Economic Analysis Division

Emerging Markets Analysis

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Emerging Markets Analysis

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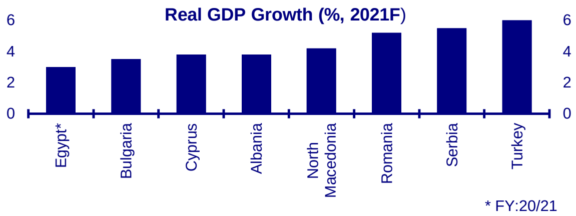
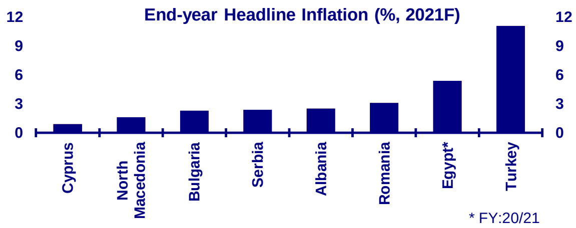
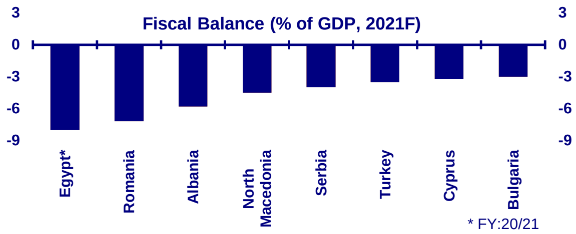
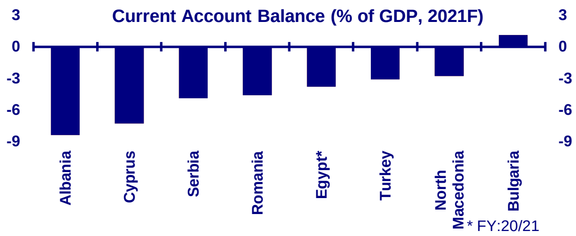
Bi-Weekly Report

23 February - 8 March 2021









Sources: National authorities & NBG estimates

Against the backdrop of a second COVID-19 wave and tighter monetary policy conditions, economic activity lost some steam in Q4:20, yet remained robust (GDP, up 5.9% y-o-y)

Despite the tight monetary policy stance, the Turkish economy is set to post another robust growth rate in FY:21, mainly due to a strong carry-over effect and positive COVID-19-related base effects

GDP contraction was contained to just 1.1% y-o-y in Q4:20 (up 2.2% q-o-q s.a.), thanks to Government support measures and public sector activity

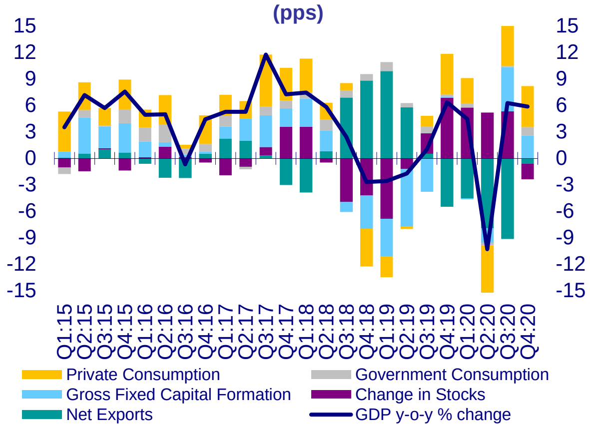
Despite a partial reversal in fiscal policy, GDP is set to rebound strongly in FY:21, more than recouping its COVID-19-induced losses

Please see disclosures on page 5

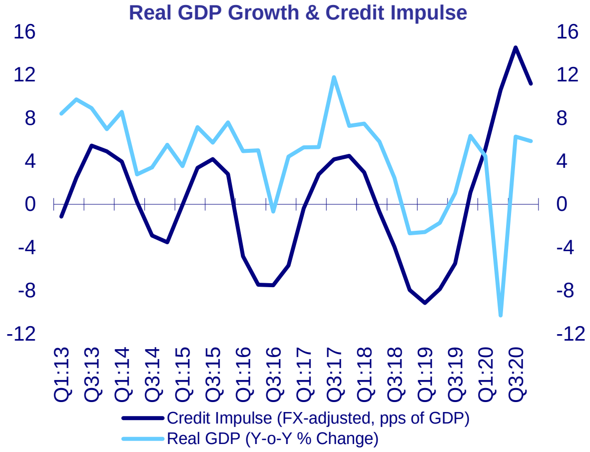
Turkey

B+ / B2 / BB- (S&P/ Moody's / Fitch)

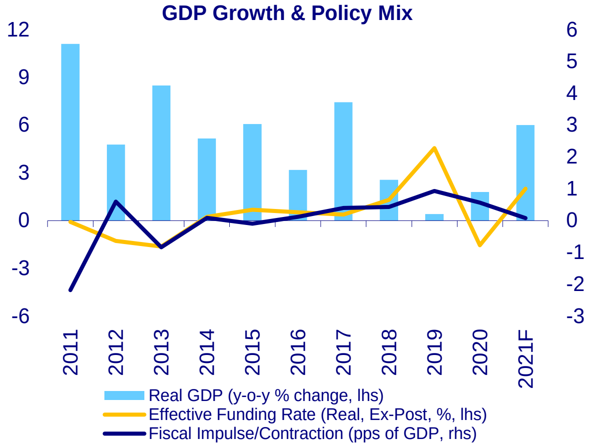
Contributions to Annual Real GDP Growth (pps)



Real GDP Growth & Credit Impulse



GDP Growth & Policy Mix



	8 Mar.	3-M F	6-M F	12-M F
1-m TRIBOR (%)	18.0	18.0	15.0	12.5
TRY/EUR	9.21	9.20	9.30	9.45
Sov. Spread (2025, bps)	440	415	380	320

	8 Mar.	1-W %	YTD %	2-Y %
ISE 100	1,530	0.2	3.6	50.7

	2018	2019	2020	2021F	2022F
Real GDP Growth (%)	2.8	0.9	0.7	6.0	3.6
Inflation (eop, %)	20.3	11.8	14.6	11.2	9.9
Cur. Acct. Bal. (% GDP)	-2.8	0.9	-5.1	-3.2	-2.7
Fiscal Bal. (% GDP)	-1.9	-2.9	-3.4	-3.5	-2.8

Sources: Reuters, Turkstat, CBRT, Ministry of Finance & NBG estimates

Against the backdrop of a second COVID-19 wave and tighter monetary policy conditions, economic activity lost some steam in Q4:20, yet remained robust (GDP, up 5.9% y-o-y). In light of strong depreciation pressures on the TRY (down 30% against the USD in 11M:20, following losses of 36% in 2018-19), the CBRT was forced to tighten its stance aggressively in Q4:20 (including a 675 bp policy rate hike to 17.0%, among the highest worldwide), eventually putting a break on previously skyrocketing credit expansion (see chart).

In this environment, private consumption remained a major growth driver, reflecting the still large credit impulse, with its contribution easing slightly, however (to 4.6 pps in Q4:20 from 5.0 pps in Q3:20), following the reinstatement of some mild social-distancing measures. At the same time, fixed investment expanded for a 2nd consecutive quarter in Q4:20 (contributing 2.6 pps to overall growth), albeit at a slower pace compared with Q3:20 (when it added 5.0 pps). This slowdown was more than offset by a lower drag from net exports (0.6 pps against a sizeable 9.1 pps in Q3:20), in line with the sharp drop in imports. The latter was attributed, *inter alia*, to the drawdown in stocks (subtracting 1.8 pps from overall growth in Q4:20) after 5 quarters of rebuilding. As a result, GDP growth eased to a still solid 5.9% y-o-y (up 1.7% q-o-q s.a.) in Q4:20 from 6.3% y-o-y (up 15.9% q-o-q s.a.) in Q3:20, when the economy re-opened from the first lockdown. All said, thanks to its ultra-accommodative monetary policy, Turkey escaped recession in FY:20, posting an eye-catching growth rate of 1.8%, which compares favourably with all its G20 peers, except China.

Despite the tight monetary policy stance, the Turkish economy is set to post another robust growth rate in FY:21, mainly due to a strong carry-over effect and positive COVID-19-related base effects. Tighter financing conditions are due to take a toll on domestic demand this year. On the flip side, however, this tightening should help restore investor confidence, which hαs been shaken by the implementation of inconsistent policies, helping to stabilize the TRY. Note, though, that, following the recent aggressive policy rate hikes policy, the TRY has recovered from its all-time lows in November, recording gains of c. 14% since then.

Regarding growth drivers, private consumption is set to remain robust this year, especially in H1, but mostly due to COVID-19-related-base effects. Although the lay-off ban (effective until March 2021) should limit employment losses in the short-term, we highlight that the structurally weak labour market (with unemployment stuck at over 12.5% since end-2018) could hinder economic growth in the longer-term. At the same time, fixed investment should continue to expand, albeit modestly, as corporate balance sheets remain under stress, due, *inter alia*, to the impact of the weak TRY (note that the non-financial sector's open FX position stands at a high of 30% of GDP).

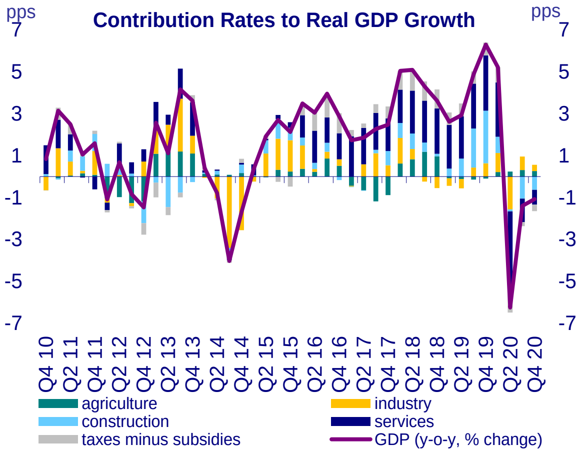
With domestic demand expanding at a more measured pace, net exports should sustain growth in FY:21, reflecting: i) stronger external demand, especially in H2, on the back of global economic recovery; and ii) competitiveness gains. However, the large share of tourism, automotive and transportation industries in Turkey's exports means the latter are not expected to revert to their pre-COVID-19 crisis levels before 2022.

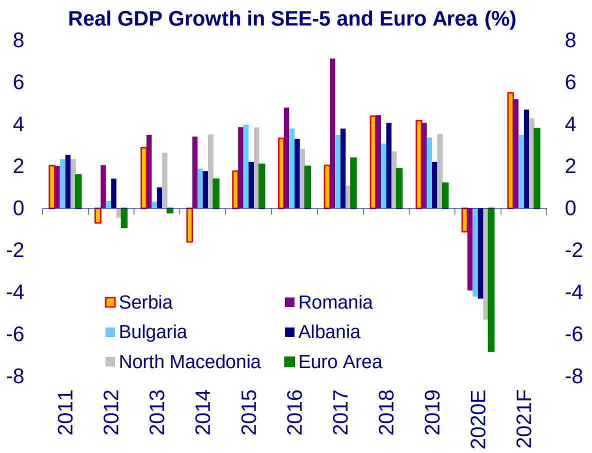
Note that fiscal policy is unlikely to help this year, with the budget deficit projected to remain broadly unchanged compared with the previous year (at a modest 3.5% of GDP).

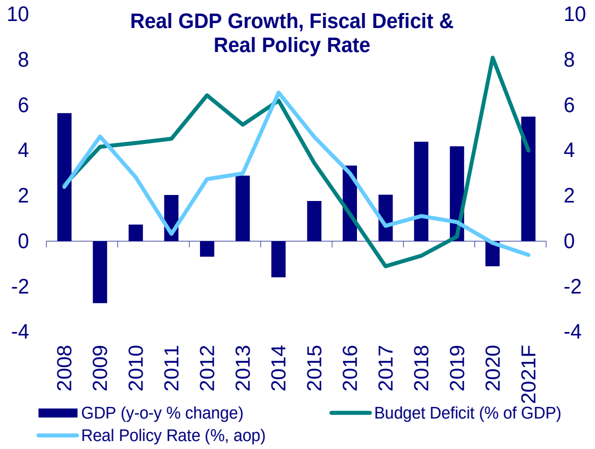
All said, in view of the sizeable carry-over from Q4:20 (c. 5.5 pps), we see GDP growth rebounding to 6.0% in FY:21. The uncertainty over the evolution of the pandemic, together with elevated geopolitical tensions (incl. potential additional EU/US sanctions) and structural vulnerabilities (as highlighted above), pose downside risks to this outlook.

Serbia

BB+ / Ba3 / BB+ (S&P / Moody's / Fitch)







	8 Mar.	3-M F	6-M F	12-M F
1-m BELIBOR (%)	0.6	0.6	0.6	0.6
RSD/EUR	117.6	117.5	117.5	117.5
Sov. Spread (2029, bps)	195	185	170	150

	8 Mar.	1-W %	YTD %	2-Y %
BELEX-15	748	0.5	0.0	7.7

	2018	2019F	2020	2021F	2022F
Real GDP Growth (%)	4.5	4.2	-1.1	5.5	4.5
Inflation (eop, %)	2.0	1.9	1.3	2.4	2.6
Cur. Acct. Bal. (% GDP)	-4.8	-6.9	-4.3	-4.9	-5.0
Fiscal Bal. (% GDP)	0.6	-0.2	-8.1	-4.0	-2.5

Sources: Reuters, NBS, OPBC, Ministry of Finance & NBG estimates

GDP contraction was contained to just 1.1% y-o-y in Q4:20 (up 2.2% q-o-q s.a.), thanks to Government support measures and public sector activity. In light of a resurgence in COVID-19 infections, domestic authorities were prompted to reinstate some (mild) social distancing measures at end-Q4:20. In this context, the services sector continued to contract in Q4:20 (shaving 0.7 pps off overall growth), but at a somewhat slower pace compared with Q3:20, due to an increased contribution from the public sector (most probably the healthcare system). Similarly, the construction sector remained a drag on overall growth in Q4:20 (subtracting 0.6 pps of GDP), albeit smaller compared with Q3:20, following a boost in public investment. Importantly, the better targeting of containment measures, both domestically and internationally, during the second COVID-19 wave prevented large-scale supply-side disruptions in the industrial sector (with its contribution to overall growth coming at 0.3 pps, a tad lower than in Q3:20).

All said, GDP dropped just 1.1% y-o-y in Q4:20, following a decline of 1.4% in Q3:20, bringing FY:20 contraction to a "shallow" 1.1%, which marks one of the best performances in Europe. This outperformance was mainly attributed to: i) the sizeable state support (including a fiscal stimulus of 7.9 pps of GDP and the provision of loan guarantees worth 1.4% of GDP); and ii) the diversified structure of the economy (with modest reliance on high-contact intensive sectors).

Despite a partial reversal in fiscal policy, GDP is set to rebound strongly in FY:21, more than recouping its COVID-19-induced losses. Our baseline scenario assumes that some sort of social distancing measures will remain in place over the next few months, pointing to a slow and uneven recovery during that period. Importantly, however, the fast COVID-19 vaccine rollout (comparing favourably with that of the EU) bodes well for sentiment and should help normalize social and economic activity by mid-year. In the event, we expect the services sector to emerge as the main driver of the economic recovery. Stronger demand-side pressures, on the back, *inter alia*, of a loose incomes policy (including hikes of 4.6% and 6.6% in public sector wages and the minimum wage, respectively, as well as a 5.9% rise in pensions) and robust credit expansion (see below), should help to this end. At the same time, the construction sector is set to overperform, driven by higher public investment (according to the FY:21 budget, up 12.5% to 5.7% of GDP). The industrial sector should also sustain growth this year, especially in H2, in line with stronger external demand from the EU, Serbia's main trade partner.

Following a sizeable fiscal impulse in the previous year, which pushed up public debt close to the EU threshold 60% of GDP, the budget deficit is set to narrow markedly this year (implying a fiscal contraction of 4.1 pps of GDP or c. 3.0 pps in cyclically-adjusted terms), reflecting the phasing-out of the emergency support schemes implemented in FY:20 and the economic recovery.

On the monetary policy front, however, conditions should remain accommodative throughout the year. Recall that the NBS has cut its key rate by 125 bps since March 2020 to a low of 1.0% (or -0.5% in *ex-post* real terms), increasing, at the same time, the amount of liquidity provided to banks. Considering the benign inflation outlook and the fact that Serbia's real policy rate is broadly in line with that of its peers, we believe that the NBS has limited room for further rate cuts. Instead, we expect the central bank to focus on stimulating further credit activity (already up 12.2% y-o-y at end-2020 against 8.9% at end-2019).

All said, we see GDP growth rebounding to 5.0% in FY:21, making Serbia one of the few countries worldwide to witness a full recovery to pre-pandemic levels before the end of the year.

TURKEY	2018	2019	2020e	2021f	2022f
Real Sector					
Nominal GDP (USD million)	777,122	761,093	719,124	803,742	870,053
GDP per capita (EUR)	8,056	8,175	7,459	7,798	8,274
GDP growth (real, %)	2.8	0.9	1.8	6.0	3.6
Unemployment rate (%, aop)	11.0	13.7	13.2	13.0	12.2
Prices and Banking					
Inflation (%, eop)	20.3	11.8	14.6	11.2	9.9
Inflation (%, aop)	16.2	15.4	12.3	14.4	10.1
Loans to the Private Sector (% change, eop)	14.2	10.8	34.8		
Customer Deposits (% change, eop)	18.5	23.5	33.0		
Loans to the Private Sector (% of GDP)	63.7	61.4	70.8		
Retail Loans (% of GDP)	13.8	13.9	16.8		
Corporate Loans (% of GDP)	49.9	47.5	54.1		
Customer Deposits (% of GDP)	50.8	54.5	62.1		
Loans to Private Sector (% of Cust. Deposits)	125.4	112.6	114.1		
Foreign Currency Loans (% of Total Loans)	39.9	38.3	34.2		
External Accounts					
Merchandise exports (USD million)	178,909	182,246	168,245	181,558	190,123
Merchandise imports (USD million)	219,635	198,997	206,123	216,736	226,102
Trade balance (USD million)	-40,726	-16,751	-37,878	-35,178	-35,979
Trade balance (% of GDP)	-5.2	-2.2	-5.3	-4.4	-4.1
Current account balance (USD million)	-21,743	6,759	-36,724	-25,535	-23,092
Current account balance (% of GDP)	-2.8	0.9	-5.1	-3.2	-2.7
Net FDI (USD million)	9,235	6,323	4,631	5,326	6,391
Net FDI (% of GDP)	1.2	0.8	0.6	0.7	0.7
International reserves (USD million)	93,027	105,696	93,277	100,000	110,000
International reserves (Months[a])	4.5	5.6	4.9	5.0	5.3
Public Finance					
Primary balance (% of GDP)	0.0	-0.5	-0.8	-0.9	-0.4
Fiscal balance (% of GDP)	-1.9	-2.9	-3.4	-3.5	-2.8
Gross public debt (% of GDP)	30.2	32.6	43.0	40.0	38.4
External Debt					
Gross external debt (USD million)	442,758	434,503	440,000	450,000	460,000
Gross external debt (% of GDP)	57.0	57.1	61.2	56.0	52.9
External debt service (USD million)	82,913	85,286	70,786	80,000	85,000
External debt service (% of reserves)	89.1	80.7	75.9	80.0	77.3
External debt service (% of exports)	34.6	36.0	37.5	36.7	35.8
Financial Markets					
Policy rate (Effective funding rate, %, eop)	24.1	11.4	17.0	13.5	11.5
Policy rate (Effective funding rate, %, aop)	17.7	20.7	10.5	16.0	12.5
1-Y T-bill rate (%, eop)	21.5	11.3	15.1	12.0	10.9
Exchange rate: USD (eop)	5.29	5.95	7.43	7.80	8.25
Exchange rate: USD (aop)	4.84	5.68	7.02	7.62	8.03

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

SERBIA	2018	2019	2020e	2021f	2022f
Real Sector					
Nominal GDP (EUR million)	42,939	46,017	46,493	50,077	53,543
GDP per capita (EUR)	6,149	6,608	6,703	7,249	7,781
GDP growth (real, %)	4.5	4.2	-1.0	5.5	4.5
Unemployment rate (%, aop)	12.7	10.4	9.0	9.6	9.2
Prices and Banking					
Inflation (%, eop)	2.0	1.9	1.3	2.4	2.6
Inflation (%, aop)	2.0	1.9	1.6	1.9	2.3
Loans to the Private Sector (% change, eop)	9.9	8.9	12.2		
Customer Deposits (% change, eop)	14.9	7.8	17.4		
Loans to the Private Sector (% of GDP)	43.5	44.4	49.4		
Retail Loans (% of GDP)	20.1	20.5	22.8		
Corporate Loans (% of GDP)	23.4	23.8	26.6		
Customer Deposits (% of GDP)	44.9	45.3	52.7		
Loans to Private Sector (% of Deposits)	96.9	98.0	93.6		
Foreign Currency Loans (% of Total Loans)	67.0	66.9	62.7		
External Accounts					
Merchandise exports (EUR million)	15,106	16,415	16,032	17,037	17,968
Merchandise imports (EUR million)	20,191	22,038	21,257	22,707	24,006
Trade balance (EUR million)	-5,085	-5,623	-5,224	-5,669	-6,038
Trade balance (% of GDP)	-11.8	-12.2	-11.2	-11.3	-11.3
Current account balance (EUR million)	-2,076	-3,161	-1,981	-2,436	-2,678
Current account balance (% of GDP)	-4.8	-6.9	-4.3	-4.9	-5.0
Net FDI (EUR million)	3,157	3,551	2,902	3,265	3,673
Net FDI (% of GDP)	7.4	7.7	6.2	6.5	6.9
International reserves (EUR million)	11,262	13,379	13,492	14,321	15,316
International reserves (Months[a])	5.4	5.7	6.4	5.9	5.9
Public Finance					
Primary balance (% of GDP)	2.8	1.8	-6.1	-2.0	-0.7
Fiscal balance (% of GDP)	0.6	-0.2	-8.1	-4.0	-2.5
Central Government debt (% of GDP)	53.6	52.0	57.4	57.3	56.1
External Debt					
Gross external debt (EUR million)	26,662	28,254	30,918	31,599	32,447
Gross external debt (% of GDP)	62.1	61.4	66.5	63.1	60.6
External debt service (EUR million)	5,600	6,400	7,400	5,800	5,000
External debt service (% of reserves)	49.7	47.8	54.8	40.5	32.6
External debt service (% of exports)	26.4	27.4	33.3	24.5	20.0
Financial Markets					
Policy rate (2-w repo rate, %, eop)	3.0	2.3	1.0	1.0	1.3
Policy rate (2-w repo rate, %, aop)	3.1	2.7	1.5	1.0	1.1
1-Y T-bill rate [b] (%, eop)	n.a.	n.a.	2.6	2.2	2.5
Exchange rate: EUR (eop)	118.2	117.5	117.5	117.5	117.5
Exchange rate: EUR (aop)	118.1	117.7	117.5	117.5	117.5

f: NBG forecasts; a: months of imports of GNFS; b: primary market