



COUNTRIES IN FOCUS:

Türkiye & Cyprus

TÜRKIYE.....1

President R. T. Erdoğan faces the toughest election in his 20-year rule

Whatever the election outcome might be, the next President would need to restore market confidence through the implementation of a consistent policy mix and structural reforms

CYPRUS2

Benefiting from cyclical tailwinds and rising interest rates, the banking sector returned “into the black” in FY:22, driven by lower provisioning and stronger pre-provision income

Banks’ profitability should come under pressure in FY:23, in view of the challenging economic outlook

APPENDIX:	
DETAILED MACROECONOMIC DATA3
REGIONAL SNAPSHOT: MACROECONOMIC INDICATORS5
FINANCIAL MARKETS6

NBG – Economic Analysis Division

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Emerging Markets Analysis

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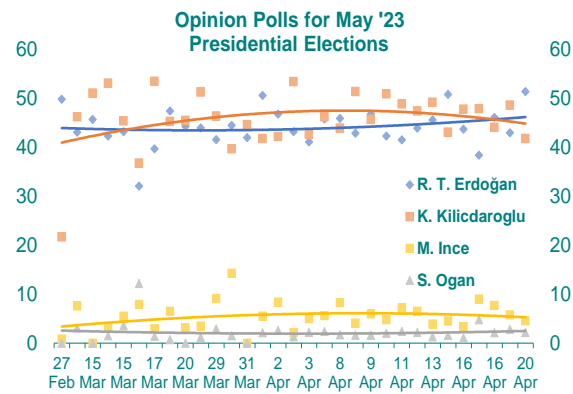
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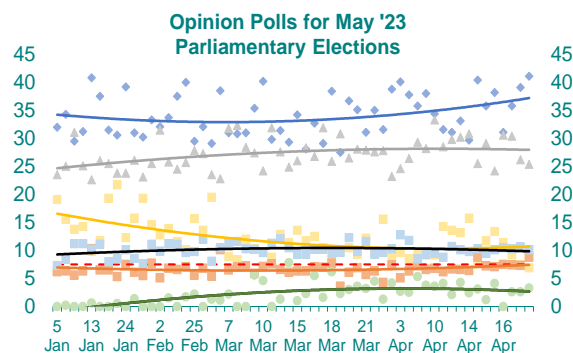
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Türkiye

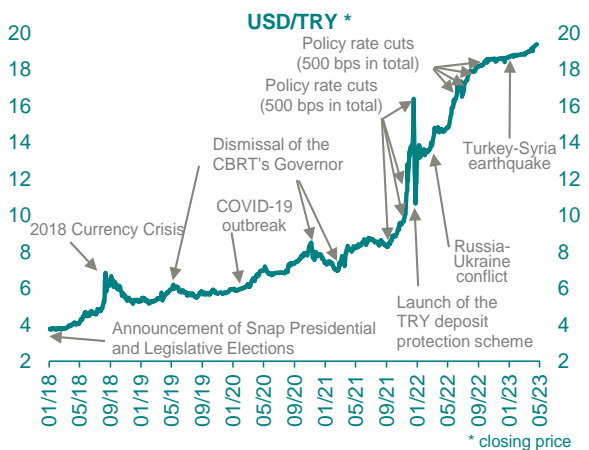
B / B3 / B (S&P/ Moody's / Fitch)



* Dots represent individual polls
** Coloured lines represent the trendline



People's Alliance: AKP, MHP
Nation Alliance: CHP*, IYI
* also Including DEVA, the Felicity Party, the Future Party and the Democrat Party



	24 Apr.	3-M F	6-M F	12-M F
O/N TLREF (%)	9.9	12.0	15.0	18.0
TRY/USD	19.41	20.20	21.00	22.00
Sov. Spread (2025, bps)	311	340	310	260

	24 Apr.	1-W %	YTD %	2-Y %
ISE 100	5,023	-0.7	-8.8	273.4

	2020	2021	2022	2023F	2024F
Real GDP Growth (%)	2.0	11.4	5.6	1.8	4.4
Inflation (eop, %)	14.6	36.1	64.3	38.0	22.0
Cur. Acct. Bal. (% GDP)	-4.4	-0.9	-5.4	-3.7	-3.0
Fiscal Bal. (% GDP)	-3.4	-2.7	-0.9	-5.5	-4.8

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

President R. T. Erdoğan faces the toughest election in his 20-year rule. Latest polls suggest that the May 14 Presidential elections will be a neck-and-neck race between incumbent President Erdoğan, backed by his Islamist-based Justice & Development Party (AKP) and the Nationalist Movement Party (MHP, together forming the People's Alliance), and the candidate of the Nation Alliance, K. Kilicdaroglu, leader of the secularist centrist Republican People's Party (CHP). Note that the Nation Alliance is a diverse coalition of opposition parties, comprising, in addition to the CHP, the centre-right nationalist Good Party (IYI) and four other small parties. In what can be viewed as tacit support to the Nation Alliance, the largest pro-Kurdish party, the left-wing People's Democratic Party (HDP, running under the ticket of the Green Left Party, YSP), which enjoys the support of more than 10.0% of the electorate, has refrained from naming a candidate of its own.

This election marks the first time over the past 20 years that Erdoğan's dominance on the domestic political stage appears to be seriously questioned. In our view, the long-standing cost-of-living crisis, generated, *inter alia*, by a series of unorthodox economic policies adopted over the past 5 years, has been a key factor behind dwindling -- yet still resilient -- support for the incumbent President. Indeed, despite structural external imbalances (largely stemming from Türkiye's complete reliance on imports to cover its energy needs), authorities have been pursuing an ultra-accommodative monetary policy that keeps the economy trapped into a vicious cycle of weakening TRY (down c. 35% against the USD since end-2021 and 80% over the past 5 years) and high inflation (up 71.6% in FY:22 and c. 25.0% in FY:18-22). The impact of the devastating earthquakes that hit Türkiye in early February, killing 48,000 people and leaving millions homeless, and the authorities' poor handling of the crisis cannot but have also taken a toll.

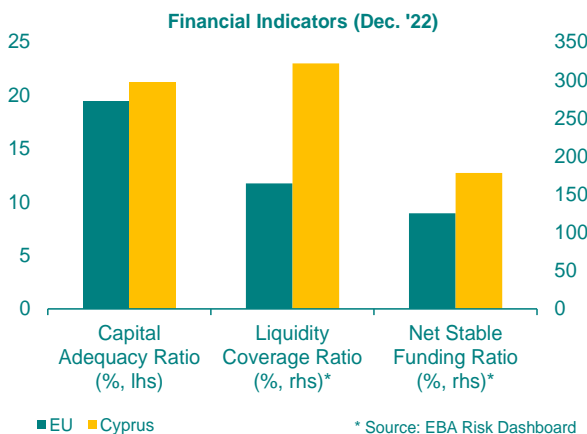
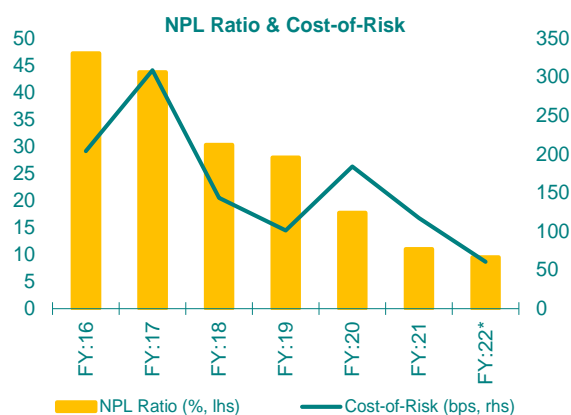
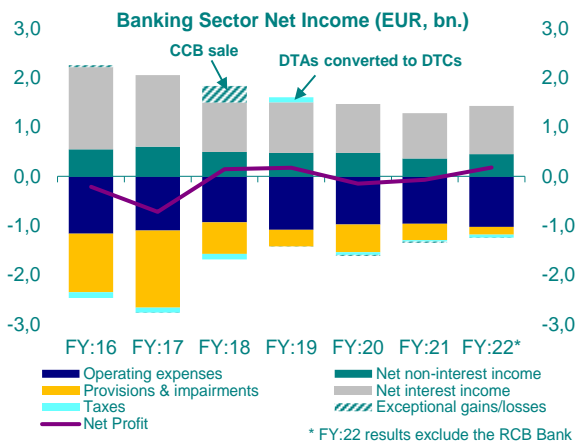
Still, with the gap in popularity between President Erdoğan and Kilicdaroglu being within statistical error, the outcome of the elections is hard to predict, especially in view of Türkiye's complex political landscape, in which religious affiliation and regional origin play influential roles in shaping voter intention. In any case, it is highly likely that a second round will be needed to decide the next President. In the event, the candidate of the alliance that will manage to control the Parliament (with legislative elections due also to be held on May 14, see chart) would be better placed to win a runoff.

Whatever the election outcome might be, the next President would need to restore market confidence through the implementation of a consistent policy mix and structural reforms. Indeed, authorities should seek to synchronize with the global monetary policy cycle, reversing excess liquidity, while securing financial stability. Recall that, in 2018, the key rate was raised by 1600 bps to c. 3.0% in real *ex-post* terms, before the TRY stabilised. For illustrative purposes, note that the real *ex-post* policy rate currently stands at c. -30.0%, the lowest worldwide, with foreign investors having long fled away from Turkish assets (foreign holdings of public debt currently account for 1.0%, down from 25.0% five years ago). Should authorities delay the adjustment, Türkiye risks snowballing into a full-fledged currency crisis and deep recession. Importantly, Türkiye's low debt metrics (with gross public debt standing at c. 32.0% of GDP, well below that of its peers) provide the authorities with ample fiscal space to ensure the orderly unwinding of the sizeable monetary stimulus.

At the same time, authorities would need to proceed with bold structural reforms, mainly aiming at restoring the rule of law. Türkiye's performance in this area has been weak, especially after the 2017 referendum, which enabled the switch to a hyper-centralised Presidential system.

Cyprus

BBB / Ba1 / BBB (S&P/ Moody's / Fitch)



	24 Apr.	3-M F	6-M F	12-M F
1-M EURIBOR (%)	3.0	3.5	3.8	3.5
EUR/USD	1.10	1.11	1.12	1.13
Sov. Spread (2028, bps)	134	135	130	120

	24 Apr.	1-W %	YTD %	2-Y %
CSE 100	108	0.5	20.7	74.6

	2020	2021	2022	2023F	2024F
Real GDP Growth (%)	-4.4	6.6	5.6	2.6	2.9
Inflation (eop, %)	-1.1	4.8	7.9	2.9	2.2
Cur. Acct. Bal. (% GDP)	-10.1	-6.8	-9.4	-8.1	-6.9
Fiscal Bal. (% GDP)	-5.8	-1.7	2.3	0.5	1.0

Sources: Reuters, CYSTAT, CBC, EBA & NBG estimates

Benefiting from cyclical tailwinds and rising interest rates, the banking sector returned “into the black” in FY:22, driven by lower provisioning and stronger pre-provision income. The banking sector posted profits of EUR 251mn in FY:22 (0.9% of GDP) against losses of EUR 30mn in FY:21, with ROAE and ROAA rebounding to (lows of) 4.4% and 0.3%, respectively, in FY:22 from -1.7% and -0.1% in FY:21. Note that, historically, Cypriot banks are placed at the bottom of EU rankings in terms of profitability, reflecting elevated impairment charges and NPL deleveraging.

Despite Cyprus’ strong economic ties with Russia, the fallout from the Russia-Ukraine conflict to domestic banks was limited, reflecting the sector’s small direct exposure to Russia and Ukraine (accounting for c. 1.0% of total loans and less than 5.0% of total deposits at end-2021). Note that RCB -- a subsidiary of Russia’s state bank VTB, accounting for 8.5% of the sector’s assets -- ceased banking operations in March, transferring part of its performing loan portfolio to the Hellenic Bank.

The cost of risk dropped in FY:22, in line with economic recovery.

Against the backdrop of robust GDP growth (up 5.6% in FY:22), banks reduced further impairment charges (down 53%), compressing the cost of risk to 61 bps in FY:22 from 117 bps in FY:21. Note that the NPL ratio moderated further to 9.5% at end-2022 from 11.0% at end-2021, remaining substantially higher than in the EU (1.8%). Adjusted for NPL sales and write-offs, the ratio is estimated to have little changed, however, highlighting the poor quality of remaining NPLs, a legacy from the 2012-13 crisis. The NPL coverage ratio stood at 47.5% at end-2022, broadly in line with the EU average.

Net Interest Income (NII) rebounded in FY:22, on rising interest rates.

After declining for 2 years, NII (accounting for 65% of total net operating income) increased markedly in FY:22 (up 6.5%), as Cypriot banks benefited from the repricing of their large cash balances with the ECB, which have been previously receiving no interest.

Net non-interest income (NNII) also strengthened in FY:22 (up 24.2%), providing a critical contribution to overall profitability, thanks to increased net fees & commission income and reduced FX losses.

At the same time, operating expenses picked-up (up 6.4%), in line with higher inflation. All said, the efficiency of the banking system improved, with cost-to-income ratio moderating to 71.9% in FY:22 from 75.3% in FY:21, remaining, however, significantly higher than the EU average (of c. 60.0%), highlighting the need for further cost optimization.

Banks’ profitability should come under pressure in FY:23, in view of the challenging economic outlook.

Economic growth is set to moderate significantly this year (to 2.6% from 5.6% in FY:22), reflecting the impact of elevated -- yet gradually easing -- inflation and tightening financing conditions. Against this backdrop and given the high private sector’s indebtedness (240% of GDP), we expect credit risk to increase, prompting banks to accelerate provisioning, especially in view of the already high share of stage 2 loans (13.1% of total loans).

Despite weak credit demand, banks should continue to benefit from rising interest rates, in view the fast repricing of loans (note that 95% of debt contracts have variable rate). Note, though, that low other revenue diversification and high operational costs pose a constraint to profitability.

Importantly, Cypriot banks are well positioned to deal with the unfolding pressures on the global banking sector, being highly-liquid (with a liquidity coverage ratio of 322%, see chart), stably funded (with a net stable funding ratio of 178%) and well-capitalised (with a total CAR of 21.4%, c. 85% of which constitutes CET1 capital). The upcoming hike in the countercyclical buffer (to 0.5% from 0%) should further strengthen banks’ resilience yet affect their appetite to provide credit (due to a high implied cost, reflecting the system’s elevated risk weighted assets).

DETAILED MACROECONOMIC DATA

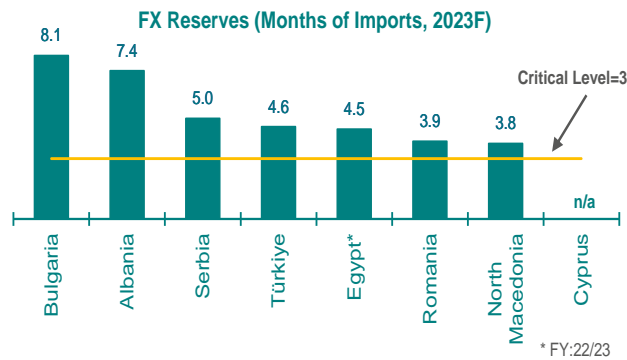
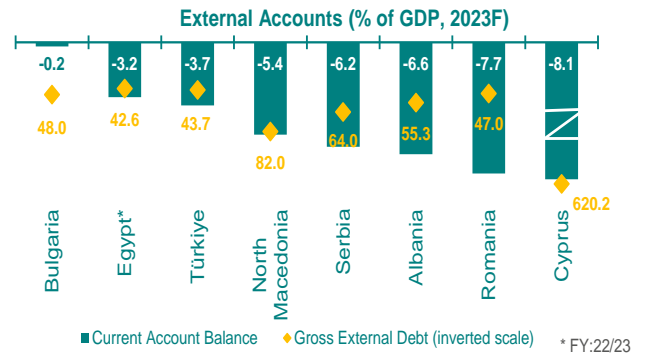
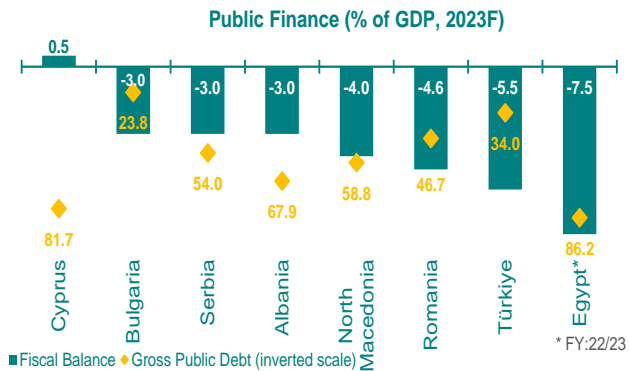
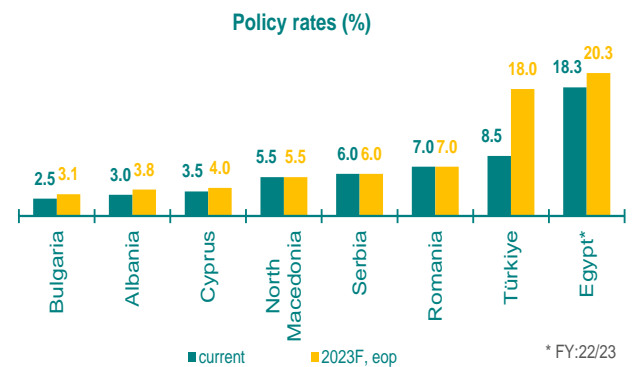
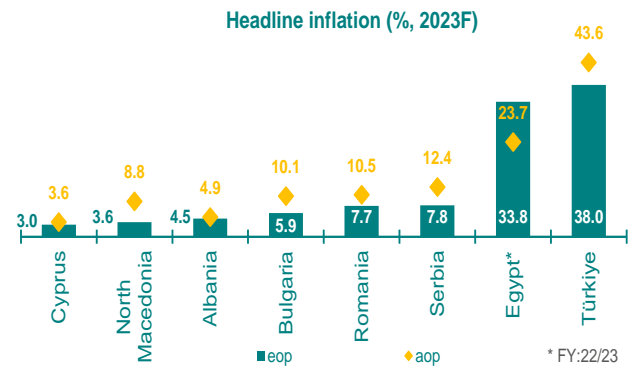
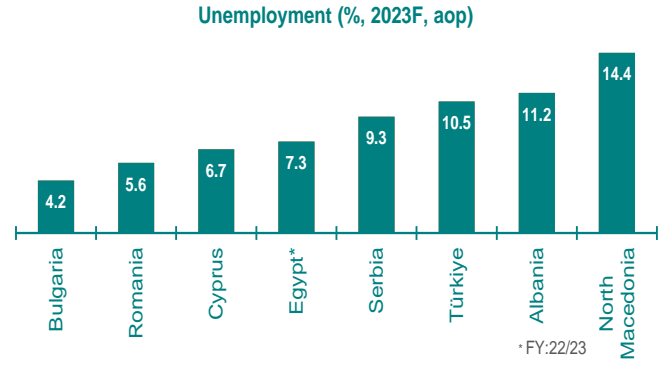
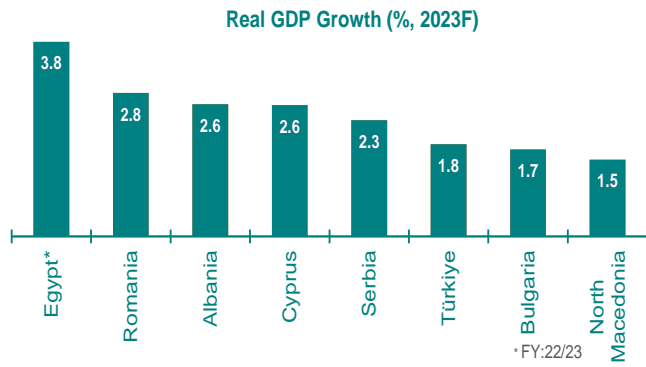
TÜRKİYE					
	2020	2021	2022	2023f	2024f
Real Sector					
Nominal GDP (USD million)	719,168	815,755	905,475	1,091,727	1,299,013
GDP per capita (USD)	8,601	9,633	10,568	12,596	14,821
GDP growth (real, %)	2.0	11.4	5.6	1.8	4.4
Unemployment rate (% aop)	13.2	12.0	10.5	10.5	10.0
Prices and Banking					
Inflation (% eop)	14.6	36.1	64.3	38.0	22.0
Inflation (% aop)	12.3	19.3	71.6	43.6	26.2
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	67.6	50.4		
Retail Loans (% of GDP)	16.8	14.5	11.2		
Corporate Loans (% of GDP)	54.1	53.1	39.2		
Customer Deposits (% of GDP)	62.1	65.5	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	259,824	278,139
Merchandise imports (USD million)	206,252	253,999	343,098	338,979	353,111
Trade balance (USD million)	-37,874	-29,313	-90,682	-79,154	-74,971
Trade balance (% of GDP)	-5.3	-3.6	-10.0	-7.3	-5.8
Current account balance (USD million)	-31,888	-7,232	-48,769	-40,668	-39,536
Current account balance (% of GDP)	-4.4	-0.9	-5.4	-3.7	-3.0
Net FDI (USD million)	4,456	6,874	8,052	8,857	10,186
Net FDI (% of GDP)	0.6	0.8	0.9	0.8	0.8
International reserves (USD million)	93,277	111,181	128,736	130,000	138,000
International reserves (Months ^a)	4.9	4.7	3.3	4.6	4.4
Public Finance					
Primary balance (% of GDP)	-0.8	-0.2	1.1	-2.8	-2.0
Fiscal balance (% of GDP)	-3.4	-2.7	-0.9	-5.5	-4.8
Gross public debt (% of GDP)	39.7	41.8	31.7	34.0	35.5
External Debt					
Gross external debt (USD million)	432,459	442,454	455,000	477,500	502,500
Gross external debt (% of GDP)	60.1	54.2	50.2	43.7	38.7
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	65.4	65.2
External debt service (% of exports)	37.5	27.6	25.4	26.2	25.9
Financial Markets					
Policy rate (Effective funding rate, % eop)	17.0	14.0	9.0	18.0	15.0
Policy rate (Effective funding rate, % aop)	10.5	17.6	12.6	12.1	16.5
10-Y T-bill rate (% eop)	12.5	23.1	9.9	15.5	14.2
Exchange rate: USD (eop)	7.43	13.32	18.69	21.50	23.00
Exchange rate: USD (aop)	7.02	8.89	16.57	20.09	22.25

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

CYPRUS					
	2020	2021	2022	2023f	2024f
Real Sector					
Nominal GDP (EUR million)	21,895	24,019	27,012	28,702	30,305
GDP per capita (EUR)	24.546	26.677	29.675	31.189	32,572
GDP growth (real, %)	-4.4	6.6	5.6	2.6	2.9
Unemployment rate (% aop)	7.6	7.5	6.8	6.7	6.5
Prices and Banking					
Inflation (% eop)	-1.1	4.8	7.9	3.0	2.2
Inflation (% aop)	-0.6	2.4	8.4	3.6	2.6
Loans to the Private Sector (% change, eop)	-5.6	-5.0	-12.1		
Customer Deposits (% change, eop)	-0.6	5.4	2.8		
Loans to the Private Sector (% of GDP)	132.0	114.3	89.3		
Retail Loans (% of GDP)	61.2	50.9	42.6		
Corporate Loans (% of GDP)	70.8	63.4	46.7		
Customer Deposits (% of GDP)	188.0	180.7	165.2		
Loans to Private Sector (% of Deposits)	70.2	63.2	54.0		
Foreign Currency Loans (% of Total Loans)	---	---	---		
External Accounts					
Merchandise exports (EUR million)	2,969	3,590	4,215	4,187	4,194
Merchandise imports (EUR million)	7,180	7,907	10,292	10,403	10,554
Trade balance (EUR million)	-4,211	-4,318	-6,076	-6,216	-6,360
Trade balance (% of GDP)	-19.2	-18.0	-22.5	-21.7	-21.0
Current account balance (EUR million)	-2,202	-1,638	-2,549	-2,319	-2,091
Current account balance (% of GDP)	-10.1	-6.8	-9.4	-8.1	-6.9
Net FDI (EUR million)	7,454	4,369	4,369	5,571	6,963
Net FDI (% of GDP)	34.0	18.2	16.2	19.4	23.0
International reserves (EUR million)	---	---	---	---	---
International reserves (Months ^a)	---	---	---	---	---
Public Finance					
Primary balance ^b (% of GDP)	-3.7	0.1	3.8	2.1	2.6
Fiscal balance ^b (% of GDP)	-5.8	-1.7	2.3	0.5	1.0
Gross public debt (% of GDP)	113.5	101.0	86.5	81.7	77.5
External Debt					
Gross external debt (EUR million)	175,543	168,003	180,003	178,003	176,003
Gross external debt (% of GDP)	801.8	699.5	666.4	620.2	580.8
External debt service (EUR million)	---	---	---	---	---
External debt service (% of reserves)	---	---	---	---	---
External debt service (% of exports)	---	---	---	---	---
Financial Markets					
Policy rate (ECB refinancing rate, % eop)	0.0	0.0	2.5	4.0	3.0
Policy rate (ECB refinancing rate, % aop)	0.0	0.0	0.7	3.7	3.6
3-Y T-bill rate (% eop)	-0.1	-0.2	2.6	3.8	3.6
Exchange rate: USD (eop)	1.221	1.137	1.070	1.120	1.160
Exchange rate: USD (aop)	1.142	1.183	1.053	1.105	1.140

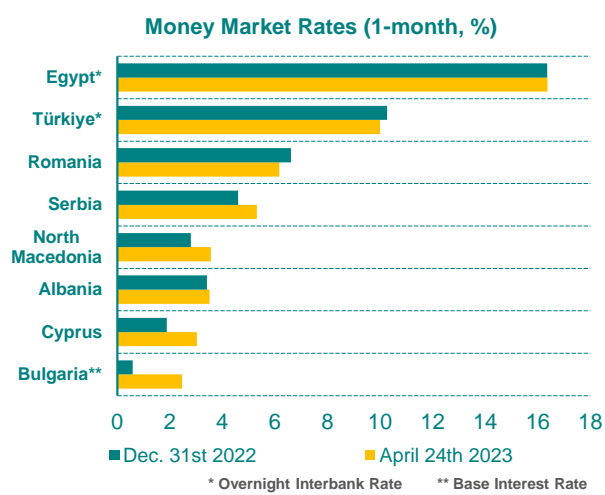
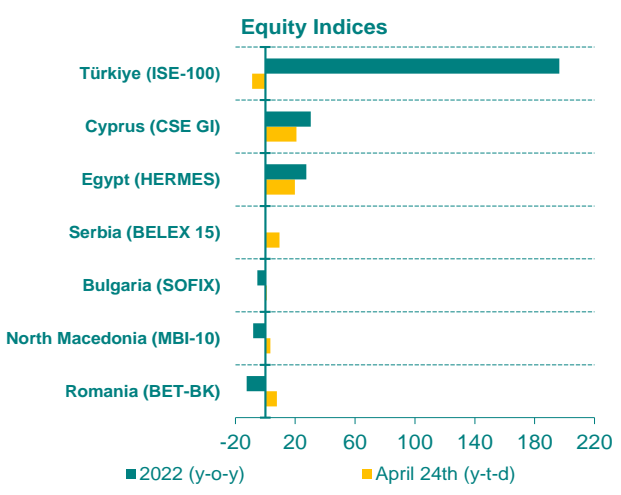
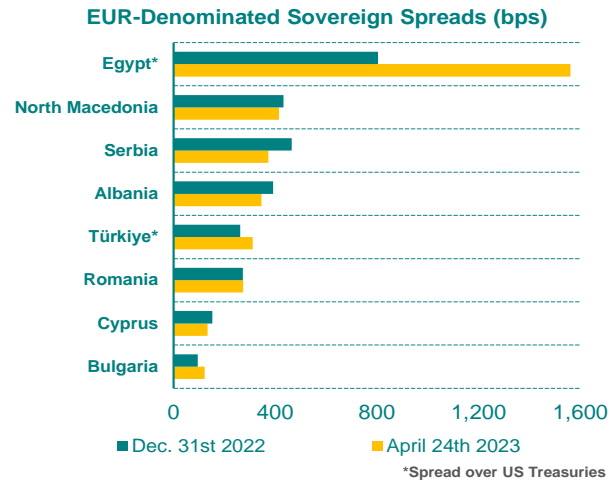
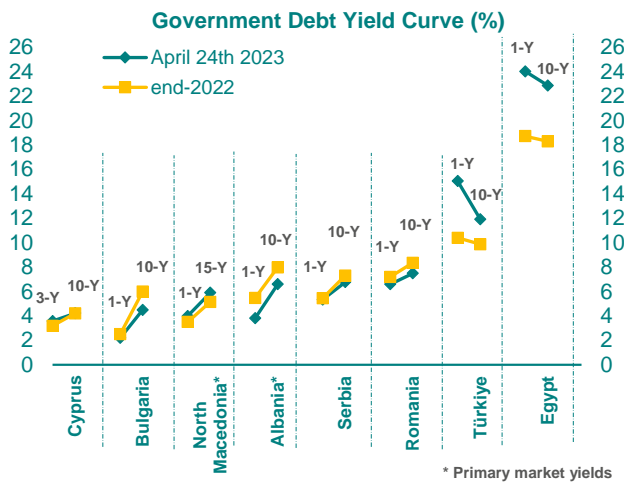
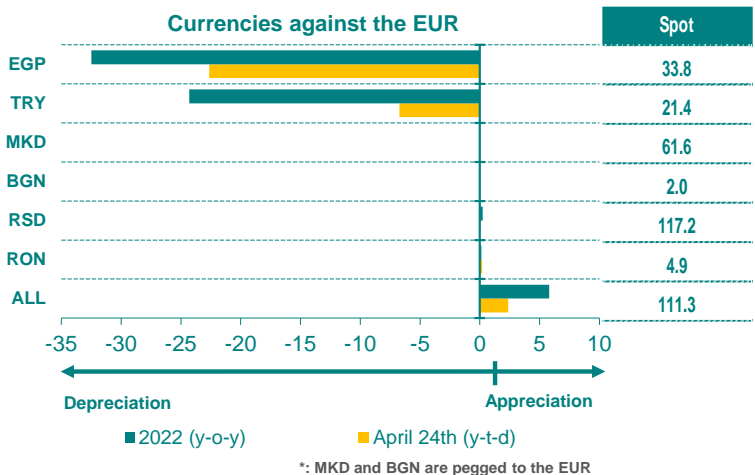
f: NBG forecasts; a: months of imports of GNFS; b: cash basis

REGIONAL SNAPSHOT: MACROECONOMIC INDICATORS



Sources: National Sources & NBG estimates

REGIONAL SNAPSHOT: FINANCIAL MARKETS



Sources: Reuters & NBG estimates

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