



**TÜRKİYE CUMHURİYET
MERKEZ BANKASI**

Economic Outlook in Turkey

**Erdem Başçı
Governor**

March 2013, London

Overview

- Capital flow volatility may cause misalignments in credit and currency.
- Credit and currency misalignments hurt both price stability and financial stability in emerging market economies.
- Macroprudential policy has proven to be effective in reducing excessively high credit growth in Turkey.
- Using macroprudential policy effectively helps to reduce currency misalignments as well.
- Improvements in price stability and financial stability also improve balanced growth prospects in Turkey.

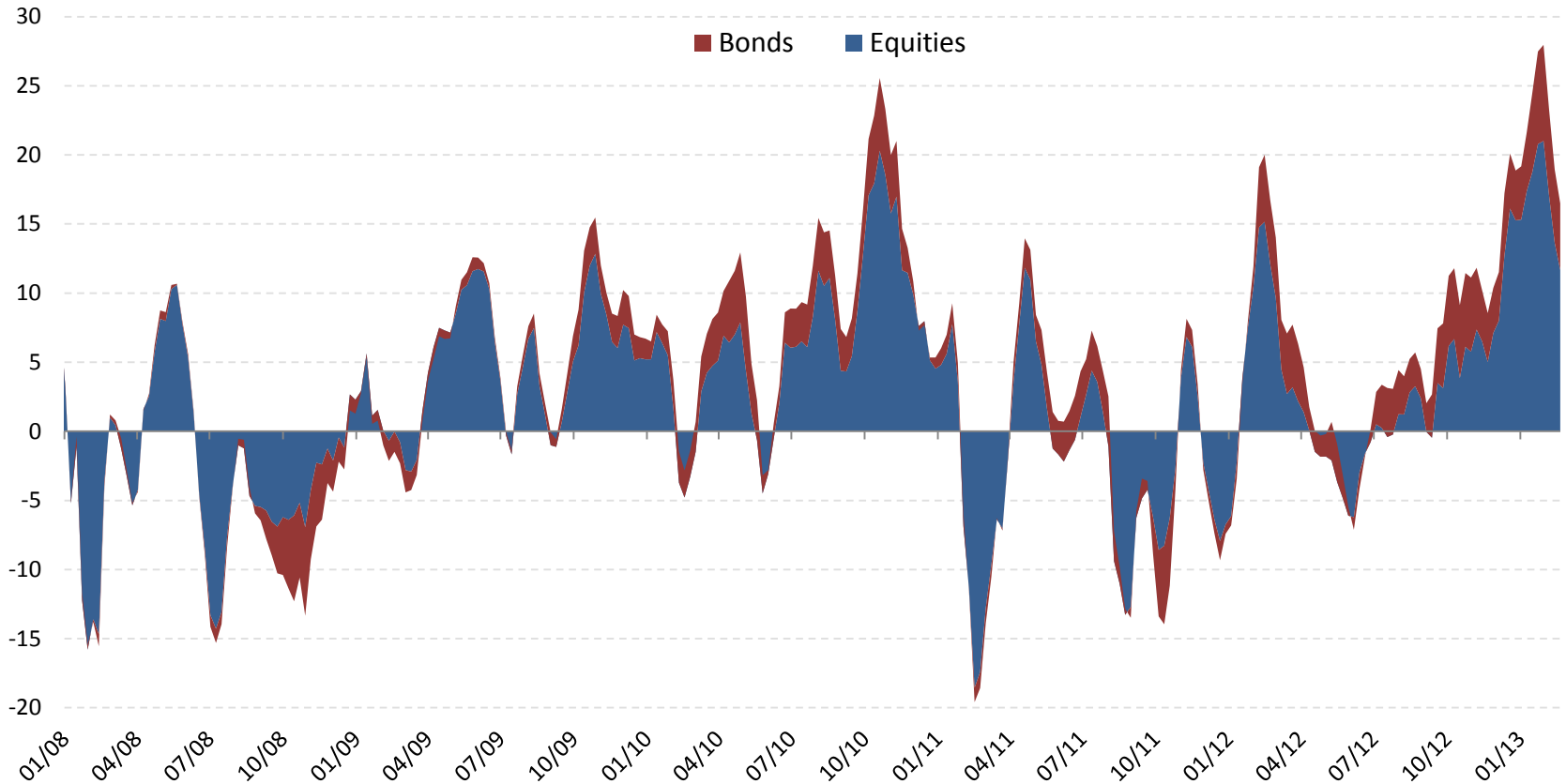
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- I. Capital Flow Volatility
- II. The Policy Framework
- III. Results
 - i. Rebalancing
 - ii. Inflation
 - iii. Growth

CAPITAL FLOW VOLATILITY

Capital Flows

Equity and Bond Flows to Emerging Market Economies (4-Week Moving Sum, Billion USD)

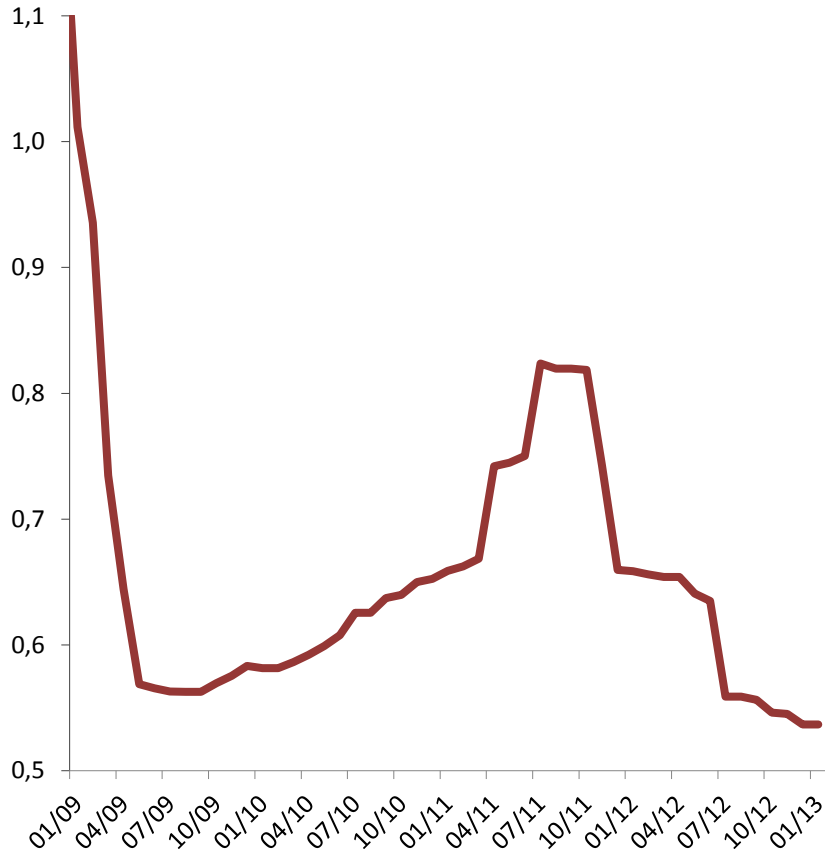


Source: Emerging Portfolio Fund Research (EPFR)

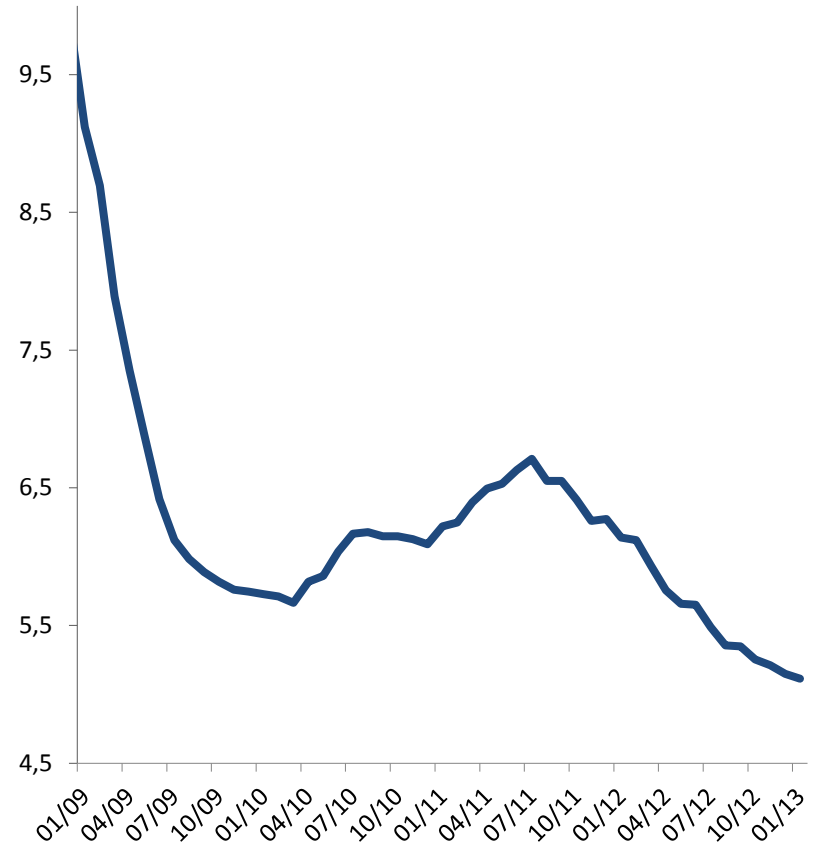
Last Observation: February 20, 2013

Global Policy Rates

Advanced Economies



Emerging Market Economies

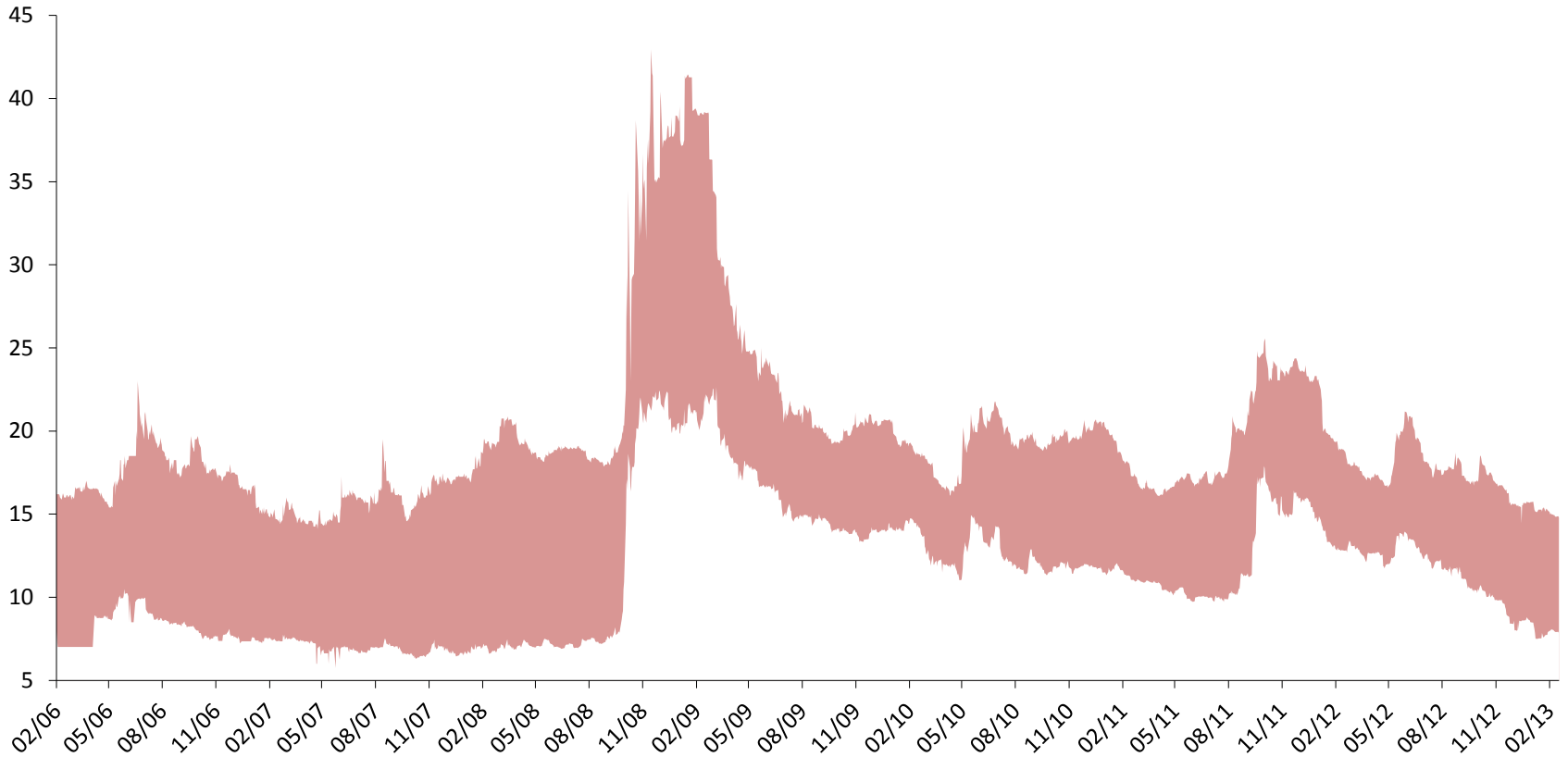


Source: Bloomberg.

Last Observation: January 2013

FX Volatility

FX Volatility in Emerging Market Economies with CAD (Percent, Implied for the next 12 months)

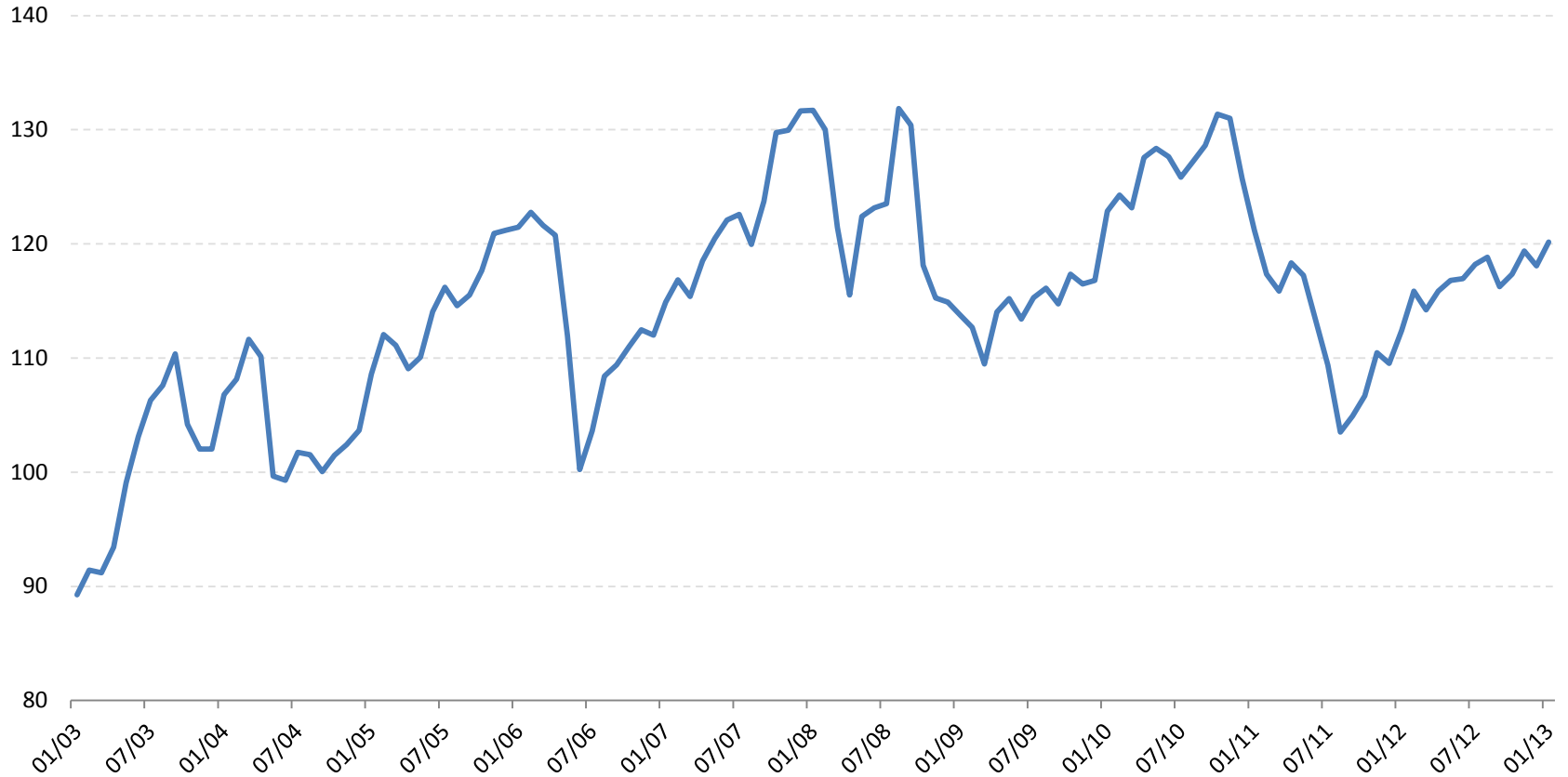


Source: Bloomberg, CBRT.

Emerging market economies that are running current account deficit are: Brazil, Chile, Colombia, Mexico, Poland, Czech Rep., S. Africa, Indonesia, Romania and Turkey.

Real Effective Exchange Rate (REER)

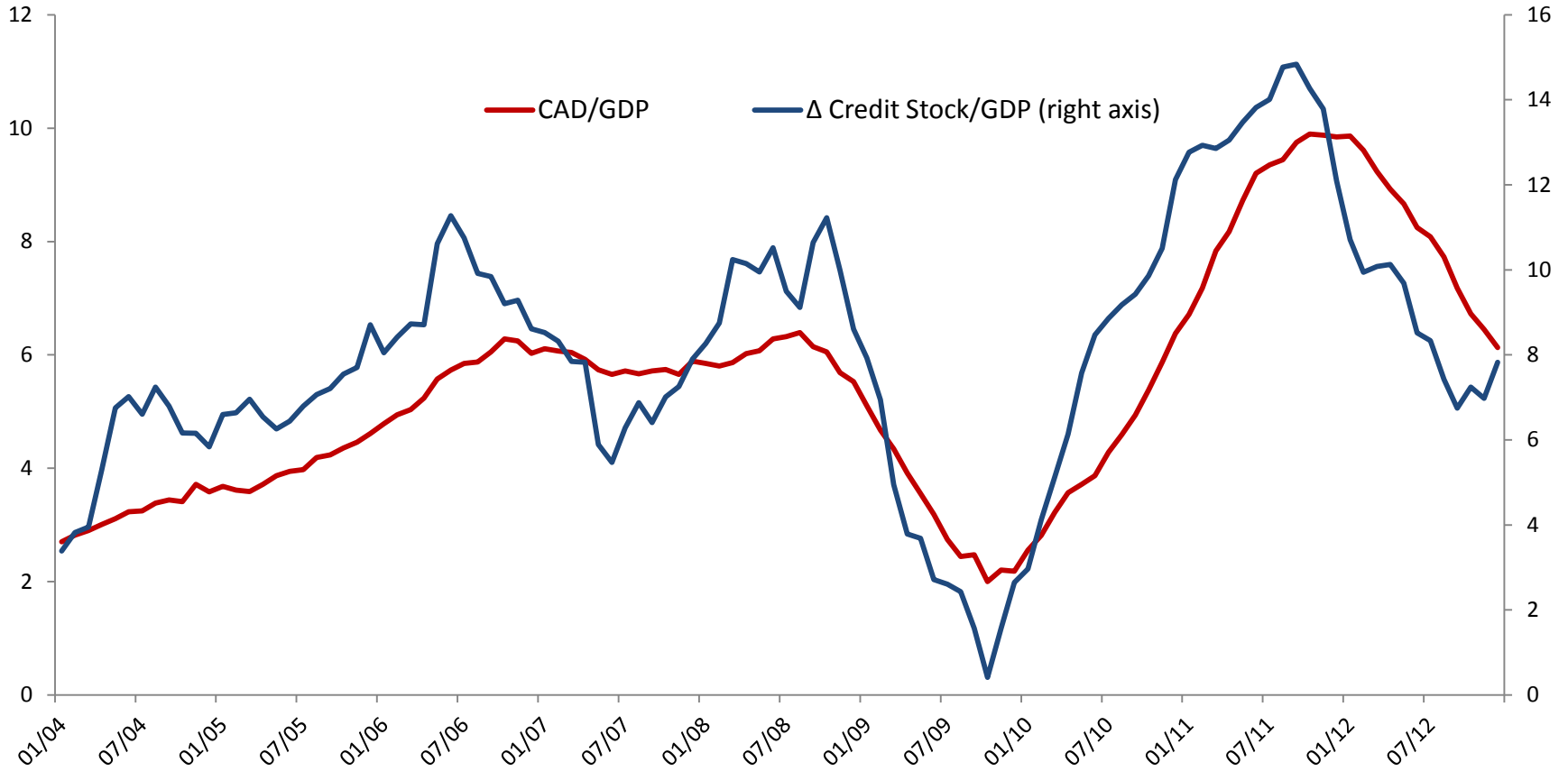
CPI Based REER (Base year: 2003)



Source: CBRT.

Credit Growth

Credit Growth and Current Account Deficit (Percent, 12-Month Cumulative)

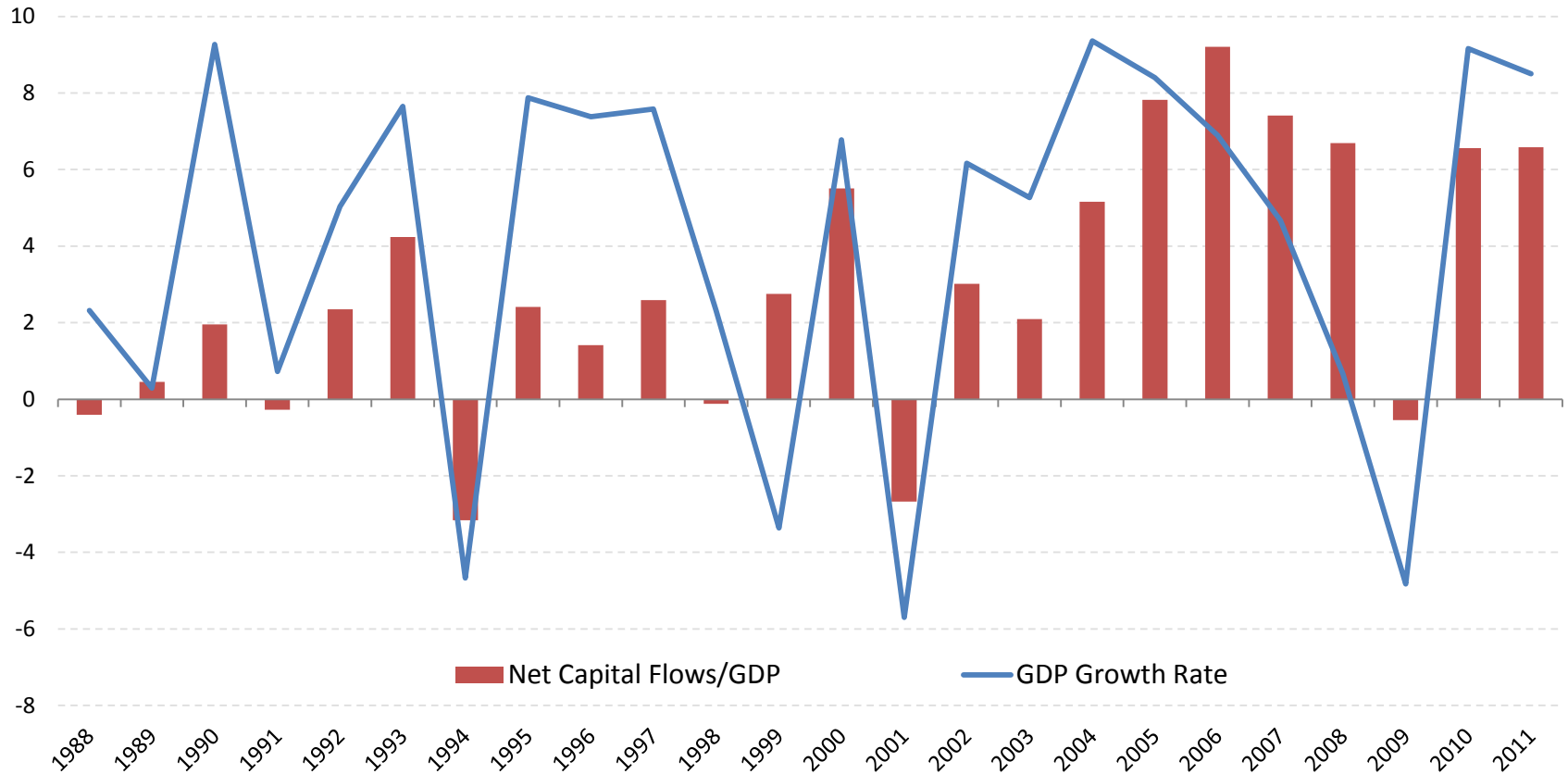


Source: CBRT.

Last Observation: December 2012

GDP Growth

Capital Flows and GDP Growth in Turkey (Percent, Annual)



Source: CBRT

THE POLICY FRAMEWORK

Policy Framework

	Old Approach	New Approach
Objectives	Price Stability	Price Stability Financial Stability
Policy Tools	Policy Rate	Structural Tools Cyclical Tools

Structural Tools

- Maturity Based Reserve Requirements
- Leverage Based Reserve Requirements
- Reserve Options Mechanism

Cyclical Tools

- Policy Rate
- Interest Rate Corridor
- TL Liquidity Management
- FX Liquidity Management

Maturity Based Reserve Requirements

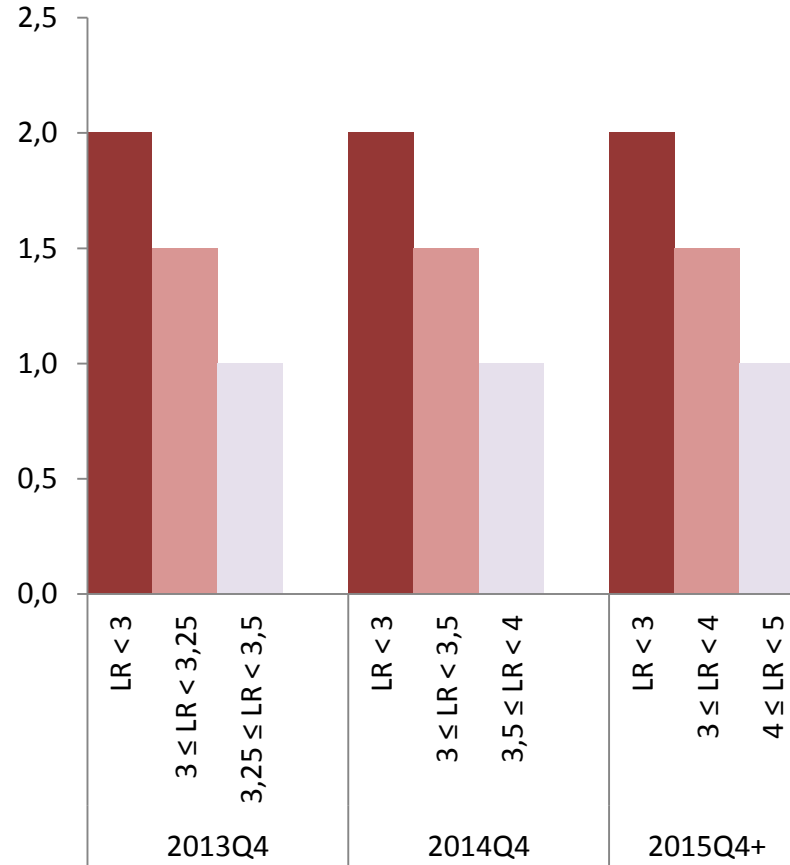
Core Liabilities

	M < 1 year	M ≥ 1 year
TL	11.17%	5%
FX	12.5%	9%

Non-Core Liabilities

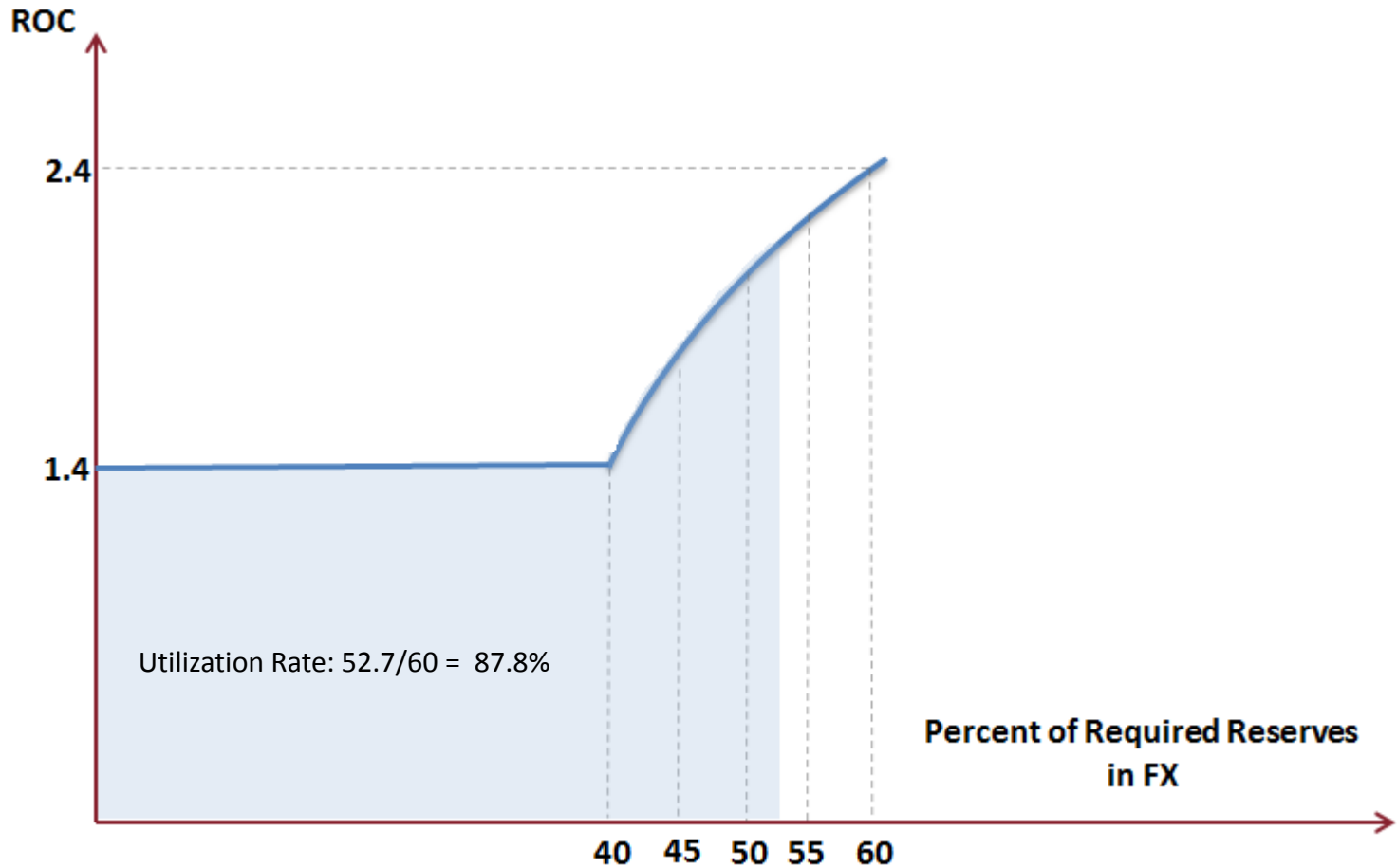
	M < 1 year	M ≥ 1 year
TL	11.5%	6.81%
FX	12.27%	6%

Leverage Based Reserve Requirements



Reserve Options Mechanism - FX

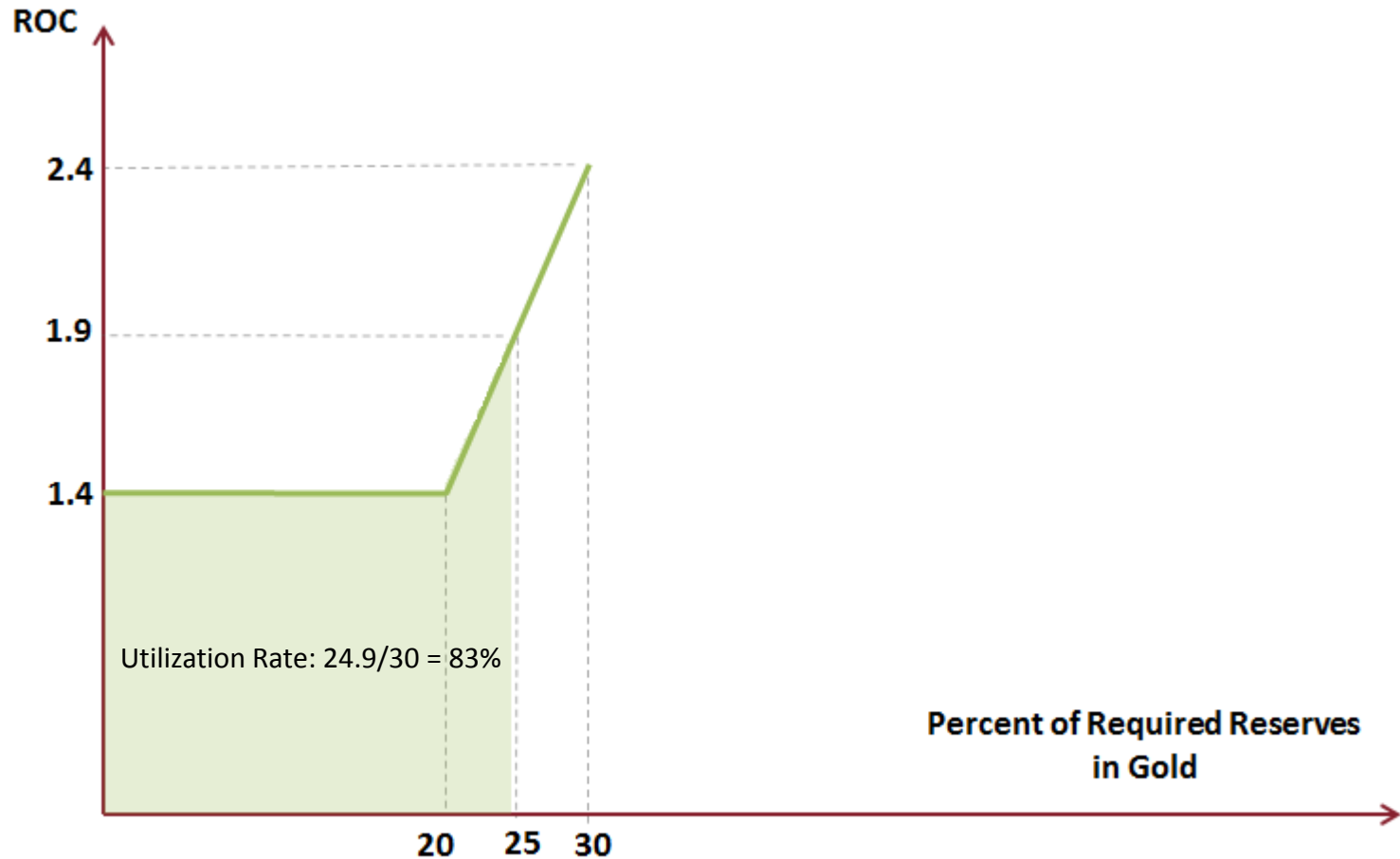
Reserve Option Coefficients (ROC)



Last Observation: February 15, 2013

Reserve Options Mechanism - Gold

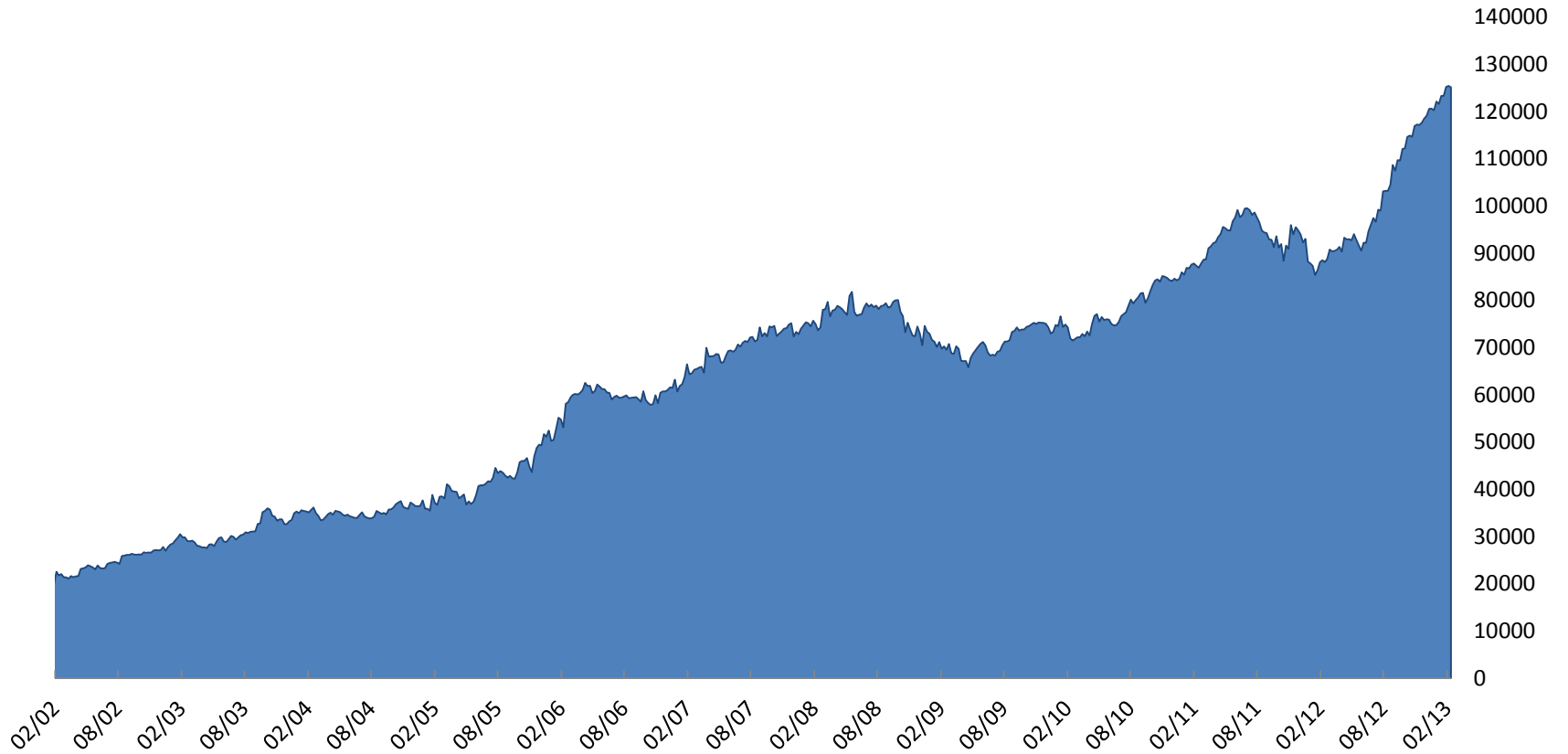
Reserve Option Coefficients (ROC)



Last Observation: February 15, 2013

CBRT Reserves

FX and Gold Reserves (Million USD)

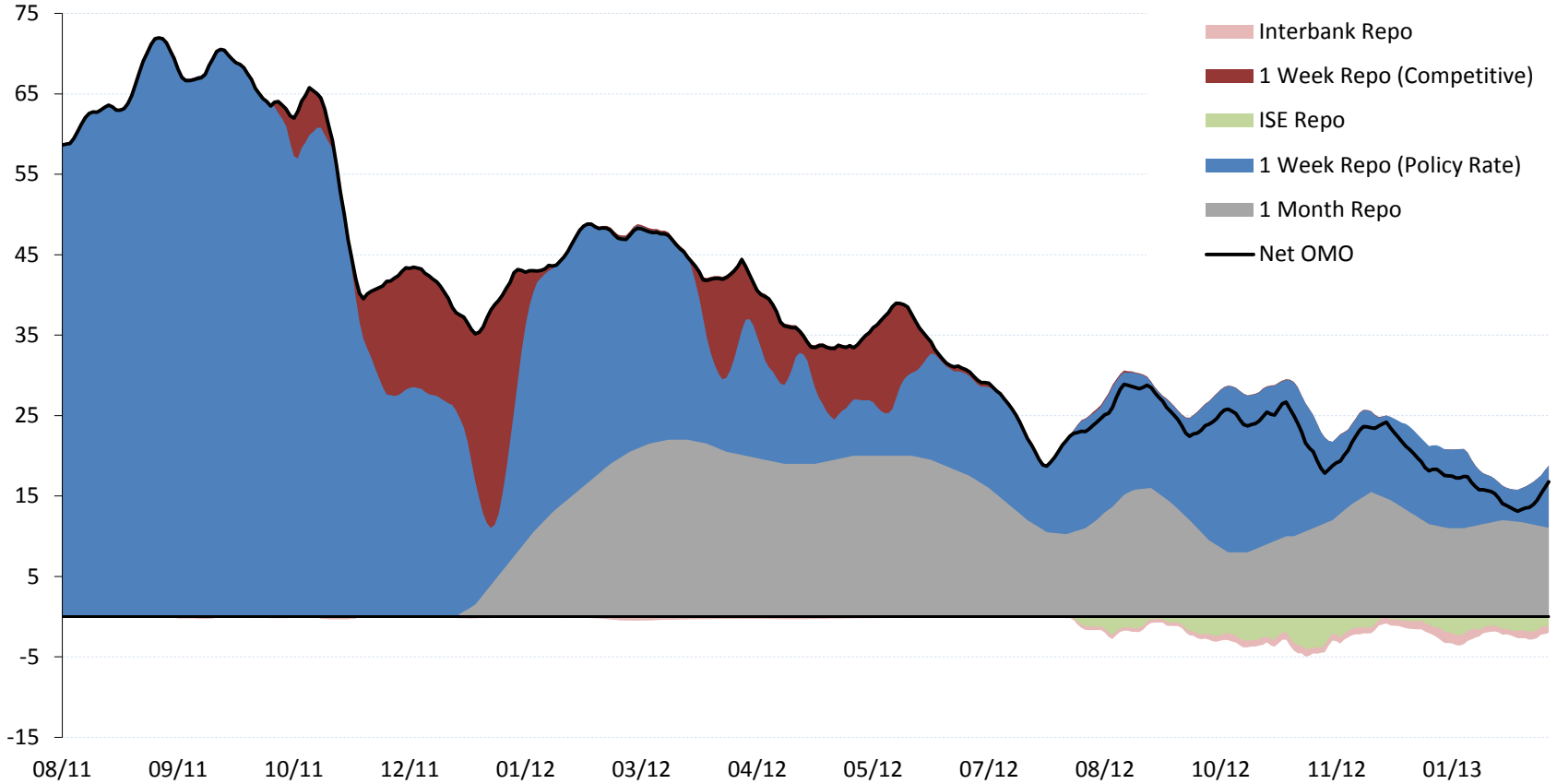


Source: CBRT

Last Observation: February 15, 2013

Liquidity Management

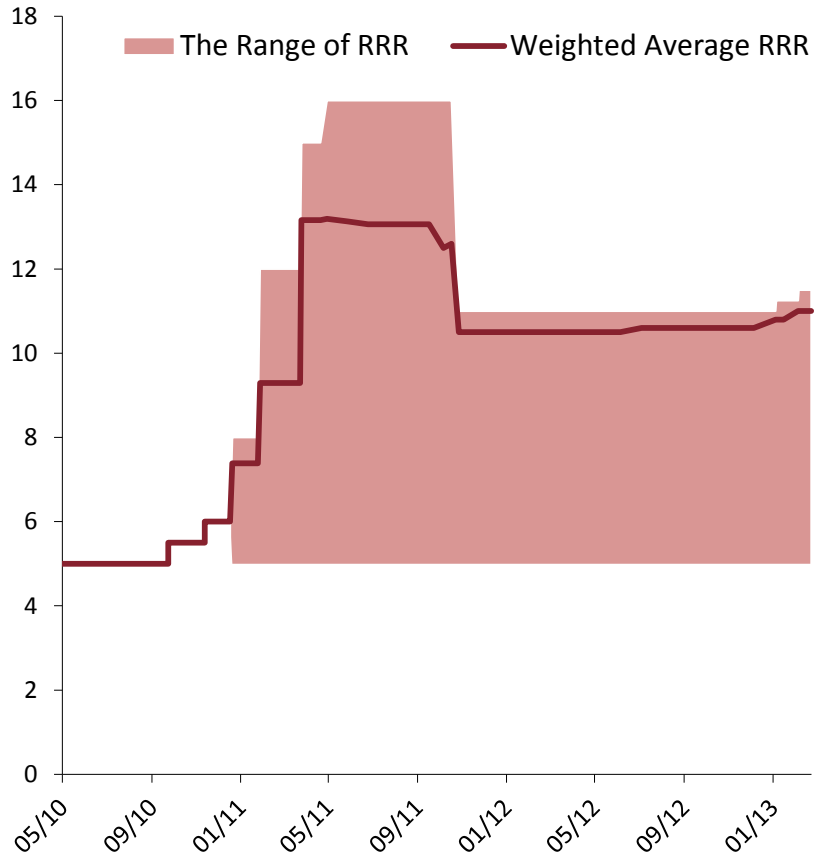
CBRT Funding (Billion TRY)



Source: CBRT

Liquidity Management

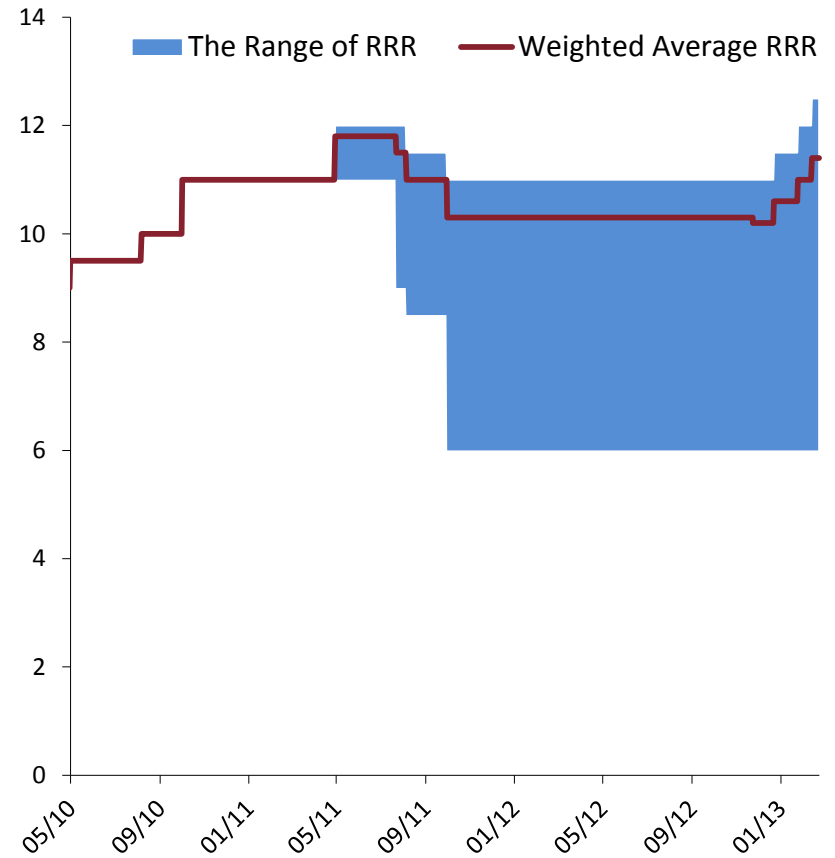
TL Reserve Requirements



Source: CBRT.

Last Observation: February 2013

FX Reserve Requirements

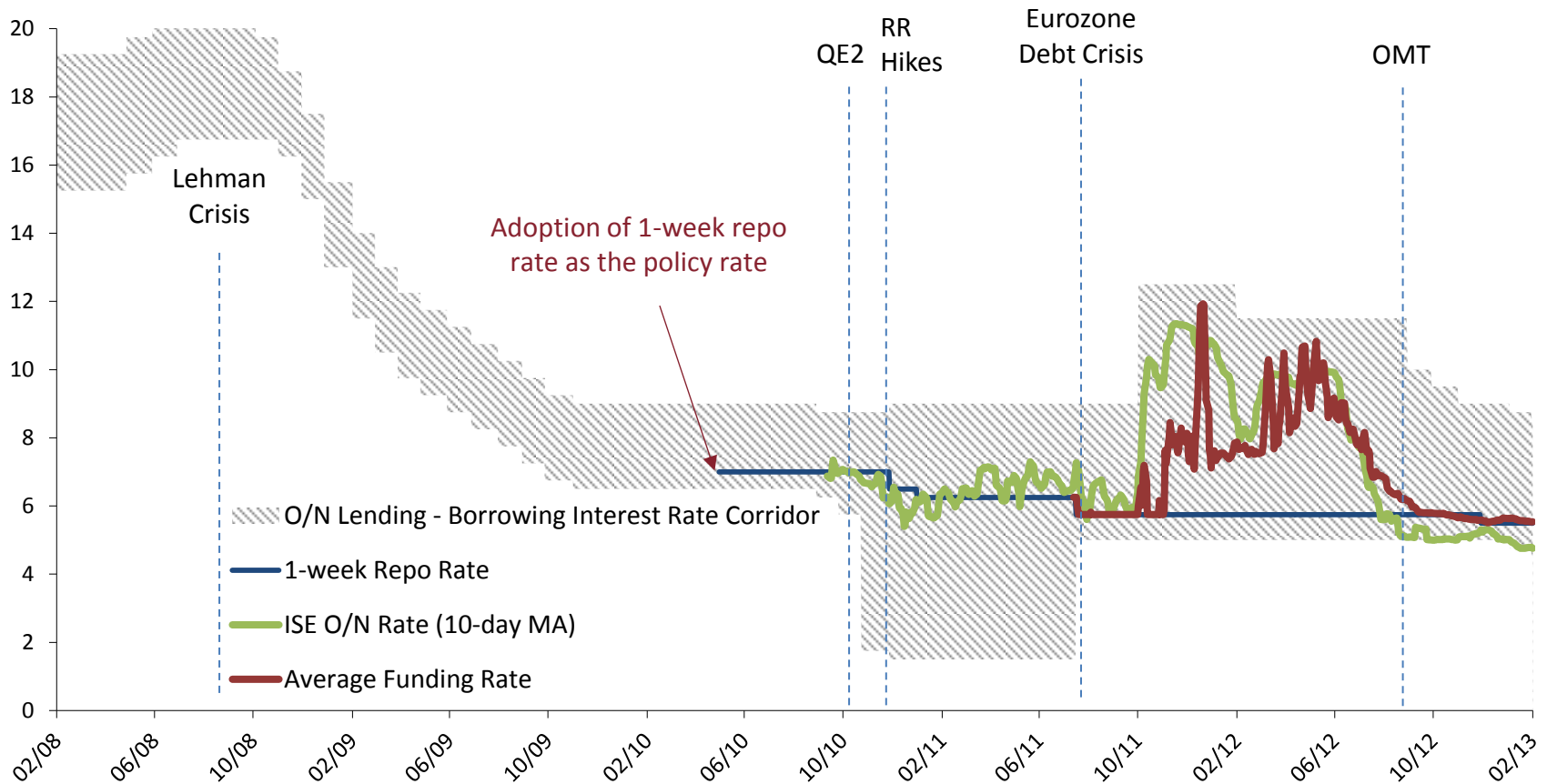


Source: CBRT.

Last Observation: February 2013

Liquidity Management

Interest Rate Corridor and Average Funding Rate (Percent)



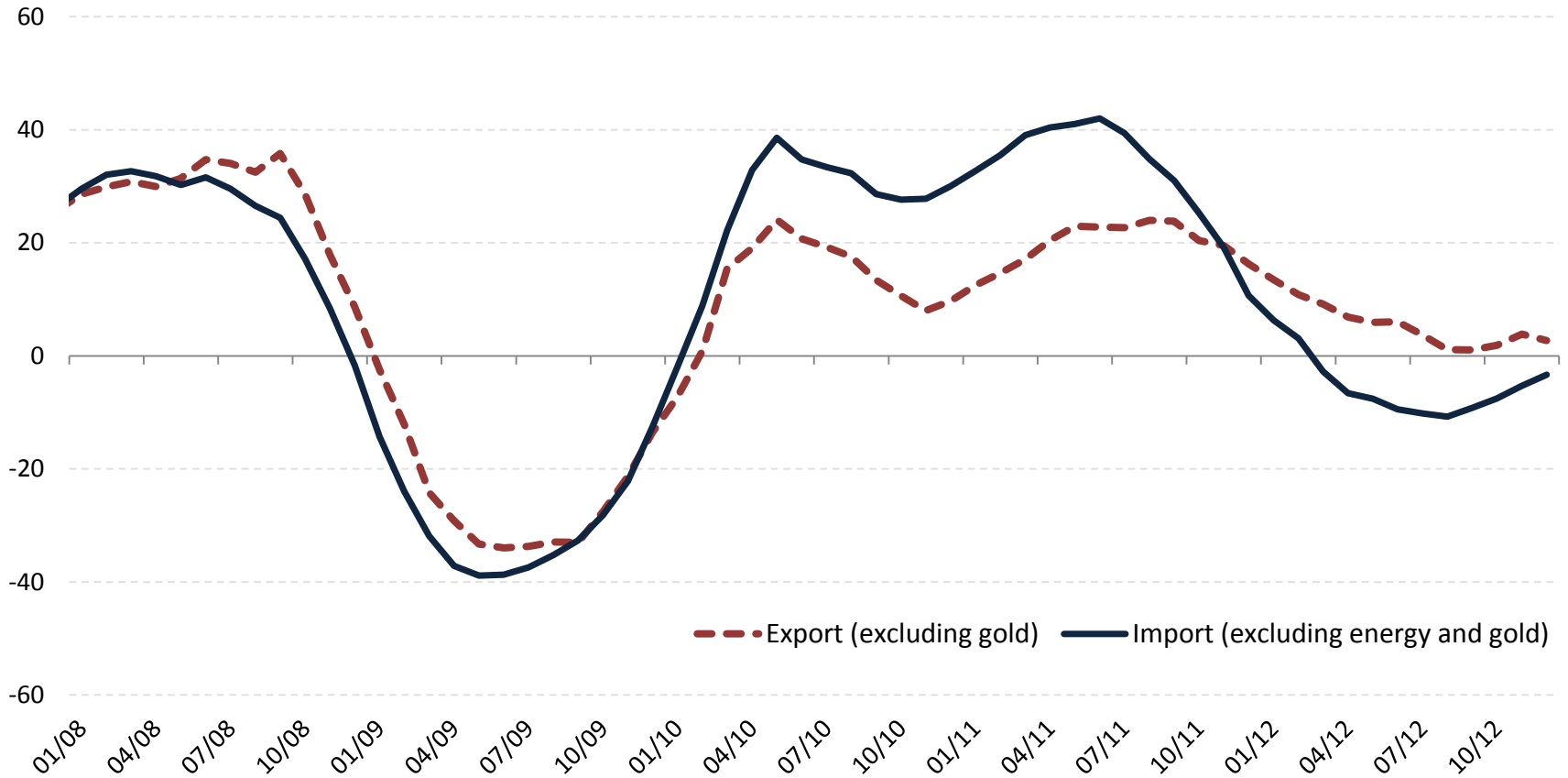
Source: ISE, CBRT.

Last Observation: February 20, 2013

REBALANCING

Rebalancing

Exports and Imports (Nominal, 6-Month MA, YoY % Change)

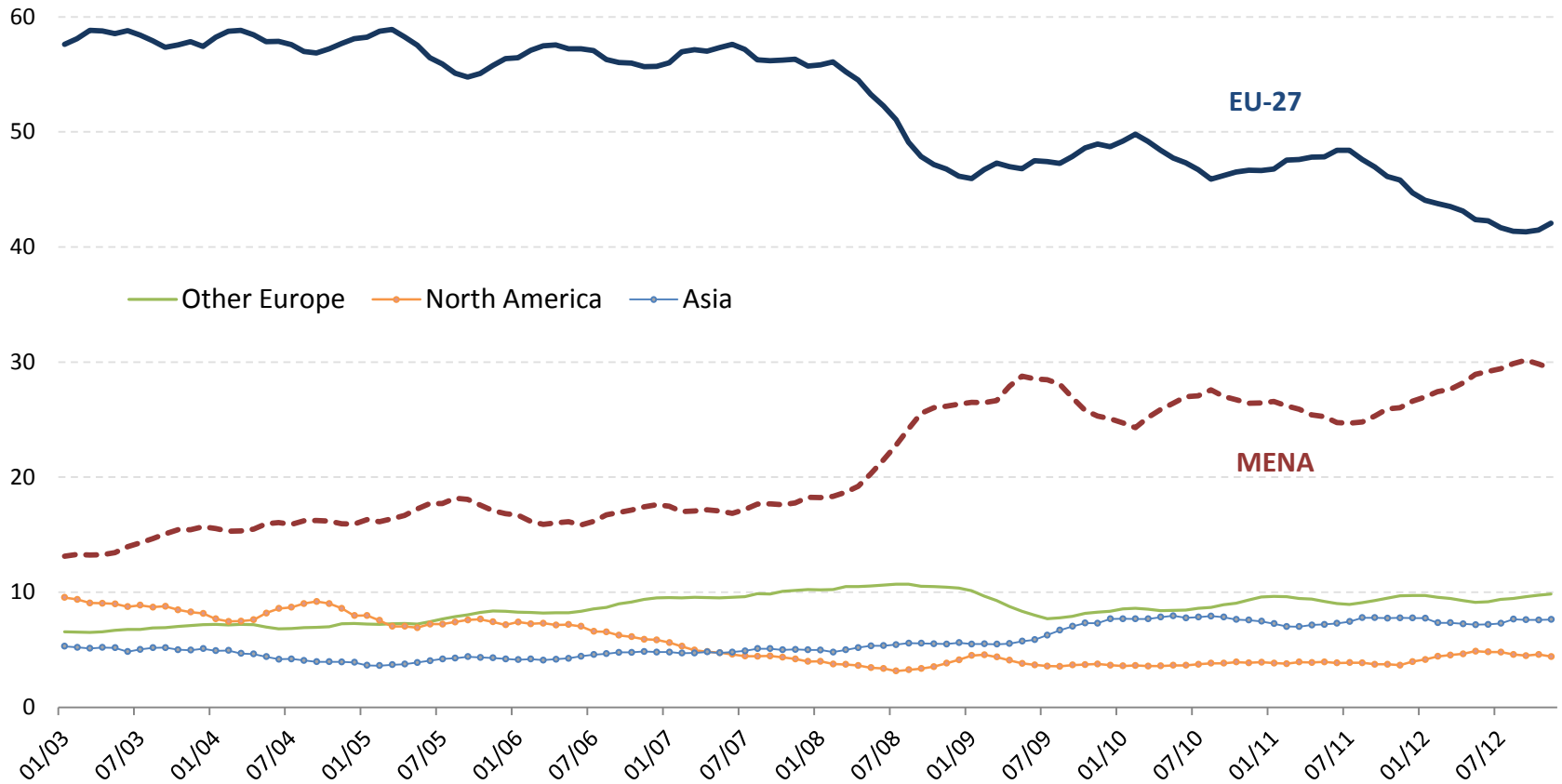


Source: TURKSTAT.

Last Observation: December 2012

Market Diversification

Exports Market Share* (6-Month Cumulative, Percent)



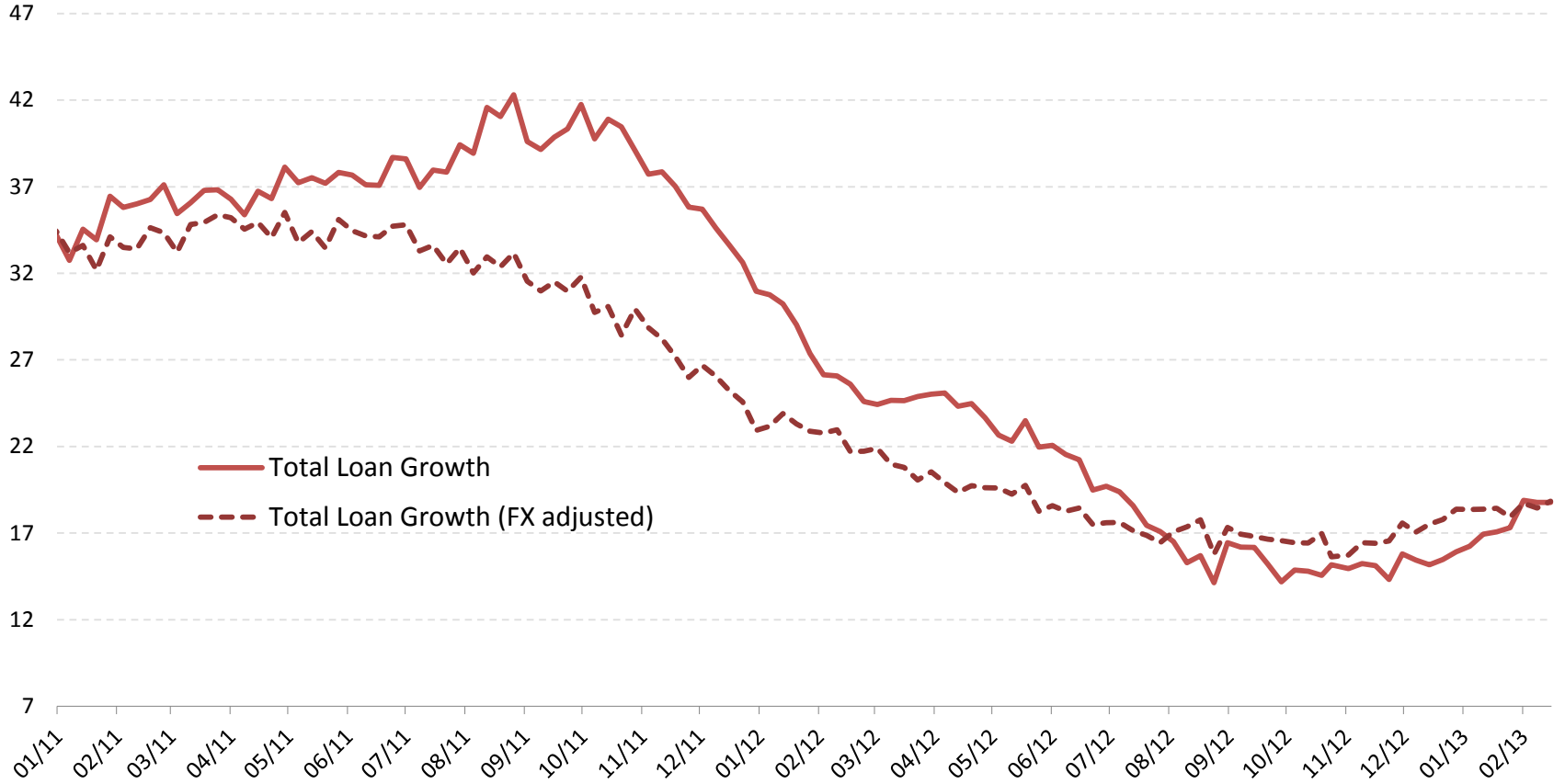
Source: TurkStat

Last Observation: November 2012

*Excluding gold.

Credit Growth

Total Loan* Growth (Year on Year Change, Percent)



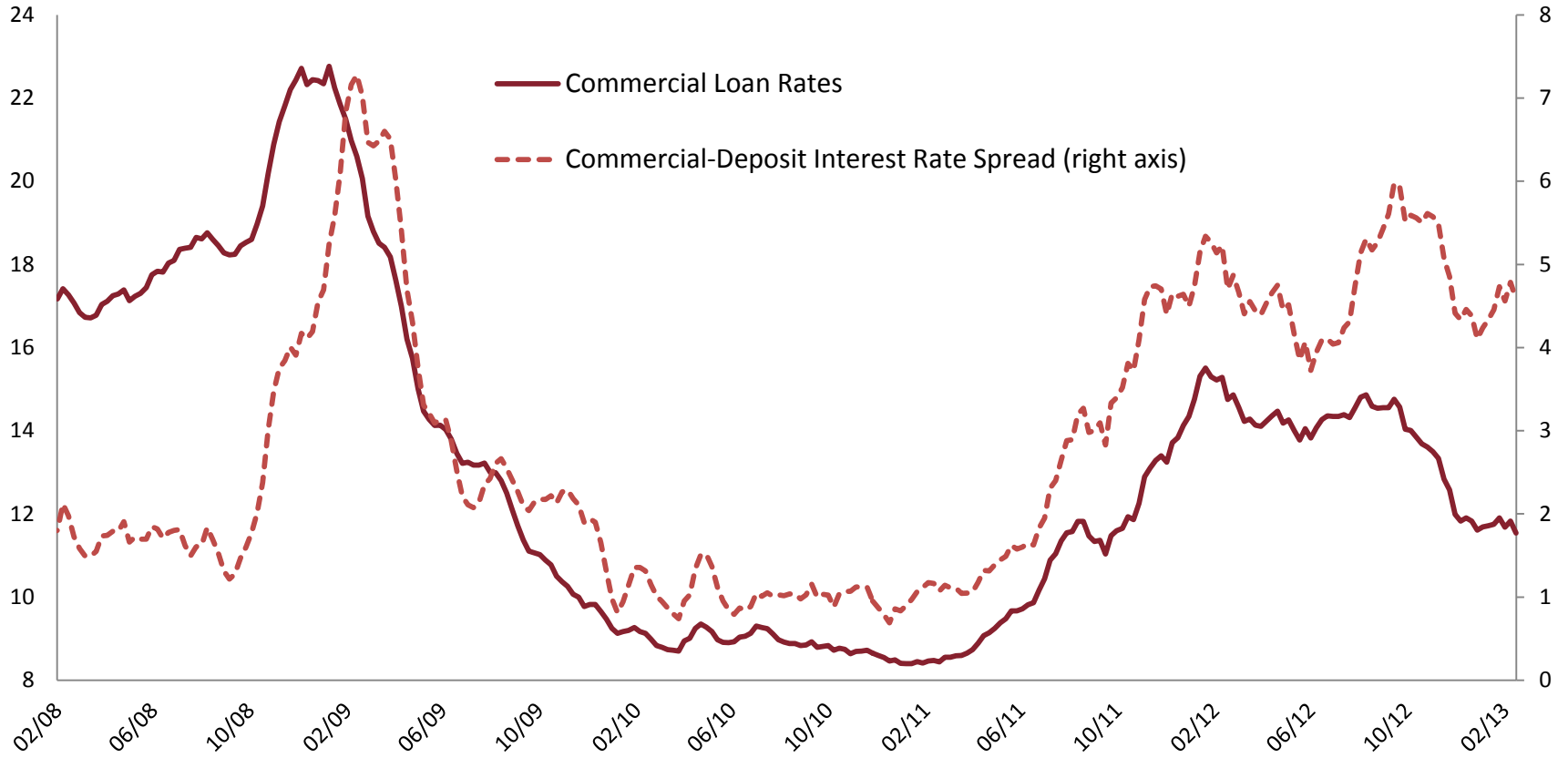
Source: CBRT.

*Total banking sector, credit cards included, NPLs excluded.

Last Observation: February 15, 2013.

Credit-Deposit Rate Spread

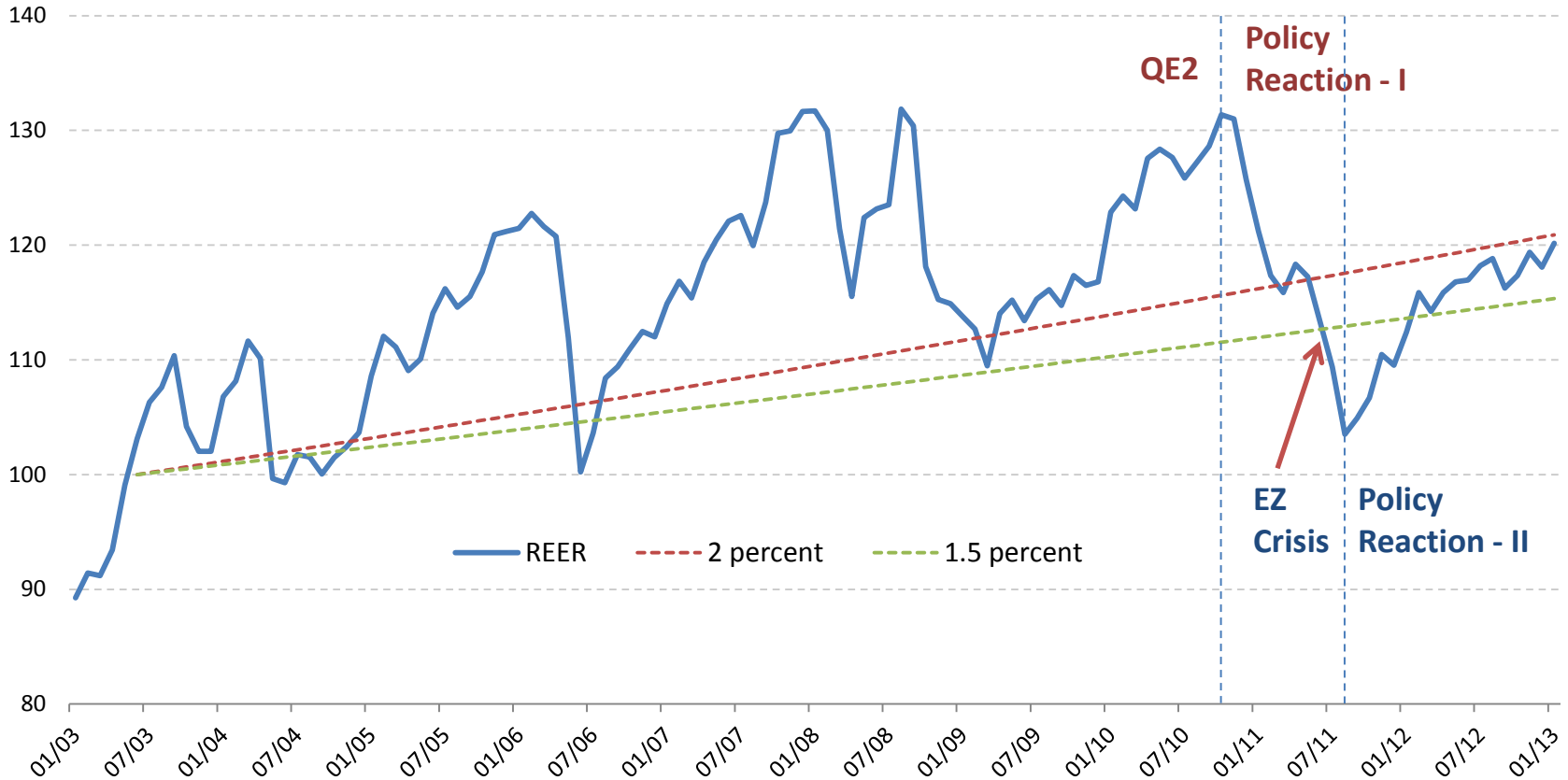
Commercial Loan Rates and Deposit Rate Difference (4-Week Moving Average, Percent)



Source: BRSA, CBRT.

Real Effective Exchange Rate (REER)

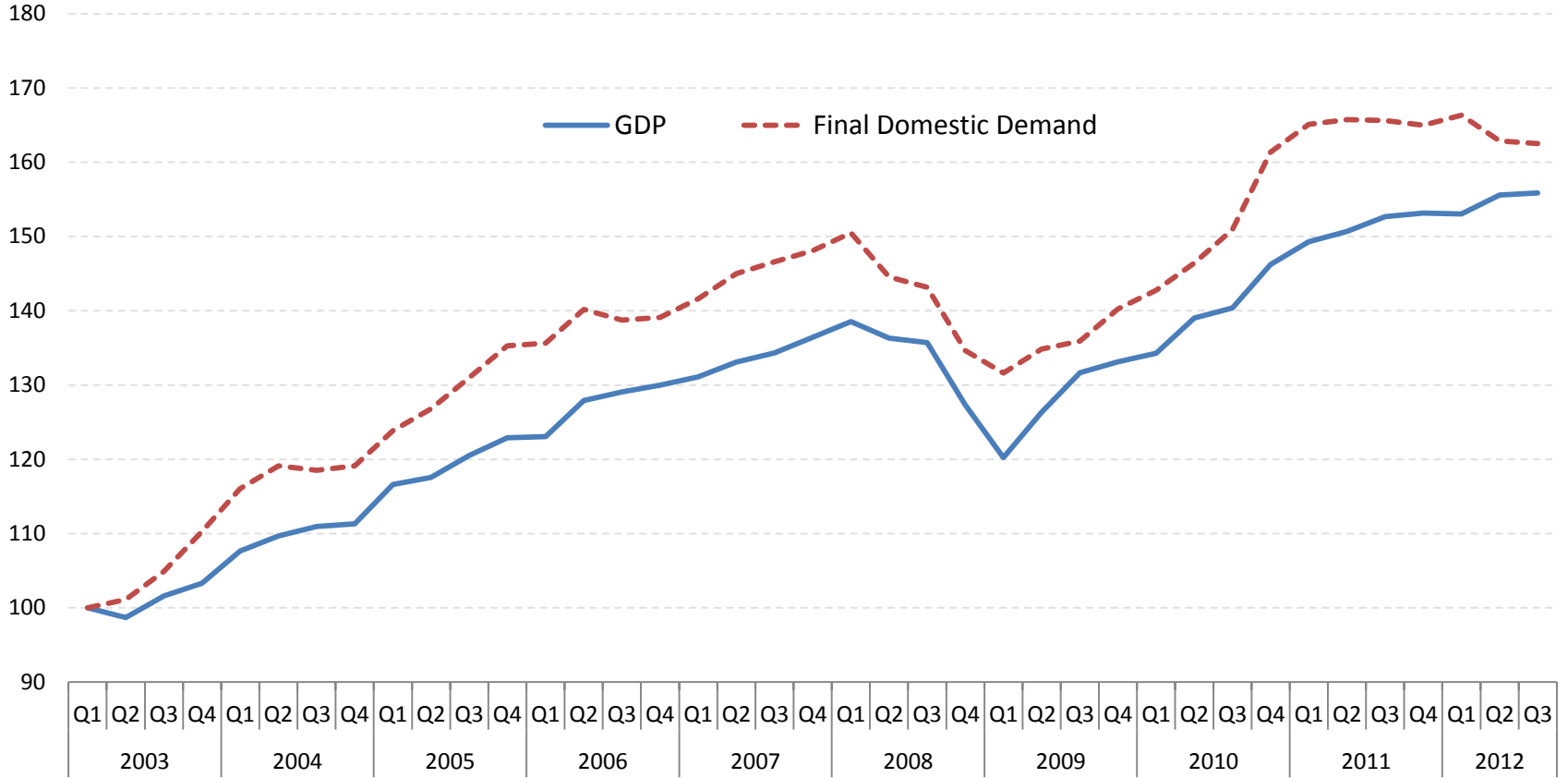
CPI Based REER (Base year: 2003)



Source: CBRT.

Rebalancing

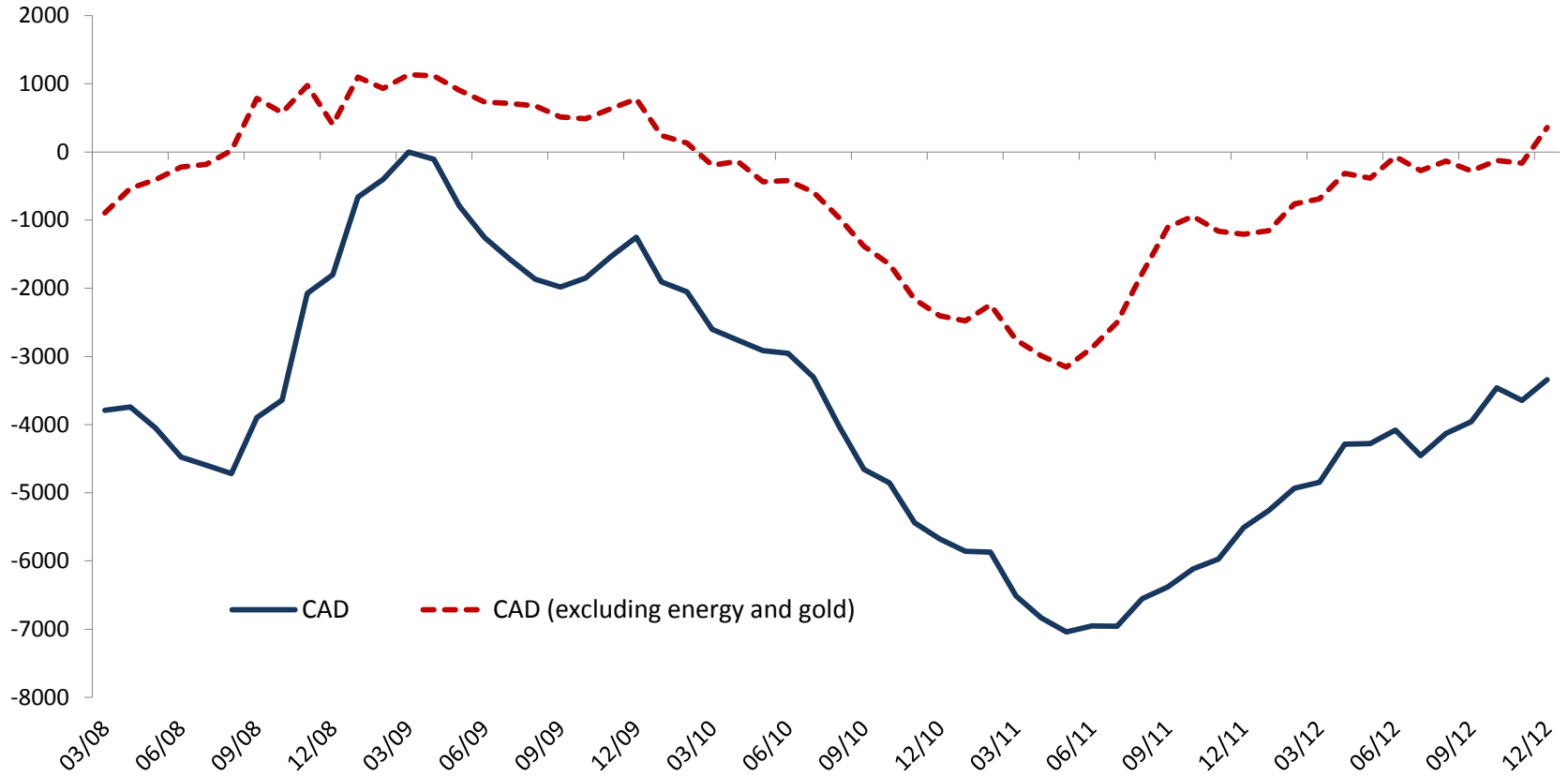
Final Domestic Demand and GDP (Seasonally Adjusted, 2003Q1=100)



Source: TurkStat, CBRT.

Rebalancing

Current Account Balance
(Seasonally Adjusted, 3-Month Average, Million USD)

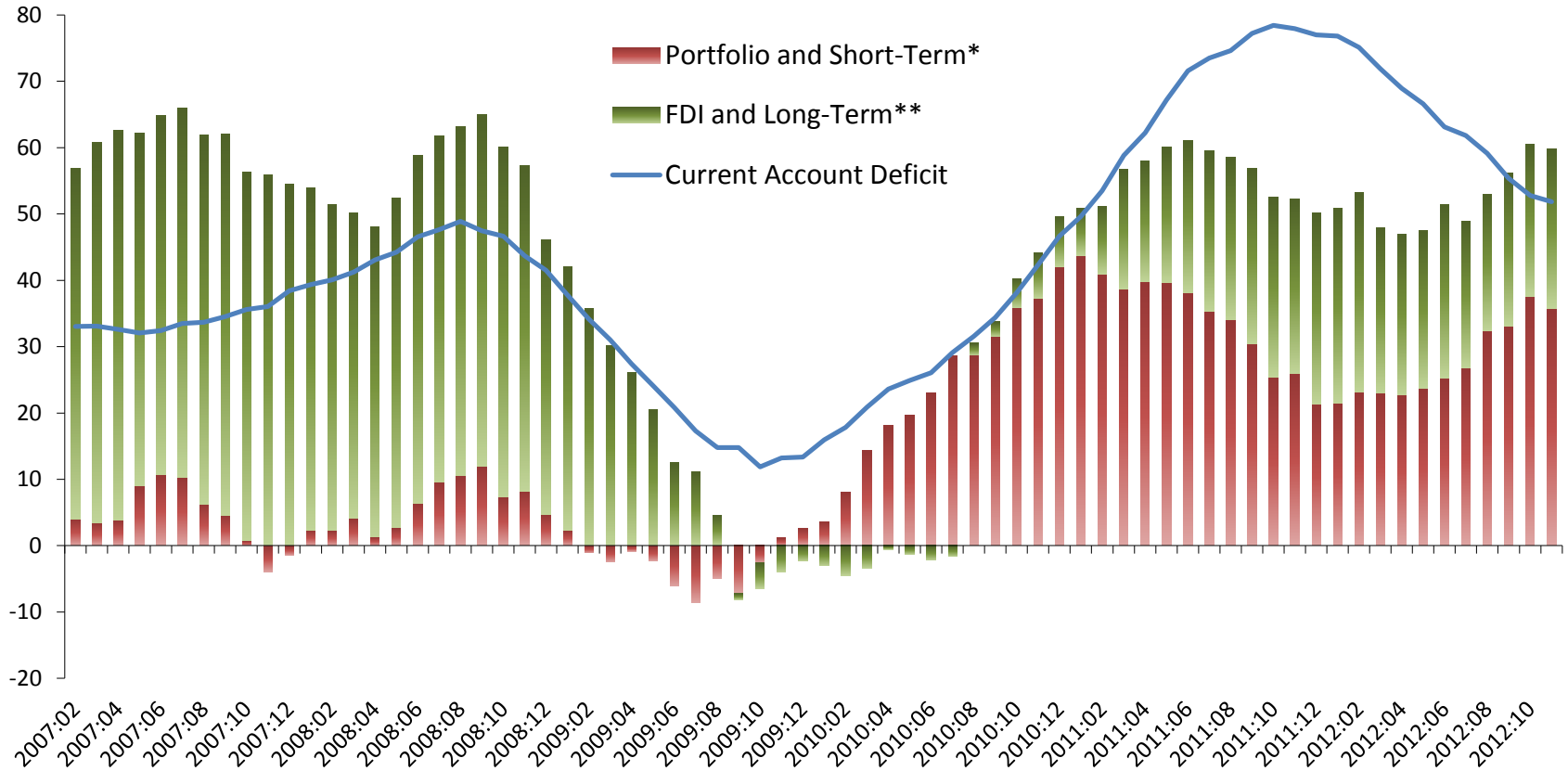


Source: CBRT.

Last Observation: December 2012

Quality of Capital Inflows

Main Sources of Current Account Deficit Finance (12-Month Cumulative, Billion USD)



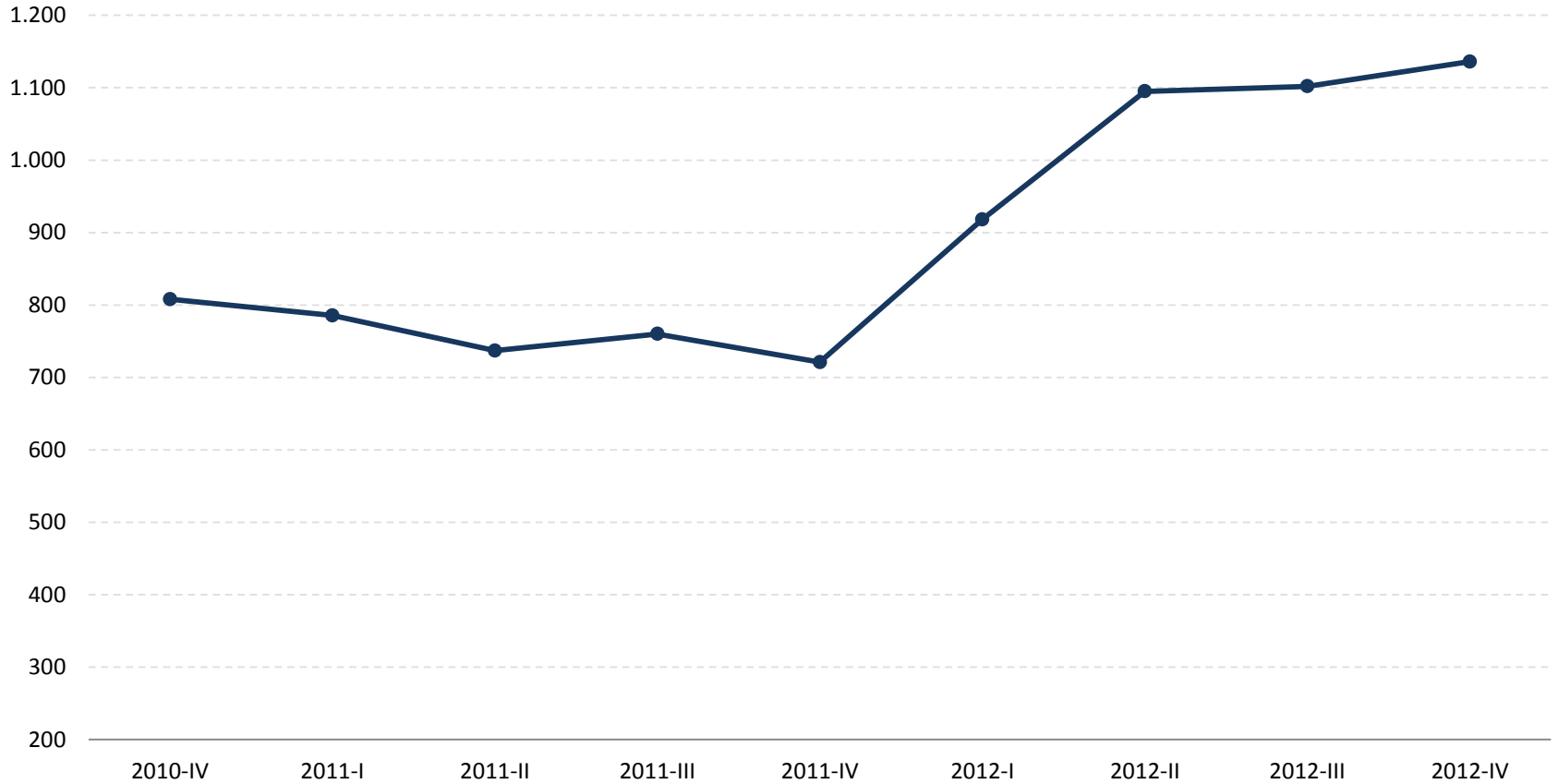
Source: CBRT.

*Short-term capital movements are sum of banking and real sectors' short term net credit and deposits in banks.

**Long-term capital movements are sum of banking and real sectors' long term net credit and bonds issued by banks and the Treasury.

Maturity of Non-Residents' Bond Holdings

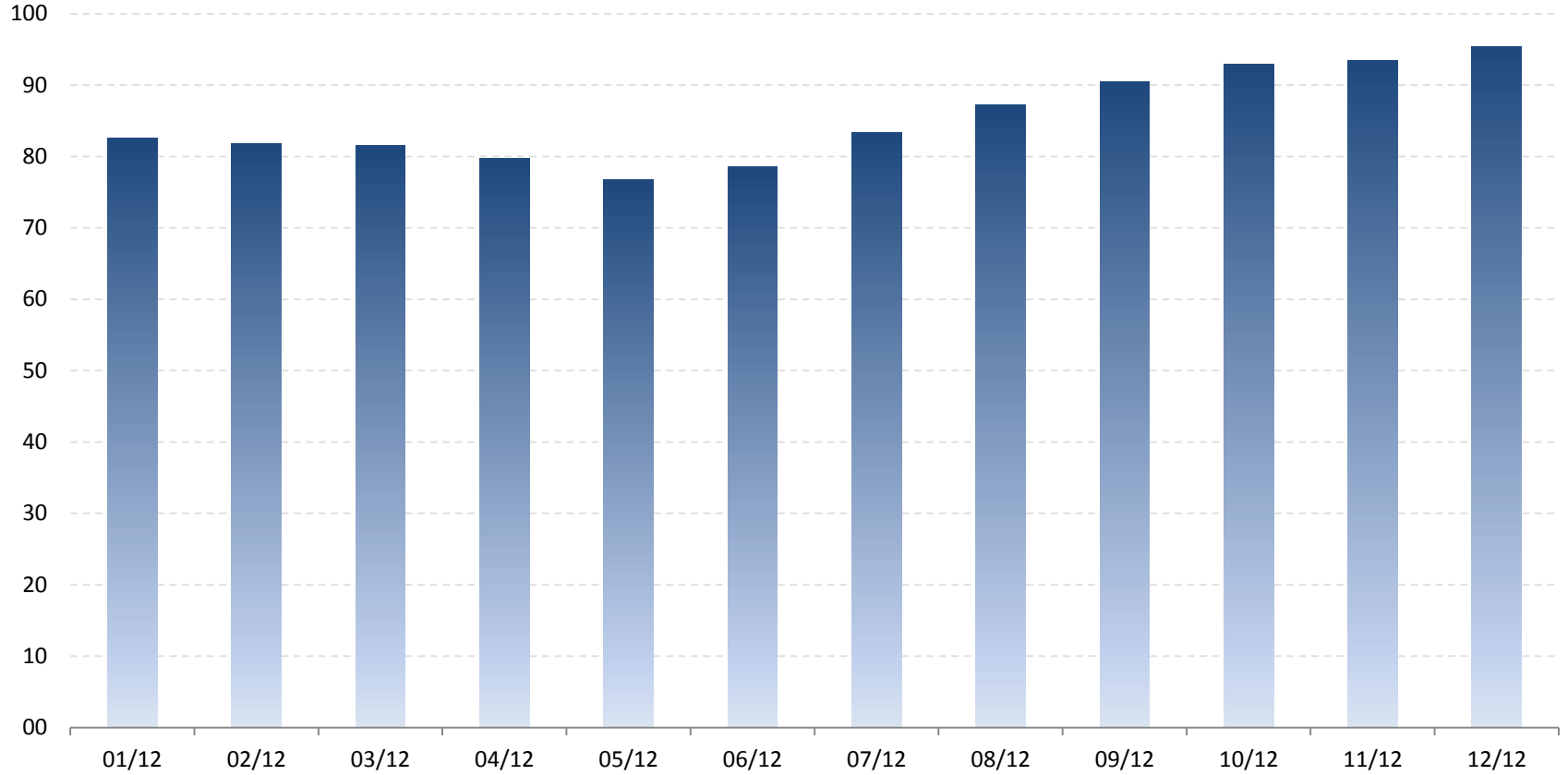
Average Maturity (Days)



Source: CBRT.

Greenspan-Guidotti Ratio

Ratio of International Reserves to Short-Term Foreign Debt (Percent)



Source: CBRT

INFLATION

Core Inflation

Annual Change

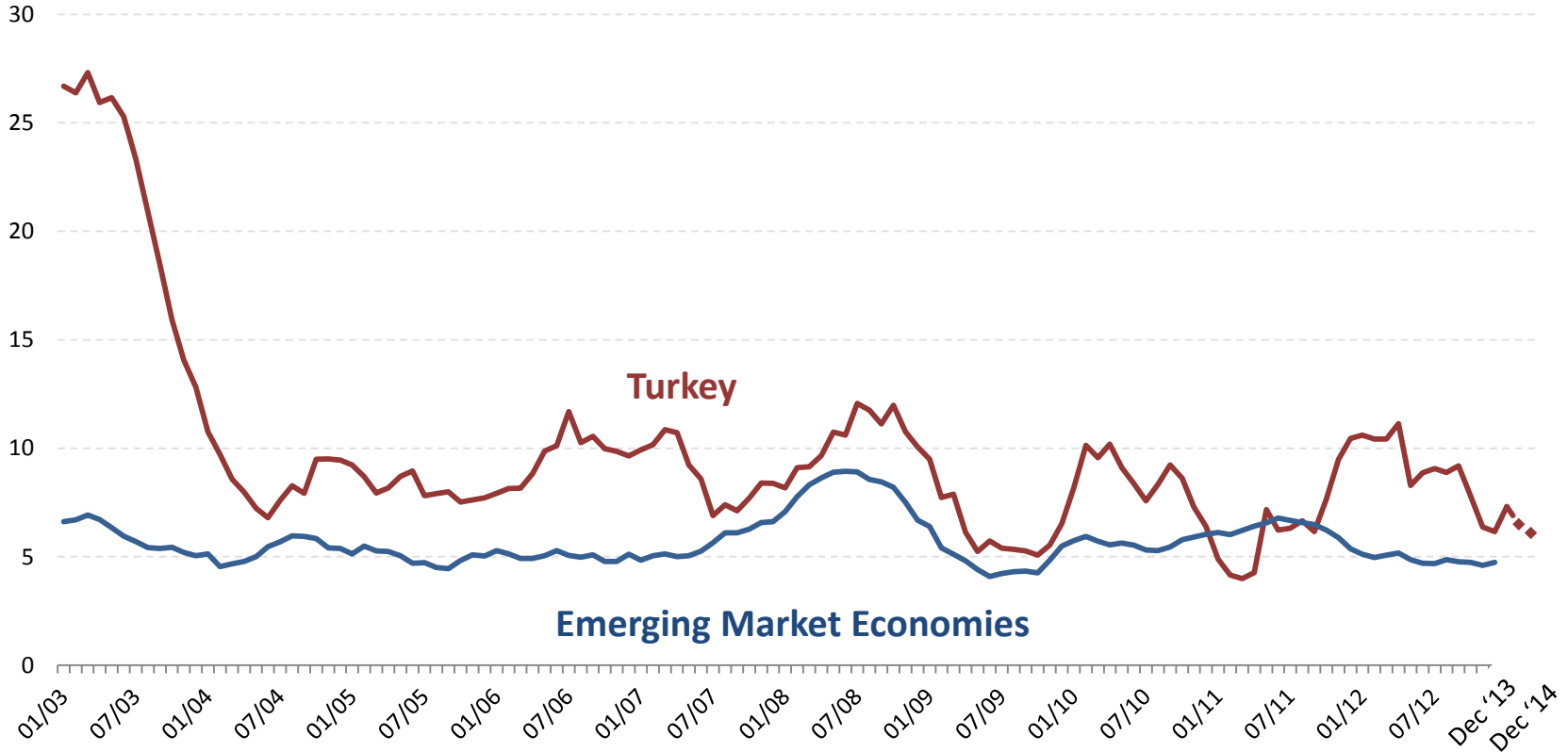


Source: TURKSTAT, CBRT.

Last Observation: January 2013

Inflation

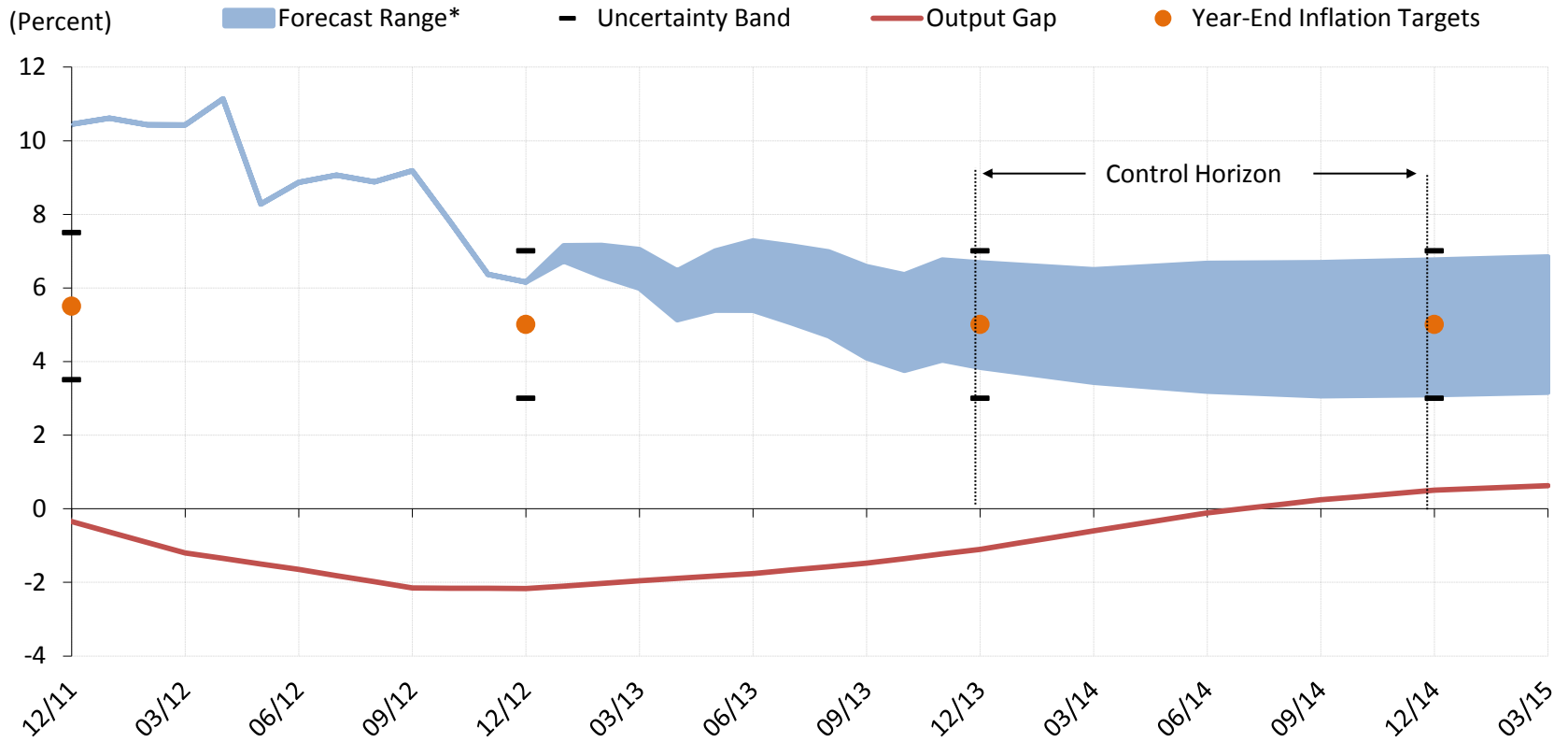
Inflation in Turkey vs. Emerging Market Economies (Percent, Weighted Average)



Source: Bloomberg, CBRT.

Emerging Market Economies: Brazil, Mexico, Czech Rep., Hungary, Poland, S. Africa, China, India, Russia, Turkey, Indonesia, Argentina, Thailand, Malaysia, Colombia, Romania, Ukraine, Vietnam, Chile, Peru, Egypt, Morocco, Lebanon, S. Arabia . *Forecasts for end-2013 and end-2014 are taken from "Consensus Forecasts".

Inflation Forecast

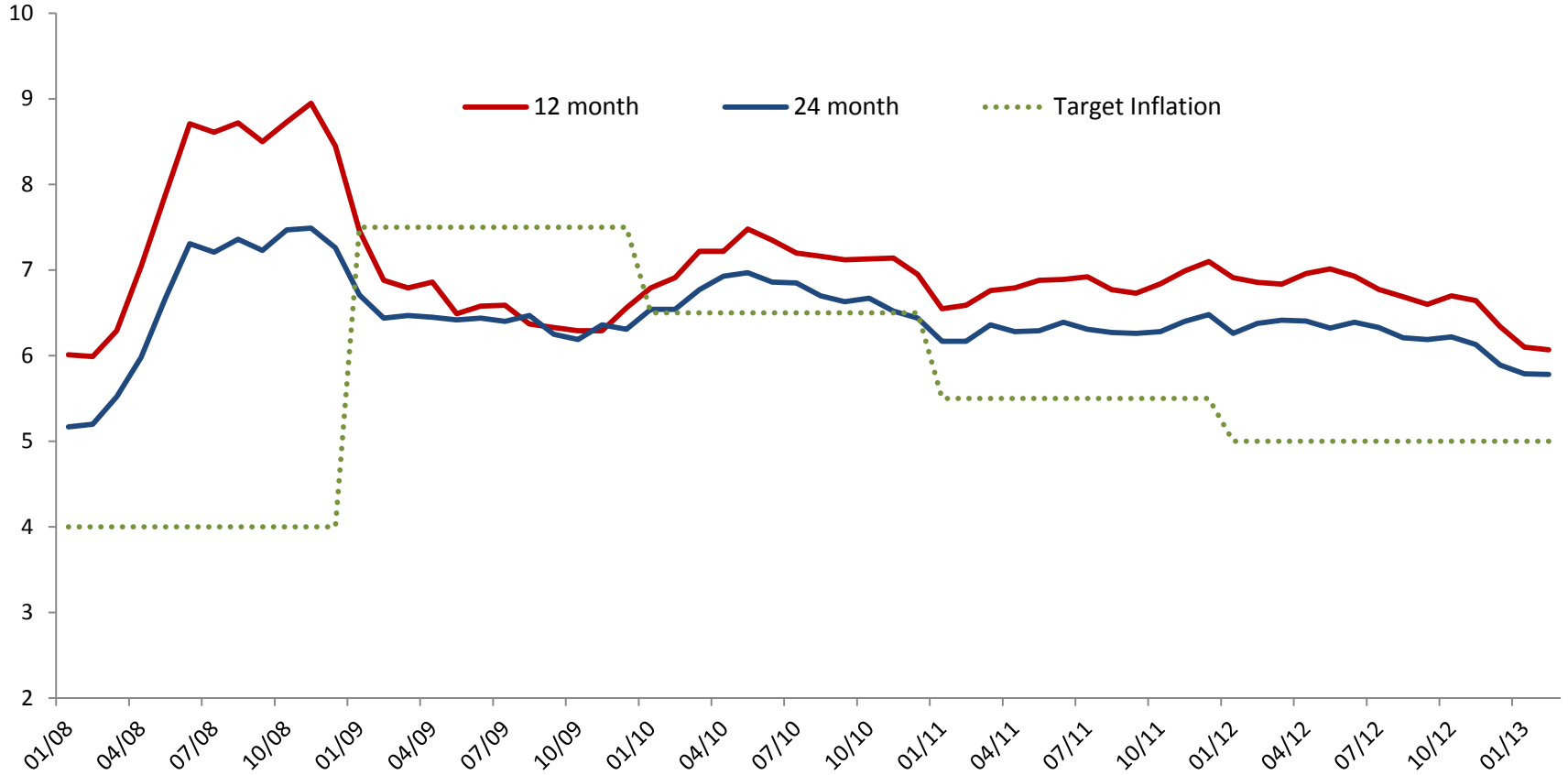


Source: CBRT.

*Shaded region indicates the 70 percent confidence interval for the forecast.

Inflation Expectations

Medium Term Inflation Expectations* (Percent)



Source: CBRT.

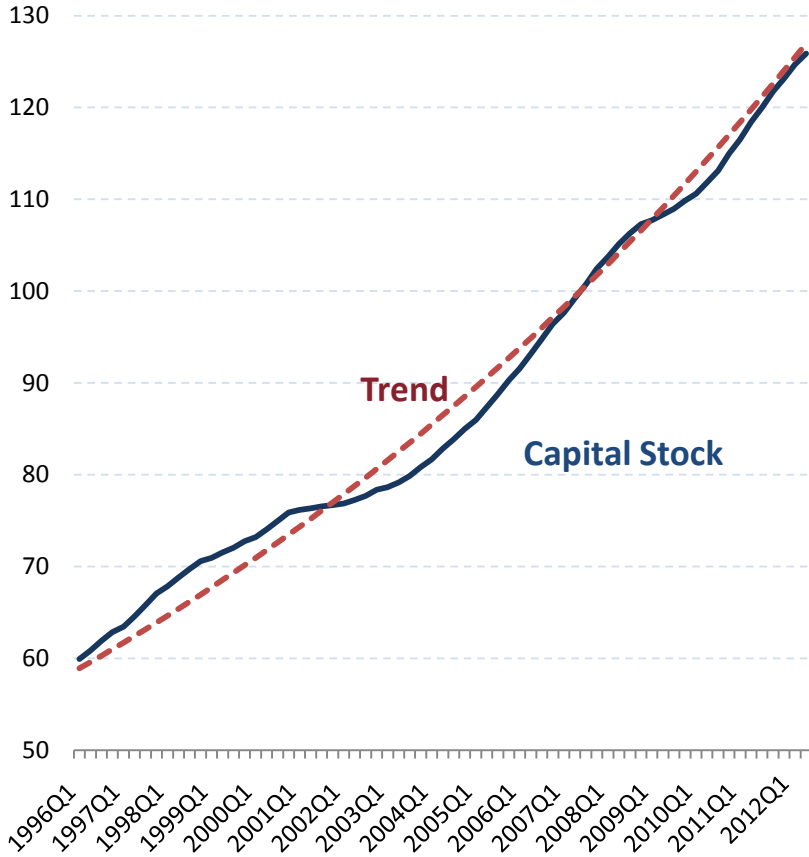
Last Observation: February 2013

*CBRT Survey of Expectations.

GROWTH

Capital

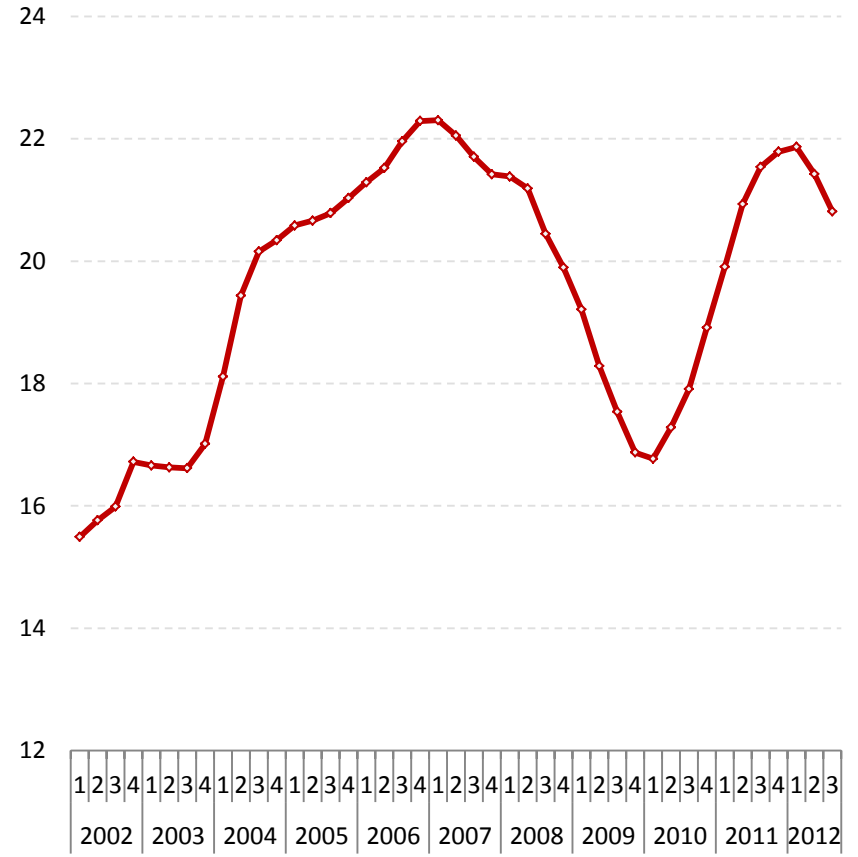
Capital Stock
(Constant Prices, 2007=100)



Source: TURKSTAT, CBRT.

Last Observation: 2012 Q3

Fixed Capital Formation*
(Percent, Ratio to GDP, Current Prices)

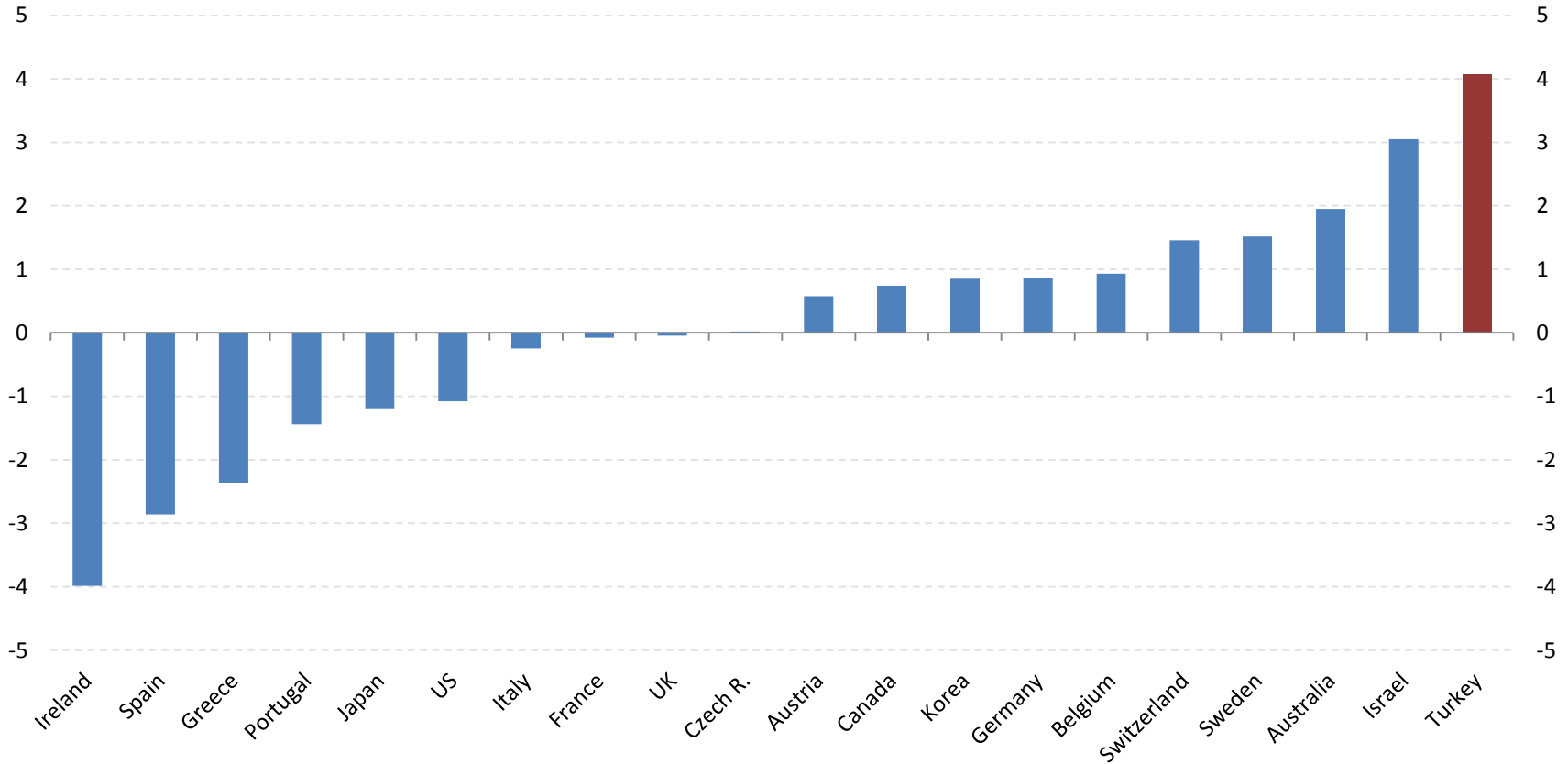


Source: TURKSTAT, CBRT.

*Annualized
Last Observation : 2012 Q3

Employment

Annual Average Growth of Employment* (Percent Growth, 2007-2011)

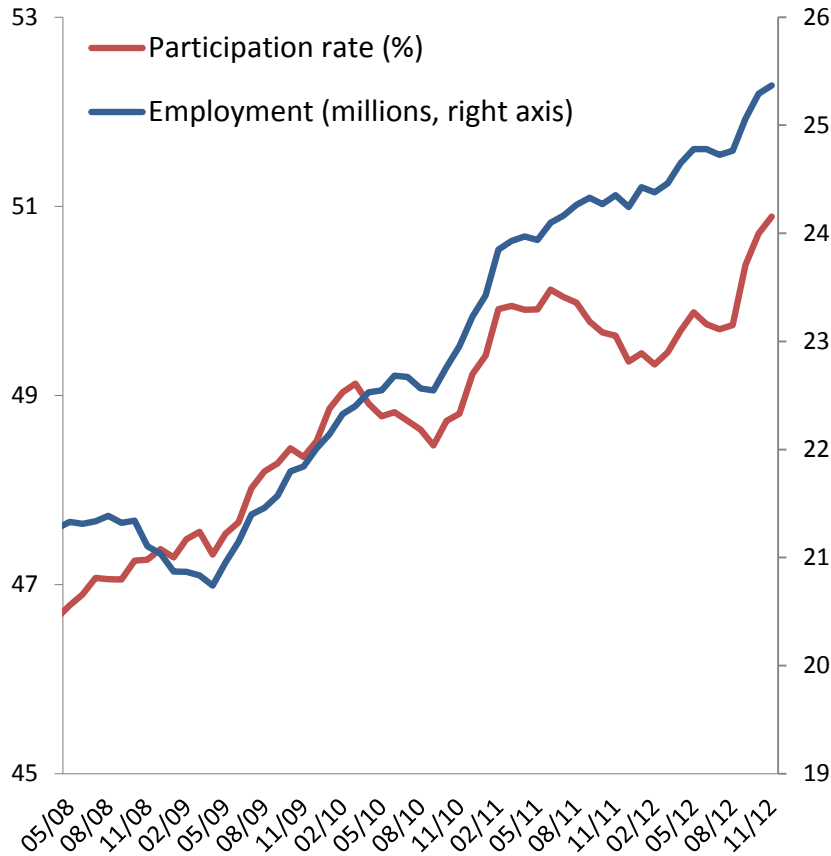


Source: IMF WEO, TURKSTAT.

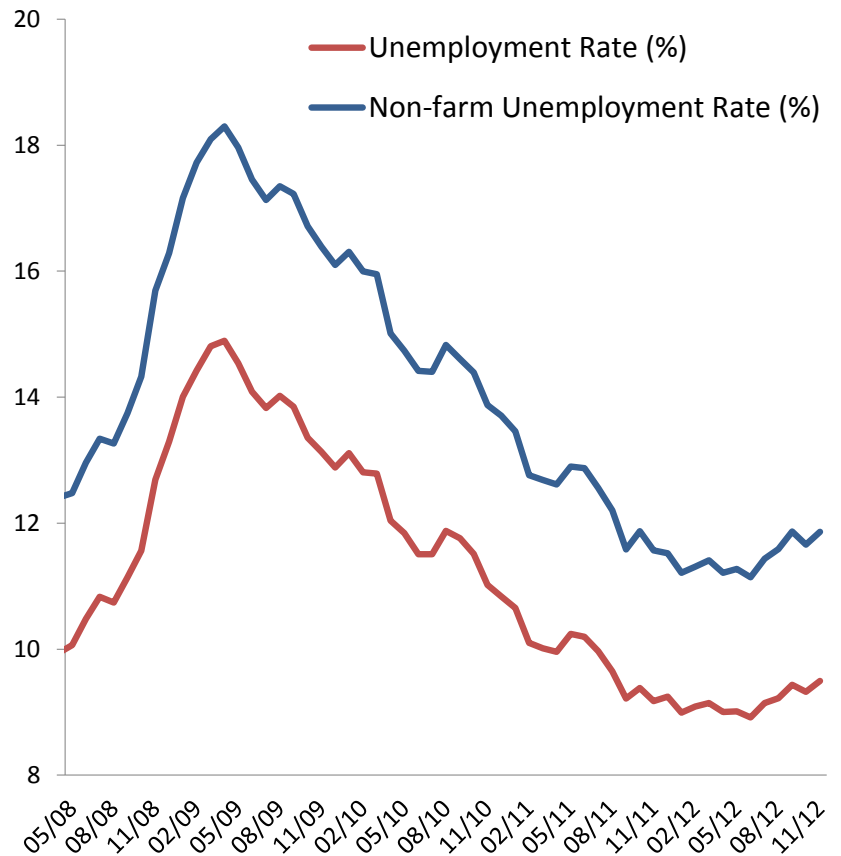
*Difference of natural logarithms

Employment

Employment and Participation (Millions, Percent)



Unemployment Rate (Percent)

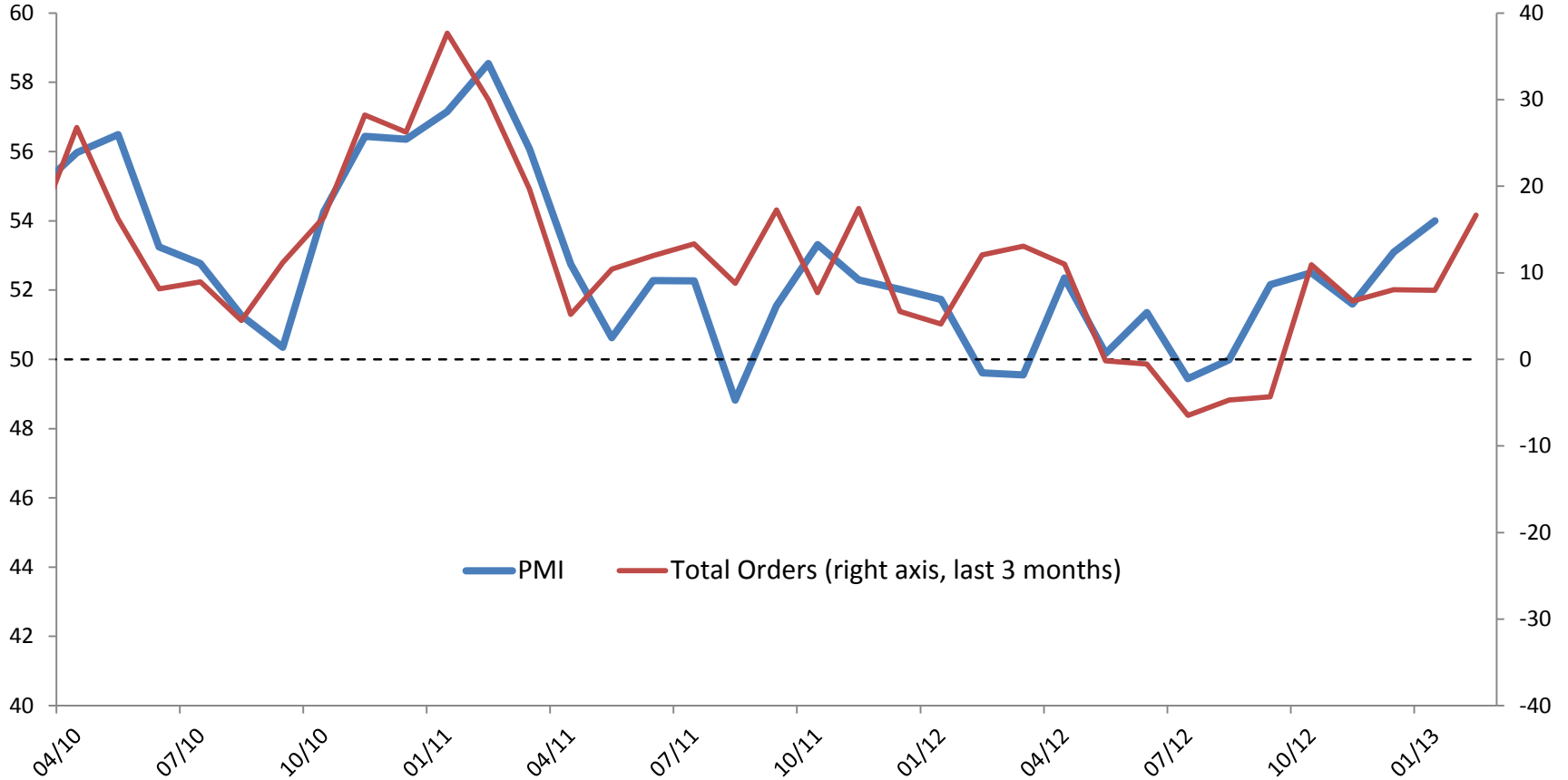


Source: TURKSTAT, Household Labor Force Survey, CBRT.

Last Observation: November 2012

Leading Indicators

Purchasing Managers' Index (PMI) and Total Orders* (Seasonally Adjusted, Monthly)



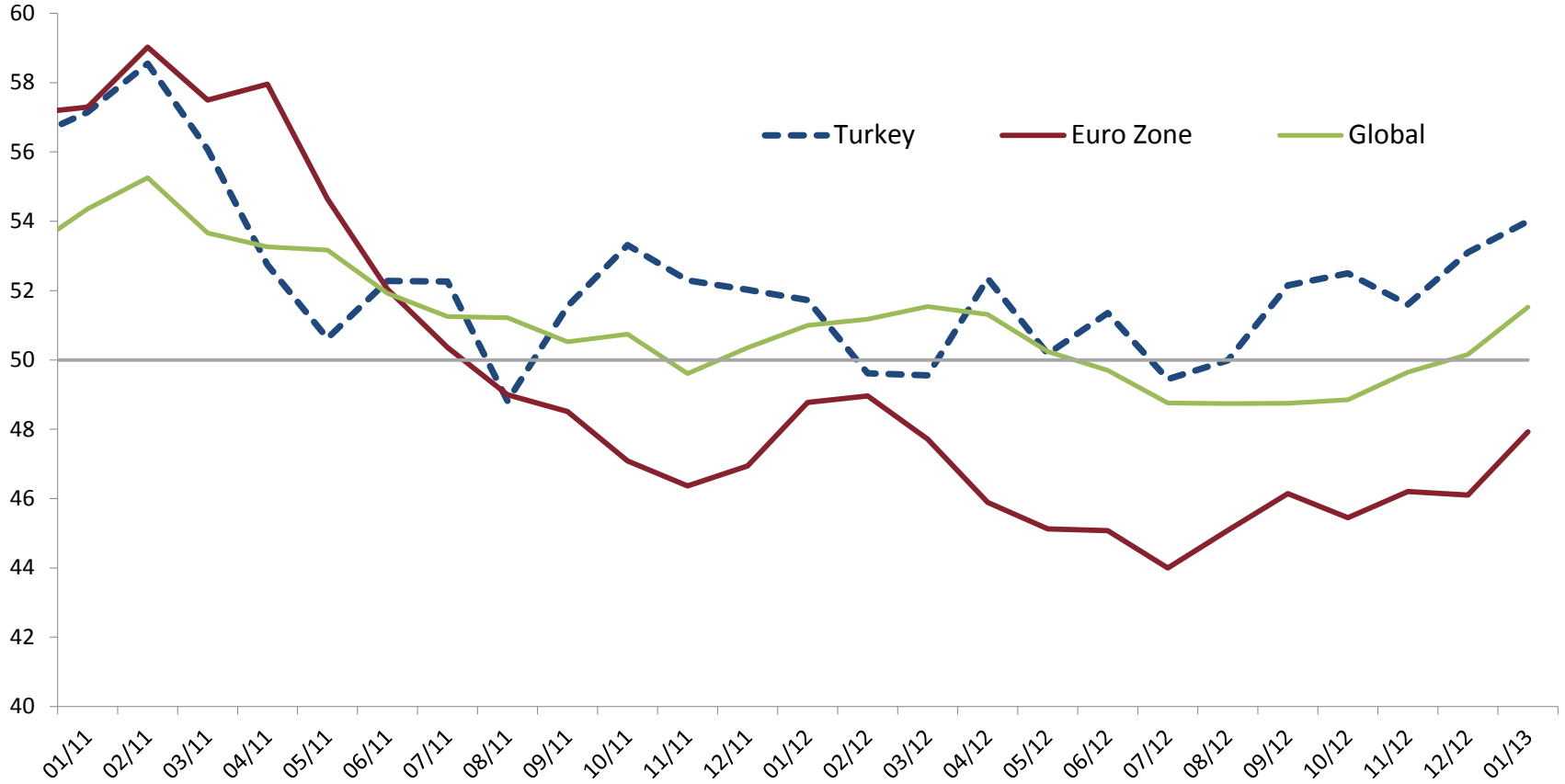
Source: TURKSTAT, MARKIT and CBRT.

Last Observation: January 2013 for PMI, February 2013 for Total Orders

*Consumer Tendency Survey, Q.11: How have your total orders developed over the past 3 months?

PMI: Turkey, Eurozone, and Global

Manufacturing PMIs (Seasonally Adjusted)



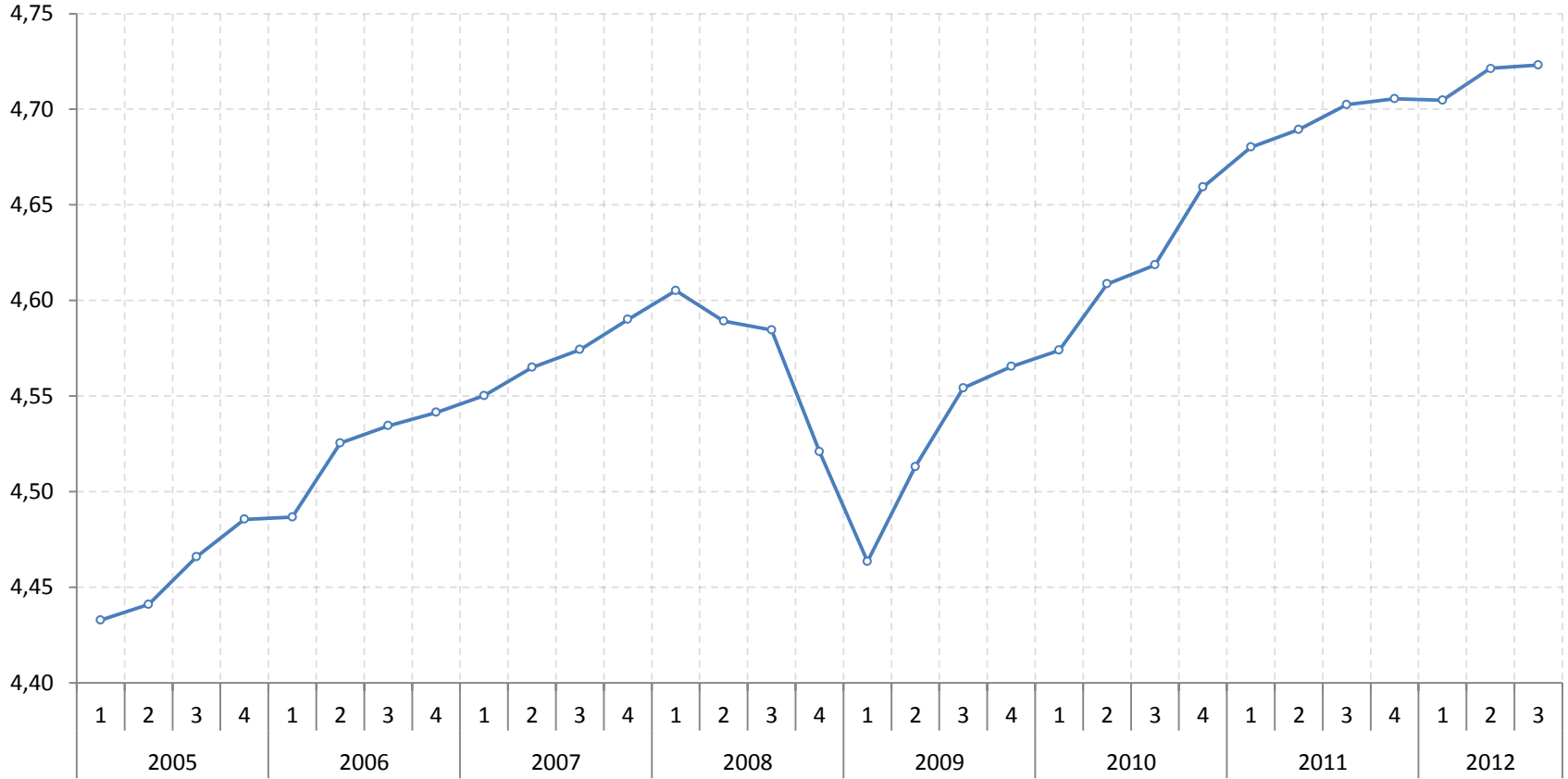
Source: MARKIT.

Last Observation: January 2013.

Gross Domestic Product

GDP

(Base Quarter: 2008Q1, Seasonally Adjusted, Natural Logarithms)



Source: TURKSTAT, CBRT.

Summary

- Capital flow volatility may cause misalignments in credit and currency.
- Credit and currency misalignments hurt both price stability and financial stability in emerging market economies.
- Macroprudential policy has proven to be effective in reducing excessively high credit growth in Turkey.
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