Creating Opportunities

Turkey: GDP growth decelerating after strong performance in 2021

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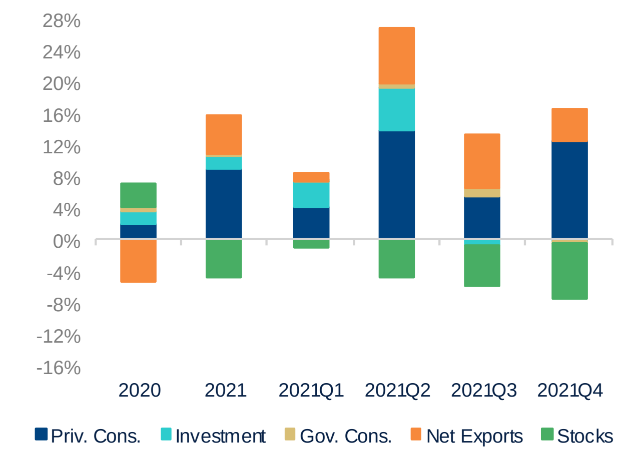
Parallel to our expectations, Turkish economy grew by 9.1% y/y in 4Q21, which resulted in a full year growth rate of 11% in 2021. The combination of strong exports and consumption resulted in a high contribution to growth from both net exports and domestic demand. Looking ahead, based on high frequency indicators and our big data information, GDP growth is already decelerating to almost 0% q/q growth rate in 1Q22, which corresponds to near 6% y/y. Russia's invasion of Ukraine and sanctions from the US, EU and other countries are clear additional downside risks on the growth outlook, which might deepen further depending on the duration of the conflict. We maintain our GDP growth forecast at 3.5% for now, given the fiscal expansionary bias.

Private consumption and net exports mainly backed 2021 GDP growth

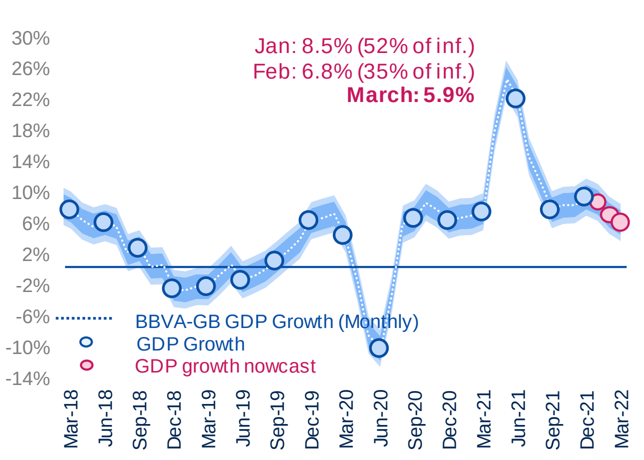
In 4Q21, domestic demand remained solid mainly due to private consumption (21.4% y/y), whereas government consumption contracted (-0.8% y/y) in 4Q21. Therefore, the contribution from consumption reached 12.2pp (12.5pp and -0.3pp, respectively). Investment once again subtracted from growth (-0.8% y/y, -0.2pp) despite the continuation of support from machinery and equipment (7% y/y). On the external side, exports remained solid (20.7% yoy), whereas imports also grew moderately by 2.6%. Thus, the contribution from net exports slowed down to 4.2pp (vs 6.9pp in 3Q21). As a result, a record high stock depletion was experienced with a subtraction of 7pp from the yearly growth rate, leading to an overall 5pp contribution from domestic demand in 4Q21. On the production side, the main contributor remained to be the services sector, followed by the industrial sector; whereas construction continued to contract. For the full year, domestic demand and net exports both contributed 6.1pp and 4.9pp, respectively. On domestic demand, support from private consumption (8.9pp) was noteworthy. On the production side, services sector took the lead (4.9pp), followed by industry (3.3pp). In contrast, financial services, agriculture and construction sectors subtracted from growth (0.4pp, 0.1pp and 0.1pp, respectively).

Figure 1. **Contributions to GDP Growth (pp, annual)**



Source: Garanti BBVA Research, Turkstat

Figure 2. **BBVA Research Monthly GDP (%yoy, 3M Avg)**



*Garanti BBVA Research monthly GDP is dynamic factor model (DFM) synthesizing high-frequency indicators to proxy monthly GDP (GBTRGDPY Index in BBG)

1Q22 GDP growth already heading south to 6% y/y

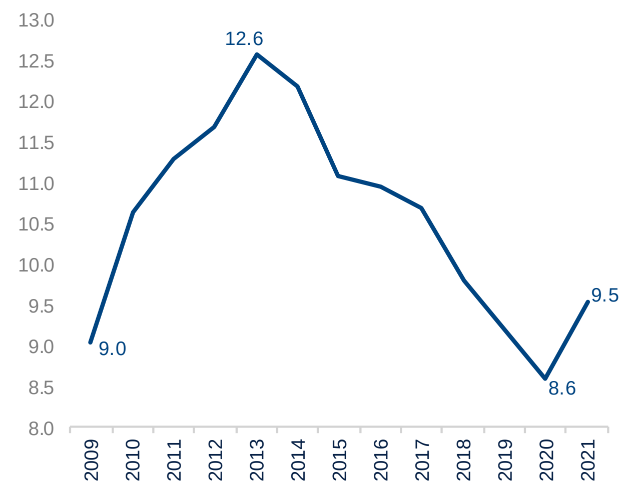
Looking ahead, leading indicators such as our high-frequency proxies, electricity production, confidence indices, manufacturing capacity utilization and PMI signal a deceleration more clearly as of February, which is confirmed by our monthly GDP indicator nowcasting an annual growth rate of 6.8% (35% of info) in February. If the recent trend is assumed to be sustained in March, our GDP nowcast for 1Q22 reaches 5.9%, implying 0% q/q growth rate.

On the expenditure side, our demand subcomponents signal that investment remains sluggish in 1Q22 after contracting in the previous two quarters, while consumption shows some moderation but still remains solid. Furthermore, the contribution from net exports declines sharply on the back of weaker exports and stronger imports. The recent uncertainty on geopolitical factors, domestic policies and expected tighter financial conditions will affect investment demand negatively. Persistent high inflation and negative real wages will reduce the purchasing power of households, which will eventually weigh on the private consumption on the downside, as well. Finally, the downside risks on tourism and export revenues led by the conflict between Ukraine and Russia might limit the expected positive contribution from net exports via direct and indirect channels. Last but not least, the elevated volatility in global financial markets and the rise in energy prices would deepen the expected negative impact on economic activity. However, supportive credit growth, looser economic policies, expected easing of supply factors in the post-pandemic period and still solid global activity could support activity. Fiscal policy will likely be used more counter-cyclically in order to absorb negative pressures, particularly on the labor market.

Welfare effects were already negative in 2021

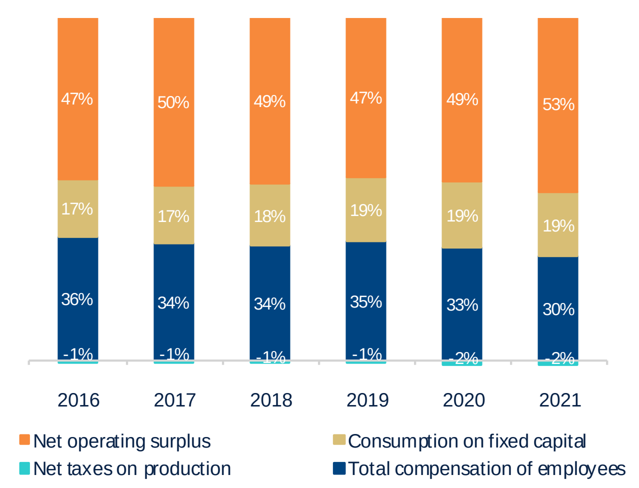
2021 GDP growth rate was realized as the highest level since 2011. Base effects clearly weighed on the upside behind this positive performance with a level near 5.5pp. However, if base effects are excluded, the growth rate still remained above the potential growth rate, which we calculate currently at 3.5-4%. Despite the sharp currency depreciation towards the end of the year, per capita income benefited from the above potential growth performance and rose to 9,539 US$ in 2021 up from 8,597 in 2020 (figure 3). It is also important to check how the welfare is distributed by means of the income channel. As seen in figure 4, the share of wages in gross value added (GVA) continued to decline significantly to 30% in 2021, after experiencing a peak of 36% in 2016, while the share of net operating surplus (net profit from capital) rose to 53% from a cyclical thorough of 47% in 2019. In sum, although per capita income has recently increased, the improvement was not evenly distributed; instead the recent jump benefited more the corporate sector in relative terms, as a reaction to increasing cost-push factors.

Figure 3. **Per Capita Income (US$ in thousand)**



Source: Garanti BBVA Research, Turkstat

Figure 4. **Shares in Gross Value Added (%)**

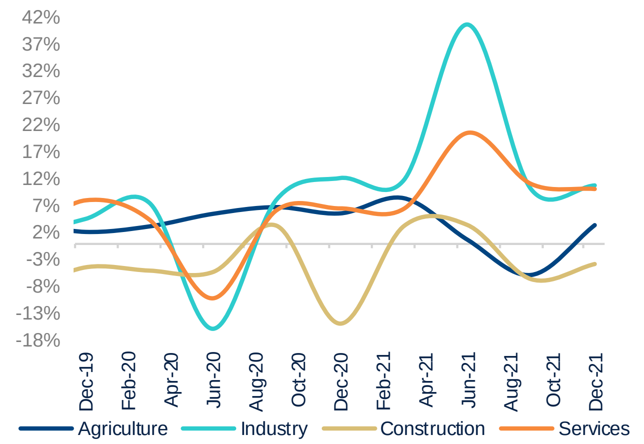


Source: Garanti BBVA Research, Turkstat

Downside risks on growth might be balanced by countercyclical policies

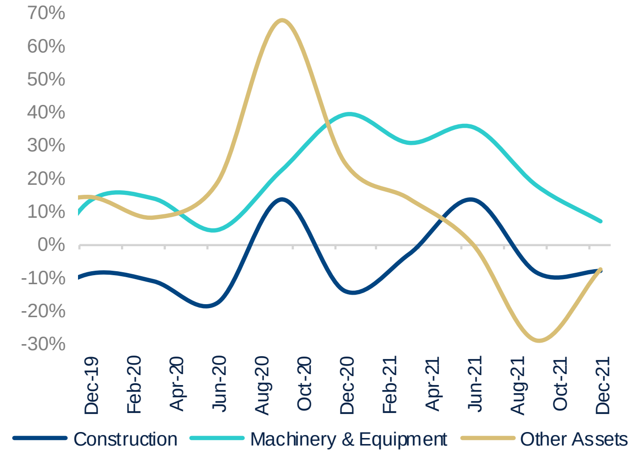
Current stress and uncertainty in financial markets and their potential impact on global demand are clear downside risks on the near term growth outlook. As confirmed by our GDP nowcast, economic activity is already decelerating, which is in line with our current 2022 GDP growth forecast of 3.5%. Nonetheless, the expansionary bias of the government, recent stimulus in credits and post-pandemic positive effects might absorb some of the pressures. Depending on the duration of the current conflict, we will evaluate the overall impact on our forecast.

Figure 5. **Sectorial GDP Growth** (YoY)



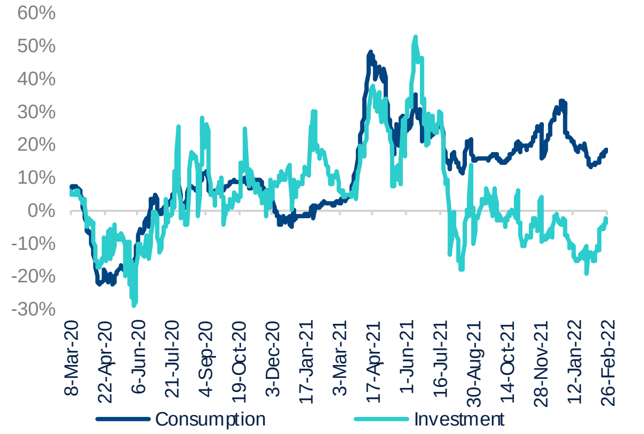
Source: Garanti BBVA Research, Turkstat

Figure 6. **Gross Fixed Capital Formation** (YoY)



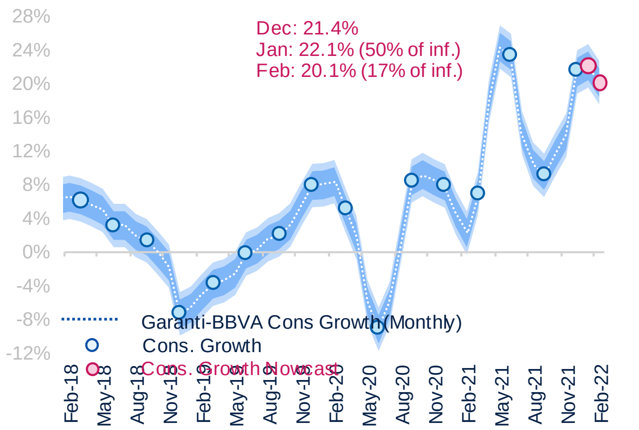
Source: Garanti BBVA Research, Turkstat

Figure 7. **BBVA Big Data Domestic Demand Indicators** (28-day yoy real changes)



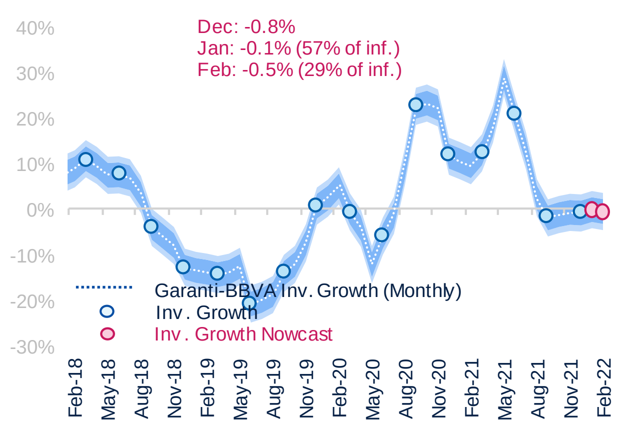
Source: Garanti BBVA Research, Turkstat

Figure 8. **BBVA Monthly Consumption Nowcast** (3m yoy)



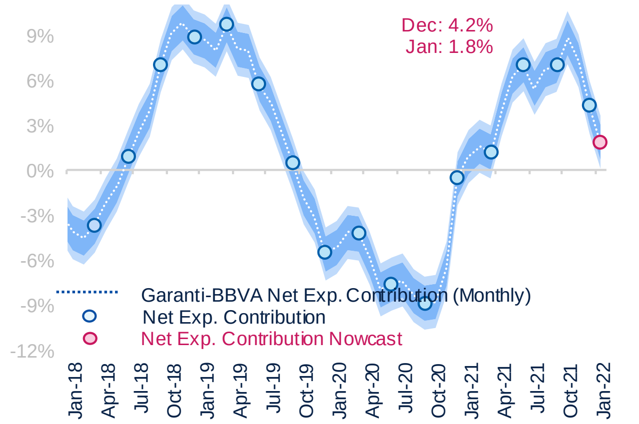
Source: Garanti BBVA Research, GBTRCGDPY Index in Bloomberg

Figure 9. **BBVA Monthly Investment Nowcast** (3m yoy)



Source: Garanti BBVA Research, GBTRIGDPY Index in Bloomberg

Figure 10. **BBVA Monthly Net Exports Nowcast** (cont. pp)



Source: Garanti BBVA Research, GBTRXGDPY and GBTRMGDPY in Bloomberg

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