

Subject: TURKISH BANKS - Vulnerabilities to tighter external financing and refinancing risk  
From: Martin Zeman <[REDACTED]>  
Date: Thu, 19 Jul 2018 09:34:47 -0400  
To: "Paul Barrett ([REDACTED])" <[REDACTED]>,  
Heiko Freitag [REDACTED]  
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Stewart Oldfield <[REDACTED]>,  
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Second email as discussed -

From: Kazim Andac  
Sent: Thursday, July 19, 2018 9:29 AM  
To: Martin Zeman <[REDACTED]>  
Subject: FW: TURKISH BANKS - Vulnerabilities to tighter external financing and refinancing risk

And this report is for external refinancing risk of TR banks

From: Kazim Andac  
Sent: 31 May 2018 09:21  
To: Kazim Andac <[REDACTED]>  
Subject: TURKISH BANKS - Vulnerabilities to tighter external financing and refinancing risk

TR BANKS - Vulnerabilities to tighter external financing and refinancing risk

<https://research.db.com/Research/Article?-rid=0900b8c08eb9cebd&kid=RP0001&documentType=R>

From: Kazim Andac - Deutsche Bank [mailto:ReplyToAnalyst@markit.esp.db.com]  
Sent: 30 May 2018 22:09  
To: Kazim Andac - [REDACTED]  
Subject: Turkish banks - Vulnerabilities to tighter external financing and refinancing risk

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Turkish banks  
Vulnerabilities to tighter external financing and refinancing risk

30 May 2018

Kazim Andac

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While the external debt rollover rate was above 100% in 1Q, potentially tighter external financing is a challenge for the persistence of top-line performance

As markets turn less market-friendly for EM, investors are questioning risks to the external funding picture of Turkey. The country's gross external financing need within 12 months is quite high at c.USD220bn (c.25% of GDP), c.USD75bn of which represents the debt rollover requirement of banks themselves. We note that capital market borrowing of TR banks has more than tripled since 2009. They are among the most exposed to FX wholesale funding (c.17% of assets) across EM, and lack of de-leveraging despite a more challenging backdrop (rekindled volatility, rising event risks, higher opportunity cost of funding due to rising USTs, etc.) makes banks more susceptible to external shocks. In this note, we opt to look at (1) how sensitive margins (NIM) and earnings could potentially lower external debt rollover, (2) we stress-test our revenue and bottom-line estimates under a scenario in which FX debt rollover ratios retreat to the levels that we witnessed at the time of the global crisis (c.70%) and (3) we assess short-term external refinancing risk.

How vulnerable are they? Every 10ppt decline in the rollover ratio reduces our NIM/earnings estimates by 6bps/c.2.5% on average, ceteris paribus

FX debt constitutes 21% of the overall funding base as of 1Q (i.e., the average of six large banks). Of FX debt stock, c.40% is short-term on average, which is dominated by syndicated loans and FX interbank, with Vakifbank and Yapi Kredi on the high end (greater exposure to short-term debt as a percentage of total), and Akbank and Garanti on the low end. Also, c.75% of the FX debt is USD-denominated, which increases vulnerability to higher US rates. Based on our estimates, every 10ppt decline in the rollover ratio reduces our NIM/earnings estimates by 6bps/c.2.5% on average – assuming that loan growth decelerates by the same amount in nominal terms (leaving all else unchanged). From an individual bank perspective, Vakifbank, Yapi Kredi and Isbank are relatively more sensitive when compared to Garanti, Akbank and Halkbank. Under a bearish scenario in which rollover ratios retreat to the levels we witnessed at the time of the global crisis (c.70%) and borrowing costs increase an 'additional' 100bps, this would mean our earnings would be c.10% lower (NIM: -30bps), with Vakifbank (-14%), Yapi Kredi (-12%), and Isbank (-10%) relatively more sensitive vs. Garanti (-5.5%), Akbank (-6%) and Halkbank (-9%).

Assessing FX refinancing risk: While the likely increase in FX borrowing costs, weaker lira, and hike in TRY rates all indicate that the risks to our NIM estimates are on the downside, we believe the external refinancing risk is very low

FX liquid assets (i.e. cash, foreign interbank and receivables from other financial institutions) constitute c.8.5% of FX assets (1Q18). However, when FX held within the Reserve Option Mechanism (ROM) in the CBT is also added to the picture (i.e., they can be replaced by unencumbered liquid g-bonds, as suggested by the CBT), share of FX liquid assets doubles to 17%. This indicates that 95% of the external debt that will mature in 12 months can be covered by short-term FX assets in the event of a 'no-rollover' scenario (i.e., almost no short-term external refinancing gap). Coverage of short-term debt with liquid assets (including reserves under ROM) stood at 134%, 112% and 106% for Garanti, Halkbank and Akbank as of 1Q, whereas the coverage was 73%, 79% and 94% in Isbank, Yapi Kredi and Vakifbank.

Valuation and recommendation: Akbank and Garanti are our top picks

The banking index retreated c.30% in the last three months, underperforming MSCI EM banks by 32%. TR banks' P/BV discount vs. MSCI EM extended to 40% against a five-year average of 14%. At 2018 ROTE of 17%, TR banks currently trade at '18E 4.6x P/E and 0.6x P/BV. Within our TR banks coverage, we have relative preference for Akbank (PT: TRY11.5) and Garanti (PT: TRY12.2) over their peers. Downside risks include prolonged capital outflows. Upside risks include easing of domestic liquidity conditions (See page 7).

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