Correction in Turkey’s external deficit continues

After reaching its peak in May last year, Turkey's external balances have corrected significantly with further adjustment in December, 2018. The Capital flow outlook remains challenging

Source: iStock

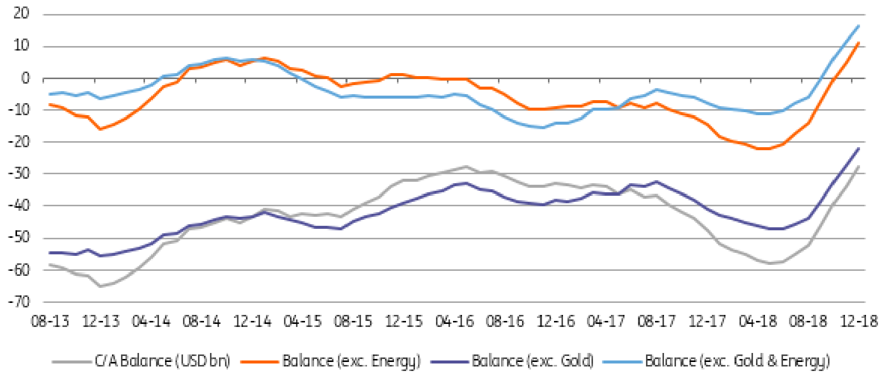
$27.6bn

12M rolling c/a deficit in Dec

More than halved since mid-18

Turkey's 12-month rolling current account deficit, on a correction path in the second half of 2018, stood at US$27.6 billion, the lowest since mid 2010. Improving price competitiveness contributing to export performance and weakening domestic demand following summer volatility, with consequent significant financial tightening, has triggered a sharp improvement in external balances in recent months. Accordingly we saw 6.5% YoY contraction in core imports (excluding gold and energy) last year, while core exports recorded 10.3% YoY growth.

External Balances (USD bn, 12M rolling)



Source: CBT, ING Bank

On a monthly basis, after four months of surplus, the current account balance turned negative at US$1.5 billion deficit in December, though the recovery in the 12M rolling figure continued. In the breakdown, the improvement over the same month of 2017 is mainly attributable to a contraction in foreign trade while services income maintained the uptrend with healthy tourism revenues and contributions from transport revenues.

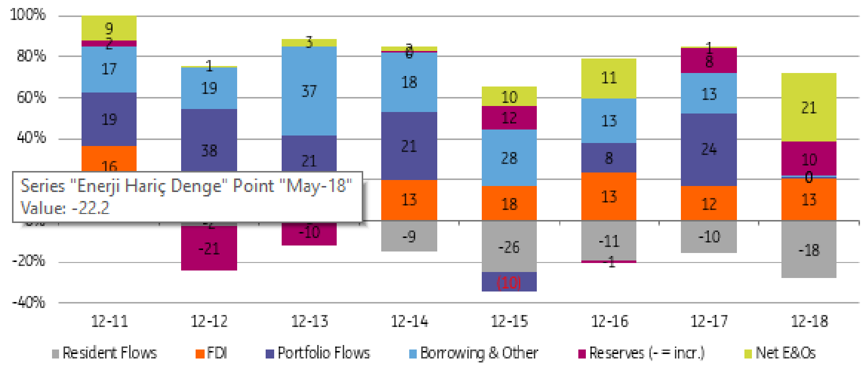
On the financing front, the capital flow outlook has remained weak with further outflows at US$0.5 billion in December alone. Despite declining assets of residents held abroad (mainly due to local banks bringing their deposits) and the contribution from monthly Foreign Direct Investment, capital flows turned out to be negative with:

1. continuing debt repayments (mainly because of banks' short and long term debt payments),
2. a decline in deposits held by foreign investors, and
3. further portfolio outflows with non-residents' sale of government debt instruments and banks' repayment of maturing Eurobonds.

Turkey relied on US$2.8 billion inflow from net errors & omissions to finance external deficit and capital outflows in December, while official reserves recorded US$0.9 billion increase.

Breakdown of C/A Financing* (12M Rolling, USDbn)

* Positive sign in reserves shows reserve accumulation



For the whole year, US$10.4 billion reserve depletion and significantly high inflows at US$21.2 billion via net errors & omissions helped finance the c/a deficit of US$27.6 billion and US$3.9 billion outflows in the capital account. These numbers show the challenging picture for external financing last year, however concerns about banks' ability to access foreign funding should be over given that the sector recorded 66% rollover rate in December up from 8% in September while the figure for 2018 was 76%.

Overall, the data shows that outflows moderated in the last quarter of 2018, though the external financing has been challenging given continuing external deleveraging. Sizeable total external financing needs in the period ahead, mostly due to private debt amortization, will likely keep Turkey sensitive to shifts in global risk appetite but the government's increasing external borrowing should help ease the pressure. On a positive note, the recovery in the trade balance will remain in place in the first half of this year given ongoing domestic demand conditions and the strength in exports with the inclusion of tourism, though the pace of external rebalancing will likely slow, before rising gradually in the second half.

Author

Muhammet Mercan
Chief Economist, Turkey
muhammet.mercan@ingbank.com.tr