	283	269	341	332
Real Estate Investment Trusts	18,119	21,538	21,465	25,878	25,818
Venture Capital Companies	1,015	1,452	1,331	1,222	1,844
<b>Equity Index</b>					
BIST-100	67,802	85,721	71,727	78,139	110,010
BIST-100 (Period High)	93,179	86,234	91,260	86,344	110,423
BIST-100 (Period Low)	63,885	61,189	69,309	68,568	76,144
<b>Foreign Investors in Equity Market</b>					
Equity Trading Volume (Cumulative, mn. \$)	171,293	160,810	167,426	169,346	122,090
Share in Total Equity Trading Volume	20%	20%	22%	25%	25%

Source: BRSA, Borsa İstanbul, CBRT, CRA, TCMA

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In the first half of 2017, the brokerage firms' aggregate profits increased by 57% year-on-year to TL 387 million. Brokerage revenues, constituting the bulk of the revenue for brokerage firms, fell by 5% to TRY 723 million. TL 391 million of these comprised of commissions on stock trading, while the industry generated TRY 194 million from leveraged transactions in 1H2017, a significant decrease from last year's figure of TL 310 million following Capital Market Board's strict regulatory changes.

With the growth of pension funds, assets managed by asset management firms increased by TRY 29 billion in 1H2017 reaching TL 140 billion. In addition to the existing voluntary private pension system, an auto-enrolment retirement scheme was introduced by the Turkish government to gradually include every wage earner in Turkey under the age of 45 with the intent to boost domestic savings and provide additional income to participants upon retirement. Since its inception in January 2017, the system added +3.3 million participants and generated an additional AUM of TL 1.3 billion for the asset management firms.

Investment funds made up TL 53 billion of the total assets under management while TL 70 billion belonged to pension funds. Asset management firms' profits rose by 49% year-on-year to TL 62 million.

Capital Markets Board introduced in February 2017 restrictive measures in relation to the forex transactions by increasing minimum margin requirements and reducing leverage ratios, severely depressing the volume of forex transactions with a 52% drop this August from last year's figure of TRY 13.4 billion. The significant decline in volume forced 6 brokerage firms specializing in forex activities to close its doors while +1,600 employees, most of whom are sales and marketing personnel, were laid off following the recent regulatory changes.

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<b>TCMA Member Information</b>			
<b>TCMA Members</b>	<b>2015</b>	<b>2016</b>	<b>2017/09</b>
No. of Brokerage Firms	95	88	82
No. of Banks	44	43	45
No. of Asset Management Companies	46	52	50
No. of Investment Trusts	9	9	9
No. of Real Estate Investment Trusts	31	31	31
No. of Venture Capital Companies	7	8	8
<b>Total</b>	<b>232</b>	<b>231</b>	<b>225</b>
<b>Investment Companies' Employees</b>	<b>2015</b>	<b>2016</b>	<b>2017/06</b>
Brokerage Firms	6,638	6,478	4,797
Asset Management Companies	698	720	708
Banks	217,504	210,910	210,369
<b>Brokerage Firms' Financials (Mn TL)</b>	<b>2015</b>	<b>2016</b>	<b>2017/06</b>
Total Assets	15,312	21,178	23,239
Current Assets	14,242	20,109	22,183
Non-Current Assets	1,070	1,069	1,057
Total Liabilities and Equities	15,312	21,178	23,239
Short-Term Liabilities	11,180	16,703	18,847
Long-Term Liabilities	122	139	99
Equity	4,010	4,336	4,293
Total Revenues	2,004	2,124	1,211
Operating Expenses (Net)	-1,701	-1,787	-891
Operating Profit/Loss	303	338	320
Net Profit/Loss	433	483	387
<b>Asset Management Firms' Financials (Mn TL)</b>	<b>2015</b>	<b>2016</b>	<b>2017/06</b>
Total Assets	507	609	603
Current Assets	472	571	564
Non-Current Assets	34	38	39
Total Liabilities and Equities	507	609	603
Short-Term Liabilities	45	49	42
Long-Term Liabilities	6	8	9
Equity	456	552	551
Total Revenues	296	347	196
Operating Expenses (Net)	-208	-255	-137
Operating Profit/Loss	88	105	59
Net Profit/Loss	91	111	62

Source: BRSA, Borsa Istanbul, CBRT, CRA, TCMA

**TURKISH CAPITAL MARKETS ASSOCIATION**

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## RECENT HIGHLIGHTS

### **Turkey Establishes Sovereign Wealth Fund**

In August 2016, the Turkish government took action to establish a sovereign wealth fund. The Fund will be active in both national and international primary and secondary markets and is expected to contribute to Turkey's long term growth. In February 2017, assets of major public entities including Borsa İstanbul (73.6%), and listed companies such as Turkish Airlines (49.12%), Halkbank (51.1%), Türk Telekom (6.68%) as well as several others were transferred over to the Fund. Public lands in several cities that previously belonged to the Treasury were also transferred over to the Fund.

### **Dramatic Changes to Leveraged Transactions**

In February 2017, the Capital Markets Board, the regulator for the capital markets in Turkey, revised the regulations on leveraged transactions. The maximum allowed leverage ratio was reduced to 10:1. Prior to this change, the maximum leverage was 50:1 for investors with less than TL 20,000 margin deposit for EUR and USD denominated transactions, and 25:1 for the other currencies. In addition to the leverage cap, the required margin deposit was raised to TL 50,000 from TL 20,000. Brokerages are given 45 days to apply the new regulations to existing accounts while new accounts will be subject to the new regulations with immediate effect.

### **Turkish Treasury Introduced Sovereign Gold Bonds and Gold Lease Certificates**

Turkish Treasury aims at diversifying the breadth of financial instruments and boost savings in the financial system by issuing Sovereign Gold Bonds and Gold Lease Certificates. The Treasury intends to bring into the economy the gold citizens keep "under the mattress" since gold is regarded as a safe haven and a traditional investment instrument among many investors in Turkey. The sales period ends on October 27 for the first issue. Investors will be paid 1.20% semi-annual return indexed to gold price. The bonds are TL-denominated with a maturity of 2 years.

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### **TCMA becomes IFSB member**

Turkey has taken major steps in recent years to become a key player in Islamic Finance. The government is working on new legislation in relation to Islamic finance services to establish and promote Turkey as an Islamic finance center. Islamic finance has a 5% market share in Turkey and the government has set a target to increase this figure to 15% by 2025. In that regard, Turkish Capital Markets Association became an observer member of the Islamic Financial Services Board (IFSB) in December 2016.

