**June Inflation …**

June inflation printed below expectations at -0.27%. Annual inflation fell to 10.9% YoY in June from 11.7% YoY in May.

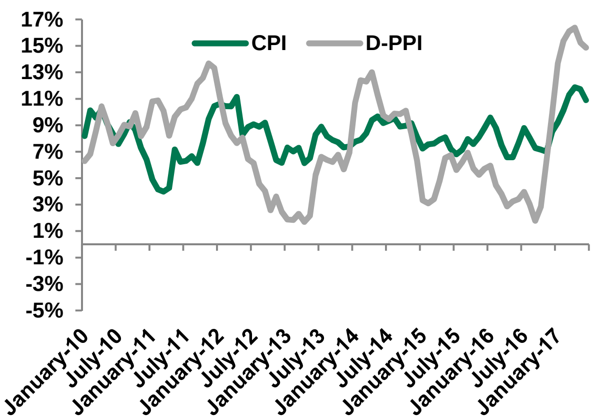
***Annual inflation declined to 10.9%***

Of note, food inflation fell to 14.3% YoY from 16.9% YoY. Energy inflation fell to 7.5% YoY from 8.7% YoY. These two items were the major drivers of lower inflation. However, further significant positive news came from core inflation – C (previously - I%) at only 0.07% MoM. Accordingly, annual core inflation fell to 9.2% from 9.4%.

Adjusted for seasonal effects, core inflation, led by core goods has been on a firm decline in June, being pushed downwards by items across the board, including the services inflation. We expect core inflation momentum to continue easing going forward, although base effects will delay/prevent a marked decline in the annual rate.

We expect annual inflation to remain high on base effects between August-September, before easing to 10% in December. Recent softness in core inflation indicators, along with rapid deceleration in food prices and lower energy prices suggest somewhat downward pressure on our inflation estimate. However, we continue to expect significant disinflation towards end of 1H2018, with inflation easing considerably toward 6.0 % YoY.

Going forward, food inflation is the only major pressure point on inflation as core momentum has shown more signs of significant easing. Given that the core inflation outlook is the one the CBRT takes more into account in monetary policy decisions, as repeatedly stated and acted upon in the past, there could be ample room for easing.




***May CAD just above deficit expectations…***

The CA deficit came in at USD5.2bn in May, just above the USD5.0bn deficit expectation. The 12mth rolling deficit rose to USD35.3bn (4.1% GDP), thus above the USD33.2bn of April.

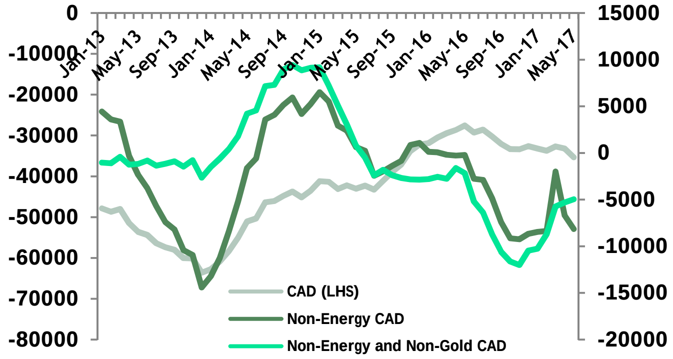
Net FDI investment was also relatively strong, bringing the country USD1.0bn in hard currency.

However, for the month, banks were still in deleveraging mode on the credit side with a net payback of USD1.0bn (Eurobond issues not included).

***12mth rolling deficit at USD35.3 bn…***

However, almost all of the USD5.5bn of inflows into Turkey were Eurobond issues of Turkish banks and the Treasury of Turkey (like in March in April). In fact, inflows into equities and local bonds were insignificant.

CBRT reserves were up by USD2.5bn in May, bringing down the ytd reserve loss to USD5.4bn. Strong portfolio inflows were behind improvement in the fx reserve situation.



**IP May 2017…**

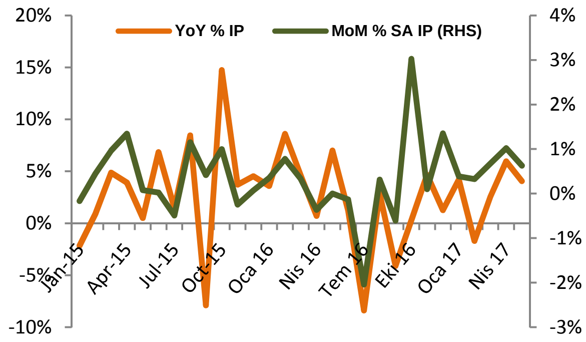
May's seasonally-adjusted industrial production contracted 1.5% MoM following a 2.2% MoM and 1.3% MoM rise in the past two consecutive months. However, despite a rather sharp downturn in the May print, 3m/3m SA IP growth rose to 2.3% (annualized 9.3%) from 2.1% (8.4%).

***Hence, GDP growth in 2Q17 had probably been as strong as in 1Q17…***

However, behind strong sequential IP growth was the surge in the capital goods manufacturing, more specifically other motor vehicles manufacturing sub-item, accounting for almost the entire increase. Nonetheless, recent IP data points to a warming of the economy. While there is an upside risk to our 5% YoY growth estimate for 1Q17 (to be announced on Monday), the acceleration signal (April IP, May PMI) points to similar YoY GDP growth in 2Q17.

Turkey's Manufacturing PMI Index registered at 54.7 in June to hit its 43-month high. Thus, the second quarter average of the index picked up notably to 53.3 from 50.2 in the first quarter, signaling continued acceleration of economic activity.

All data bodes well for a blockbuster GDP growth number for 2Q17, quite possibly exceeding 1Q17's 5.0% YoY.




**CBRT kept interest rates constant as expected…**

As widely expected, the Monetary Policy Committee has kept short term interest rates constant at the following levels.
O/N lending rate: 9.25%
Late Liquidity: 12:25%
O/N borrowing rate: 7.25%
1 week repo rate: 8.00%

***CBRT maintained its interest rates…***

Recently released data indicates that the recovery in economic activity has gained pace.

Although recent improvements in cost factors and expected partial correction in food prices will contribute to disinflation, currently elevated levels of inflation pose risks to pricing behavior. Accordingly, the Committee decided to maintain its tight monetary policy stance.

Still high inflation expectations&improving growth outlook could prompt the Bank to remain on a cautious path, despite the positive trajectory of core inflation. So far, the average cost of funding has stood firmly near 12% (late liquidity window rate), despite a weaker USD. We anticipate that the exchange rate will stabilize beypnd 2017, whereby core inflation will enter a long period of decline. We expect that even if is temporarily towards the end of 1Y2018, the annual rate of inflation may decline rapidly towards 6%. Given a high food/core inflation base for next year, and improving CA Dynamics, inflation could behave very positively in 1H2018, whereby CBRT rate cuts towards 4Q17 are likely.