

CENTRAL BANK OF THE REPUBLIC OF TURKEY

Growth and Financial System

Durmuş YILMAZ

Governor

February, 2011

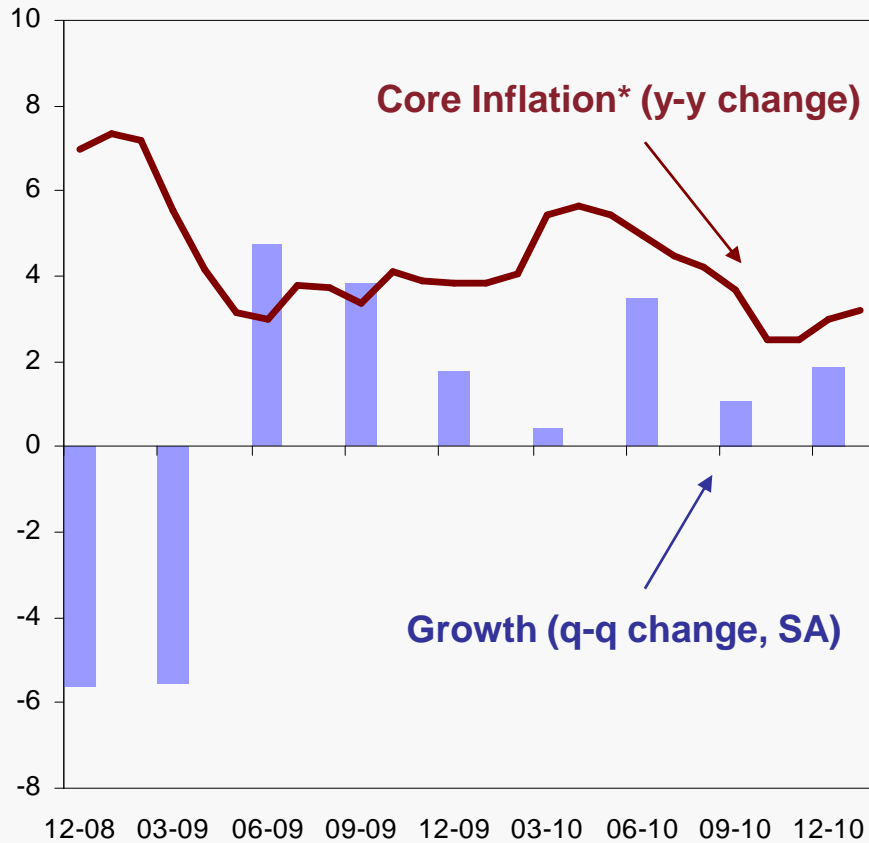
Presentation Outline

- I. Recent Developments in the Turkish Economy**
- II. Monetary Policy**
- III. Policy Outcomes**

I. Recent Developments in the Turkish Economy

Rapid Recovery ...

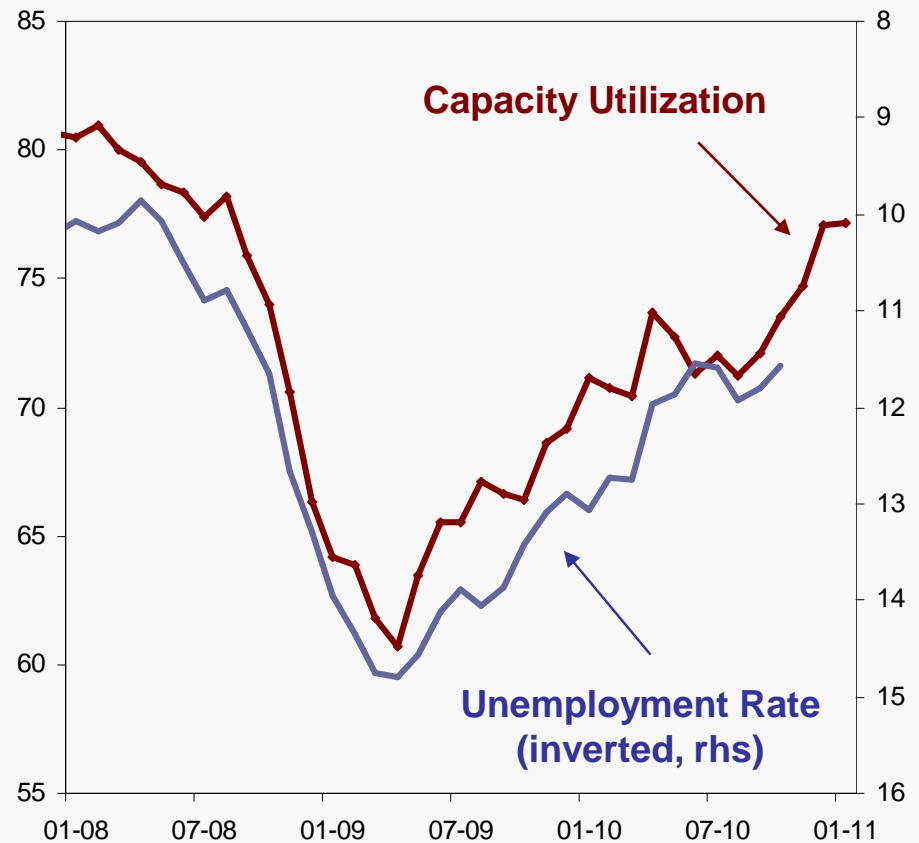
Growth and Inflation



* I index

Source: TURKSTAT, CBRT

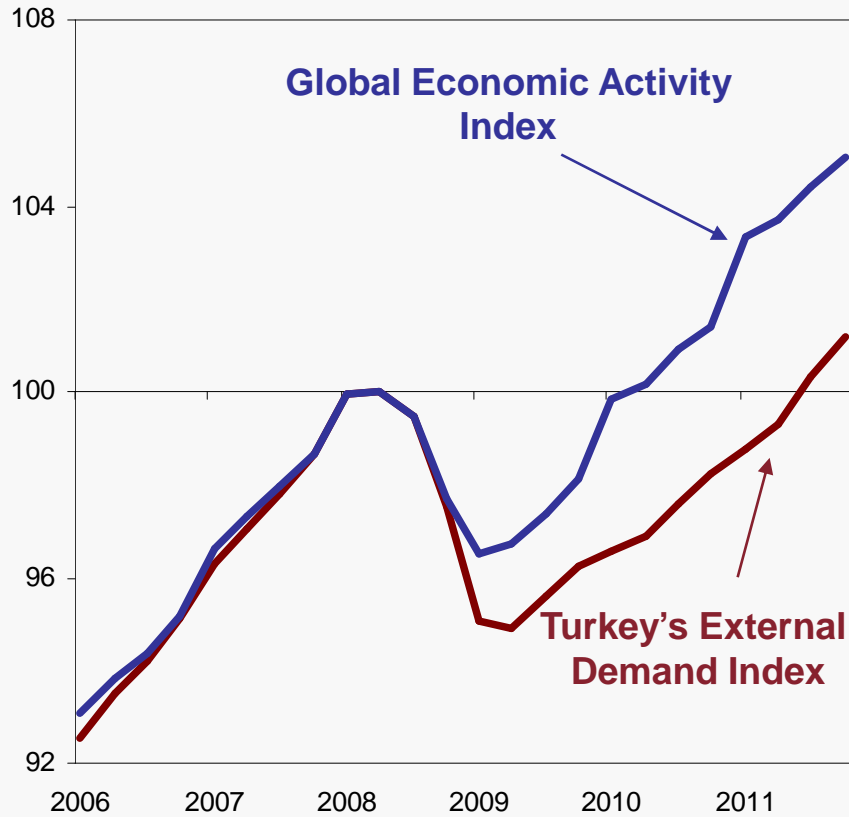
Capacity Utilization and Unemployment Rates



Source: TURKSTAT, CBRT

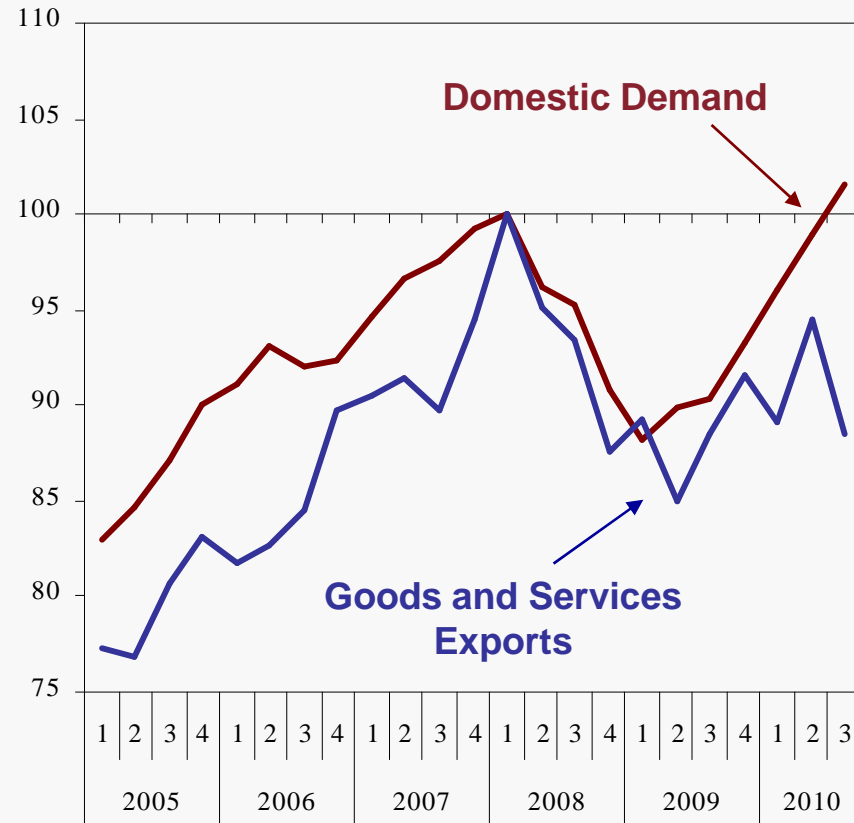
... but unbalanced

Domestic Demand and Exports
(2008 Q1=100)



Source: TURKSTAT, CBRT

Turkey's External Demand Index*
(June 2008=100)

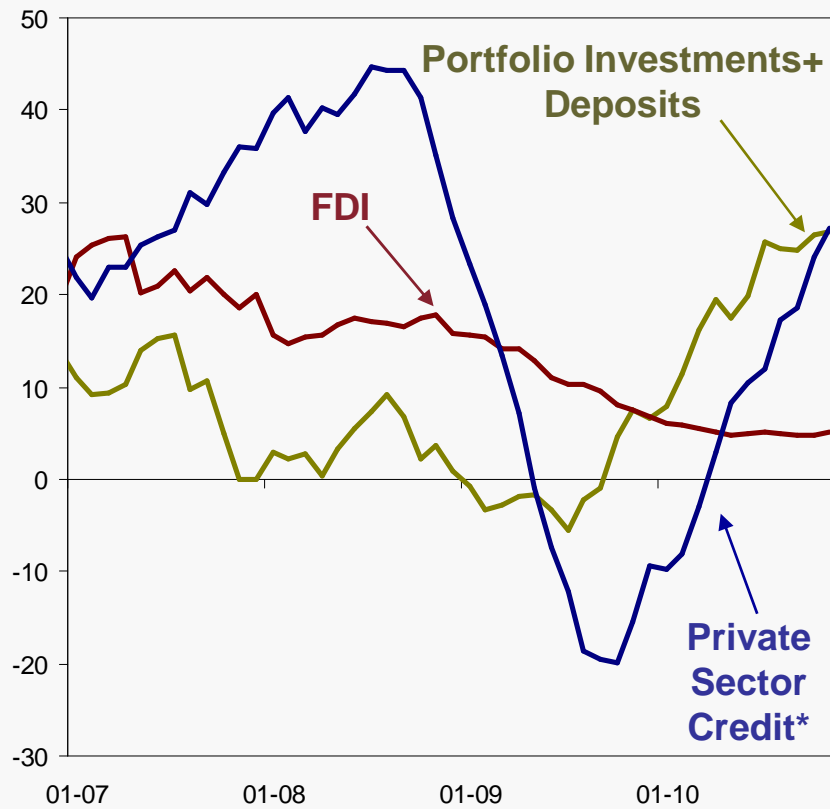


* The shares of countries within the exports of Turkey and weighted GDP data are employed in the calculation of the external demand index of Turkey.

Source: Bloomberg, Consensus Forecasts, IMF WEO, TURKSTAT, CBRT

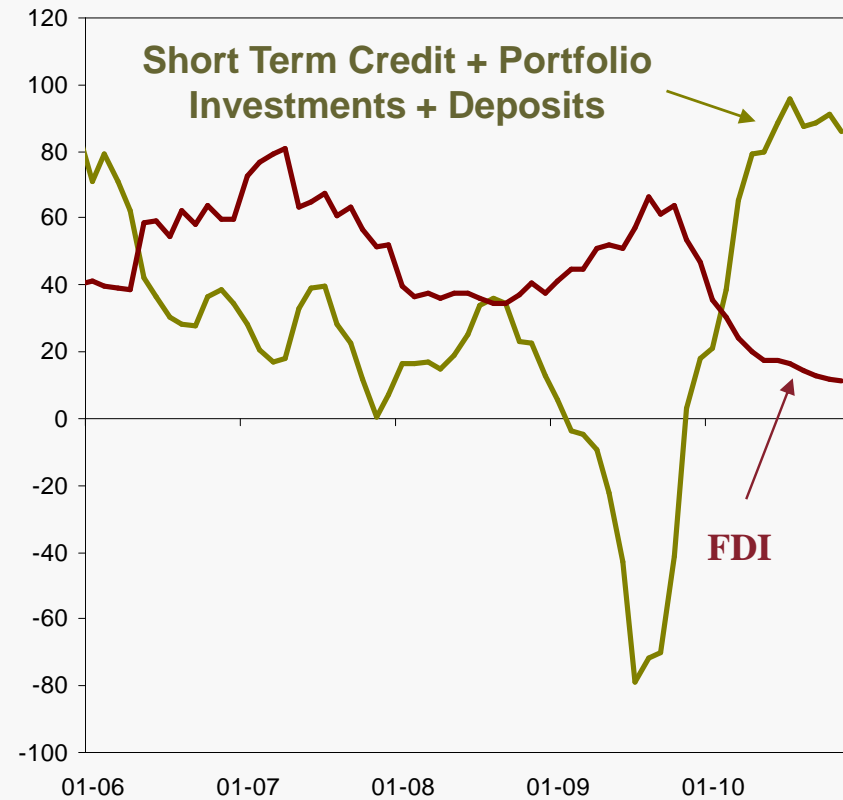
Composition of Capital Flows

Composition of Capital Flows
(12-month rolling sum, billion USD)



* After controlling for the effect of change in Decree No. 32
Source: TURKSTAT, CBRT

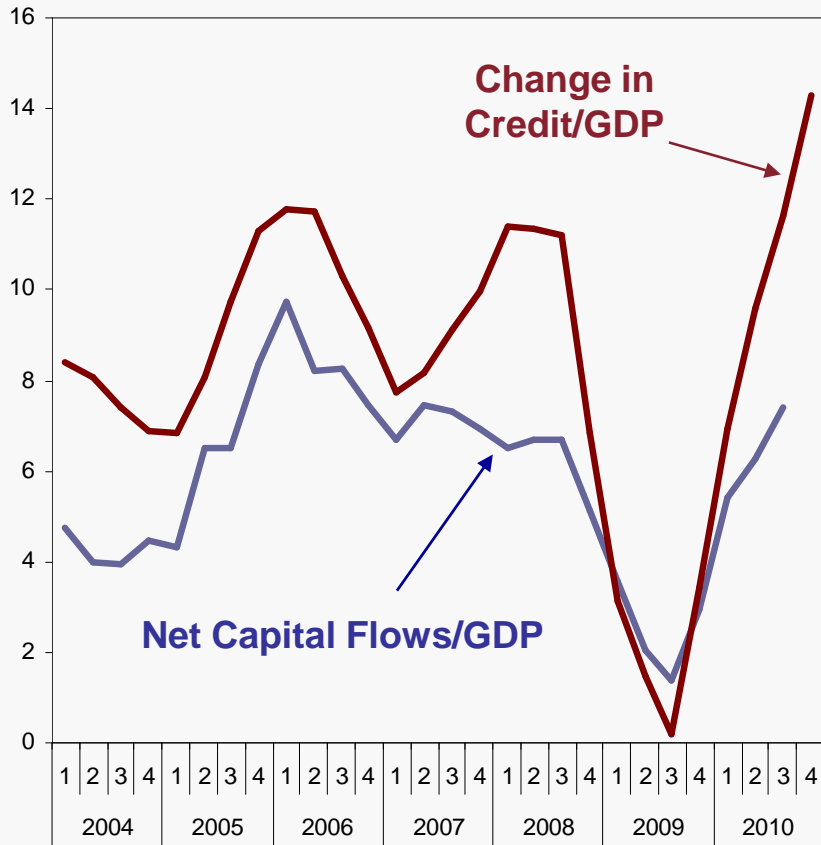
Finance of Current Account Deficit
(percentage of CAD)



Source: TURKSTAT, CBRT

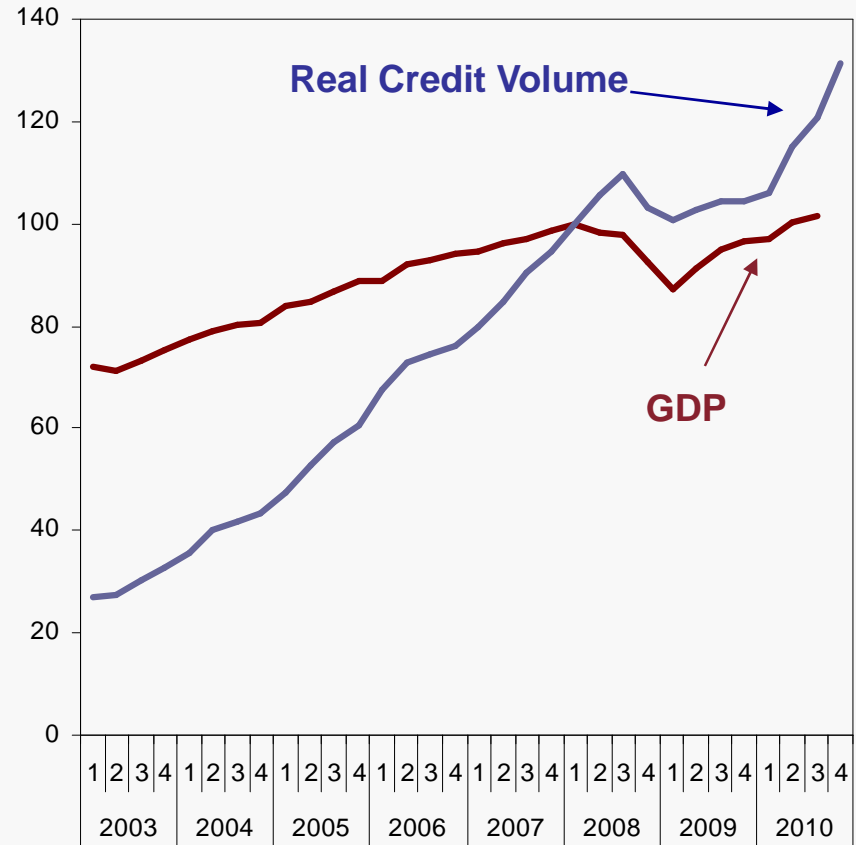
Acceleration in Credit Growth

Capital Flows and Credit Growth
(percent)



Source: TurkStat, CBRT

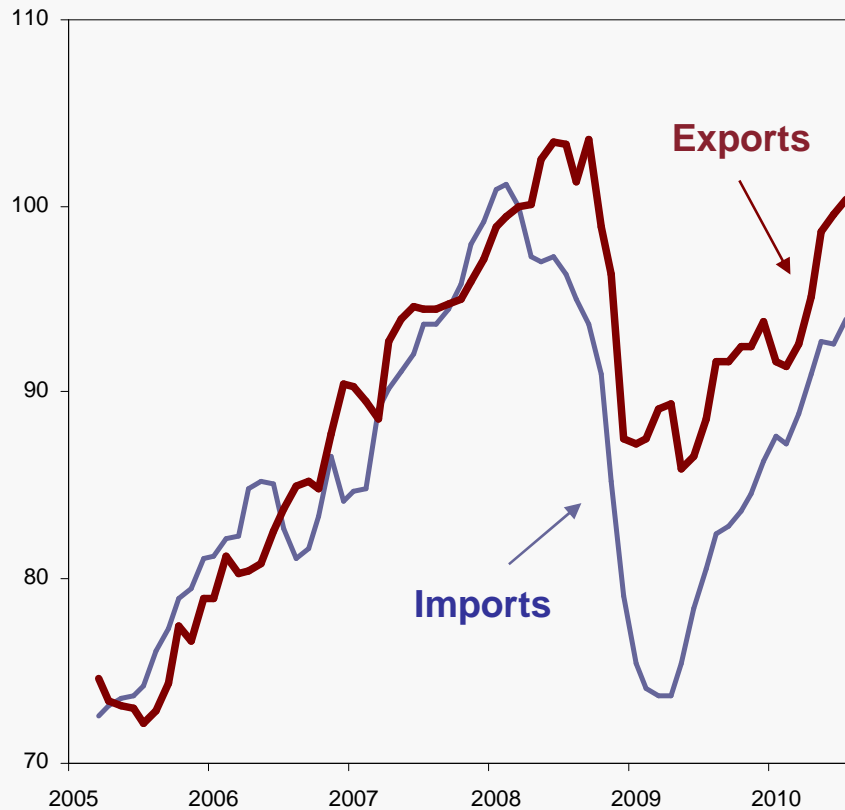
Real GDP and Credit Volume
(2008 Q1=100)



Source: BRSA, TurkStat, CBRT

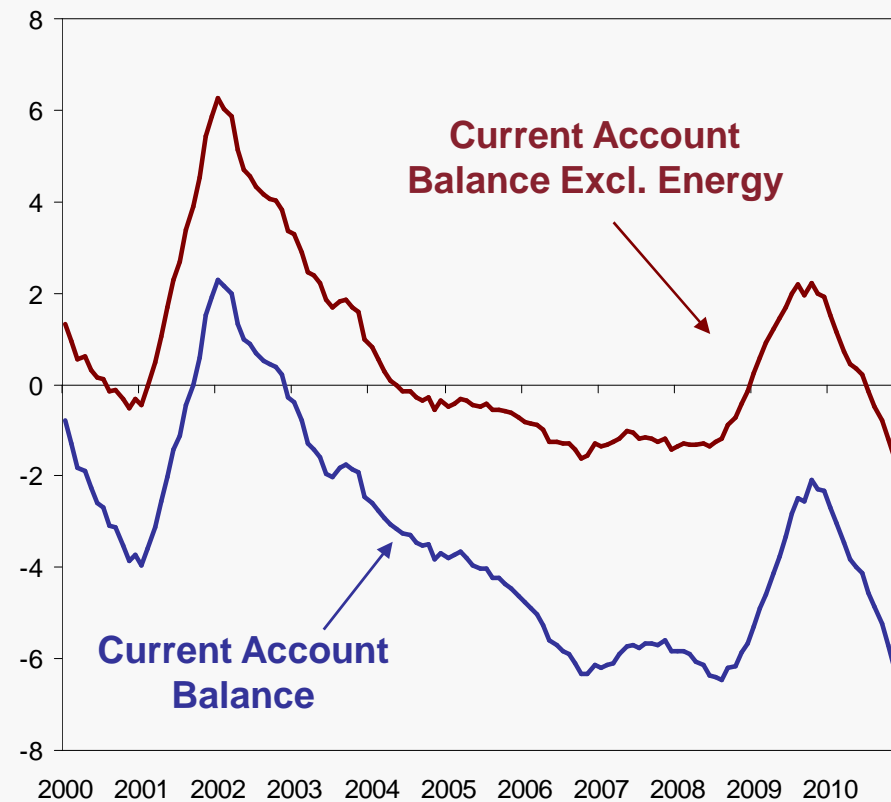
Widening Current Account Deficit

Exports and Imports
(2008 Q1 = 100)



Source: TurkStat, CBRT

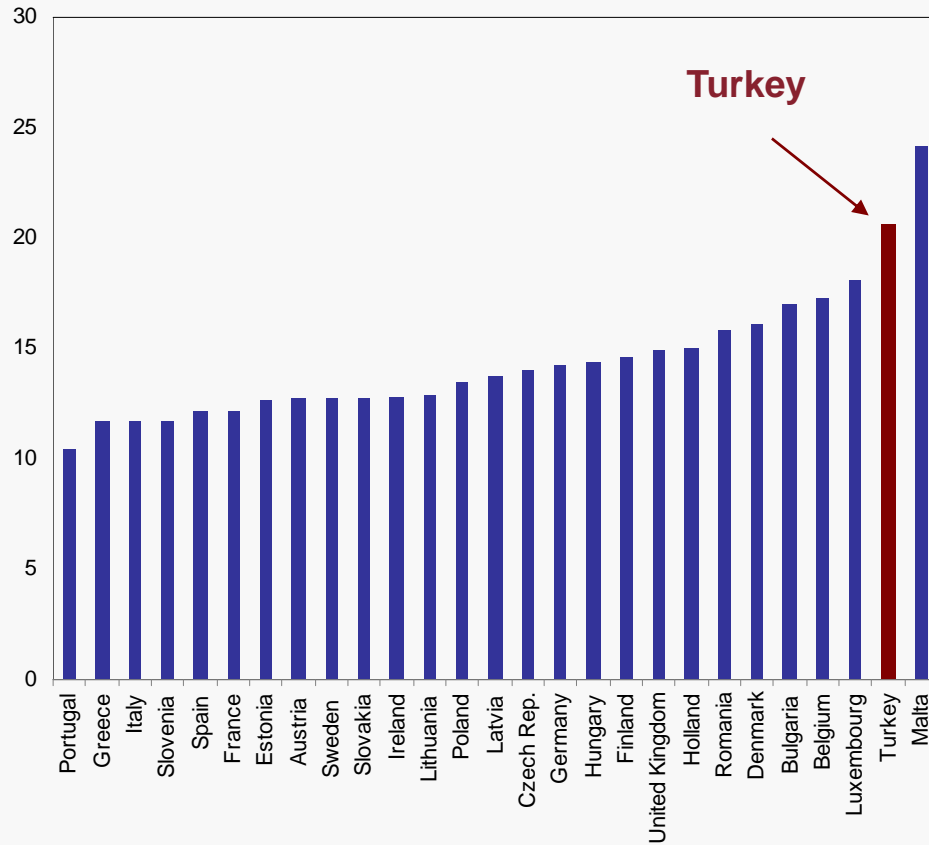
Current Account Deficit
(ratio to GDP, percent)



Source: TurkStat, CBRT

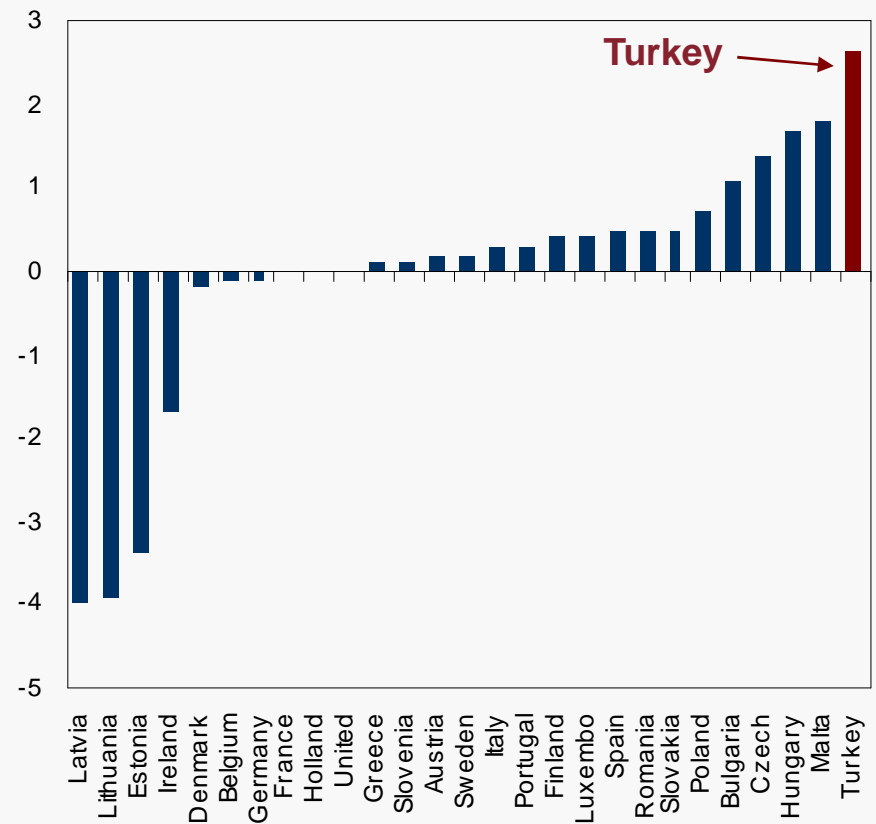
Strength of the Banking System

Capital Adequacy Ratio as of 2009
(percent)



Source: Eurostat, CBT

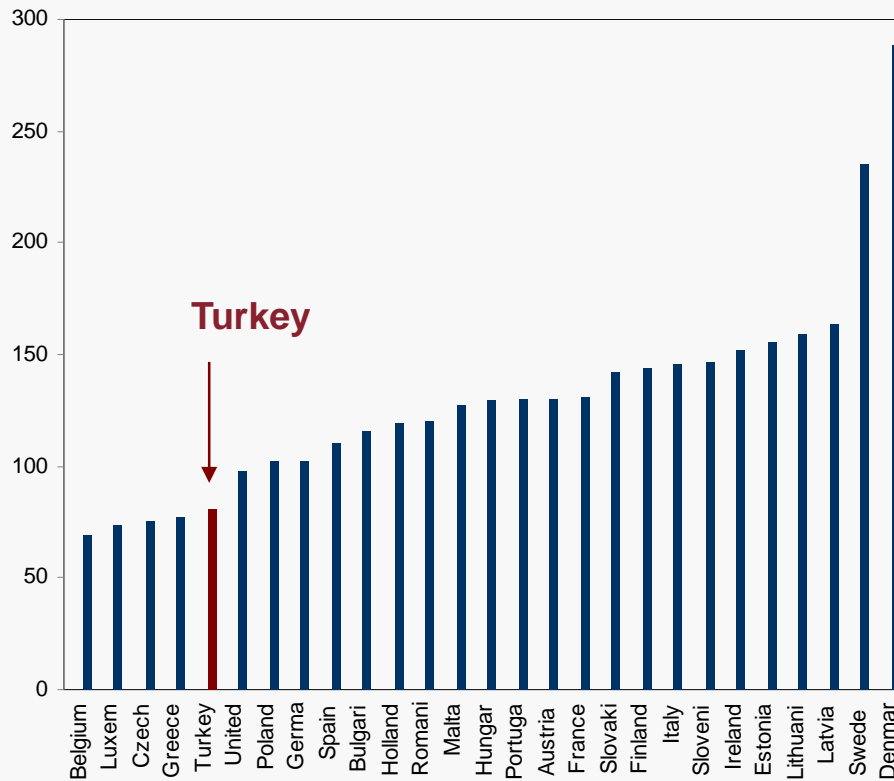
Return on Assets as of 2009
(percent)



Source: Eurostat, CBT

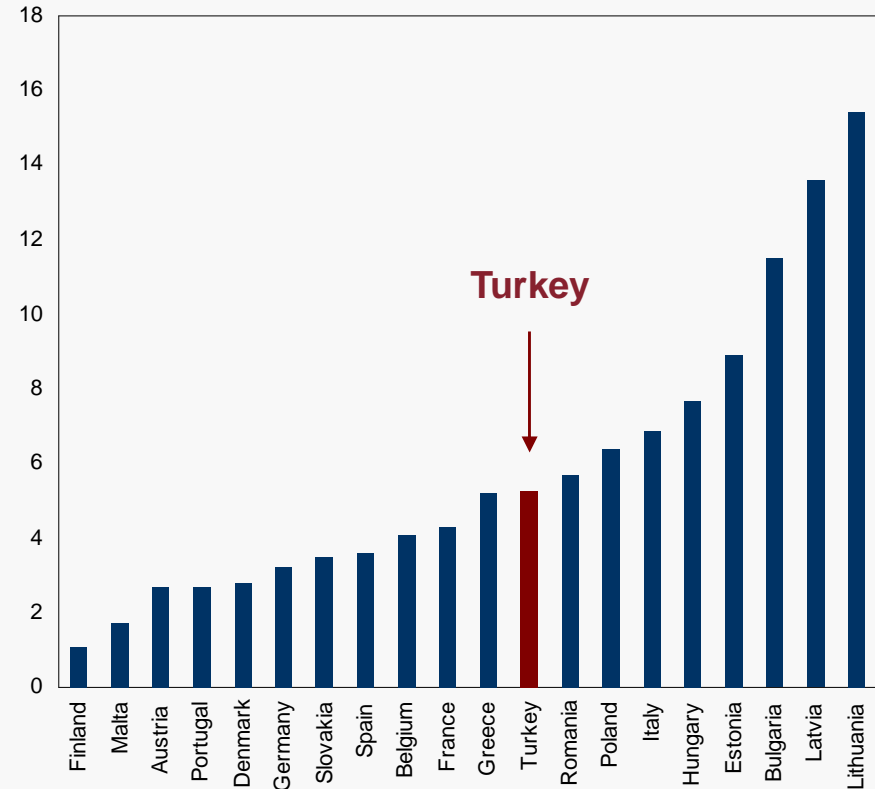
Strength of the Banking System

Loan to Deposit Ratio as of 2009
(percent)



Source: Eurostat, CBT

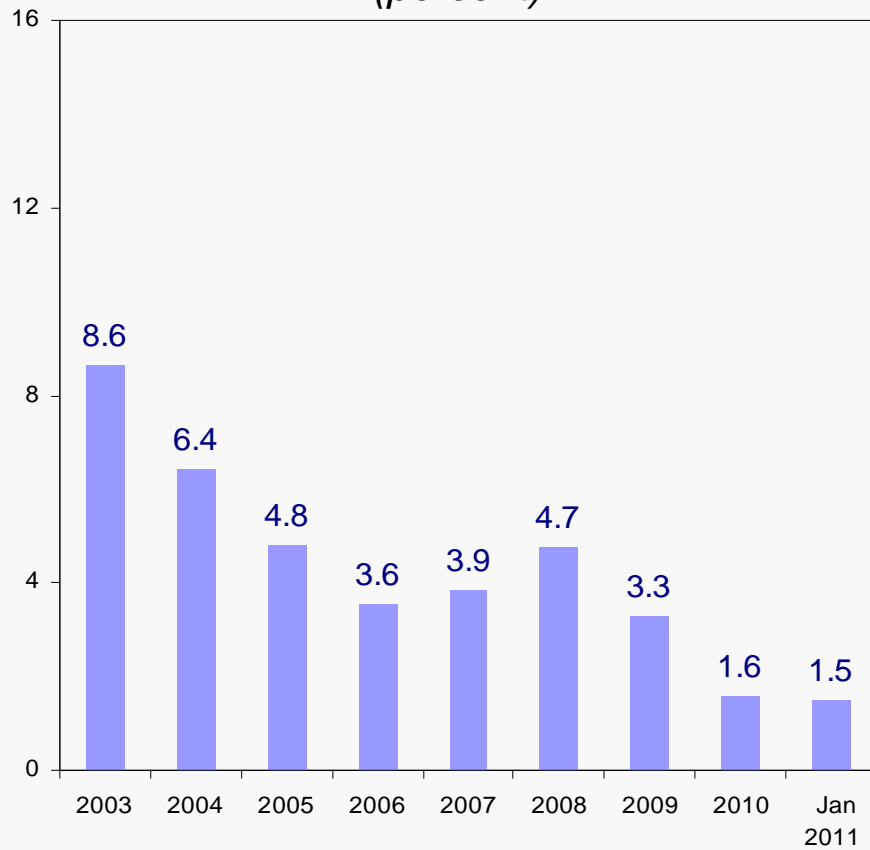
Non-Performing Loans Ratio as of 2009
(percent)



Source: Eurostat, CBT

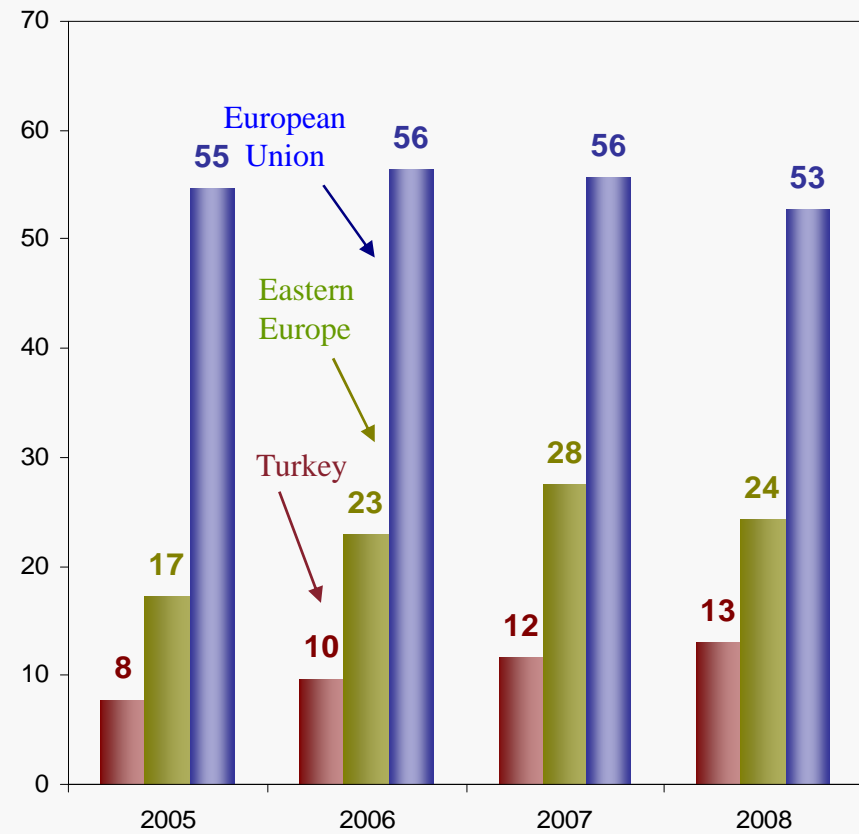
Household Debt Remains Low

Ratio of FX-Indexed Consumer Loans to Total Consumer Loans (percent)



Source: CBT

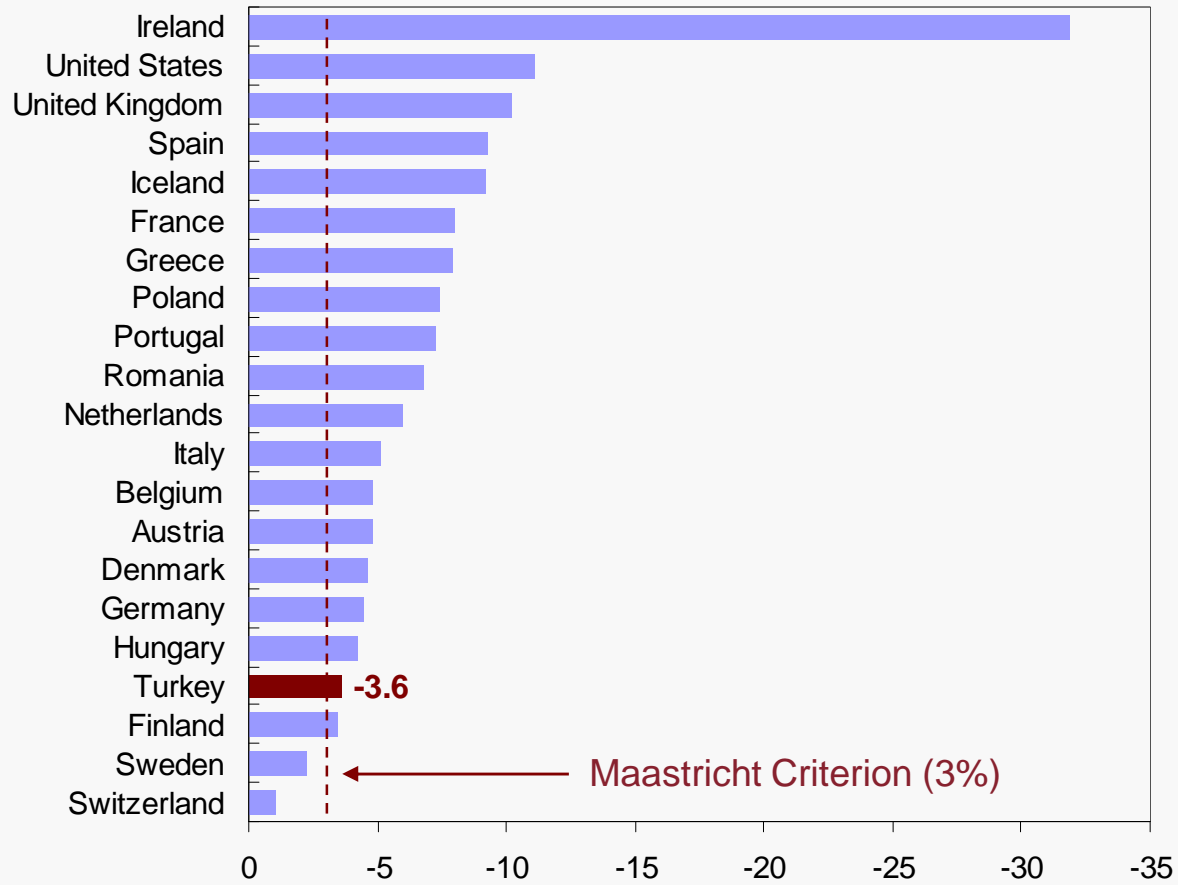
Ratio of Household Liabilities to GDP (percent)



Source: European Central Bank, CBT

Budget Deficit

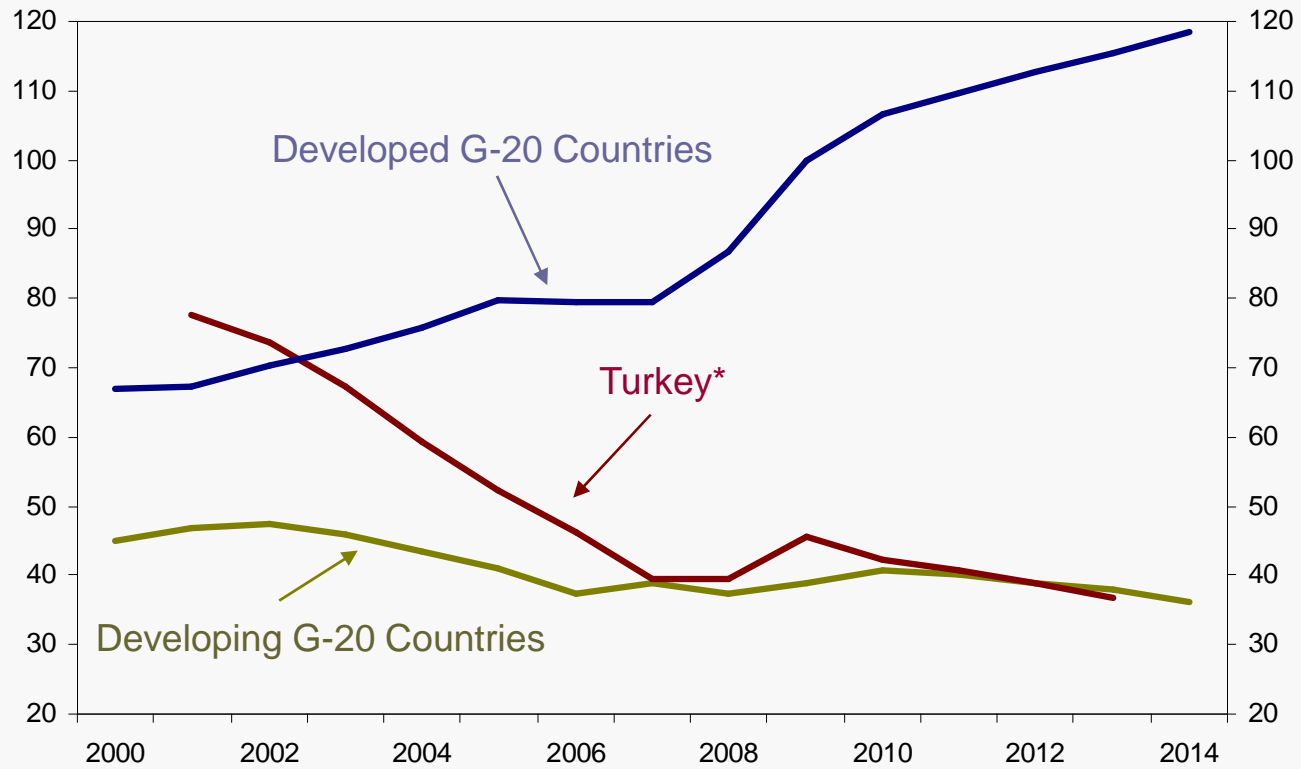
2010 Budget Deficit Estimates
(percent of GDP)



Source: Terasury, IMF, CBRT

Fiscal Discipline

Public Debt Stock
(Ratio to GDP)



*Medium-Term Program (2011 -2013) Targets
Source: IMF WEO October 2010, Treasury, BRSA, CBT

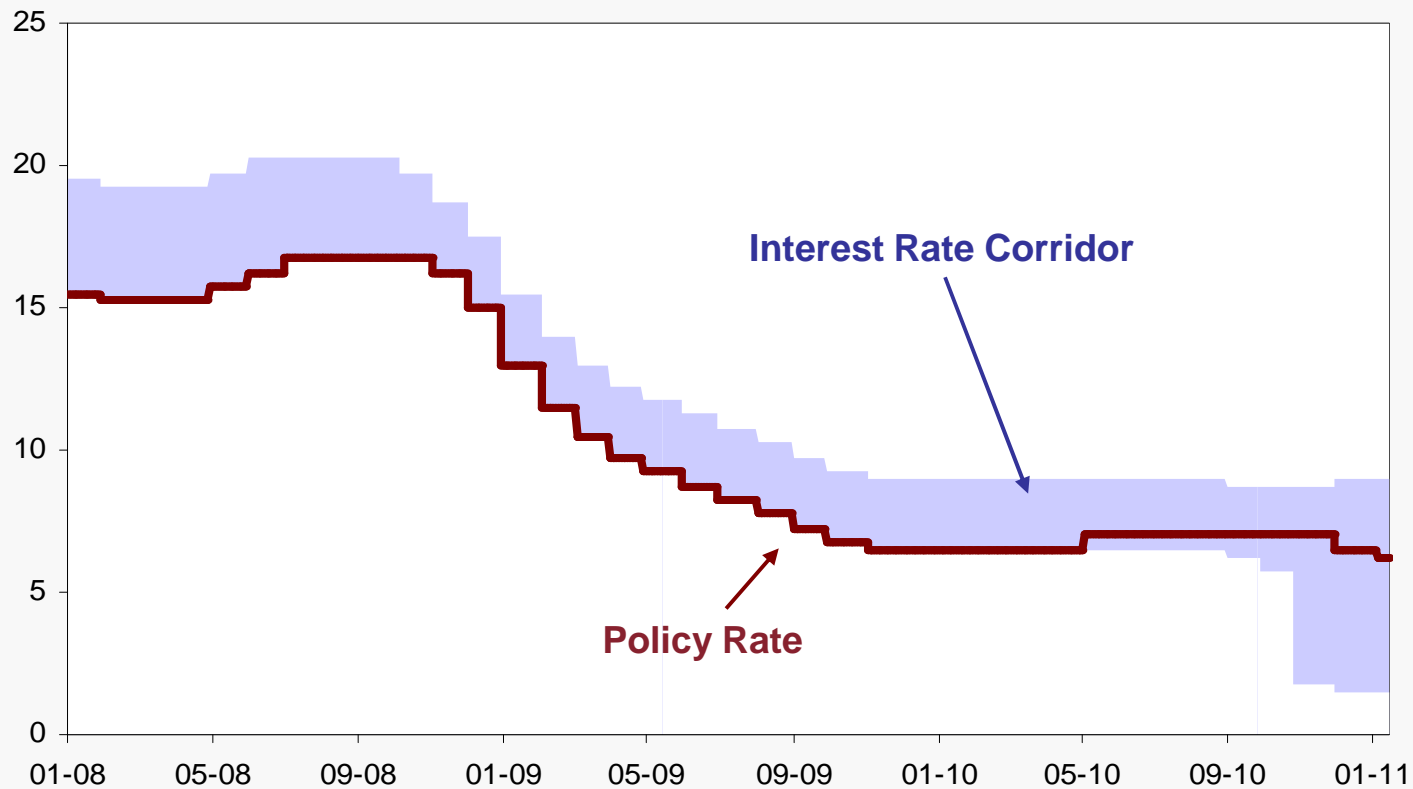
II. Monetary Policy

Phases in Monetary Policy

- **Phase-1:** Full liquidity support (after the collapse of Lehman Brothers, September 2008)
- **Phase-2:** Exit Strategy (April 2010)
- **Phase-3:** New Policy Mix (starting from November 2010)

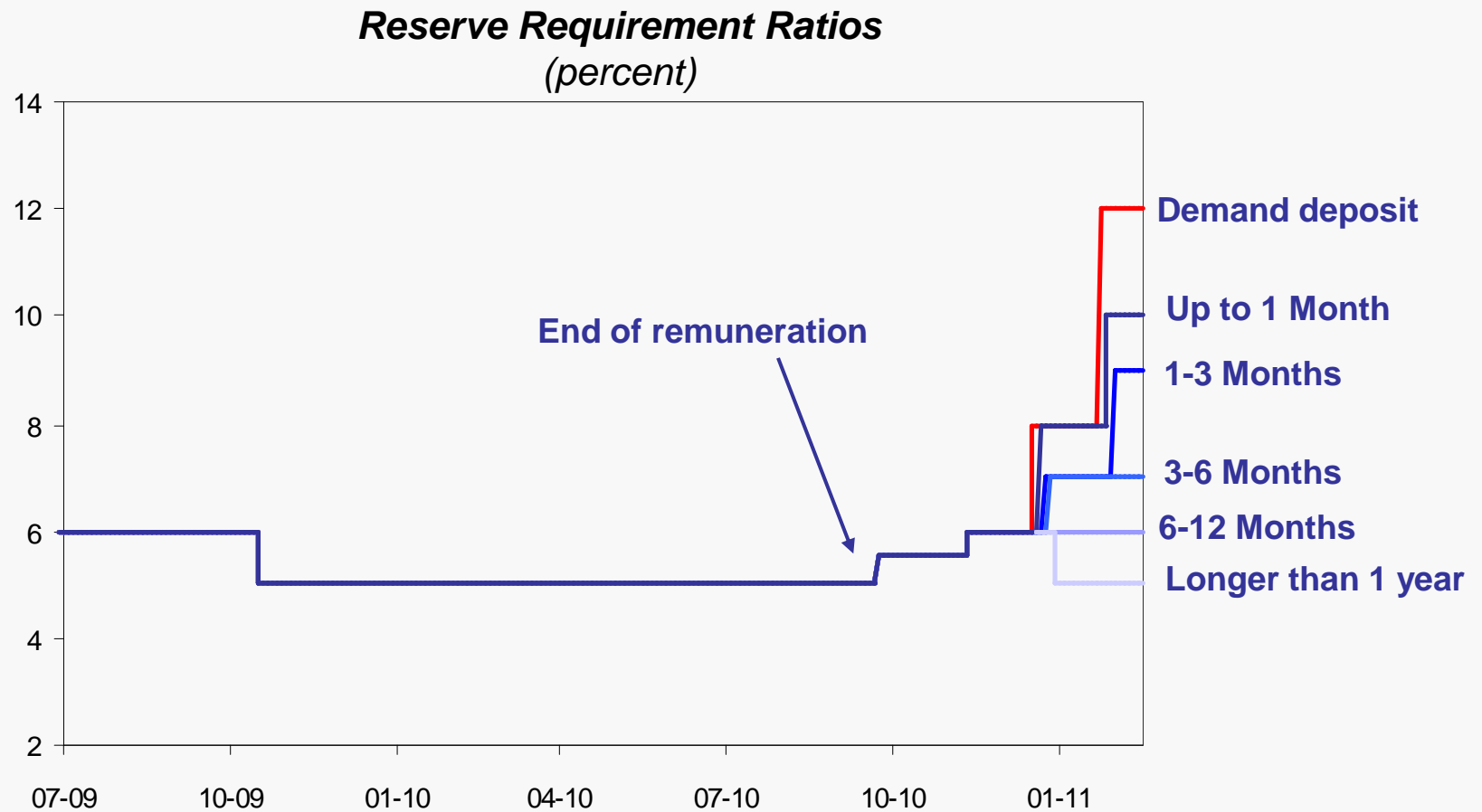
The Policy Rate and Interest Rate Corridor

Policy Rate and Interest Rate Corridor
(percent)



Source: CBRT

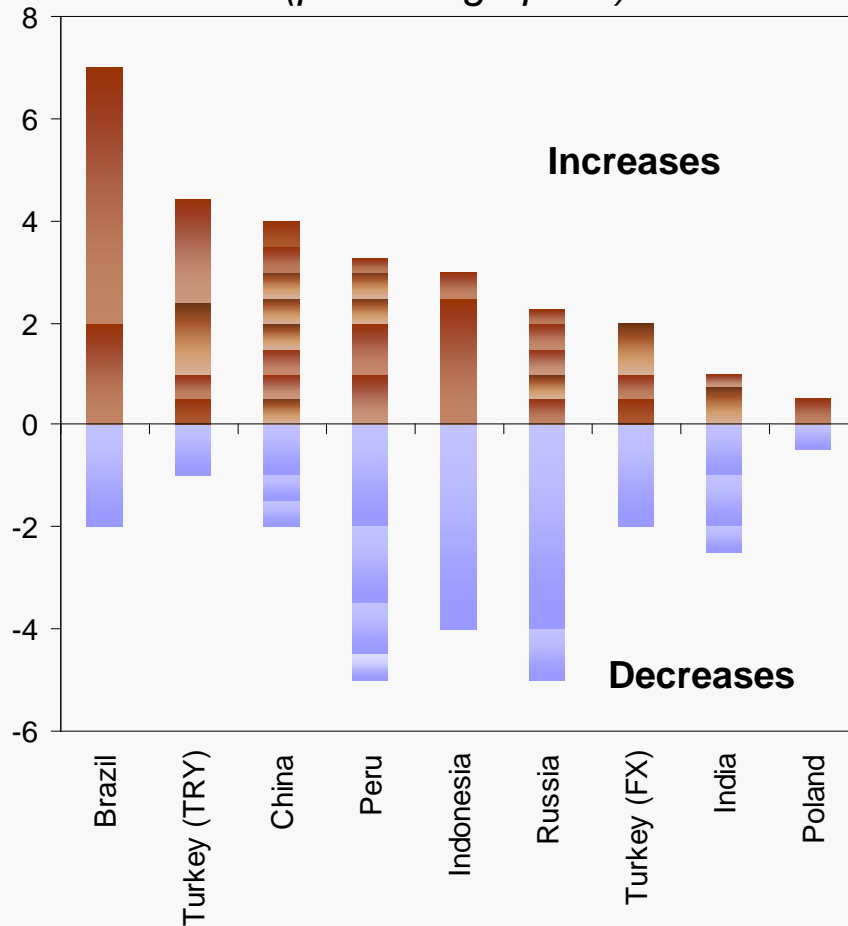
Reserve Requirements as a Macroprudential Tool



Source: CBRT

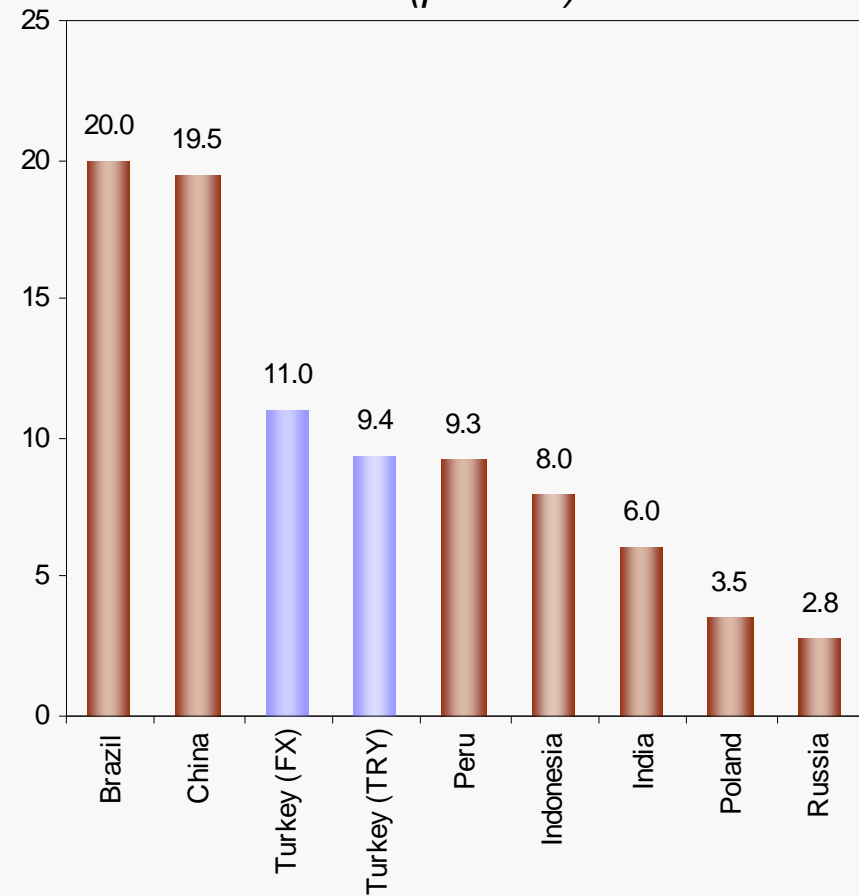
Reserve Requirements as a Macprudential Tool

Change Since the Start of the Crisis
(percentage point)



Source: Central Banks, CBT

Current Rates
(percent)



Source: Central Banks, CBT

The New Policy Mix

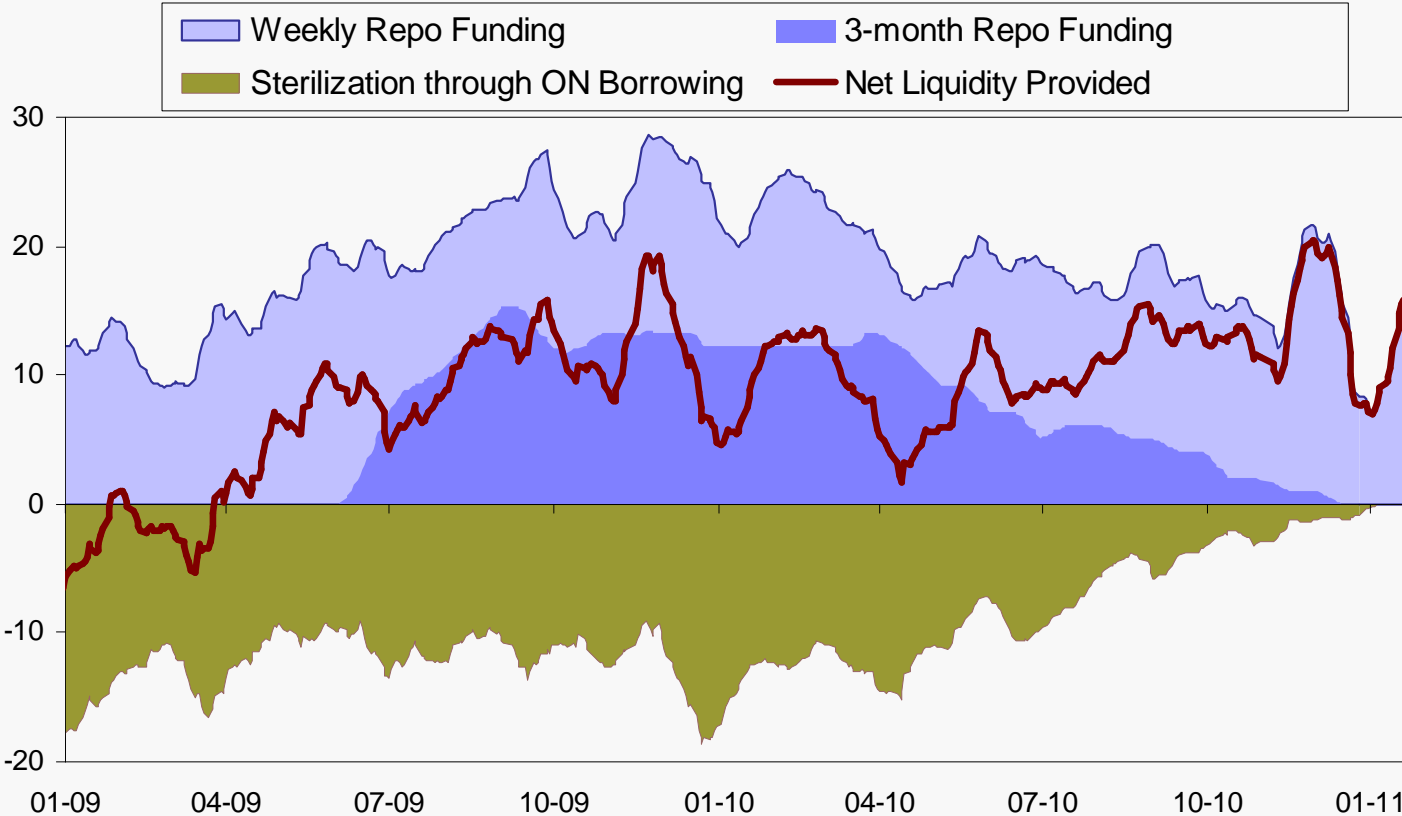
A lower policy rate, a wider interest rate corridor and higher reserve requirements

- The framework we adopt in spirit is not significantly different from the conventional inflation targeting framework.
- The only difference is that, previously our policy instrument was the one week repo rate, but now our instrument is a “policy mix”
- We seek to use these instruments in the right combination in order to cope with both inflation and macro-financial risks.
- The monetary policy stance in this framework is not only determined by the path of policy rates, but as a combination of all the policy instruments.

III. Policy Outcomes

Liquidity

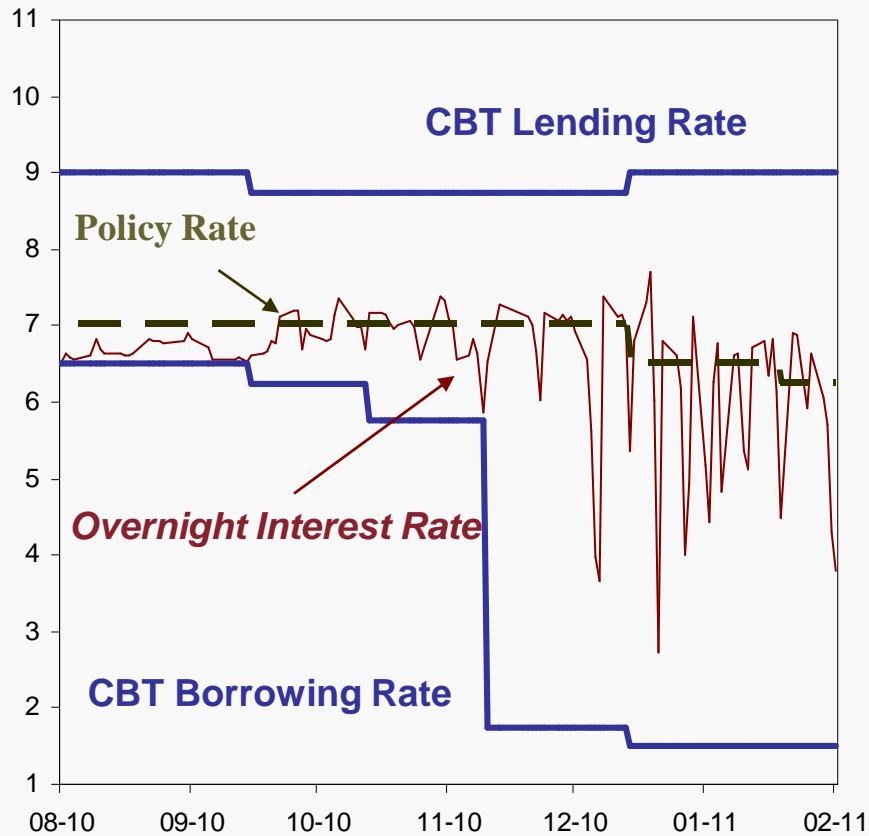
Central Bank Liquidity
(billion TRY)



Source: ISE, CBRT

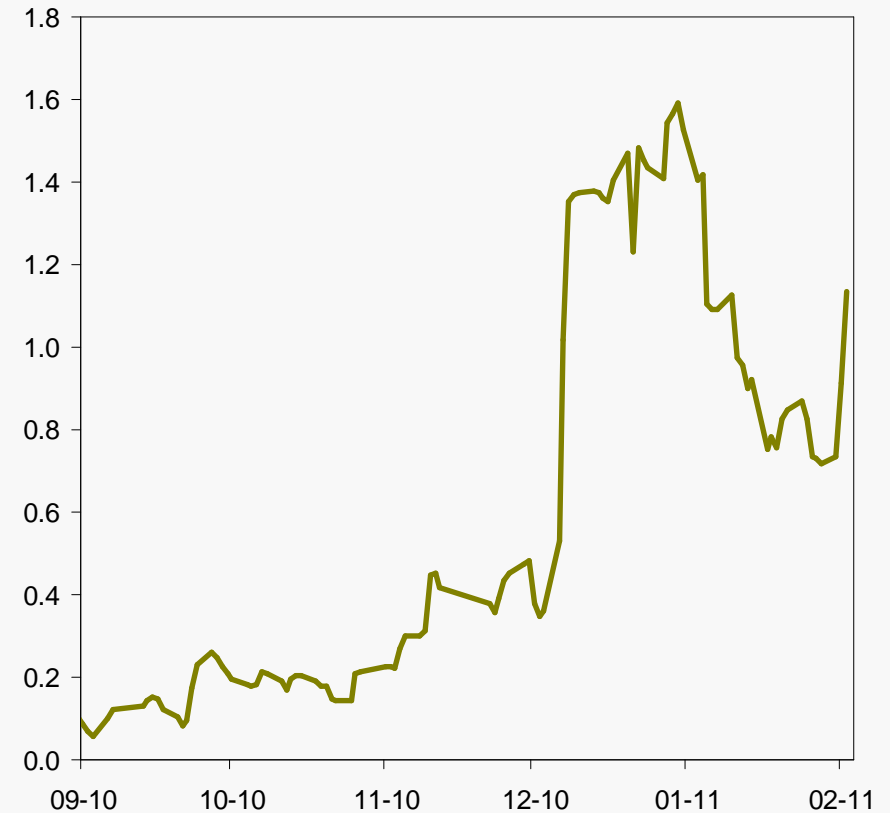
Volatility in Overnight Rates

Overnight Interest Rates (percent)



Source: ISE, CBRT

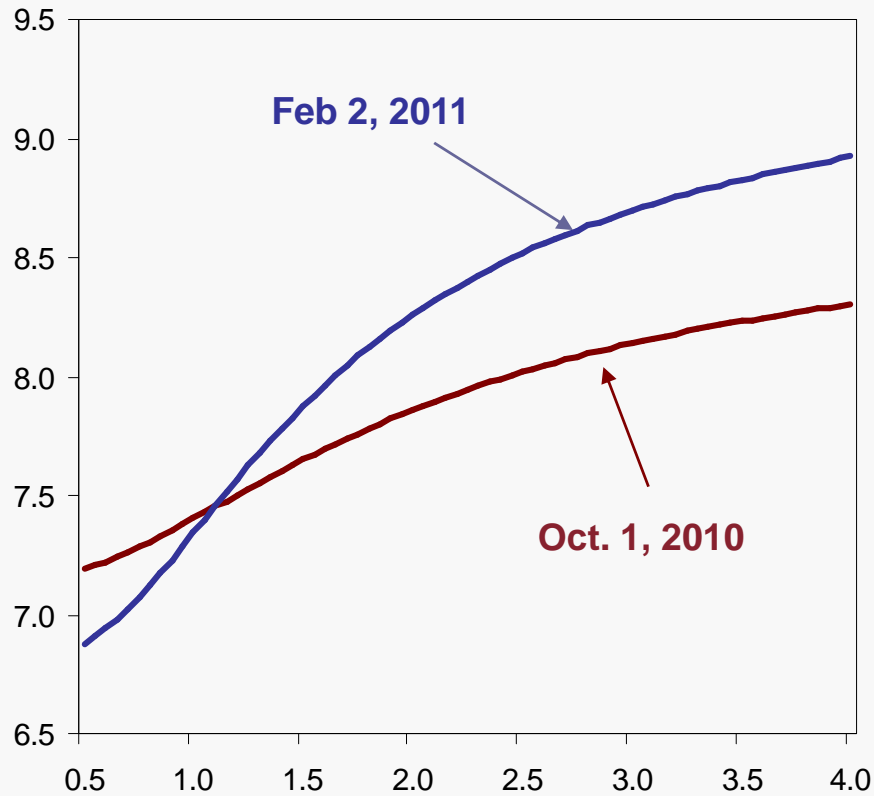
Volatility in Overnight Interest Rates (2-week standard deviation)



Source: ISE, CBRT

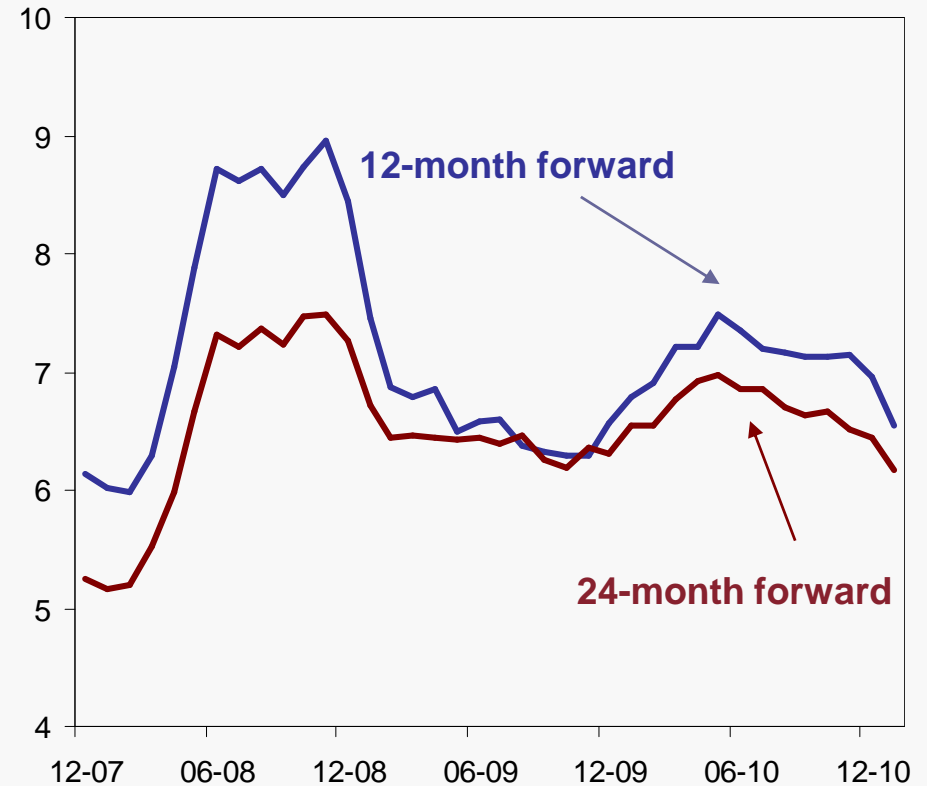
Yield Curve and Inflation Expectations

Yield Curve*
(percent)



* Calculated from the compounded returns on bonds quoted in ISE Bills and Bonds Market by using ENS method.
Source: ISE, CBRT

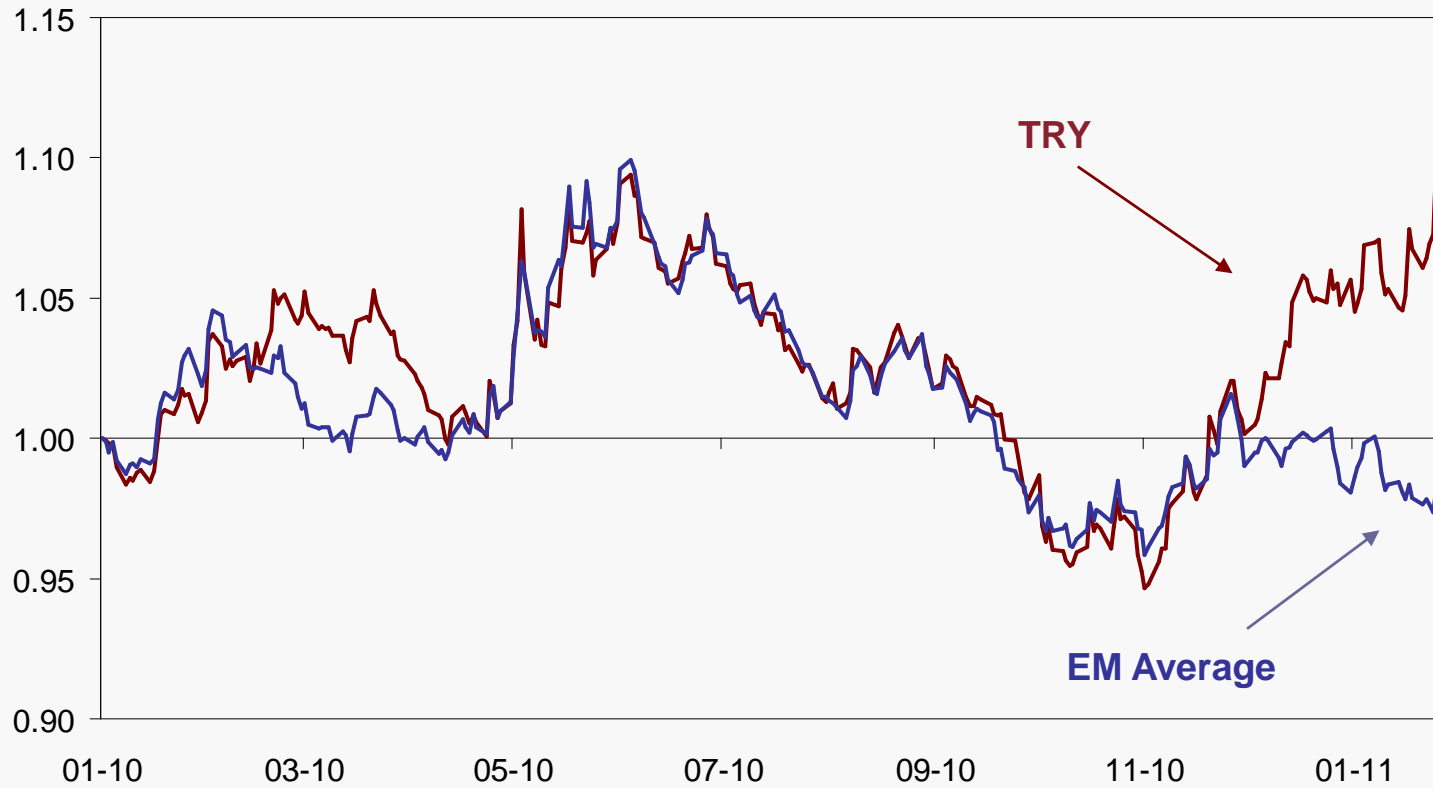
Inflation Expectations*
(percent)



* CBRT Expectations Survey results from the second survey period.
Source: ISE, CBRT

Initial Impact on Currency

TRY and Other EM Currencies against USD*
(4 Jan 2010=1)

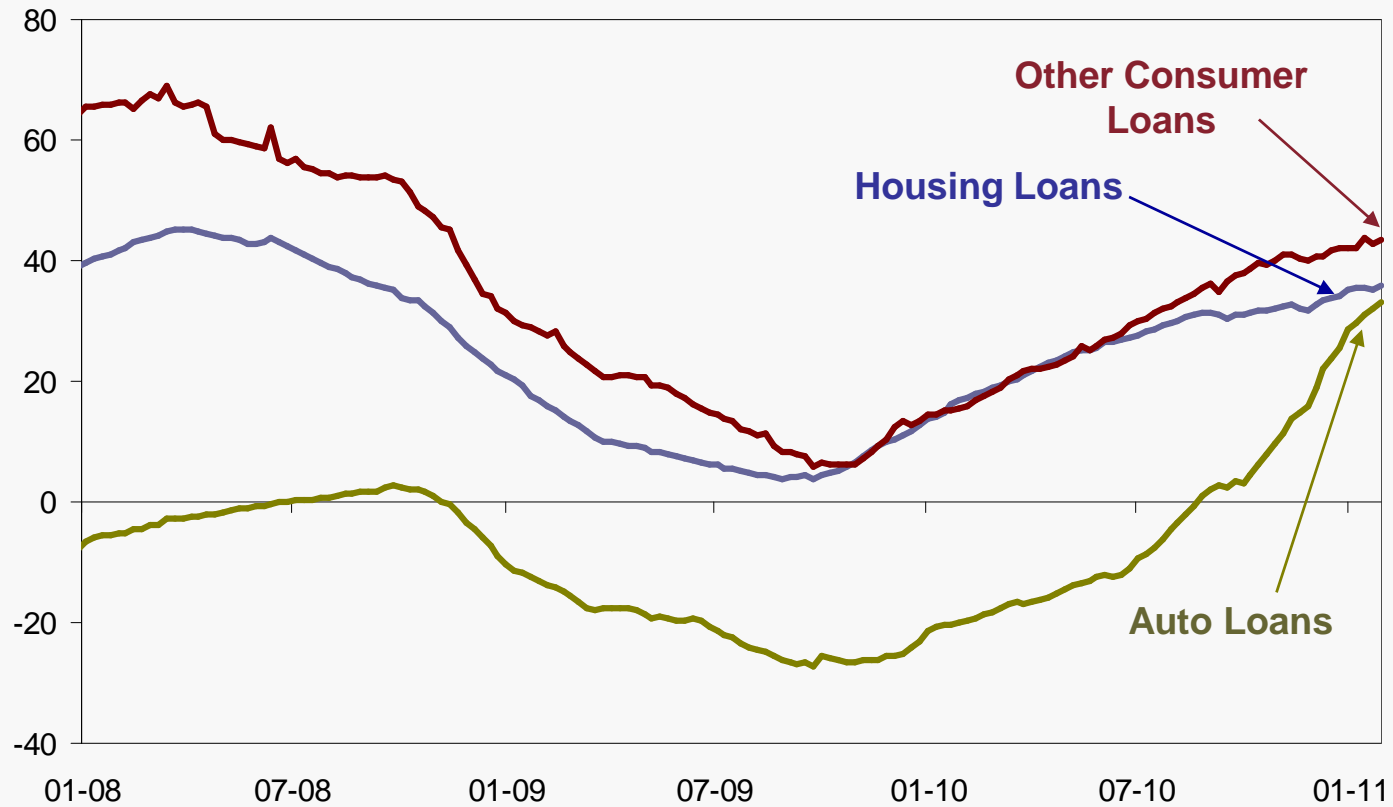


*Average of emerging market currencies, including Brazil, Chile, Czech Republic, Hungary, Mexico, Poland, South Africa, Indonesia, South Korea and Colombia.

Source: Bloomberg, CBRT

Household Loans

Household Loans
(year-on-year change, percent)



Source: CBRT

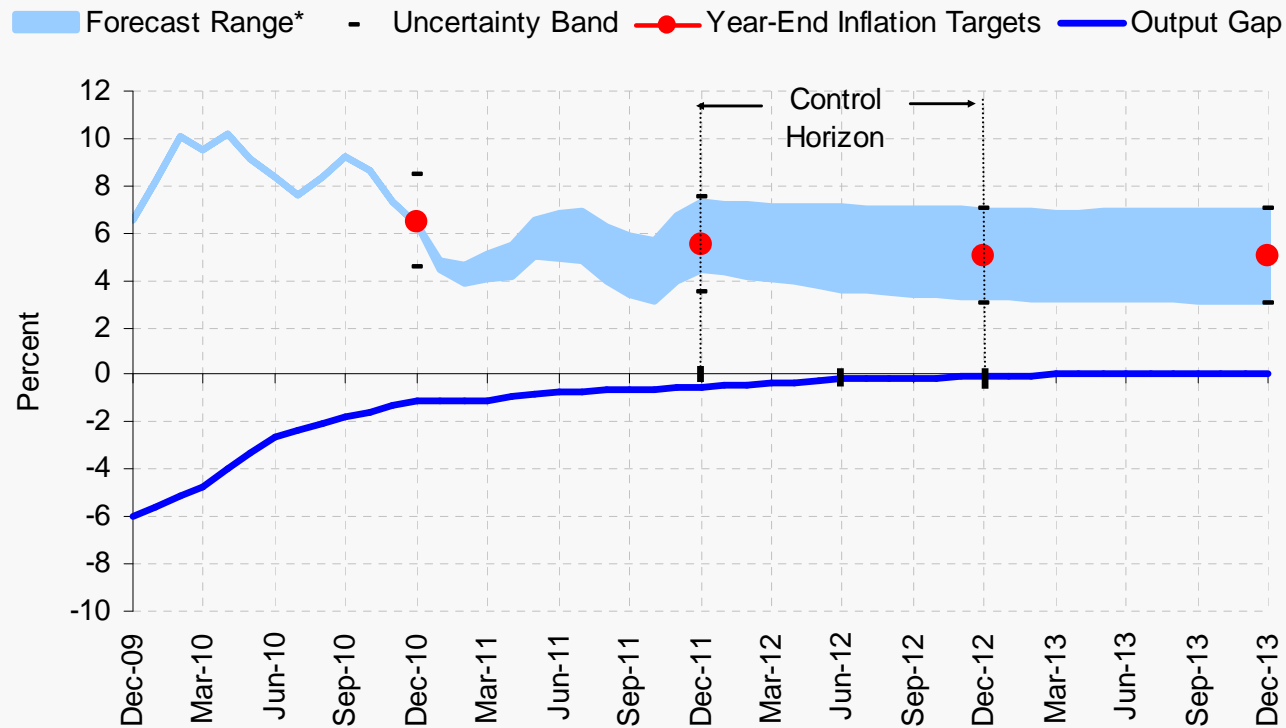
Measures by Other Authorities

1. Fiscal discipline
2. No FX loans to households
3. Domestic currency bond market
4. Loan/value restrictions
5. Tax hikes on certain consumer loans
6. Restrictions on credit card borrowing

Outlook for Inflation and Economic Activity

The Baseline Scenario envisages a gradual tightening by changing the mix of the policy rate and reserve requirement ratios. Such a tightening should not only aim at slowing down credit growth and domestic demand, but also reduce macroprudential concerns.

Inflation and Output Gap Forecasts



Source: CBRT

Overall Assessment

- Low interest rates across the globe, soaring imports driven by strong credit growth amid increased short-term capital inflows, and weaker foreign demand caused the current account deficit to widen rapidly in 2010.
- The new monetary policy strategy envisions the use of multiple instruments to manage both internal and external balances.
- Given the economic situation, the combination of lower policy rates and higher reserve requirement ratios is the most appropriate policy mix in terms of jointly upholding financial stability and price stability.

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