

COUNTRIES IN FOCUS:

Türkiye & Cyprus

TÜRKIYE1

Having signaled the end of its aggressive hiking cycle (up 3,650 bps since June), the CBRT maintained rates unchanged at a (2-decade) high of 45.0% at its February meeting, while hanging on to hawkish bias

The first policy rate cut is expected in late-2024, when inflation is projected to return to a sustained downtrend

Against the backdrop of tightened financing conditions, GDP growth is set to moderate to 3.0% in FY:24 on weaker private consumption

CYPRUS2

Following another year of robust performance, tourism activity nearly returned to its pre-pandemic level in FY:23

Nonetheless, subdued economic growth in the EU and a highly uncertain regional geopolitical backdrop are due to weigh on tourist inflows this year

APPENDIX:

DETAILED MACROECONOMIC DATA3

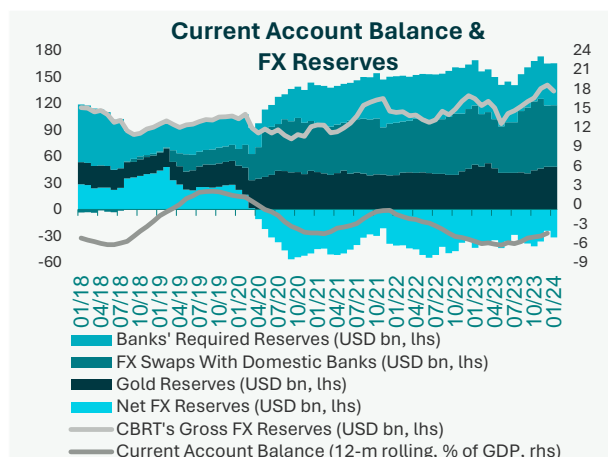
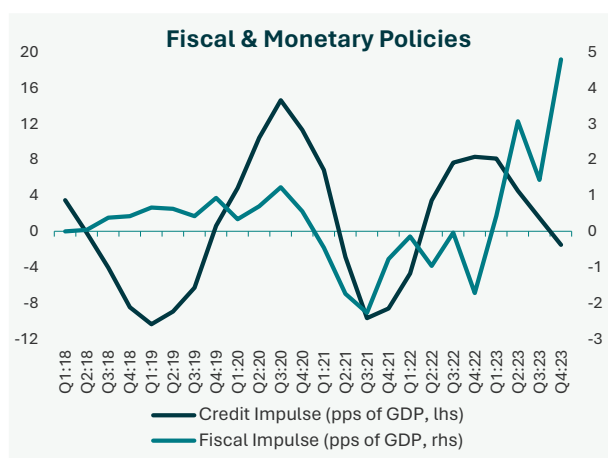
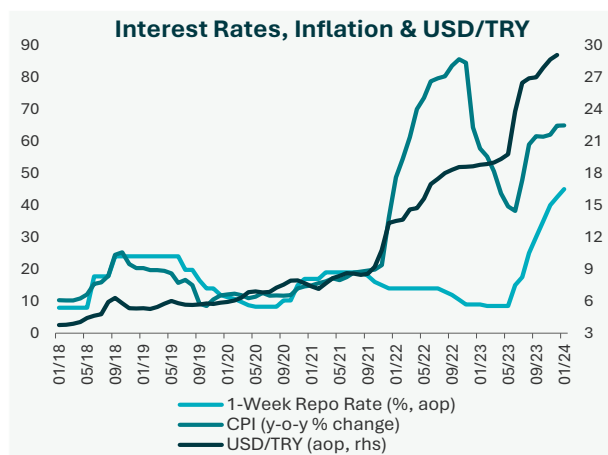
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Türkiye

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



	19 Feb	3-M F	6-M F	12-M F
O/N TLREF (%)	44.9	45.0	45.0	35.0
TRY/USD	30.81	31.65	32.45	33.35
Sov. Spread (2027, bps)	241	245	230	200

	19 Feb	1-W %	YTD %	2-Y %
ISE 100	9,196	0.2	23.1	352.5

	2021	2022	2023E	2024F	2025F
Real GDP Growth (%)	11.4	5.5	4.4	3.0	3.6
Inflation (eop, %)	36.1	64.3	64.2	40.0	22.0
Cur. Acct. Bal. (% GDP)	-0.9	-5.4	-4.5	-3.0	-2.5
Fiscal Bal. (% GDP)	-2.6	-0.9	-5.7	-5.0	-3.6

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

Having signaled the end of its aggressive hiking cycle (up 3,650 bps since June), the CBRT maintained rates unchanged at a (2-decade) high of 45.0% at its February meeting, while hanging on to hawkish bias. The February meeting was the first under the governorship of, F. Karahan, who replaced H. G. Erkan at the helm of the CBRT. Recall that the latter had been appointed by President Erdoğan, following his re-election in May, with the task to reverse past years' unconventional policies, which has thrown Türkiye into a deep currency crisis (see below).

Note that the massive increase in interest rates has been complemented by credit and quantitative tightening measures (including hikes in reserve requirements), 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 CBRT's hawkish turn has been welcomed by investors, with the TRY now facing much weaker depreciation pressures, reflecting still significant -- yet narrowing -- external imbalances. Indeed, the TRY has lost less than 15.0% of its value against the USD since mid-2023, following losses of c. 30.0% in H1:23 and 80.0% in FY:18-22.

Considering the still negative real policy rate (c. -12.0% in ex-post terms) and the size of monetary stimulus injected into the economy (with FX-adjusted credit impulse having just turned negative, see chart), authorities have a long way to go before Türkiye's imbalances get unwind, given, *inter alia*, the loose fiscal policy (mostly driven by post-earthquake reconstruction activity) and elevated economic sentiment. 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 pursued over the past years had trapped the economy into a vicious cycle of weakening TRY and high inflation (up 53.1% in FY:23 following 71.6% in FY:22 and c. 25.0% in FY:18-22), which was, however, had been accompanied by strong GDP growth (up 4.5% in FY:18-23).

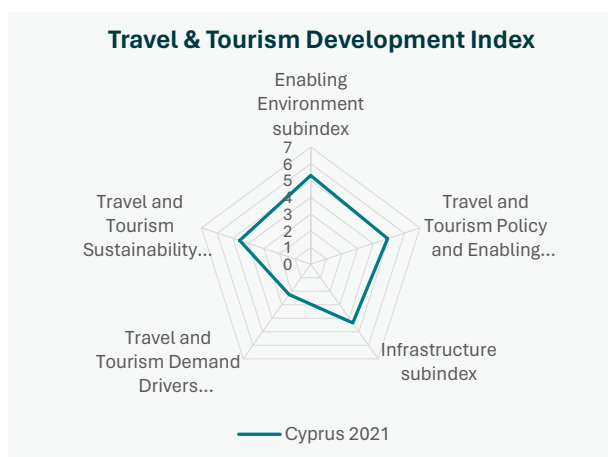
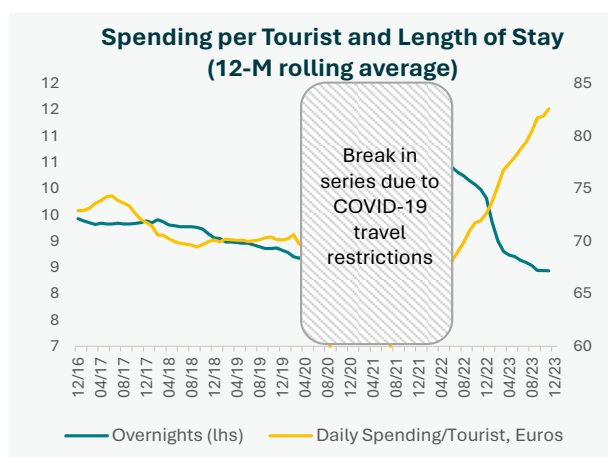
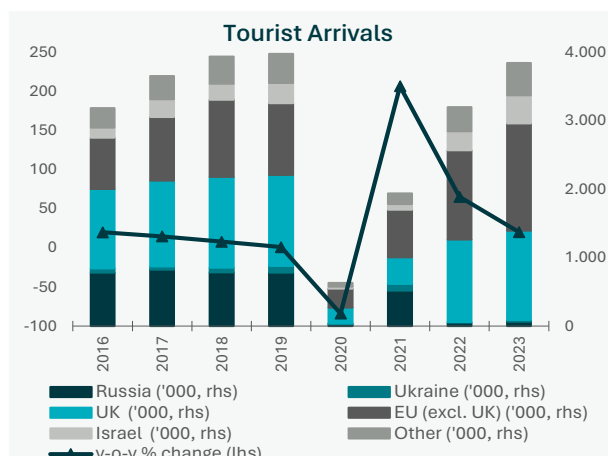
Worryingly, the CBRT is short of ammunition to defend the ailing TRY during the adjustment period, as -- despite recent trends -- its net FX reserves remain negative. This means that authorities would continue relying on non-market financing flows from Türkiye's partners to close the external financing gap, at least in the short-term, with FX volatility remaining elevated, at the same time.

Assuming no inflation surprise (with related risks being skewed to the upside, however, reflecting, *inter alia*, repercussions from geopolitical tensions, deferred hikes in administered prices as well as the continuing easing in incomes policy), the CBRT is expected to remain on hold until late-2024, when inflation is projected to embark on a sustained downward trend. Given President Erdoğan's track record of populist policy shifts, the uncertainty surrounding our forecast is large, especially until the March '24 local elections.

Against this backdrop, we expect GDP growth to slow further down in the period ahead on weaker private consumption. Barring post-earthquake reconstruction activity, gross fixed capital formation is also set to lose momentum, due to tightening financing conditions and the impact of the weak TRY on corporates' balance sheets. On the other hand, with domestic and external demand gradually decoupling, net exports should start adding to growth, reflecting, *inter alia*, gains in price competitiveness. All said, we see GDP growth easing to 3.0% in FY:24 from 4.4% in FY:23, but with a more balanced structure. Note that the high indebtedness of the private sector (amounting to c. 185% of GDP, over 40% of which is FX-denominated) poses a threat to macro-financial stability.

Cyprus

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



	19 Feb	3-M F	6-M F	12-M F
1-M EURIBOR (%)	3.9	3.9	3.6	2.9
EUR/USD	1.08	1.08	1.09	1.10
Sov. Spread (2028, bps)	76	85	83	80

	19 Feb	1-W %	YTD %	2-Y %
CSE 100	142	1.0	4.5	100.1

	2021	2022	2023E	2024F	2025F
Real GDP Growth (%)	9.9	5.1	2.5	2.7	3.0
Inflation (eop, %)	4.8	7.9	1.6	2.8	2.0
Cur. Acct. Bal. (% GDP)	-6.1	-7.9	-9.0	-8.5	-7.7
Fiscal Bal. (% GDP)	-1.9	2.4	2.2	2.2	2.0

Sources: Reuters, CYSTAT, CBC, & NBS estimates

Following another year of robust performance, tourism activity nearly returned to its pre-pandemic level in FY:23. Despite economic headwinds from elevated inflation and high interest rates, tourist arrivals to Cyprus increased at a robust pace of 20.1% in FY:23, to over 3.8mn, only slightly behind the record-high levels seen in 2019, thanks to still strong global pent-up household demand for tourism services.

As compared to pre-pandemic levels, the Cypriot tourism sector seems to be slightly underperforming other tourism-reliant euro area economies, such as Greece, Portugal, Spain & Italy. Still, Cyprus' performance is outstanding, considering that the island has lost its 2nd most important source market, namely Russia (accounting for a whopping 27.0% of total arrivals in FY:21), following an EU ban on Russian flights, imposed in the aftermath of the Russia-Ukraine conflict. The loss of the Russian market has been broadly offset by increased arrivals from the EU (especially Poland and Romania) and Israel (prior to the eruption of the Gaza crisis), with the UK remaining the primary source market (accounting for 34.0% of total arrivals).

Reflecting underlying pressures on households' disposable income and weak sentiment, tourists spent less days on the island (with the average number of overnight stays dropping by 1½ to c. 8½ on average in FY:23). Unsurprisingly, spending per tourist per stay rose by c. 12.0%, at the same time, in line with elevated inflation. As a result, tourism receipts increased broadly at the same pace with tourist arrivals, providing a critical contribution to GDP growth.

According to the World Travel & Tourism Council's estimates, Cyprus' tourism sector & related activities accounted for more than 12.0% of FY:22 GDP, while employing a similar share of workers. Note that staff shortages in the sector are acute and are currently being addressed by (mostly Ukrainian) refugees and temporary non-EU workers.

Subdued economic growth in the EU and a highly uncertain regional geopolitical backdrop are due to weigh on tourist inflows this year.

Growth in Cyprus' tourism sector should be affected this year by sluggish economic expansion in the EU (where GDP is projected to rise by 0.9% following an increase of 0.5% in FY:23) and tourists' concomitant turn to more affordable holiday destinations, on the one hand, and reduced tourist flows from Israel (Cyprus' 2nd largest source country in FY:23, accounting for c. 11.0% of total arrivals), due to ongoing tensions in Gaza, on the other hand. Indeed, cancellations of bookings from Israel are being recorded since end-2023. As a result and given authorities' active efforts to diversify further source markets, tourist arrivals to Cyprus should struggle to reach the previous year's level.

Note that Cyprus' almost complete reliance on air connectivity renders its tourism sector quite vulnerable to global energy price increases. Climate change would also pose a challenge in the years to come. On a positive note, the continuing upgrade of the island's tourism infrastructure profile through large projects (including marinas, golf courses and the largest casino in EU, the construction of which was completed in mid-2023) should help increase its attractiveness for tourists.

According to the World Economic Forum's Travel & Tourism Development Index (2022), which assess "the factors and policies that enable the sustainable and resilient development of the industry", Cyprus ranks in the 30th position among 86 high-income countries (31st overall). Increased international openness and ICT readiness as well as the high priority the sector receives (in terms of funds allocated) both from policymakers and investors are Cyprus' strongest points, which are counterbalanced, however, by weak price competitiveness and the island's poor ground infrastructure and relative lack of natural and cultural resources.

DETAILED MACROECONOMIC DATA

TÜRKİYE					
	2021	2022	2023e	2024f	2025f
Real Sector					
Nominal GDP (USD million)	816,582	905,789	1,009,042	1,233,399	1,486,297
GDP per capita (USD)	9,643	10,621	11,697	14,138	16,853
GDP growth (real, %)	11.4	5.5	4.4	3.0	3.6
Unemployment rate (% aop)	12.0	10.5	10.0	10.3	10.0
Prices and Banking					
Inflation (% eop)	36.1	64.3	64.2	40.0	22.0
Inflation (% aop)	19.3	71.6	53.1	55.9	26.6
Loans to the Private Sector (% change, eop)	37.0	54.5	53.7		
Customer Deposits (% change, eop)	51.5	68.0	67.1		
Loans to the Private Sector (% of GDP)	67.5	50.4	48.5		
Retail Loans (% of GDP)	14.4	11.2	12.4		
Corporate Loans (% of GDP)	53.1	39.2	36.1		
Customer Deposits (% of GDP)	65.4	53.1	55.5		
Loans to Private Sector (% of Cust. Deposits)	103.2	94.9	87.3		
Foreign Currency Loans (% of Total Loans)	42.2	32.6	32.5		
External Accounts					
Merchandise exports (USD million)	224,673	253,352	251,166	269,979	290,029
Merchandise imports (USD million)	253,994	342,952	337,725	353,898	375,122
Trade balance (USD million)	-29,321	-89,600	-86,559	-83,918	85,093
Trade balance (% of GDP)	-3.6	-9.9	-8.6	-6.8	-5.7
Current account balance (USD million)	-7,398	-49,085	-45,150	-37,190	-37,607
Current account balance (% of GDP)	-0.9	-5.4	-4.5	-3.0	-2.5
Net FDI (USD million)	6,444	8,731	4,678	2,105	3,158
Net FDI (% of GDP)	0.8	1.0	0.5	0.2	0.2
International reserves (USD million)	111,181	128,736	140,884	150,000	165,000
International reserves (Months ^a)	4.7	3.3	5.0	4.8	4.9
Public Finance					
Primary balance (% of GDP)	-0.2	1.1	-2.9	-2.0	-0.7
Fiscal balance (% of GDP)	-2.6	-0.9	-5.7	-5.0	-3.6
Gross public debt (% of GDP)	40.4	30.8	33.0	34.0	34.0
External Debt					
Gross external debt (USD million)	437,557	459,261	488,000	508,000	528,000
Gross external debt (% of GDP)	53.6	50.7	48.4	41.2	35.5
External debt service (USD million)	74,954	67,079	75,000	80,000	85,000
External debt service (% of reserves)	67.4	52.1	53.2	53.3	51.5
External debt service (% of exports)	27.8	21.2	23.9	23.7	23.4
Financial Markets					
Policy rate (Effective funding rate, % eop)	14.0	9.0	42.5	40.0	24.0
Policy rate (Effective funding rate, % aop)	17.6	12.6	20.7	44.4	28.5
10-Y T-bond rate (% eop)	23.1	9.9	23.7	23.5	21.0
Exchange rate: USD (eop)	13.32	18.69	29.48	33.00	35.00
Exchange rate: USD (aop)	8.89	16.57	23.78	31.24	34.00

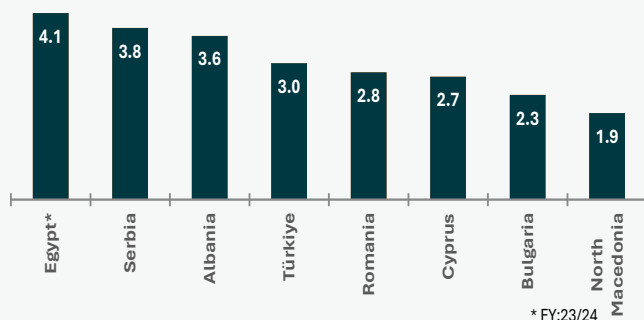
f: NBG forecasts; a: months of imports of GNFS

CYPRUS					
	2021	2022	2023e	2024f	2025f
Real Sector					
Nominal GDP (EUR million)	24,928	27,777	29,488	30,736	32,413
GDP per capita (EUR)	27.687	30.516	32.043	33,090	34,527
GDP growth (real, %)	9.9	5.1	2.5	2.7	3.0
Unemployment rate (% aop)	7.5	6.8	6.2	6.0	5.8
Prices and Banking					
Inflation (% eop)	4.8	7.9	1.6	2.8	2.0
Inflation (% aop)	2.4	8.4	3.6	1.6	2.3
Loans to the Private Sector (% change, eop)	-5.0	-12.1	-5.0		
Customer Deposits (% change, eop)	5.4	2.9	-0.6		
Loans to the Private Sector (% of GDP)	110.1	86.8	77.7		
Retail Loans (% of GDP)	49.0	41.3	37.9		
Corporate Loans (% of GDP)	61.1	45.5	39.8		
Customer Deposits (% of GDP)	174.1	160.7	150.6		
Loans to Private Sector (% of Deposits)	63.2	54.0	51.6		
Foreign Currency Loans (% of Total Loans)	---	---	---		
External Accounts					
Merchandise exports (EUR million)	3,693	4,581	4,604	4,742	4,895
Merchandise imports (EUR million)	8,092	10,555	11,447	11,870	12,441
Trade balance (EUR million)	-4,398	-5,973	-6,843	-7,128	-7,546
Trade balance (% of GDP)	-17.6	-21.5	-23.2	-23.2	-23.3
Current account balance (EUR million)	-1,514	-2,203	-2,658	-2,601	-2,503
Current account balance (% of GDP)	-6.1	-7.9	-9.0	-8.5	-7.7
Net FDI (EUR million)	7,748	8,446	6,334	8,235	9,882
Net FDI (% of GDP)	31.1	30.4	21.5	26.8	30.5
International reserves (EUR million)	---	---	---	---	---
International reserves (Months ^a)	---	---	---	---	---
Public Finance					
Primary balance ^b (% of GDP)	-0.1	3.9	3.6	3.5	3.4
Fiscal balance ^b (% of GDP)	-1.9	2.4	2.2	2.2	2.0
Gross public debt (% of GDP)	99.3	85.6	81.5	75.2	69.5
External Debt					
Gross external debt (EUR million)	172,529	169,326	168,326	166,826	165,326
Gross external debt (% of GDP)	692.1	609.6	570.8	542.4	510.1
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	2.5	4.5	3.5	3.0
Policy rate (ECB refinancing rate, % aop)	0.0	0.7	3.8	4.1	3.3
10-Y T-bond rate (% eop)	0.7	4.2	3.2	3.5	3.5
Exchange rate: USD (eop)	1.137	1.070	1.104	1.100	1.130
Exchange rate: USD (aop)	1.183	1.053	1.081	1.090	1.115

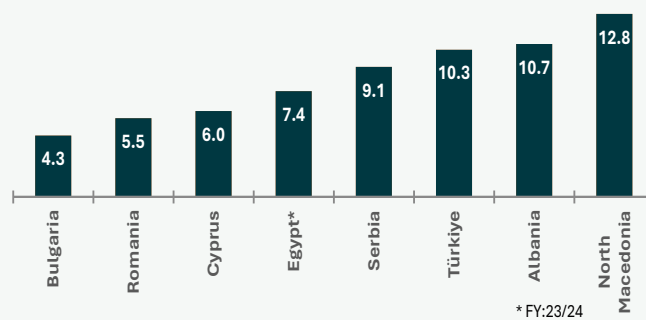
f: NBG forecasts; a: months of imports of GNFS; b: cash basis

REGIONAL SNAPSHOT: MACROECONOMIC INDICATORS

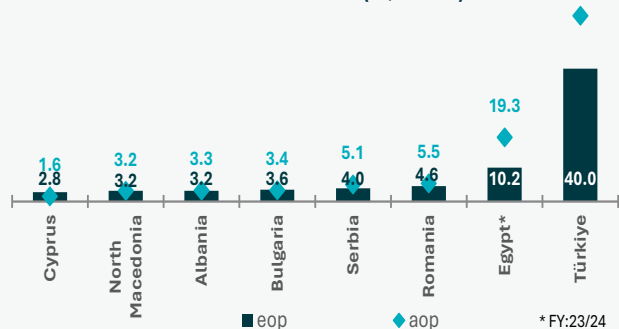
Real GDP Growth (% , 2024F)



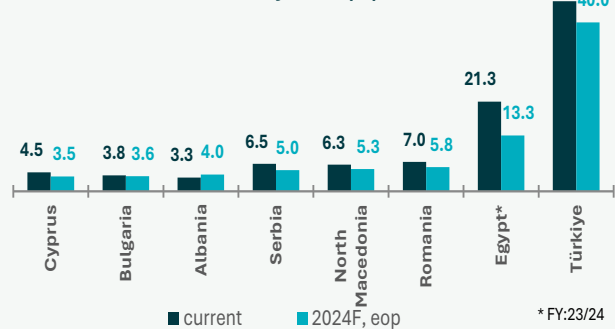
Unemployment (% , 2024F, aop)



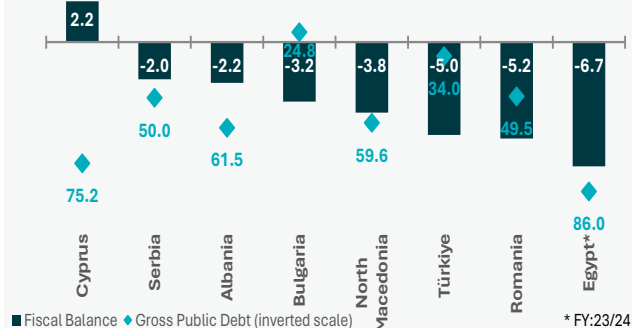
Headline inflation (% , 2024F)



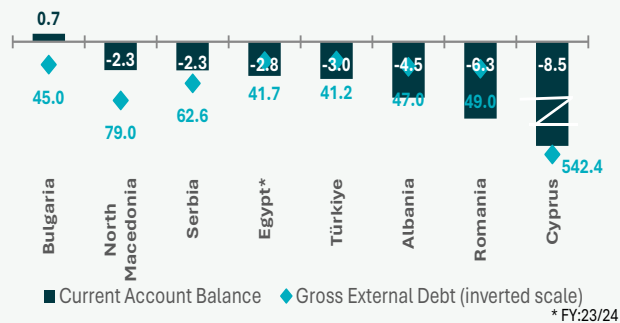
Policy rates (%)



Public Finance (% of GDP, 2024F)



External Accounts (% of GDP, 2024F)

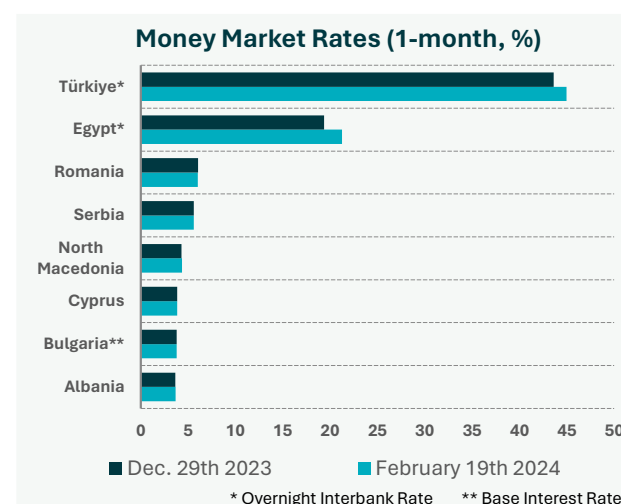
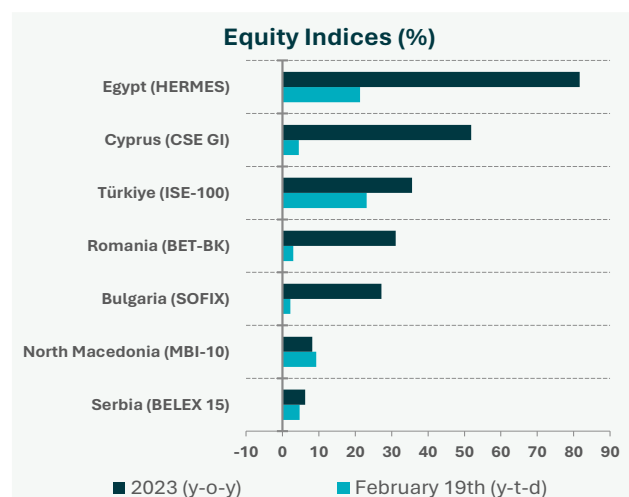
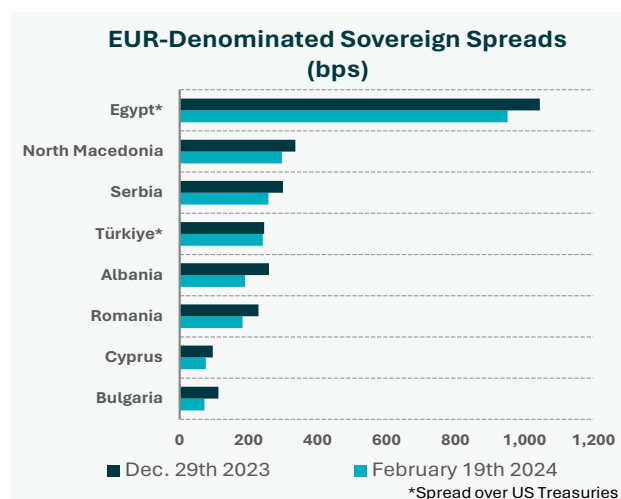
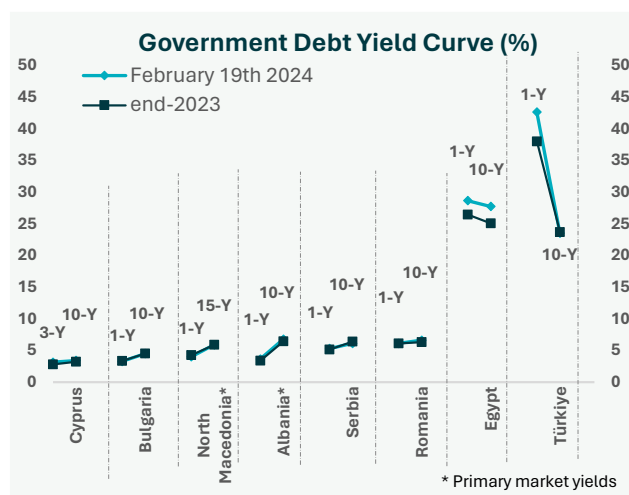
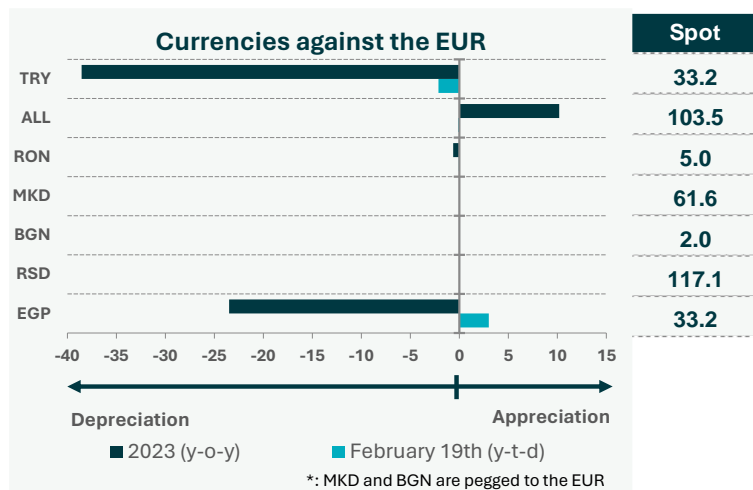


FX Reserves (Months of Imports, 2024F)



Sources: National Sources & NBG estimates

REGIONAL SNAPSHOT: FINANCIAL MARKETS



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