



EXECUTIVE SUMMARY

- Foreign investors' bond portfolio includes \$10B of GDDS, \$45.1B of Eurobond issued by the Treasury, \$38.1B of FX-denominated PSBs issued abroad and \$0.3B worth of PSBs issued domestically. We've calculated the sum as \$93.5B.
- Recent developments about Turkey's surprise decision to fire its central bank governor.
- 20.7% of the net borrowing limit of TRY50.8B was used by Treasury in the first two months of the year.
- Turkey's white goods export volume grew 19% to 1.94M on an annual basis in February.
- Justice and Development Party's (AK Party) seventh ordinary congress will be held in Ankara today. Justice and Deputy Chairman Mahir Unal confirmed the rumors about the possible changes in the cabinet.
- The Consumer Confidence Index (CCI) which is jointly calculated by TurkStat and CBRT is expected to be announced today 10 AM (GMT+3).

Dive deep on the positions (except stock exchange) of foreign investors in Turkey

In the course of volatility in the FX, we will try to reveal the ownership level of foreign investors in Government Domestic Debt Securities, Private Sector Bonds and Eurobonds by using CBRT's weekly data on portfolio movements of non-residents, as of 6th of November when Agbal was appointed as CBRT's governor.

Our preliminary finding is that share of foreign portfolio in all bonds is in a moderate upward trend after reaching historical lows before 6th of November.

Other details are following;

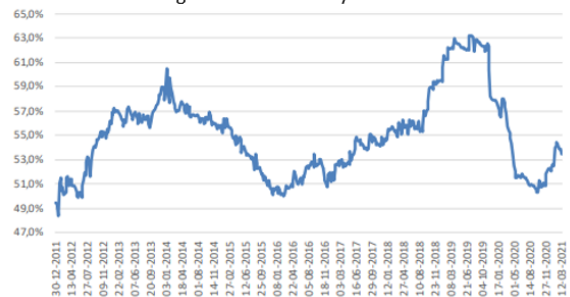
- The stock value of the foreign portfolio of Government Domestic Debt Securities is reached \$10B with a 6.9% share. This value indicates that the share of foreigners recovered from the rate of 3.3% on November 6th which was the all-time low.

Foreign Share – Government Domestic Debt Securities

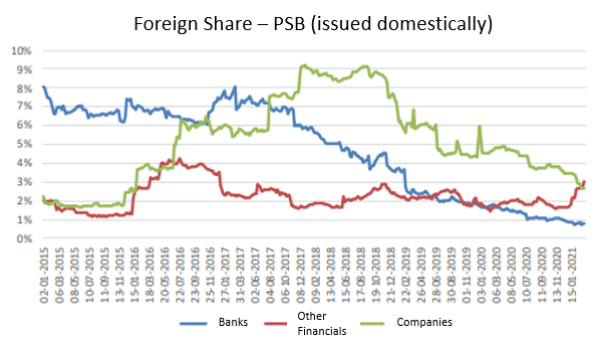
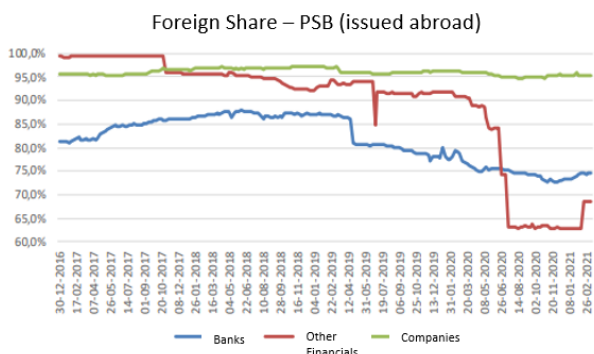


- The stock value of the Eurobond instrument exported by the Treasury in foreign markets is \$84.3B. Excluding foreign branches of domestic banks, foreign investors rose to 53.5% with \$45.1B. This value was near its historic low at \$39.9B (50.7%) before November 6.

Foreign Share – Treasury Eurobond



- The FX-denominated Private Sector Bonds (PSB) stock issued by banks, other financial institutions and companies abroad reached a total of \$48.5B. The foreign share is at a high level with \$29B (74.5% - banks), \$108M (68.6% - other financial institutions) and \$9B (95.3% - companies), respectively. The share of foreigners in bank Private Sector Bonds was close to 88% before 2018. Before November 6th, it fell to the lowest level of the series with 72.8%.



To sum up; foreign investors' bond portfolio includes \$10B of GDDS, \$45.1B of Eurobond issued by the Treasury, \$38.1B of FX-denominated PSBs issued abroad and \$0.3B worth of PSBs issued domestically. We've calculated the sum as \$93.5B. As the indicator for the foreign investor's taking derivative position purchase in favor of TRY; we are following the change of the banks' off-balance sheet FX position.

After the massive outflows in 2020, along with the economic management changes as of 6th of November, significant inflows (around \$14B) have been observed.

Groundhog day for Turkish economy

The CBRT governor Naci Agbal was replaced by Prof Sahap Kavcioglu by way of presidential decree on early Saturday. Thus, Agbal was the third central bank governor who have been dismissed by President Recep Tayyip Erdogan in less than two years.

The new central bank governor, Mr. Kavcioglu, is a banking professor and worked many years as a banker, including the role as the Deputy CEO at Halkbank. He is also former member of parliament of the ruling party and columnist for the pro-government Yeni Safak newspaper where he has been repeatedly writing that higher interest rates lead to higher inflation, adopting the unorthodox view of Mr. Erdogan.

In fact, Kavcioglu explicitly criticized Agbal's recent decision to rates hiking by 200 bps, pointing out the negative impact of high interest rates on growth. Then two days after the Central Bank's policy rate increase from 17% to 19% in order to achieve price stability, CBRT Governor Naci Agbal was sacked who had been credited as a key figure in pulling the lira back from its all-time low levels.

Kavcioglu pledged to use monetary-policy tools effectively to tackle inflation on Sunday morning. He also stated the bank's next MPC meeting will take place according to scheduled on April 15. Additionally, Treasury and Finance Minister Lutfi Elvan said on Monday that Turkey will not compromise from the free-market mechanism, and continue to liberal foreign-exchange regime. Yet, Turkey's surprise decision to fire its central bank governor has jumped uncertainty. The removal, undermined any recently gained credibility of the country's monetary policy and inflamed concerns about return to unorthodox policies.

Agbal tried to recover the credibility of the CBRT with his strong communication and bold actions. He hiked rates significantly to 19% from 10.25%, without any hesitation unlike its predecessor since taking over in November. At the same time, by emphasizing that the reform steps to be taken in the field of law will support the disinflationary process, he approached the current situation in the country in a realistic way.

The use of more than \$100B FX reserves to support the currency could not prevent the lira from depreciating to its all-time low levels against the US dollar last year.

Nevertheless, the appetite of foreign investors for Turkish assets started to raise and according to our calculation overseas inflows to Turkey through swaps totaled around \$14B during the brief tenure of Agbal.

Thus, the shock firing of central bank governor Agbal may bust investors belief in "Turkey's story".

International organizations including JP Morgan, Morgan Stanley, BofA and Moody's analyzed the developments and warned about the next steps. JP Morgan stated that there is no room for a significant change in monetary policy due to high inflation, dependency to external financing and tightening in global financial conditions. They also noted that they will keep their forecast for Turkey, for now. In the meantime, they have an expectation from CBRT to drop rates by 100 bps in September as a next step.

Morgan Stanley said that FX intervention can be expected to dampen the upward movement in exchange rates, but the authorities' scope for action will be constrained due to limited reserves. "If the CBRT in the end maintains the current policy of positive real rates under the new governor, then we would still expect – despite a weaker TRY – a sustained fall in inflation from late 2021.", the bank also noted.

BoFA strategists stated that the change in the CBRT took place at a time when foreign positioning in TRY is the highest of the past decade, on par with the peak in 2017. At the same time, it was stated in the report that volatility in US rates during this era may cause more outflows from emerging domestic markets. BofA also noted that year-end inflation forecast is 12% based on the assumption that the CBRT hold rates 19% until the end of 3Q.

Ratings agency Moody's declared that the Turkey's decision to dismiss its central bank governor "increases the risk of renewed pressure on the exchange rate and the surprise move is also further evidence of the complete lack of policy predictability in Turkey and confirms our view of serious institutional weakening in the country over the past several years."

The Treasury reached 20% of the borrowing limit in the first two months of the year

In regards to the Treasury's General Budget Financing data, the Treasury's net borrowing in February reached TRY18.9B. This amount was composed of TRY9.6B net domestic borrowing and TRY0.6B net foreign debt payment.

Although the cash balance gave a surplus of TRY20.2B in February, an increase in the Treasury's account around TRY39.3B was observed due to high net borrowing.

Treasury's total TL and FX deposits at the CBRT rose to TRY179B from TRY149.5B at the end of February MoM. Thus, 20.7% of the net borrowing limit of TRY50.8B was used in the first two months of the year. This amount was TRY49.5B in the same period of the previous year. As is known, the Treasury's net borrowing limit for 2021 is the difference between general budget revenues and expenditure appropriations. In other words, the borrowing ceiling for this year was determined as TRY246B. However, the Minister of Economy and the President may increase this limit by 10% to TRY270B.

Funding cost and overnight repo rate increased

The Central Bank's total OMO funding Bank inclined to TRY333B, TRY71B was provided by one week repo (19%) tender. Therefore, the average funding cost closed by 18.32%. Meanwhile, upon CBRT's withdrawn liquidity amount through 17.5% quotation declined to TRY6.8B, whereas net funding amount rose up to TRY326.2B.

Valid overnight repo interest average hiked to 19.15% compared to yesterday and occurred above CBRT's policy rate.

On the other side, \$18M of transactions were made in CBRT Turkish Lira Currency Swap Market one-week maturity. Thus, FX swap stock reached \$31.2B.

Total transaction amount in CBRT's Turkish Lira-Gold swap was closed with a transaction of 2600kg. The short position amounted to \$5B.

There was no transaction amounted by Istanbul Stock Exchange (ISE), while the swap stock dropped to \$8.3B, the CBRT data showed. The total short position reduced to \$44.4B at the end of the day.

White goods production maintained its strength with the contribution of strong domestic and foreign demand

Domestic sales in February white goods sector surged %42 annually and hit 794K units, the White Goods Manufacturers' Association of Turkey said. The association also noted that Turkey's white goods export volume grew 19% to 1.94M on an annual basis in February. Thus, with the contribution of strong domestic and foreign demand, white goods production volume increased by 29% to 2.9M units YoY in the month.

Erdogan may reshuffle Turkish Cabinet today

Justice and Development Party's (AK Party) Deputy Chairman Mahir Ünal confirmed the rumors about the possible changes in the cabinet by speaking to the press:

"When the change is discussed, there is inevitably a dynamism in the whole system. There will be a new arrangement for 2023, not only for the party but also for the (president's) team. We will see this in the coming days."

Justice and Development Party's (AK Party) seventh ordinary congress will be held in Ankara today. Changes are expected in the Central Decision and Board of Directors, which is the highest decision-making body of the party and

Subsequently, there are some rumors about changes in the members of the Central Executive Board (MYK) of 16 people, called "A team". The change in the AK Party MKYK is expected to be different from the change in the AK Party congresses held so far. It is stated in the MKYK that the structure consisting mainly of deputies will change, the number of non-MPs in MKYK will increase, and new names who have not done politics in the AK Party so far may be included in addition to the former deputies. Erdogan is expected to establish an "election cabinet" in a sense that aims to win the 2023 elections. A cabinet revision is expected to be carried out by dividing some ministries and the establishment of new ministries. In addition to that there are some rumors about dismissal of some ministers, and shifts in some ministries. It is expected that the cabinet change will take place before the congress, and some names outside the cabinet may be transferred to the party. With the cabinet revision to be carried out, the rumors that the names coming from politics will be given more space are increasing. It is also stated that some ministries may be divided due to the increased workload, and the number of deputy presidents could be increased to two.

CCI will be announced today 10:00 AM – GMT+3

The Consumer Confidence Index (CCI) which is jointly calculated by TurkStat and CBRT is expected to announce today 10 AM (GMT+3). Seasonally adjusted Consumer Confidence Index was stood at 84.5 in February, up 1.5% MoM. According to preliminary data released by the Bloomberg HT, CCI declined slightly in the first half of March. The index had declined to 78.1 in April due to uncertainties of the Covid-19.

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