Türkiye: Mild deceleration in activity so far

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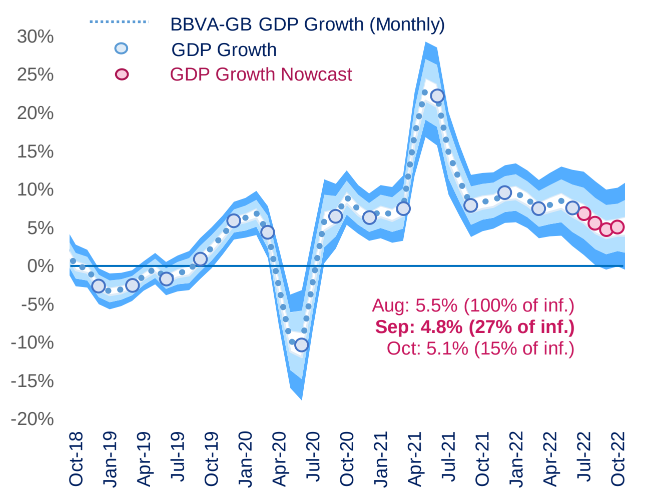
Industrial production (IP) surprised to the downside and grew 4.1% y/y in August (vs. 6% expected), implying 3.7% y/y in July-August period (vs. 10.7% in 2Q). In seasonal and calendar adjusted series, IP improved only partially with 2.4% m/m, after a 6.1% m/m decline in July. According to our big data proxies and other high frequency indicators, our monthly GDP indicator nowcasts a quarterly GDP growth of 0-0.5% for 3Q, which corresponds to a yearly growth rate of near 5% with 27% of information. The deceleration signals are stronger for early indicators of production while government efforts to restrict credit growth in certain sectors put downside risks on the near term growth outlook. However, strong economic activity during the first half of the year, continuation of loose economic policies, new credit packages and other potential populist measures ahead of the elections lead us to maintian our 2022 GDP growth forecast at 6%. We expect 2023 GDP growth to be 3.5%.

August IP recovery not enough to compensate July contraction

In seasonal and calendar adjusted series, IP recovered in August (2.4% m/m) on the back of a broad-based growth in subcomponents. Yet, neither of them showed enough compensation to revert the contraction in July (-6.1% m/m). Therefore, in terms of quarterly trends, IP contracted by 3.9% in July-August period compared to 0.9% in 2Q22 on the back of a sharp adjustment in intermediate goods production, which was followed by consumer (mainly non-durables), capital and energy goods, respectively.

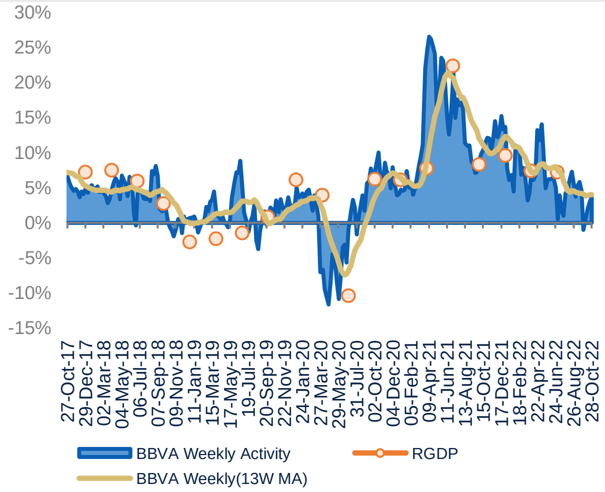
In sectorial details, there were only a few sectors in the manufacturing industry (motor vehicles, other transportation and machinery) that were able to grow in July-August period compared to 2Q. As a result, there was a wide-spread worsening in the production of both export-oriented and domestic demand driven sectors, implying a significant adjustment in early 3Q and confirming the downward pressure on exports led by the recession signals in Europe and tighter global financial conditions. Also, manufacturing capacity utilization rate declined to 77.3% on average in 3Q (vs. 77.9% in 2Q), manufacturing PMI (46.9 in Sep. vs. 47.4 in Aug. and 48.8 in 2Q) and electricity production (0.5% y/y in 2Q and -4.6% y/y in 3Q) remained contractionary. Yet, we nowcast a quarterly GDP growth of 0-0.5% in 3Q with complementing information from September activity indicators and our Big Data proxies, which could still imply an annual GDP growth of near 5% after the strong 7.5% growth in the first half of the year. We also introduce the Garanti BBVA Research weekly GDP tracker as our latest advance on the nowcasting exercise. It shows a deceleration to around 4% annual GDP growth as of mid-October (Figure 2).

Figure 1. **Garanti BBVA Monthly GDP Indicator*** (yoy, 3-month moving avg.)



*Garanti BBVA monthly GDP is an average of different model results synthesizing high-frequency indicators to proxy monthly GDP (GBTRGDPY Index in BBG)

Figure 2. **Garanti BBVA Weekly GDP Tracker*** (YoY)



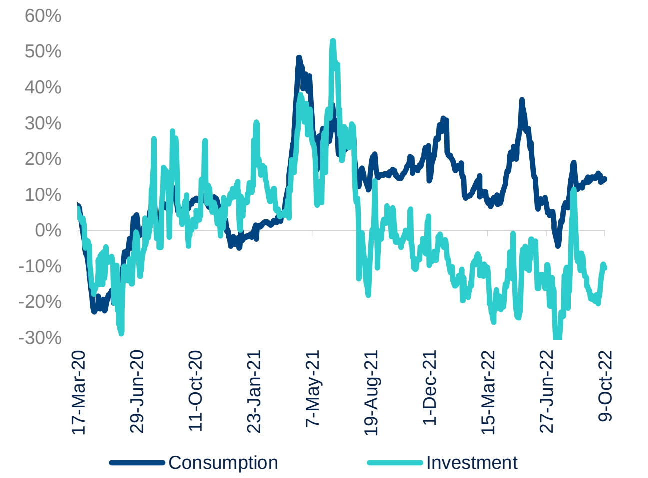
Source: Garanti BBVA Research, Turkstat, for methodology please check *our research*

Consumption remains strong, no contribution from investment

In terms of demand components, there has been a limited evidence of a slow down in domestic demand as our big data demand indicators point out. In spite of a continuing high inflation environment, private consumption remains to be the main driving factor behind overall GDP growth with a very limited slow-down as of early October. Meanwhile, deceleration is more evident in investment expenditures as our investment nowcast model shows a yearly growth (3ma) of almost zero in early October. Moreover, as the momentum for imports keeps its pace and exports weaken more clearly, contribution from net exports also started to weaken in 3Q, which was an important part of growth performance for the last six quarters. Overall, these numbers point to a gradual deceleration in economic activity with a more distorted outlook in terms of demand sub-components.

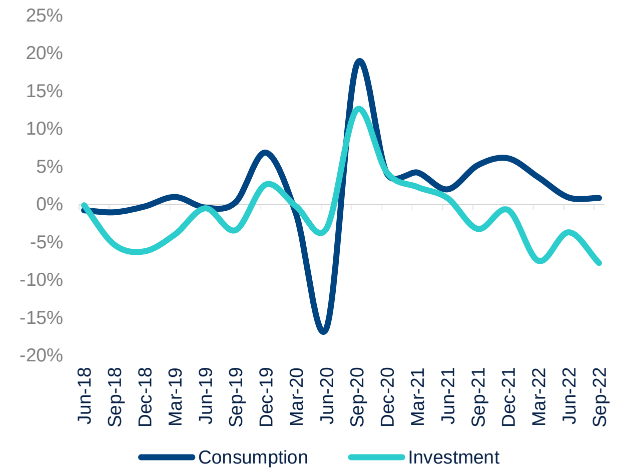
Since the demand side of the economy -particularly consumption- seems to be much stronger supported by the continuing employment gains, we might still observe some depletion from inventories. Yet, continuation of import demand in a need of renewing inventories would still keep inflationary risks alive.

Figure 3 **Garanti BBVA Big Data Domestic Demand Indicators** (28-day sum, adjusted by CPI and PPI, YoY)



Source: Garanti BBVA Research, Turkstat

Figure 2 **Garanti BBVA Big Data Domestic Demand Indicators** (qoq, adjusted by CPI and PPI)



Source: Garanti BBVA Research, Turkstat

2022 GDP growth expected to reach 6%

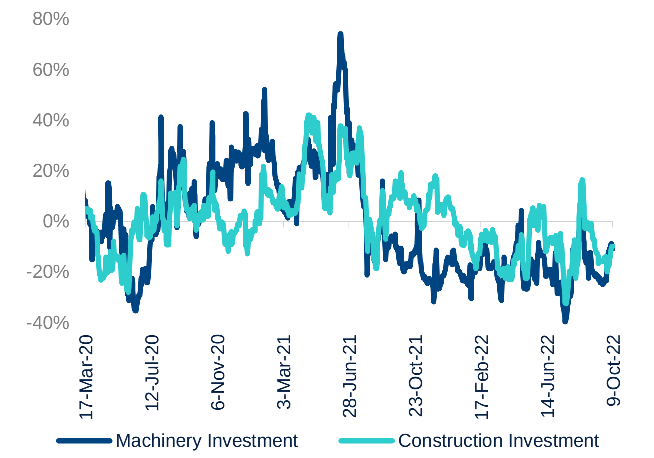
Larger negative real interest rates, credit and fiscal impulses and resilient external demand helped economic activity to grow above its potential in the first half of the year, and both domestic and external demand contributed positively. Looking ahead, much tighter global financial conditions and clear downside risks to external demand -particularly recession in Europe- create uncertainty on the near term growth outlook. Moroever, side effects from the recent so-called macro-prudential measures have started to add noise in terms of financial stability.

According to our nowcasts, GDP growth has started to decelerate more clearly as of 3Q but the slow-down so far proved to be milder than expected with still positive q/q growth rates. The political decision to maintain pro-growth policies at all costs leads us to expect more countercyclical fiscal measures ahead of the elections in addition to the continuation of ultra-loose monetary policy. Therefore, we expect 2022 GDP growth to reach 6%, implying a strong momentum for the start of next year, which would help to maintain the growth rate close to potential in 2023 (3.5%). Since this would mean delaying a harsh adjustment, elevated current account deficit, substantial financial stability risks and high inflation will continue for some time.

Figure 3 **Garanti BBVA Big Data Consumption Indicators** (28-day sum, adjusted by CPI, YoY)

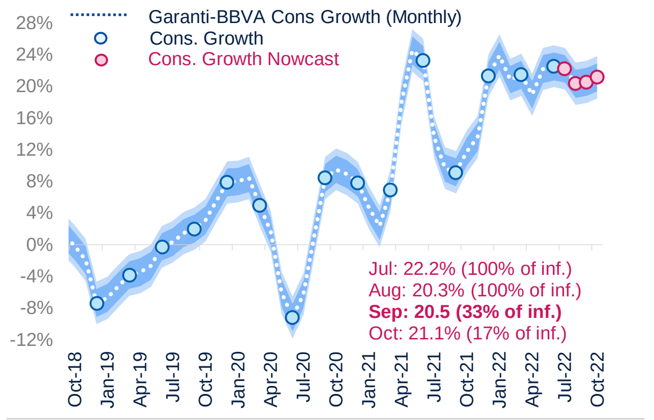
Source: Garanti BBVA Research, Turkstat

Figure 4. **Garanti BBVA Big Data Investment Indicators** (28-day sum, adjusted by PPI, YoY)



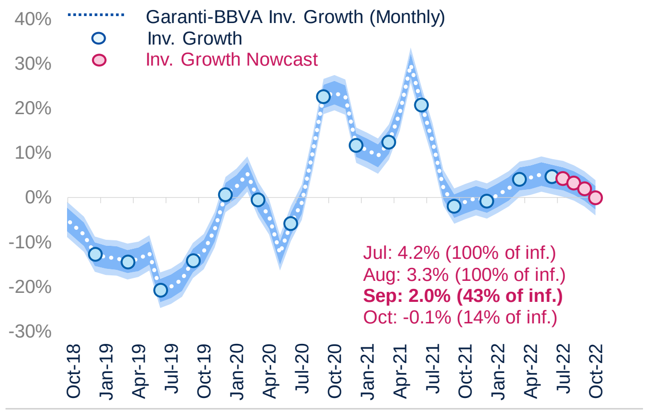
Source: Garanti BBVA Research, Turkstat

Figure 5. **Garanti BBVA Monthly Consumption Nowcast** (3m yoy)



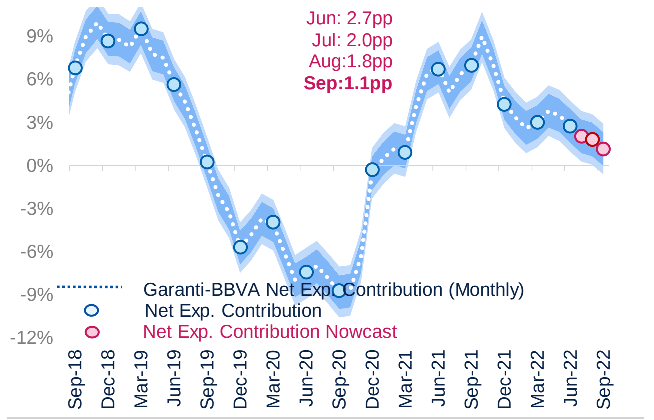
Source: Garanti BBVA Research, GBTRCGDPY Index in Bloomberg

Figure 6. **Garanti BBVA Monthly Investment Nowcast** (3m yoy)



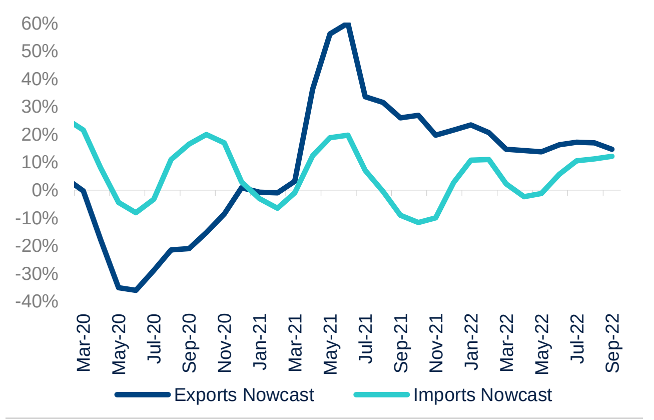
Source: Garanti BBVA Research, GBTRIGDPY Index in Bloomberg

Figure 7. **Garanti BBVA Monthly Net Exports Nowcast** (contribution, pp)



Source: Garanti BBVA Research, GBTRXGDPY and GBTRMGDPY in Bloomberg

Figure 8. **Garanti BBVA Monthly Foreign Trade Nowcasts** (3m yoy)



Source: Garanti BBVA Research, GBTRXGDPY and GBTRMGDPY in Bloomberg

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