

# Weekly Bulletin

March 23-27, 2009

## Focus of this week

**Mar-23** US, Existing Home Sales, Feb, cons: 4.45M, prev: 4.49M  
 Timothy Geithner will announce the plan on banking sector  
 Speech of Trichet

**Mar-25** US, New Home Sales, Feb, cons: 300K, prev: 309K  
 US, Durable Good Orders, Feb, cons: -2%, prev: -5.2%  
 US, Crude Inventories, prev: 1942K

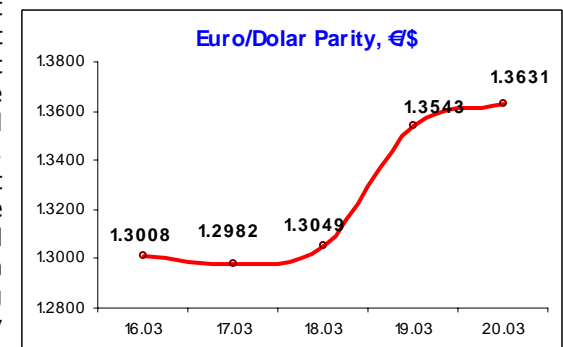
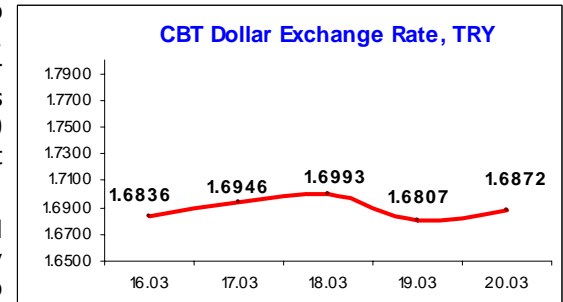
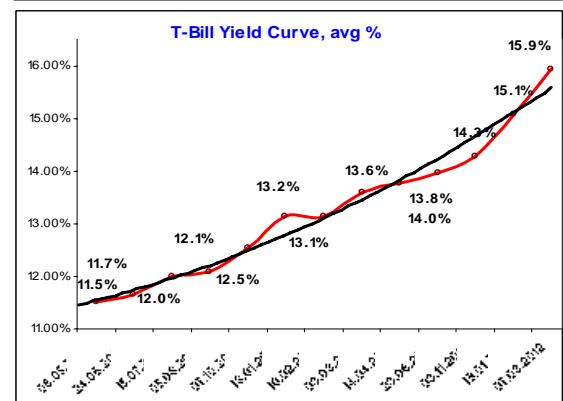
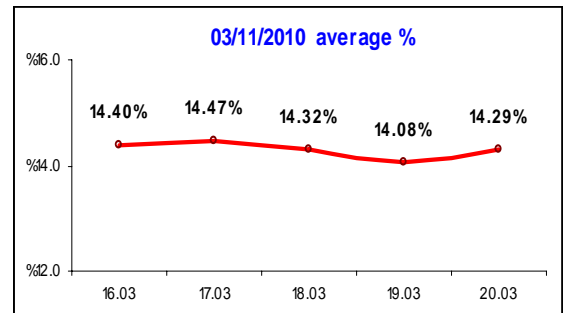
**Mar-26** US, GDP, Q4, cons: -6.6%, prev: -6.2%  
 US, Initial Claims, cons: 650K  
 Presentation of Geithner at Senate

**Mar-27** US, Personal Income, Feb, cons: -0.1%, prev: 0.4%  
 US, Personal Spending, Feb, cons: 0.3%, prev: 0.6%  
 US, Mich Sentiment-Rev, Mar, cons: 56  
 UK, GDP, Q4, prev: -0.7%

**Mar-29** Local Elections

**STRATEGY:** Atilla Yeşilada, a good old friend of mine, stipulates from time to time that he is the cosmic strategist. Well, I am the more mundane one then, although no one would recognize the consequences of this division of labour as far as lamentations of two bears go. Yes, I am still bearish. This week is another matter, and we might see the 100 day-moving average at 25,000 being tested in the short run and if the optimism prevails, the index may test 27,000 on the coming days.

**ECONOMICS:** Is there any surprise on the budget front? No, it was all expected. The January-February cumulative budget deficit reached the yearly target already. Hence, we need zero deficits in the remainder of the year to keep up with the (unrealistic) budget estimates. Of course, this will not happen since the special tax reductions' revenue effect lies ahead and is not in the figures yet. Not only interest expenditures rose, but also the current transfers item jumped because of transfers to social security institutions. The Ministry of Finance explained that interest expenditures rose seasonally, and that the increase does not contradict with the initial forecasts. Nonetheless, the budget deficit will pop up in March also, and it is not clear whether it would come in line with a reasonably balanced –yet deficitary- path in the forthcoming months. We recapitulate the thesis according to which industrial production –and along with it the GDP itself- would post record lows between March and July. The problem with the tax rate cuts and the spending elements of the budget lies elsewhere. It is very likely to see a temporary revival in growth accounts due to cuts and public spending, but first we do not postulate a public expenditure-to-GDP multiplier that exceeds one, and second the revival will be rather short-lived. While inflationary second-round effects are no cause for concern, the 2009 impact on the budget deficit should remain significant. The trade-off does not look bright: a temporary relief in exchange for a lasting fiscal deterioration is of no avail.



Inflation %	Feb-09	Jan-09	12 month
PPI	1.17	0.23	6.43
CPI	-0.34	0.29	7.73

**POLITICS&VISION:** This section pays tribute to the time-honoured classic of Sheldon Wolin, Politics and Vision, 1960. Is there a political risk ahead, after the municipality elections that have already garnered a general election aura? Well, possibly the answer is a qualified yes. Antonio Gramsci referred to the concept of passive revolution, in conjunction with the war of position and this much is very well known. Over the so many years the Islamic current overtly or covertly tried to gain influence, affluence, and potency, it has aspired in its main body politic to a passive revolution. The Turkish Islamic bourgeoisie is every bit as much as cultural a bourgeoisie as the secular bourgeoisie, and it is no longer in the making as a fraction of (a) class. It has already surfaced out at the expense of the traditional business elite, and its ongoing embourgeoisement looks irreversible. Indeed, the ruling party is an Islamic party, the only question being whether this party, an alliance of sects and orders, could be transformed or would transform itself to a the equivalent of Christian Democrats in Europe. The Islamic character is not only a matter of genesis or roots, but it is an undeniable feature of the existing body politic of the ruling conservative political movement. Similarly, the economic and political might of this movement is already well entrenched into the cultural map of Turkish society as well as, in parts, of the state apparatus. How the Republic is being remade in the process of a long-lasting war of attrition remains a central question.

**EQUITY:** The local stock market tested 24,000 consecutive times last week as international equities responded to the stimulus, especially after the Fed's USD1 billion plan announcement on Wednesday, which is bound to inject fresh liquidity in the US banking system. The ISE100 index traded in 23,700-24,100 range on Friday and closed slightly over 24,000 with 0.29% daily and 1.79% weekly gain. The dollar eased down to 1.6750 against lira on Friday after testing 1.7100 in the previous days. US equities setback at the end of the week while the announcement that the US Treasury Secretary Geithner will unveil the "bad bank" plan, which aims to clear up the toxic assets from the banks' balance sheets, boosts the markets on Monday. The US futures trade with gains more than 2% while the gains in Asian markets have reached 4%. Some of the other issues that the markets will care for will be the US House hearing on AIG, durable goods orders and the final reading on the fourth quarter GDP. The markets will also get US existing home sales of February today. The dollar has started the week at 1.6740-50 range against lira, slightly lower than Friday while the bond yields are testing below 14.00% once again. The ISE100 index is expected to align with foreign markets and start the day up at 24,200-500 range. Increases over 24,000 will be critical.

**FIXED INCOME & CURRENCY:** In the last trading day of the week, opening at 1.7150 levels, primarily due to local bank selloffs \$/TL, fell to 1.6750, and completed the week at 1.6850. Through positive global environment, interbank dollar quotations started the week at 1.6760 where we expect it to fluctuate within 1.65-1.70 interval. After MPC's rate cut decision, selloffs were observed in the bond market. Benchmark compound rate moved at 14.37%-14.09% band, and closed at 14.13% on Friday. Opening at 14.05% level we expect benchmark compound rate to be traded at 14.25%-13.75% interval.

### March 2009– Monthly Domestic Debt Service

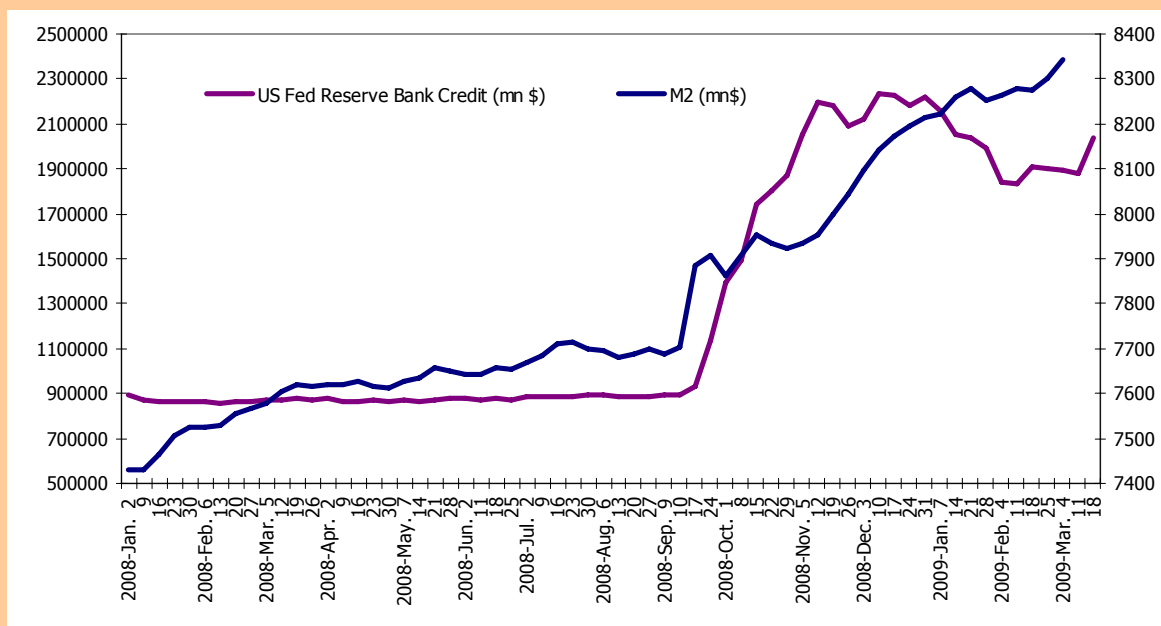
Date	To the Markets	Other	TOTAL
4-March	1,295	319	1,615
11-March	2,320	47	2,367
18-March	122	5	126
<b>TOTAL</b>	<b>3,737</b>	<b>371</b>	<b>4,108</b>

## Gündüz Fındıkçioğlu, PhD

Now the IMF deal looks closer, the CBT opened up FX auctions and supplied the market with daily liquidity of USD50 million, and the nominal exchange rate setback is in the agenda. We were expecting this to happen just before the elections, but the prospect of breaking the 1.82 resistance, and struggling with 1.85 was in the agenda. Therefore, the intervention(s) came early. Now what? Two things can happen: (1) despite the IMF deal we pass through yet another ordeal and, short of financing at least 55-60% of FX liabilities, the real sector's demand for dollars step up once again in the future, and for good (2) The IMF money covers the financing gap, and we stay calm on the FX front for the visible future. Exports decline nonetheless and a permanent setback to 1.5 USD/TRY is not warranted in our opinion. We expect volatility strikes in the remainder of the year. I also think the new equilibrium-to-be should depict an entirely different pattern: low real rates of interest with respect to the past; higher real exchange rates; lower sustainable growth for 2010-2011; much lower current account deficits even when growth resumes. Turkey should avoid at all costs a repetition of 2002-2007, which anyway does not look replicable.

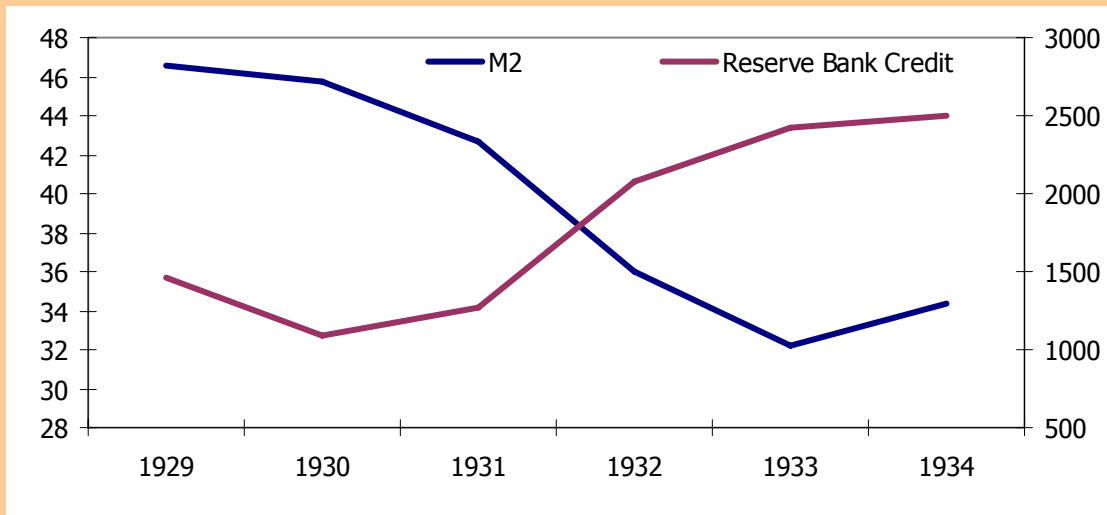
On the other hand, the most recent Fed move and the avenue it opens up may cause a stir in the future. With the Fed's BS mounting to unprecedented levels, fears of "USD blues" that could cause it to lose its status as reserve money –since Helicopter Ben is in the making- curtailed market enthusiasm. The EUR rose by a weekly-unseen speed consequently. Now, not all Fed lending is inflationary, and not all Fed BS expansion creates "new money." However, if we choose to use a widely cited euphemism, the last move is bound to add to money printing. It looks like using part of the holdings as an off-BS item to support the Term Securities Lending Facility (TSLF) and asking the Treasury to start a Supplementary Financing Program (SFP) through which the Treasury would sell securities to the public directly but keep the receipts in the Fed's accounts was only the beginning. On January 15, Fed's reserve credit dropped by USD108bn to USD2.040 billion, and the total drop since December 17 was around USD250 billion. The most recent decline was due to lower TAF and extended discount window borrowings and a cut in currency swaps outstanding. The end-of-year effect was already behind us, so the drop is TAF and the discount window. The question was whether the tendency of Fed reserve credit book to shrink would continue or not. It was not clear the Fed was going to buy up to USD500 billion of MBS. Hence, the Fed BS January movement was probably a temporary improvement.

What did happen in February then? The Fed posted a sharp drop in reserve credit by USD149 billion and the reserve credit book fell to USD1840 billion, the most bizarre thing observers have recorded since some time. Repos were nil! Swaps were down by USD77 billion to USD338 billion. Excess reserves were at USD642 billion where the peak reserve level was USD850 billion. Foreign official and international accounts bought an extra USD15 billion in treasuries and sold USD8 billion in agencies.



Enters March, when the Fed outlook changes anew, with a big bang type quantitative easing explanation from Bernanke. The real expansion will come up with TALF (Term Asset-Backed Securities Loan Facility) and it is about USD1 billion. Short-term, mostly 3 months Fed loans, although they are being rolled over regularly, are of no genuine concern. However, the longer term Fed reserve credits may be conducive to inflation.

On the other hand, consider the graphic displaying M2 and reserve credits between 1929 and 1934. Although reserve credits, and henceforth the Fed's BS expanded during that period, M2 actually shrank. Bernanke knows this very well since he is also an expert on the Great Depression. We ought to watch monetary developments from that angle as well.



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