



COUNTRIES IN FOCUS:

Türkiye & Bulgaria

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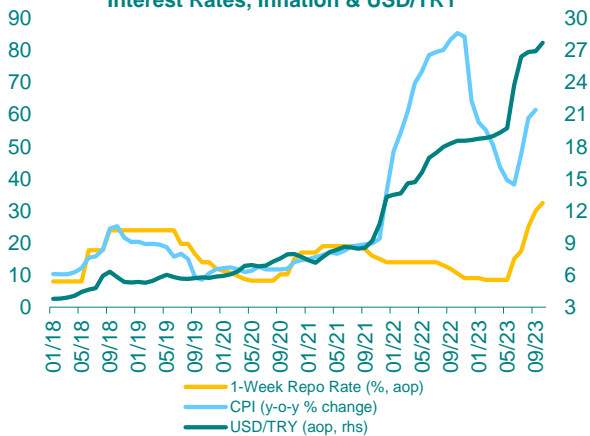
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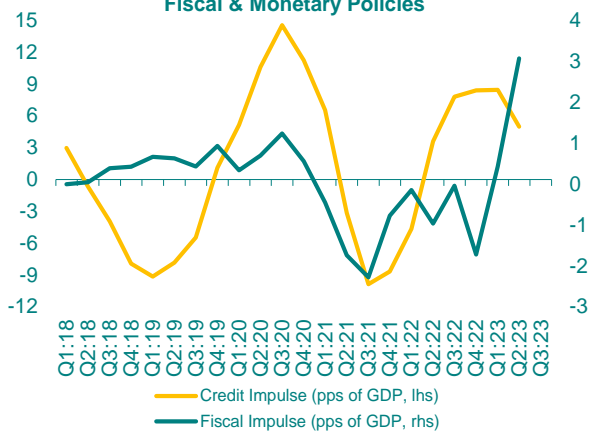
Türkiye

B / B3 / B (S&P / Moody's / Fitch)

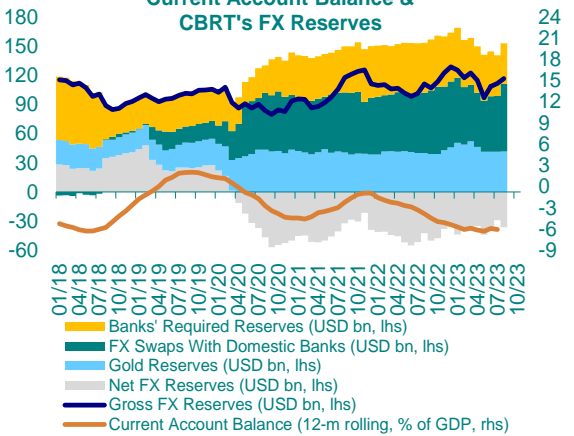
Interest Rates, Inflation & USD/TRY



Fiscal & Monetary Policies



Current Account Balance & CBRT's FX Reserves



	16 Oct.	3-M F	6-M F	12-M F
O/N TLREF (%)	29.1	35.0	35.0	35.0
TRY/USD	27.90	29.00	30.00	32.00
Sov. Spread (2027, bps)	358	340	325	300

	16 Oct.	1-W %	YTD %	2-Y %
ISE 100	7,935	-3.2	44.0	462.9

	2020	2021	2022	2023F	2024F
Real GDP Growth (%)	1.9	11.4	5.5	4.2	2.2
Inflation (eop, %)	14.6	36.1	64.3	66.0	30.0
Cur. Acct. Bal. (% GDP)	-4.4	-0.9	-5.3	-5.0	-3.3
Fiscal Bal. (% GDP)	-3.4	-2.6	-0.9	-5.2	-4.5

Sources: Reuters, CBRT, BDDK, Turkstat & NBG estimates

The CBRT continues to hike rates aggressively, with the end of the cycle, however, being not far away.

In mid-September, the CBRT raised its key rate further by a whopping 500 bps to a near two-decade high of 30.0%, bringing the total hikes since the change of guard at the helm of the CBRT, in June, to 2150 bps. Recall that in the wake of his re-election and in a bid to calm markets, which were expecting return to conventional policies, President Erdoğan appointed former banker in the US, H. G. Erkan, as the CBRT's new Governor -- the 5th since 2019.

The reversal in interest rates has been complemented by selective credit and quantitative tightening measures, aiming, *inter alia*, at rebalancing lending away from consumers and towards businesses. At the same time, the CBRT has been proceeding with a partial roll-back of macro-prudential regulations stemming dollarization, including its (costly) FX-protected deposit scheme. The latter was introduced in late-2021 to contain FX depreciation pressures, with FX-protected deposits having since surged to c. USD 120bn, equivalent to c. 25% of total deposits.

The CBRT's hawkish turn has been welcomed by investors (with S&P revising its outlook on Türkiye to "stable" from "negative" at end-September), bringing some relief in the FX market, with the TRY continuing to depreciate, but at a much slower pace than before, currently standing at an all-time low of 27.9 against the USD.

Considering the still deeply negative real policy rate (c. -20.0% in *ex-post* terms or -6.0% based on 12-M inflation expectations) and the size of the monetary stimulus injected into the economy, authorities have a long way to go before Türkiye's imbalances get effectively unwind. Recall that, in light of the structural external deficit (largely stemming from Türkiye's complete reliance on imports to cover its energy needs), the ultra-accommodative monetary policy authorities have been pursuing over the past years has trapped the economy into a vicious cycle of weakening TRY (down 35% against the USD between end-2021 and the May '23 elections and 80% in FY:18-22) and high inflation (up 71.6% in FY:22 and c. 25.0% in FY:18-22), which was, however, has been accompanied by strong GDP growth (up 4.5% in FY:18-22).

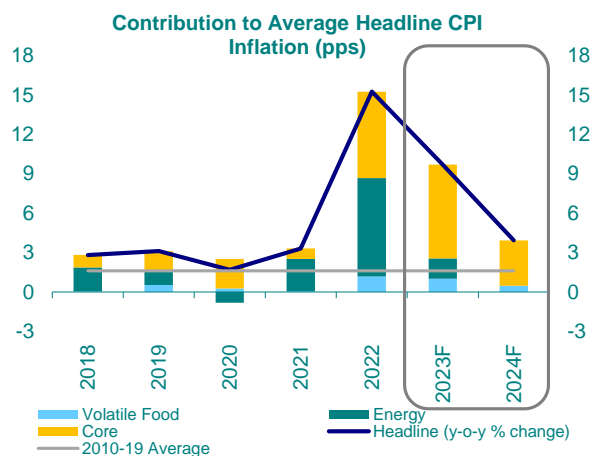
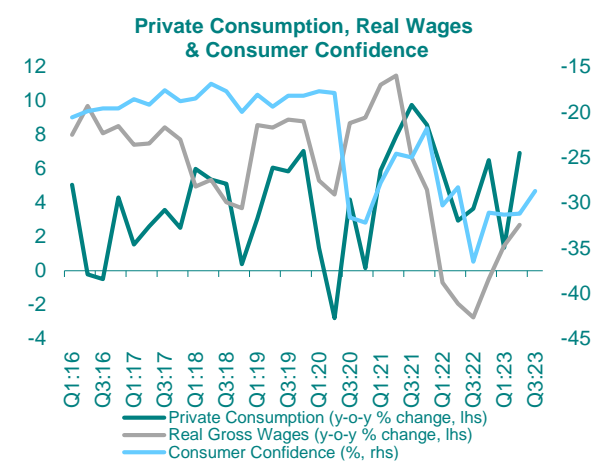
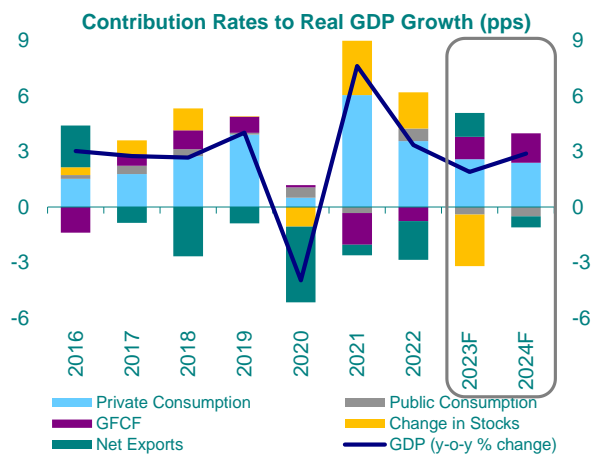
Note that the CBRT is short of ammunition to defend the TRY during the adjustment period, as -- despite recent trends -- its net FX reserves remain negative. This means that authorities would have to continue relying on non-market financing flows from Türkiye's partners -- including GCC states, especially UAE, and Russia -- to close the external financing gap, at least in the short-term.

Looking ahead, the CBRT should continue hiking rates, while unwinding its complex macro-prudential regulations protecting the TRY. Assuming no inflation surprise (with related risks being highly skewed to the upside, however, reflecting, *inter alia*, rising global oil prices as well as the ongoing easing in incomes policy and the hikes in indirect taxes to fund the widening budget deficit), we see the policy rate at 35.0% by end-2023 and remaining at that level by late-2024 (when the real *ex-ante* policy rate is projected to hover around 0%). Given President Erdoğan's track record of populist policy shifts, the uncertainty surrounding our forecast is large. Worryingly, the political factor is expected to remain at play at least until the March '24 local elections.

Leaving aside political considerations, the CBRT's cautious approach to policy normalization should be mainly attributed to its bid to safeguard macro-financial stability. Indeed, in the event of a drastic withdrawal of excess liquidity from the market, the already highly debt-burdened private sector (with a total exposure of c. 185% of GDP, over 40% of which is FX-denominated) would see its debt repayment capacity coming under (further) severe strain, stressing, *inter alia*, banks, given the latter's tight liquidity position (with a loan-to-deposit ratio of 98%).

Bulgaria

BBB / Baa2 / BBB (S&P / Moody's / Fitch)



Strong (EU-funded) investment activity and resilient private consumption should underpin economic growth in the period ahead. Looking ahead, we expect fund absorption under the RFF to improve over the next quarters, catalyzing investment from the private sector, despite restrictive financing conditions. Note that, despite the relatively favourable market environment over the past 2 years, the investment-to-GDP ratio has dropped markedly (to 16.0%, well below the EU average of more than 22.0%), highlighting not only the crucial role of political stability (with significant delays on key legislative reforms having led so far to poor implementation of the country's RFF plan), but also the need to enhance further the business environment.

On the other hand, private consumption, the traditional pillar of growth in the economy, should remain resilient, albeit with limited upside potential. Indeed, tight labour market conditions (with real *ex-post* wage growth having returned into positive territory as of Q1:23) and improving economic sentiment should support consumer spending, broadly counterbalancing the impact of elevated inflation and high debt-servicing costs. Worryingly, stubbornly high core inflation, sticky supply-driven food inflation and the renewed surge in global oil prices mean that the road to disinflation would be slow and bumpy (see also below).

At the same time, net exports are unlikely to add to GDP growth, in view of sluggish economic expansion in the EU. Note that Bulgaria's export performance has been less affected than its peers', thanks to a relatively smaller deterioration in its terms-of-trade (reflecting the large share of raw and low-added value products in exports as well as the impact of the generous state subsidy scheme to businesses) and increased -- in terms of volumes -- (coal-based) electricity exports.

All said, we see GDP growth easing to 1.8% in FY:23 from 3.4% in FY:22, overperforming compared with the EU average (up c. 1.0%). Assuming inflation loosens its grip on the economy in FY:24, we see GDP growth picking up to 2.5%, still below its long-term potential.

Political stability is key to economic growth. Recall that in June, nearly 2 months after the April election, the 5th held over the past 2 years, the Parliament voted in a coalition Government, backed by the country's largest political forces, the GERB and the "We Continue the Change" parties. The deal between the two parties and former bitter feuds provides for a 18-month rotational Government.

Should the deal between the two coalition partners break, Bulgaria could face a new political deadlock, given that no political party appears to be able to muster an absolute majority if elections were to be held now. Despite elevated political noise related to the upcoming local election, we expect the Government to complete its term. Importantly, the risk of serious policy slippage is limited, given political parties' consensus on Bulgaria's strategic goals and the anchors provided by the currency board and the inclusion of the BGN into the ERM II.

Euro adoption to be delayed at least until 2025. Recall that delays in the adoption of necessary legislation, mainly due to political instability, and elevated inflation prompted authorities to defer the target date for euro adoption by 1 year to 2025. Although inflation has started to ease recently, it remains significantly above that of the 3 best performing EU states, with Bulgaria unlikely to meet the price criterion by the deadline of mid-2024 so as to ensure accession in 2025.

Worryingly, there are serious concerns over the prospect of sustainable inflation convergence. Indeed, under a fixed exchange rate regime, improvements in productivity would be eventually translated into higher inflation (Balassa-Samuelson effect). Note that prices in Bulgaria currently stands at c. 60% of the euro area average, confirming the significant upside potential for inflation.

	16 Oct.	3-M F	6-M F	12-M F
Base Interest Rate (%)	3.6	3.8	3.8	3.6
BGN/EUR	1.96	1.96	1.96	1.96
Sov. Spread (2027, bps)	102	100	97	92

	16 Oct.	1-W %	YTD %	2-Y %
SOFIX	748	-1.0	24.4	30.2

	2020	2021	2022	2023F	2024F
Real GDP Growth (%)	-4.0	7.6	3.4	1.8	2.5
Inflation (eop, %)	0.1	7.8	16.9	5.3	3.5
Cur. Acct. Bal. (% GDP)	0.0	-1.7	-1.4	0.1	0.3
Fiscal Bal. (% GDP)	-2.9	-2.8	-0.8	-3.0	-2.5

Sources: Reuters, NSI & NBG estimates

DETAILED MACROECONOMIC DATA

TÜRKİYE					
	2020	2021	2022	2023f	2024f
Real Sector					
Nominal GDP (USD million)	719,217	816,582	905,789	1,015,921	1,191,319
GDP per capita (USD)	8,602	9,643	10,572	11,721	13,592
GDP growth (real, %)	1.9	11.4	5.5	4.2	2.2
Unemployment rate (% aop)	13.2	12.0	10.5	10.0	10.3
Prices and Banking					
Inflation (% eop)	14.6	36.1	64.3	66.0	30.0
Inflation (% aop)	12.3	19.3	71.6	53.6	50.4
Loans to the Private Sector (% change, eop)	34.8	37.0	54.5		
Customer Deposits (% change, eop)	33.0	51.5	68.0		
Loans to the Private Sector (% of GDP)	70.8	67.5	50.4		
Retail Loans (% of GDP)	16.8	14.4	11.2		
Corporate Loans (% of GDP)	54.1	53.1	39.2		
Customer Deposits (% of GDP)	62.1	65.4	53.1		
Loans to Private Sector (% of Cust. Deposits)	114.1	103.2	94.9		
Foreign Currency Loans (% of Total Loans)	34.2	42.2	32.6		
External Accounts					
Merchandise exports (USD million)	168,378	224,686	252,416	258,307	277,629
Merchandise imports (USD million)	206,252	253,999	342,899	351,826	364,519
Trade balance (USD million)	-37,874	-29,313	-90,483	-93,519	-86,890
Trade balance (% of GDP)	-5.3	-3.6	-10.0	-9.2	-7.3
Current account balance (USD million)	-31,888	-7,232	-48,405	-51,139	-39,092
Current account balance (% of GDP)	-4.4	-0.9	-5.3	-5.0	-3.3
Net FDI (USD million)	4,456	6,874	8,412	9,253	10,641
Net FDI (% of GDP)	0.6	0.8	0.9	0.9	0.9
International reserves (USD million)	93,277	111,181	128,736	125,000	132,500
International reserves (Months ^a)	4.9	4.7	3.3	4.1	4.2
Public Finance					
Primary balance (% of GDP)	-0.8	-0.2	1.1	-2.7	-1.5
Fiscal balance (% of GDP)	-3.4	-2.6	-0.9	-5.2	-4.5
Gross public debt (% of GDP)	39.6	41.8	31.7	34.0	35.0
External Debt					
Gross external debt (USD million)	429,177	437,281	458,699	490,000	520,000
Gross external debt (% of GDP)	59.7	53.6	50.6	48.2	43.6
External debt service (USD million)	70,931	74,311	80,000	85,000	90,000
External debt service (% of reserves)	76.0	66.8	62.1	68.0	67.9
External debt service (% of exports)	37.5	27.6	25.4	26.3	25.9
Financial Markets					
Policy rate (Effective funding rate, % eop)	17.0	14.0	9.0	35.0	30.0
Policy rate (Effective funding rate, % aop)	10.5	17.6	12.6	19.4	34.6
10-Y T-bill rate (% eop)	12.5	23.1	9.9	24.0	19.0
Exchange rate: USD (eop)	7.43	13.32	18.69	29.00	33.00
Exchange rate: USD (aop)	7.02	8.89	16.57	23.65	31.00

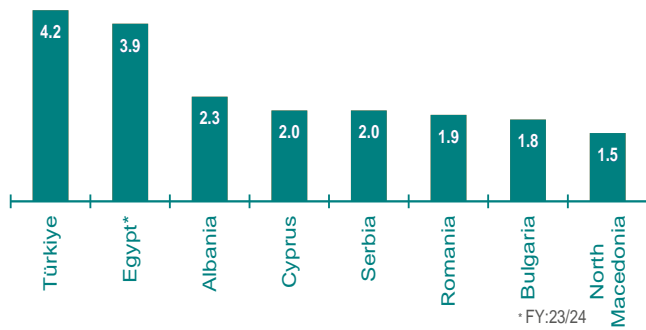
f: NBG forecasts; a: months of imports of GNFS

BULGARIA					
	2020	2021	2022	2023f	2024f
Real Sector					
Nominal GDP (EUR million)	61,638	71,076	84,559	94,431	100,567
GDP per capita (EUR)	8,911	10,393	12,439	13,975	14,972
GDP growth (real, %)	-4.0	7.6	3.4	1.8	2.5
Unemployment rate(ILO definition, %, aop)	6.1	5.3	4.3	4.3	4.2
Prices and Banking					
Inflation (% eop)	0.1	7.8	16.9	5.3	3.5
Inflation (% aop)	1.7	3.3	15.2	9.7	3.9
Loans to the Private Sector (% change, eop)	4.5	8.3	12.2		
Customer Deposits (% change, eop)	10.2	9.0	14.4		
Loans to the Private Sector (% of GDP)	50.7	47.6	44.9		
Retail Loans (% of GDP)	20.8	20.5	19.8		
Corporate Loans (% of GDP)	29.9	27.1	25.1		
Customer Deposits (% of GDP)	73.1	69.1	66.4		
Loans to Private Sector (% of Deposits)	69.4	68.9	67.6		
Foreign Currency Loans (% of Total Loans)	31.1	28.7	25.7		
External Accounts					
Merchandise exports (EUR million)	27,272	34,405	47,145	45,281	47,665
Merchandise imports (EUR million)	29,213	37,291	52,219	49,890	52,490
Trade balance (EUR million)	-1,941	-2,887	-5,074	-4,609	-4,825
Trade balance (% of GDP)	-3.1	-4.1	-6.0	-4.9	-4.8
Current account balance (EUR million)	0,024	-1,225	-1,200	0,056	0,285
Current account balance (% of GDP)	0.0	-1.7	-1.4	0.1	0.3
Net FDI (EUR million)	2,759	1,249	2,098	2,098	2,151
Net FDI (% of GDP)	4.5	1.8	2.5	2.2	2.1
International reserves (EUR million)	30,848	34,597	38,424	38,928	39,864
International reserves (Months ^a)	11.1	9.8	7.8	8.2	7.9
Public Finance					
Primary balance (% of GDP)	-2.4	-2.4	-0.4	-2.5	-2.0
Fiscal balance (% of GDP)	-2.9	-2.8	-0.8	-3.0	-2.5
Gross public debt ^b (% of GDP)	24.5	23.9	22.9	23.5	24.6
External Debt					
Gross external debt (EUR million)	38,991	41,214	44,431	45,327	45,859
Gross external debt (% of GDP)	63.3	58.0	52.5	48.0	45.6
External debt service (EUR million)	7,041	7,000	8,200	7,100	7,250
External debt service (% of reserves)	22.8	20.2	21.3	18.2	18.2
External debt service (% of exports)	20.4	16.1	13.8	12.1	11.7
Financial Markets					
Base Interest Rate (% eop)	0.0	0.0	1.3	3.8	3.4
Base Interest Rate (% aop)	0.0	0.0	0.2	2.9	3.6
10-Y Bond Yield (% eop)	0.4	0.7	6.0	4.3	4.0
Exchange rate: EUR (eop)	1.956	1.956	1.956	1.956	1.956
Exchange rate: EUR (aop)	1.956	1.956	1.956	1.956	1.956

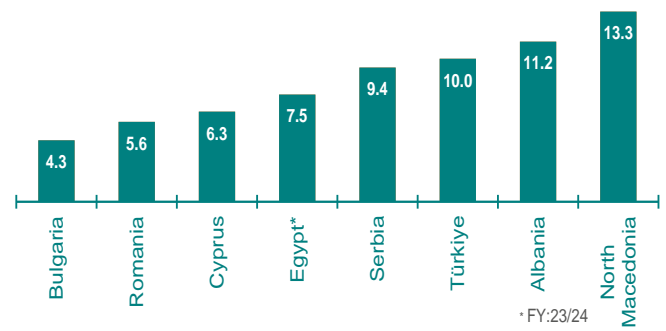
f: NBG forecasts; a: months of imports of GNFS; b: ESA 2010

REGIONAL SNAPSHOT: MACROECONOMIC INDICATORS

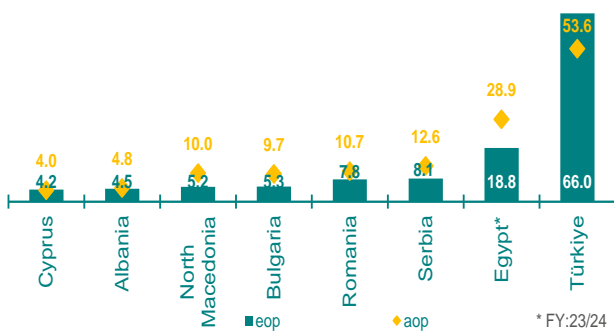
Real GDP Growth (% , 2023F)



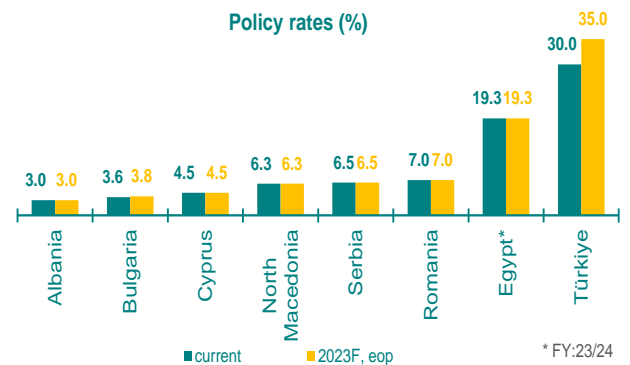
Unemployment (% , 2023F, aop)



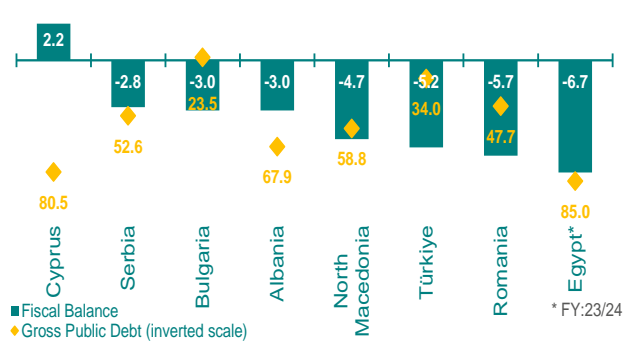
Headline inflation (% , 2023F)



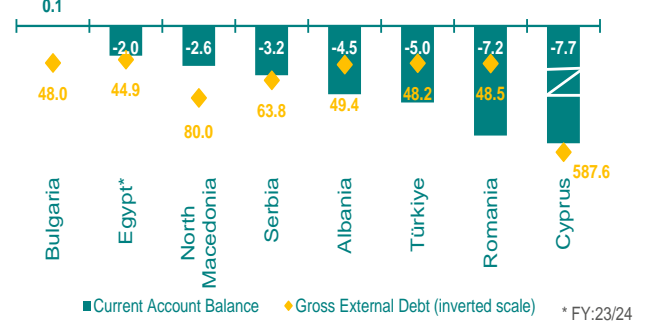
Policy rates (%)



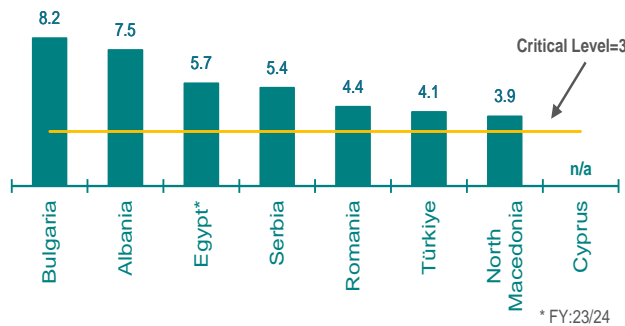
Public Finance (% of GDP, 2023F)



External Accounts (% of GDP, 2023F)

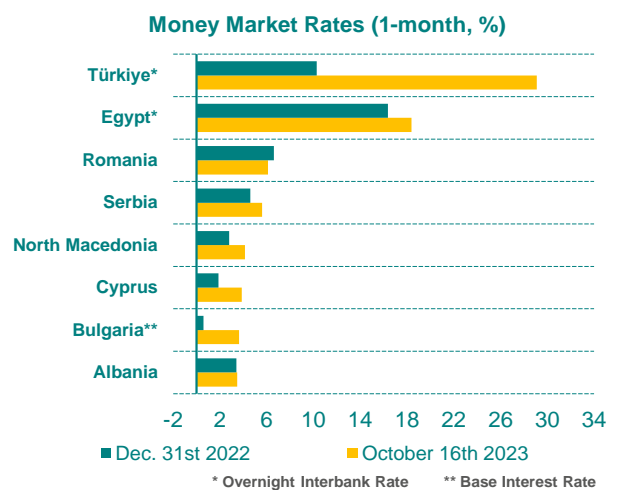
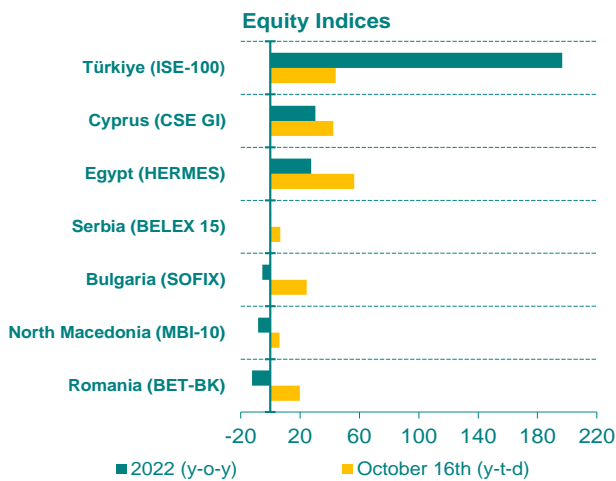
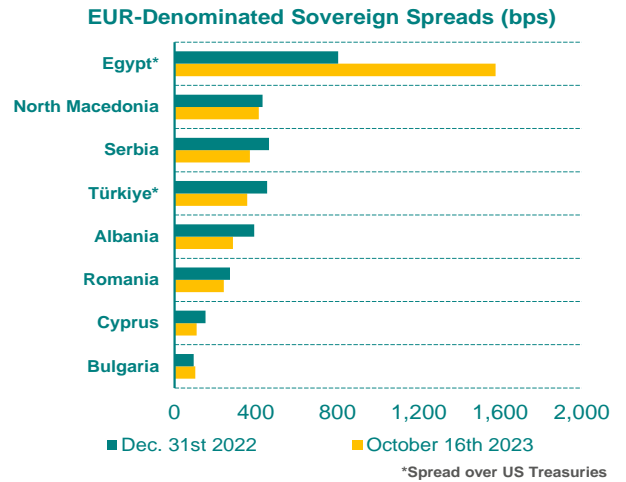
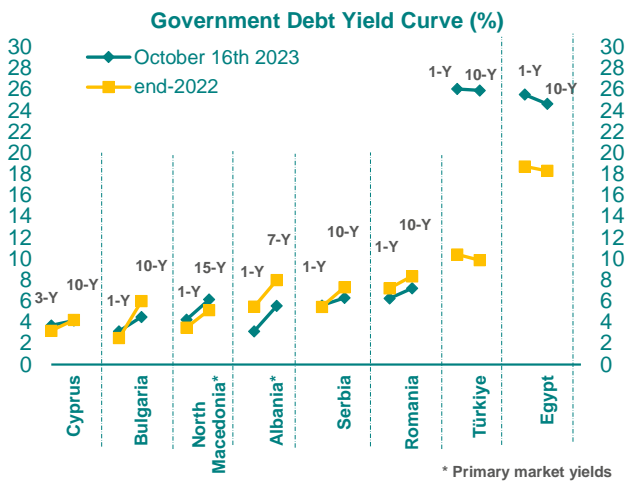
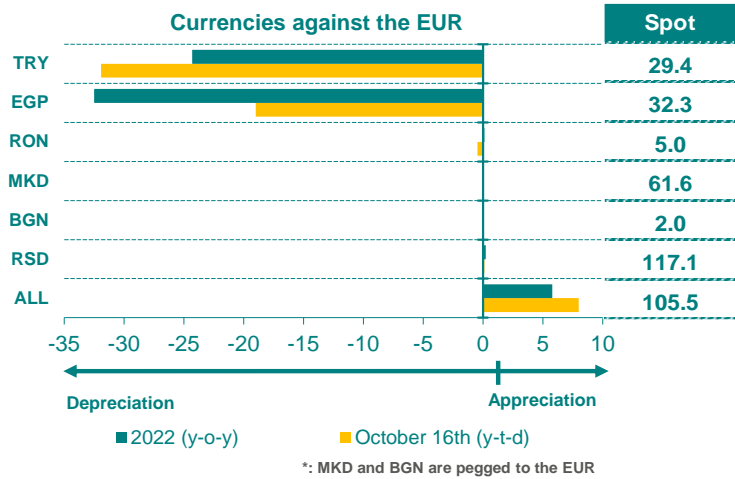


FX Reserves (Months of Imports, 2023F)



Sources: National Sources & NBG estimates

REGIONAL SNAPSHOT: FINANCIAL MARKETS



Sources: Reuters & NBG estimates

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