35. TÜRKIYE

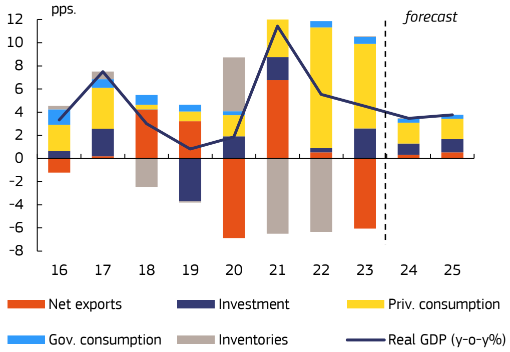
Domestic demand is subsiding slowly, with a still upbeat economic activity in the first quarter of 2024. The significantly tighter monetary and fiscal stance is forecast to bring a more pronounced reduction in domestic demand and further moderation of economic growth, enabling a gradual decline of imbalances, including inflation. Domestic policy uncertainty declined significantly, but managing the rebalancing of the economy is likely to remain challenging. Earthquake reconstruction and policy normalisation costs are expected to continue weighing on the budget, but the deficit is forecast to decline and government debt to remain moderate.

Domestic demand subsiding slowly

In the last quarter of 2023, economic growth remained robust at 1.0% quarter on quarter, despite a slowdown in domestic demand. Annual GDP growth was still buoyant at 4.5% despite a significant deceleration of household consumption growth, to single digits for the first time in two years. High frequency indicators point to a still upbeat economic activity in the first quarter of 2024. Economic confidence has improved since the beginning of the year, industrial production rebounded, increasing strongly in February, and the manufacturing Purchasing Managers Index increased to 49.8 in the first quarter, skirting the threshold indicating expansion.

Economic rebalancing is expected to accelerate in the second half of the year

Graph II.35.1: **Türkiye - Real GDP growth and contributions**



The ongoing policy normalisation, with a significantly tighter monetary and fiscal stance since mid-2023, is expected to continue and to lead to a more pronounced reduction in domestic demand before the end of the year. Household consumption growth, in particular, is expected to decelerate rapidly as the labour market cools down, the effect of the wage hike at the end of 2023 tapers off, and consumers lower their inflation expectations. The strong moderation of household consumption growth is seen as the main driver of economic rebalancing. Public consumption growth is also set to be more subdued following the recently announced restraint on spending, excluding expenditure related to earthquake recovery activities. Reconstruction works are expected to contribute to continued investment growth in an otherwise restrictive environment.

In view of the outlook for more subdued economic activity, and after three years of very strong performance, employment growth is expected to subside and the unemployment rate to increase in 2024.

‘Soft landing’ and a gradual unwinding of imbalances

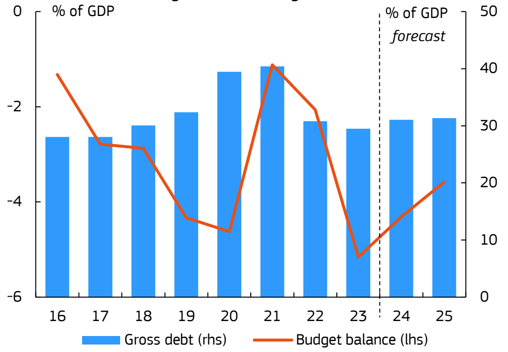
The forecast envisages a ‘soft landing’, with lower real GDP growth and a gradual unwinding of imbalances. The contribution of net exports to growth is forecast to turn slightly positive in the next two years, as the recovery in exports consolidates and import growth moderates. The current account deficit narrowed in 2023 because of improved terms of trade and reduced non-monetary gold imports, reflecting improved confidence. It is expected to fall further in the next two years, approaching levels that could allow the sustainable rebuilding of foreign exchange reserves by the central bank.

Decisive policy action has brought some results, but inflation remains very high. It is expected to peak at around 70% year on year in May 2024, and inflation expectations are still elevated. The disinflation process is expected to take time, going beyond the forecast horizon, and maintaining a tight monetary policy stance remains key to firmly consolidating the disinflation process and anchoring inflation expectations.

Living with uncertainty

Geopolitical and external risks and uncertainty have been very high for many years. Although the Turkish economy has navigated them relatively well so far, they remain an ever-present factor that could disrupt policy making and economic developments. Domestic policy uncertainty declined significantly, but managing the normalisation of economic policies and the continuing gradual adjustment of domestic demand is likely to remain challenging.

Graph II.35.2: **Türkiye - General government budget balance and gross debt**



Earthquake recovery and policy normalisation costs to weigh on the budget

The central government budget deficit-to-GDP ratio is estimated to have increased to 5.2% in 2023 because of large earthquake-related costs and an increase in pre-election spending last year. The underlying fiscal stance was also clouded by the cost of policy normalisation, manifested by the high loss recorded by the central bank in 2023 which is not yet officially impacting on budgetary accounts. The relatively strong revenue performance last year is expected to continue in 2024 and, together with the expected under-execution of expenditure, to bring the budget deficit-to-GDP ratio below the target of 6.4%. However, as earthquake recovery efforts extend into 2025, the budget deficit is forecast to remain elevated. In view of that, the government debt-to-GDP ratio is expected to slowly increase, but to remain moderate in the next two years.

Table II.35.1:

Main features of country forecast - TÜRKIYE

		2023			Annual percentage change					
	bn TRY	Curr. prices	% GDP	04-19	2020	2021	2022	2023	2024	2025
GDP		26276.3	100.0	5.3	1.9	11.4	5.5	**4.5**	**3.5**	**3.8**
Private Consumption		15608.7	59.4	4.6	3.2	15.4	18.9	**12.8**	**3.0**	**3.0**
Public Consumption		3577.9	13.6	5.5	2.2	3.0	4.2	**5.2**	**2.5**	**2.5**
Gross fixed capital formation		8506.1	32.4	6.9	7.3	7.2	1.3	**8.9**	**3.0**	**3.1**
Exports (goods and services)		8479.1	32.3	6.3	-14.6	25.1	9.9	**-2.7**	**2.9**	**4.3**
Imports (goods and services)		9116.3	34.7	4.7	6.8	1.7	8.6	**11.7**	**1.7**	**2.5**
GNI (GDP deflator)		25819.2	98.3	5.3	2.2	11.3	5.6	**4.1**	**3.8**	**4.1**
Contribution to GDP growth:	Domestic demand			5.5	4.1	11.2	11.3	**10.5**	**3.1**	**3.3**
	Inventories			-0.4	4.7	-6.5	-6.3	**0.1**	**0.0**	**0.0**
	Net exports			0.5	-6.9	6.8	0.5	**-6.0**	**0.3**	**0.5**
Employment				1.8	-4.5	7.5	6.6	**2.9**	**1.8**	**2.0**
Unemployment rate (a)				10.0	13.2	12.0	10.6	**9.5**	**10.2**	**10.2**
Compensation of employees / head				12.2	12.4	22.4	70.5	**110.0**	**64.0**	**41.3**
Unit labour costs whole economy				8.5	5.4	18.1	72.2	**106.7**	**61.4**	**38.8**
Saving rate of households (b)				:	:	:	:	**:**	**:**	**:**
GDP deflator				9.1	14.8	29.0	96.0	**67.5**	**58.7**	**36.5**
Consumer price index				9.4	12.3	19.6	72.3	**53.9**	**57.4**	**31.5**
Terms of trade goods				:	:	:	:	**:**	**:**	**:**
Trade balance (goods) (c)				-1.3	-1.8	-3.6	-9.9	**-7.9**	**-7.0**	**-6.2**
Current-account balance (c)				-4.0	-4.8	-1.6	-5.4	**-4.1**	**-2.7**	**-2.1**
General government balance (c)				-1.8	-4.6	-1.1	-2.1	**-5.2**	**-4.3**	**-3.6**
Structural budget balance (d)				:	:	:	:	**:**	**:**	**:**
General government gross debt (c)				36.6	39.4	40.4	30.8	**29.5**	**31.1**	**31.3**

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.