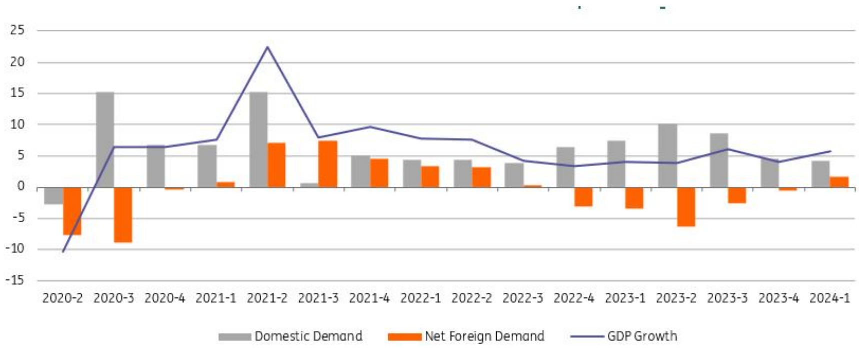
Turkey sees continued strength in domestic demand

Turkey's first-quarter GDP recorded another strong performance, mainly driven by private consumption. Despite further signs of rebalancing evident in the positive contribution from net exports and a tight stance on policy, domestic demand remained robust

Istanbul, Turkey

Turkish GDP growth in the first quarter came in at 5.7% on a year-on-year basis, aligned with both the market consensus and our call. This came on the back of continued strength in domestic demand and a positive contribution from net exports. First quarter GDP translated into a quarter-on-quarter growth rate of 2.4% after seasonal adjustments, showing a gain in momentum when compared to a relatively modest reading of 1.0% in the fourth quarter. The accelerating sequential performance is attributable to the positive turn of investments and government spending after a negative reading a quarter ago, as well as the supportive impact of net exports despite the contractionary effect of inventory build-up and moderation in private consumption.

Quarterly Growth (%, YoY)



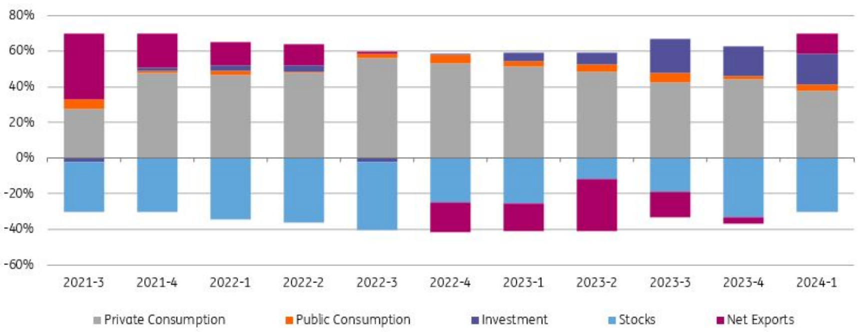
Source: TurkStat, ING

When we look at the breakdown on expenditures:

- Private consumption has lost steam at its lowest level since the pandemic – though has remained robust at 7.2% YoY. Continuing strength likely reflects forward-brought consumption ahead of local elections in addition to the impact of wage hikes and accelerating credit card expenditures and consumer loan growth. Accordingly, it has lifted headline GDP by 5.5ppt despite the Central Bank of Turkey's rate hikes.
- Investment appetite has been robust, with 10.3% YoY growth translating into a 2.6ppt contribution to GDP expansion. This is mainly because of continued double-digit growth in machinery equipment (11.9% YoY in the first quarter) and an acceleration in construction investments to 9.6% YoY.
- Firstly, public consumption has continued to contribute positively to headline GDP since early 2021, and accelerated in comparison to the previous quarter with a 3.9% YoY increase – lifting first quarter growth by a mere 0.5ppt. Secondly, inventory build-up shaved 4.4ppt off growth, and finally, net exports pulled headline growth up by 1.6ppt after five quarters of negative contribution. This is attributable to a contraction in imports and an acceleration in exports growth.

In the sectoral breakdown, services turned out to be the biggest contributor again. Industry followed, with industrial production data in the first quarter illustrating a revival. A recovery in the construction sector and a higher contribution to the headline GDP rate in recent quarters also attracted attention, likely attributable to rebuilding efforts in the earthquake region.

Drivers of growth (ppt contribution)



Source: TurkStat, ING

Overall, economic activity in Turkey was stronger in the first quarter due to wage hikes and fiscal stimulus. However, following the surge in loan demand in the run-up to the local elections, the CBT has come forward with policy action – including an unexpected rate hike in March, and moves to control both the Turkish lira and FX lending growth as well as sterilising the liquidity in the system.

Banking sector data shows that these actions led to a slowdown in credit growth, including a sharp decline in consumer credit card spending. We will likely see further deceleration with the recently imposed cap on FX loans expansion. Given this backdrop, while early indicators for the second quarter point to some weakening in activity (which is still moderate so far), growth is expected to lose significant momentum throughout the remainder of the year with tightening financial conditions, slowing real wage growth and a likely increase in the unemployment rate.

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