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Economic Watch

Turkey: A more realistic New Economic Program

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Turkey's New Economic Program (NEP) hinders a rebalancing of the economy with fiscal consolidation in the short term in a more realistic framework. The NEP is more consistent with expectations and now assumes a three years´ negative output gap. Despite the lower economic growth, fiscal policy is more prudent with the budget deficit converging gradually to 1.7%. The Government relies more intensively on the expenditure side (1.3% of GDP savings) while envisages extra revenues equivalent to 0.4% of GDP. All in all, the prudent stance of the fiscal policy is now more adequate and should complement the already tight monetary policy conditions to rebalance the economy.

A more realistic macro program with fiscal consolidation in place

The program assumes a soft landing after a relatively positive 2018 growth (3.8%). The growth targets of 2.3% for 2019 (1.5% BBVA Research) and 3.5% for 2020 (2.5% BBVA Research) look more reasonable. The rapid rise in unemployment rate is consistent with lower growth rates while inflation estimates are in line with market expectations. Still, they would be conditional on exchange rate assumptions (somehow optimistic relative to market expectations).

The fiscal accounts look now more consistent with the current conditions. The program envisages a public deficit below 2% of GDP next year, given the deterioration of the economic cycle implies higher consolidation efforts than the previous plan. The medium term target of 1.7% is consistent with our expectations and the primary surplus of 1.3% should help to restore the traditional fiscal anchor. For next year, the Government plans to save 60bnTL (1.3% of GDP) with main savings coming from postponing investment (0.7% of GDP), reducing incentives (0.3% of GDP), cutting social security (0.2% of GDP) and to a lesser extent reducing current expenditures (0.1%). The Government foresees higher interest expenditures consistent with the new market conditions (2.2% and 2.8% of GDP in 2018 and 2019, respectively). On the revenue side, the Government will generate extra revenues by 16bnTL (0.4% of GDP) in 2019 but there is still lack of details on how to acquire that level. Under the General Government balance assumptions, tax revenues to GDP ratio stays almost the same at 17.4% in 2019; while a reduction of 0.5pp in non-tax revenues and 0.4pp in social funds is forecasted (see Table 2).

New Economic Program- Macroeconomic Forecasts	2017	2018e	2019f	2020f	2021f
GDP Growth (%)	**7.4**	**3.8**	**2.3**	**3.5**	**5.0**
Domestic Demand Contribution (pp)	**7.3**	**2.4**	**0.8**	**3.3**	**4.8**
External Demand Contribution (pp)	**0.1**	**1.4**	**1.5**	**0.2**	**0.2**
Unemployment Rate (%)	**10.9**	**11.3**	**12.1**	**11.9**	**10.8**
USD/TRY (Year Avg)	**3.6**	**4.9**	**5.6**	**6.0**	**6.2**
Inflation Rate (eoy %)	**11.9**	**20.8**	**15.9**	**9.8**	**6.0**
Central Gov. Budget Balance (% GDP)	**-1.5**	**-1.9**	**-1.8**	**-1.9**	**-1.7**
Central Gov. Primary Balance (% GDP)	**0.3**	**0.1**	**0.8**	**1.0**	**1.3**
Current Account Balance (% GDP)	**-5.6**	**-4.7**	**-3.3**	**-2.7**	**-2.6**
EU Defined Gov. Debt (% GDP)	**28.3**	**31.1**	**28.5**	**28.2**	**27.2**

A more coherent policy mix to correct imbalances

Today's program provides a more prudent fiscal stance, which will support the already sharply tightened monetary policy to rebalance the economy to a more sustainable path. Given the recent monetary policy decision and the new fiscal plan, some uncertainties on policies should be removed; though, still some challenges remain.

General Government Balance (% GDP)	2017	2018e	2019f	2020f	2021f
Revenues	33.1	32.7	32.0	31.8	31.5
Tax Revenues	17.7	17.2	17.4	17.6	17.9
Non-Tax Revenues	1.5	1.9	1.4	1.4	1.4
Factor Income	4.7	4.5	4.5	3.9	3.6
Social Funds	9.0	8.9	8.5	8.5	8.3
Privatization Revenues	0.2	0.2	0.2	0.4	0.3
Expenditures	34.9	35.1	33.6	33.5	33.1
Primary Expenditures	33.0	32.9	30.8	30.5	30.0
Current Expenditures	15.5	15.8	15.1	14.9	14.6
Capital Expenditures	3.7	3.6	2.4	2.2	2.2
Transfer Expenditures	15.8	15.7	16.1	16.3	16.3
Interest Expenditures	1.9	2.2	2.8	3.0	3.1
General Government Budget Balance	-1.8	-2.4	-1.6	-1.7	-1.6
Central Government Budget	-1.5	-1.9	-1.8	-1.9	-1.7
Local Governments	-0.5	-0.6	-0.1	-0.1	-0.2
Extra Budgetary Funds	-0.3	-0.1	0.0	0.0	0.0
Unemployment Insurance Fund	0.4	0.3	0.4	0.4	0.2
Social Security Institutions	-0.5	-0.6	-0.6	-0.7	-0.7
General Health Insurance	0.6	0.6	0.6	0.7	0.7
General Government Primary Balance	0.1	-0.2	1.2	1.3	1.5

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