



# **Turkish Monetary Policy Experience with the Recent Financial Crisis**

Central Bank of Turkey

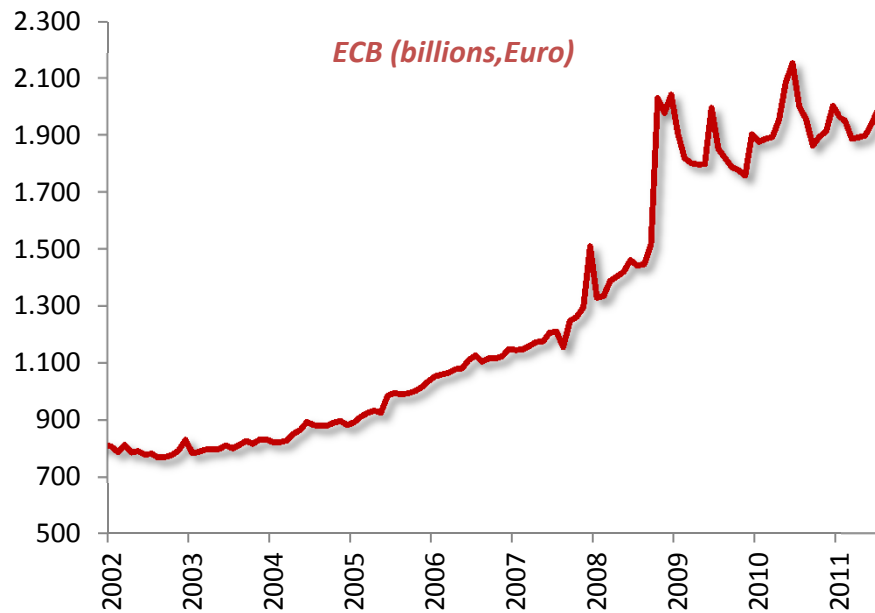
4 May 2012

Istanbul

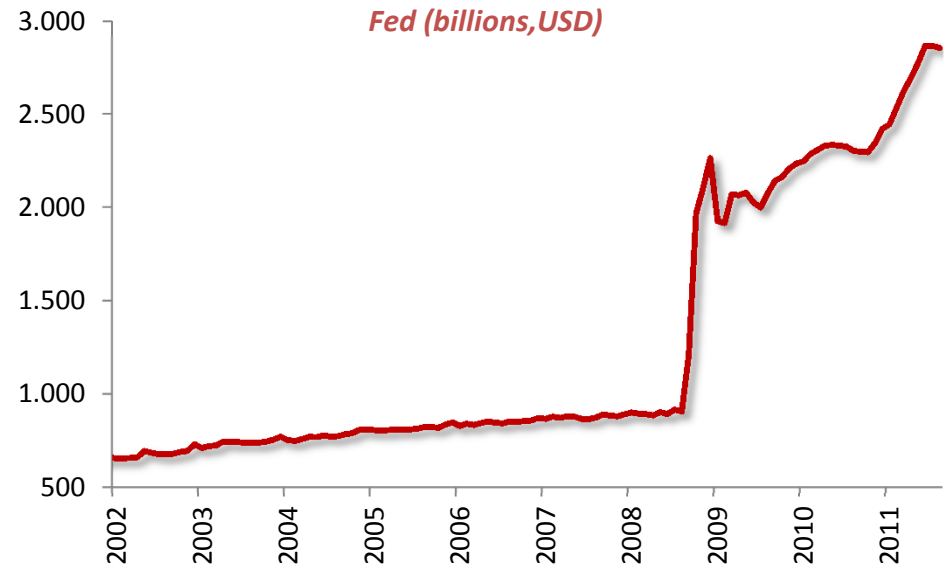
- Overview of monetary policy strategy since 2010 Q4
- Financial and price stability outcomes
- Outlook

# QE in Advanced Economies...

## Central Bank Balance Sheets



Source: ECB.



Source: FED.

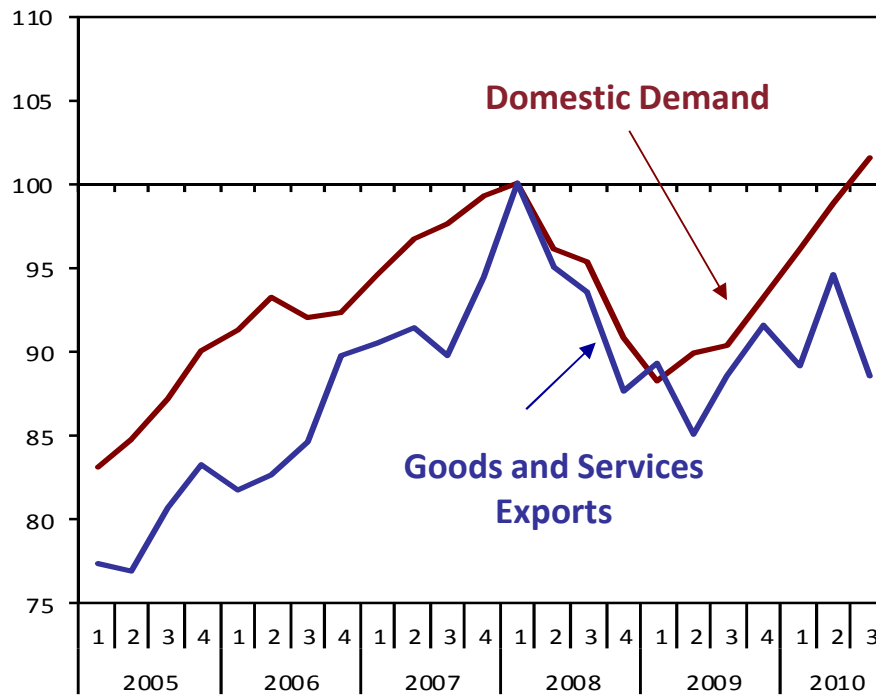
## Reflections on emerging economies...

- ☐ Increasing capital inflows
- ☐ Appreciation of real exchange rates
- ☐ Rapid credit expansion

# Reflections on Turkish economy...

**Rapid but unbalanced growth - strong domestic demand versus sluggish external demand**

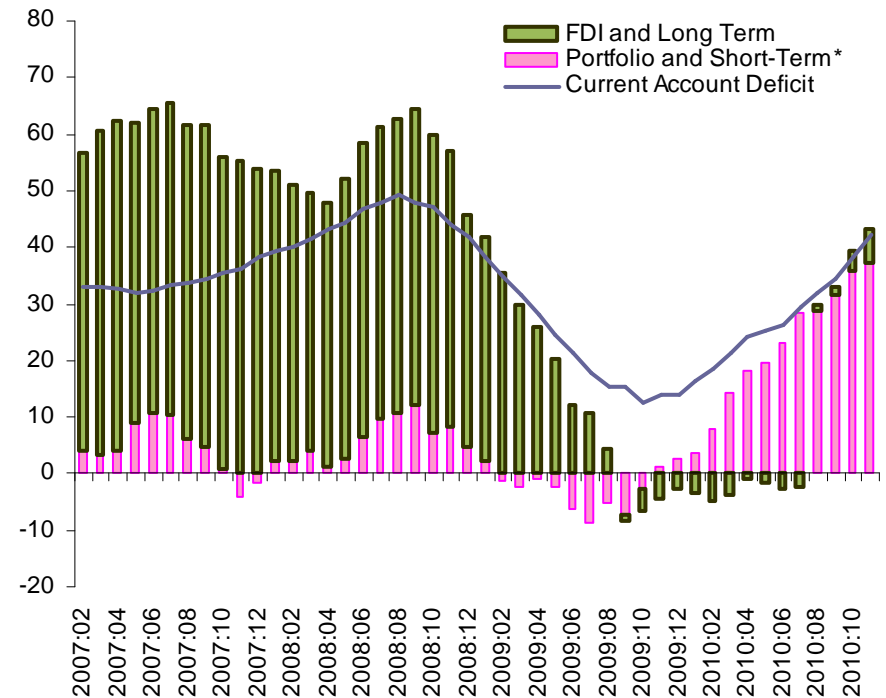
*Domestic Demand and Exports\*  
(2008 Q1=100)*



Source: TURKSTAT, CBRT

**CAD Widening, Mostly Financed by Short term Capital Inflows**

*Main Sources of Current Account Deficit Finance  
(12-months cumulative, billions USD)*

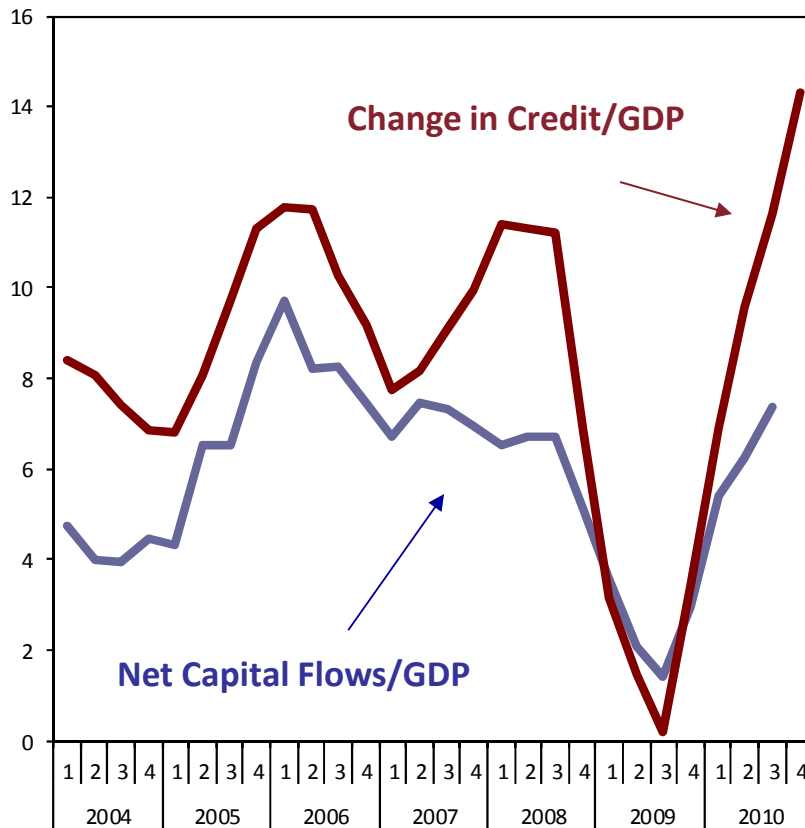


\*Portfolio and Short-Term: Equities, Domestic government bonds, short-term credits of banks and non-banks and deposits held in banks.

Source: CBRT.

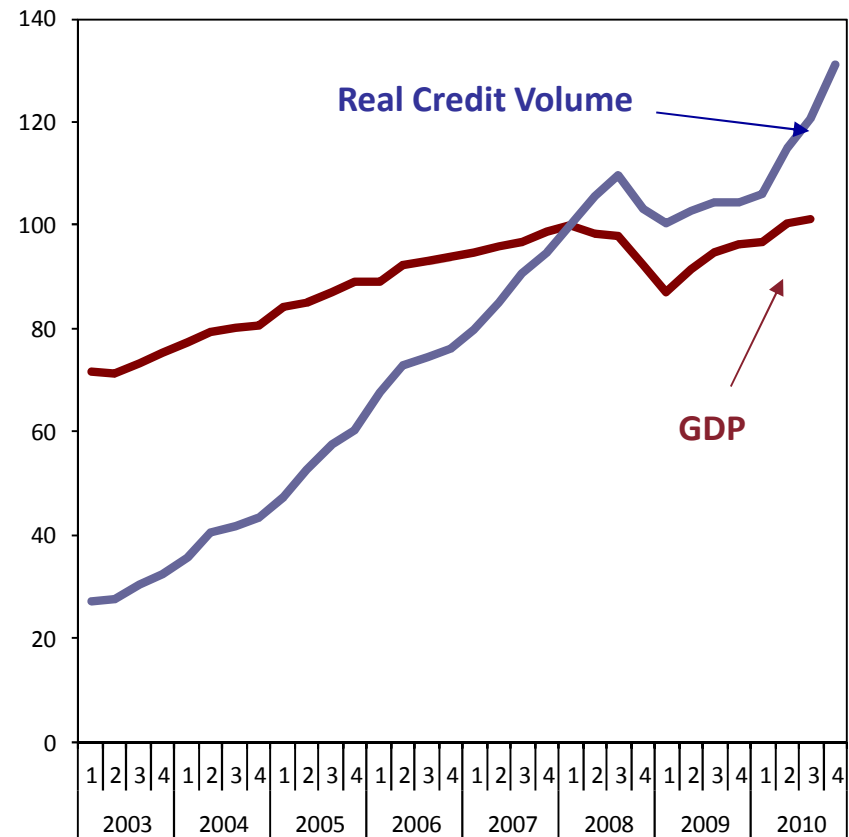
# Credit expansion gaining pace...

*Capital Flows and Credit Growth  
(percent)*



Source: TurkStat, CBRT

*Real GDP and Credit Volume  
(2008 Q1=100)*



Source: BRSA, TurkStat, CBRT

- *Composition of growth is not balanced - strong domestic demand versus sluggish external demand*
- *Capital flows are strengthening, but its composition is tilted towards short term investments*
- *Credit expansion gaining pace and current account deficit widening rapidly, increasing the vulnerability of the economy against sudden reversals in risk appetite, thus raising concerns for financial stability*



*Need for a different, yet prudent approach in monetary policy.*

# New Approach to Monetary Policy

## **BEFORE CRISIS**

*Single Goal : price stability*

*Single Instrument : short term  
policy rates*

## **AFTER CRISIS**

*Multiple Goals : price st. & financial st.*

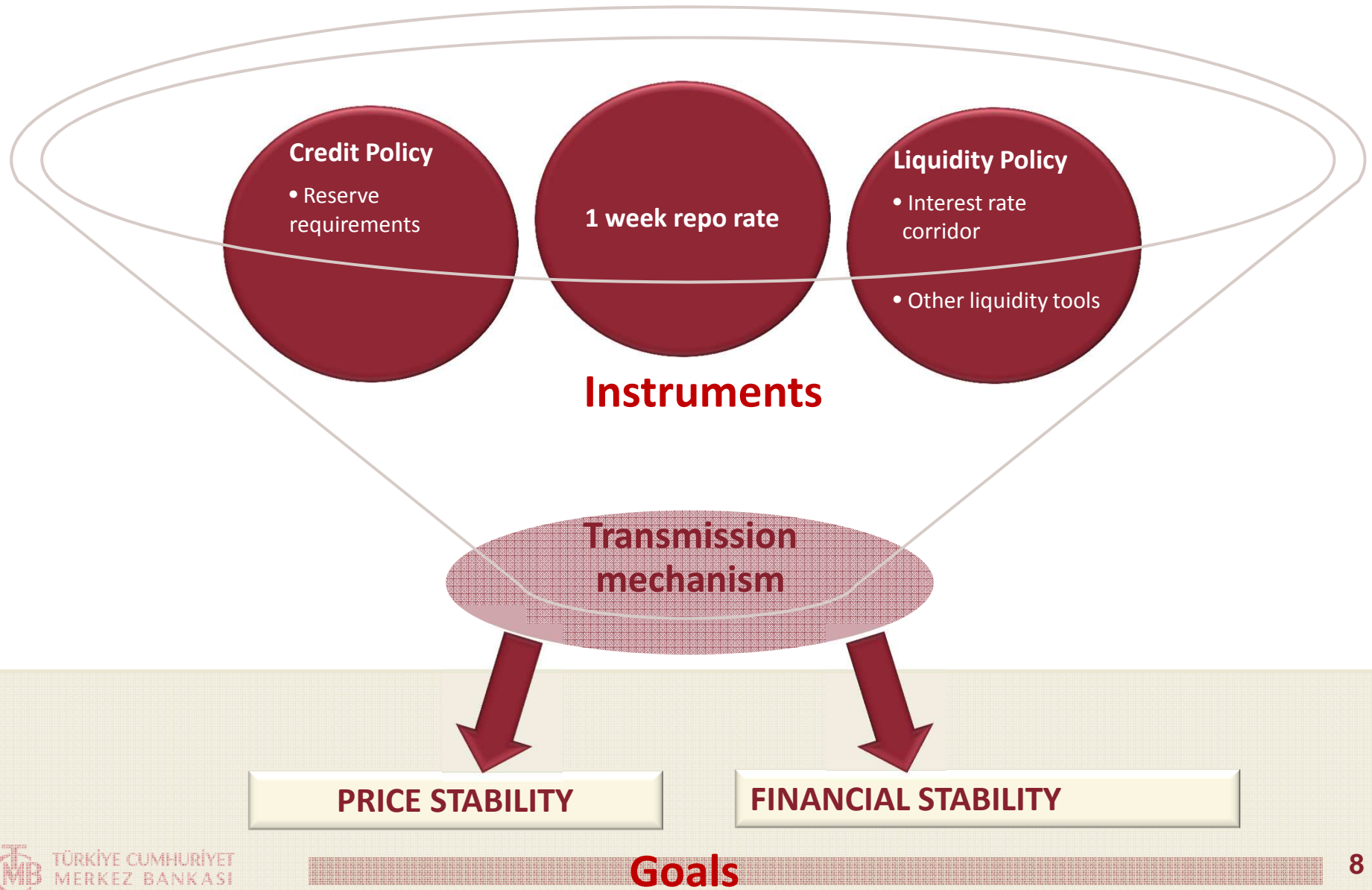
*Multiple Instruments : macroprudential  
tools and policy rates*

### **CBRT;**

❑ *modified existing framework of IT by explicitly highlighting the increasing role of financial stability in its objective function since mid-2010.*

❑ *geared its policies towards two intermediate objectives:*

- *discouraging 'short term' capital inflows*
- *containing domestic credit growth.*





*Using macroprudential tools in coordination with all the relevant public authorities.*

## ***CBRT's New Policy Mix:***

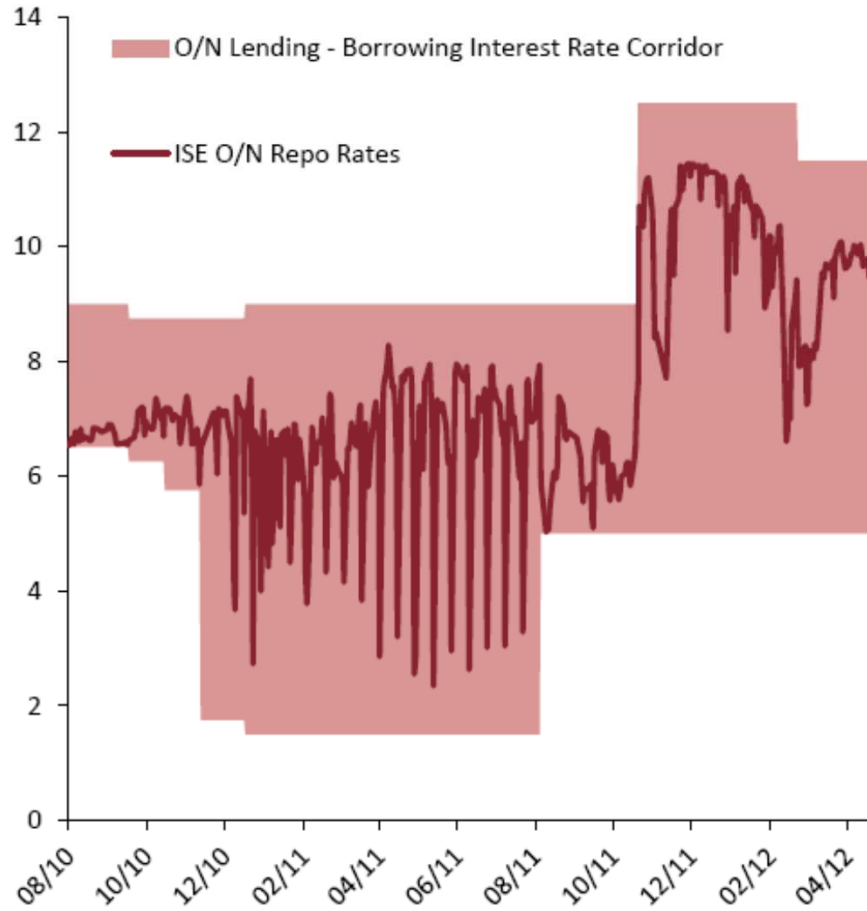
*'the required reserve ratios'*  
&  
*'the interest rate corridor'*

## ***Measures by other authorities:***

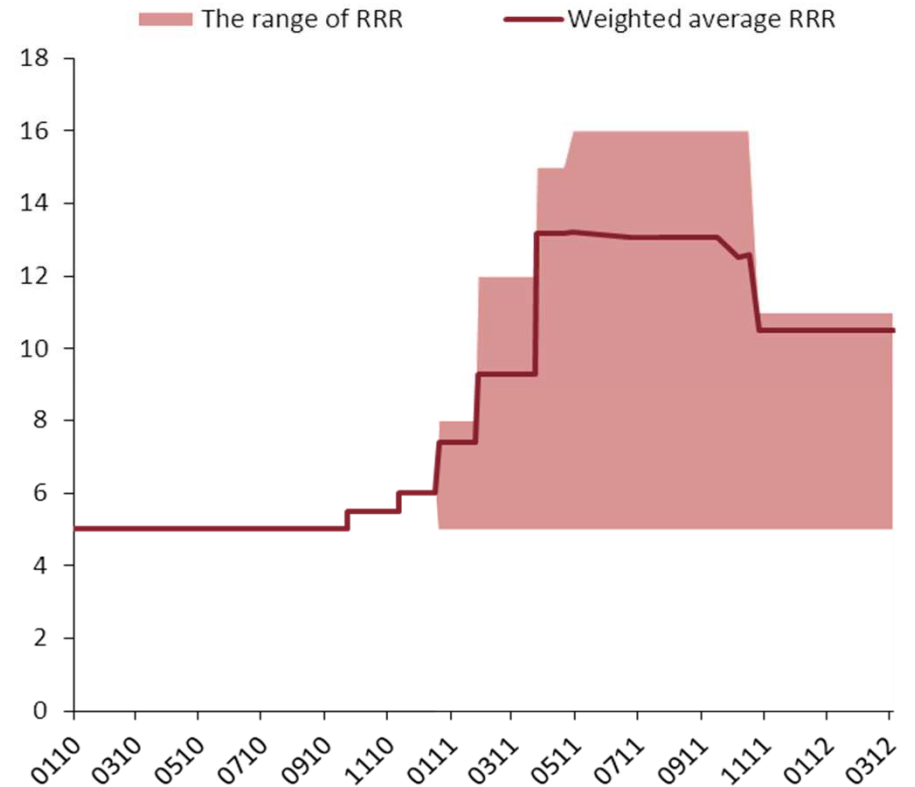
- *Fiscal discipline*
- *No FX loans to households*
- *Domestic currency bond market*
- *Loan/value restrictions*
- *Tax hikes on certain consumer loans*
- *Restrictions on credit card borrowing*

- November 2010 – August 2011
  - Discourage short-term capital inflows
  - Control credit growth
  - Prevent excessive appreciation of the Turkish lira
  
- August – October 2011
  - Response to capital outflows
  - Support domestic activity
  
- October 2011 - present
  - Control inflation
  - Monitor credit growth

## CBRT Policy Rates (Percent)



## TL Required Reserve Ratios (Percent)



## **Initial Impact of the New Policy Mix on Financial Markets**

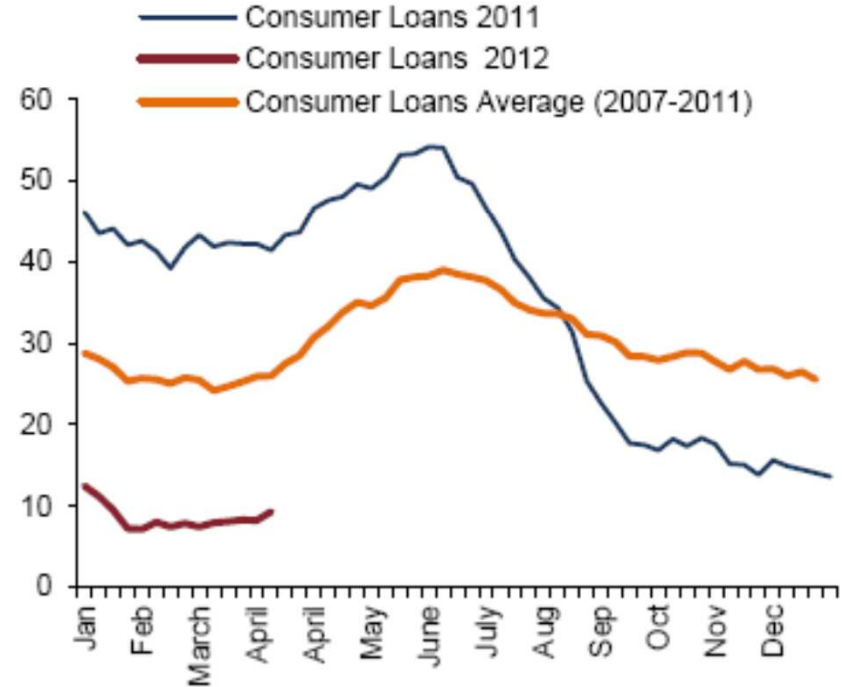
# Effect on Exchange Rates & Loan Growth

TL and Emerging Market Currencies\*  
(01.11.2010 = 1)



\* Average of emerging market currencies including Brazil, Chile, Czech Republic, Hungary, Mexico, Poland, South Africa, Indonesia, South Korea and Colombia, against USD. Increases denote depreciation of the currency.

Loan Growth Rates\*  
(Percent, 13-Week Average, Annualized)



\* Adjusted for the exchange rate effect.

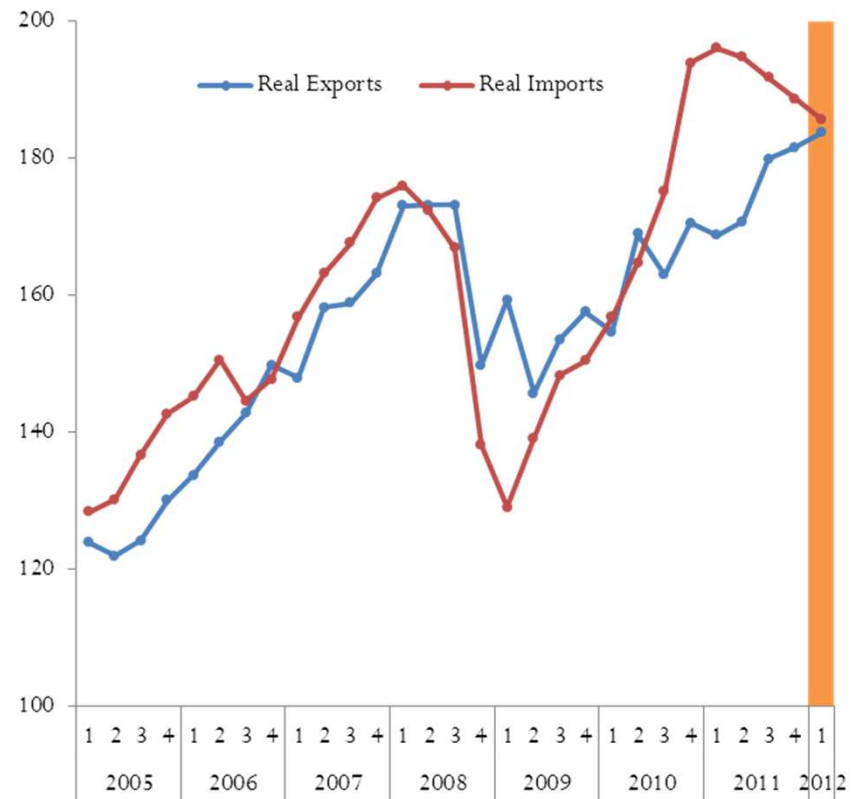
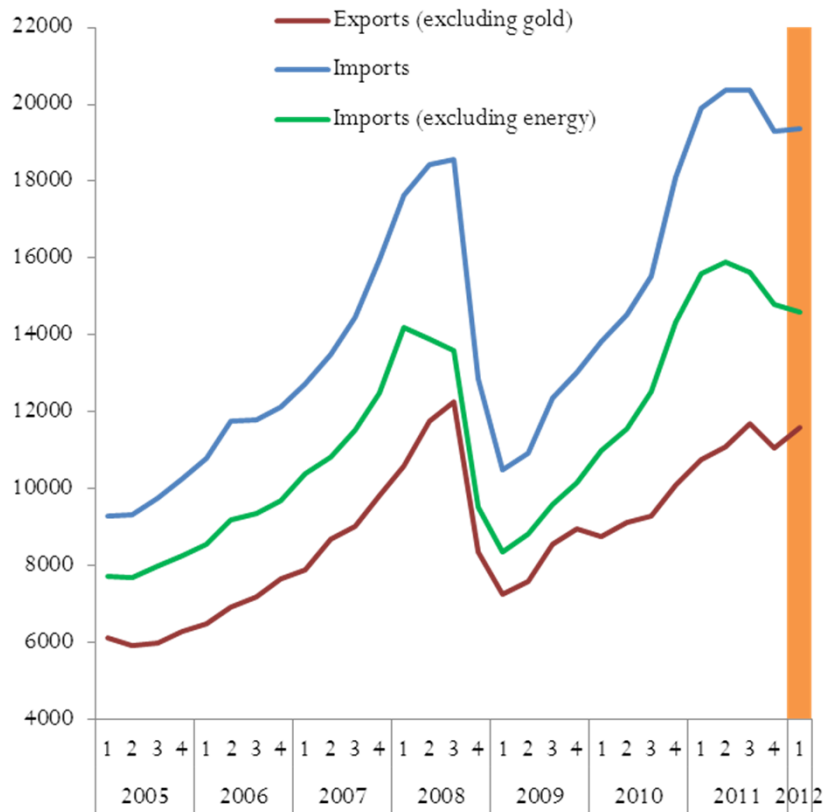
\* Average of normalized exchange rates of Brazil, Chile, Czech Republic, Hungary, Mexico, Poland, S. Africa, Indonesia, South Korea and Colombia. Increases imply depreciation of domestic currency against USD.

Source: Bloomberg, CBRT.

Latest Observations: February 24, 2012

# Rebalancing between the domestic and external demand

## Exports and Imports\* (seasonally adjusted)

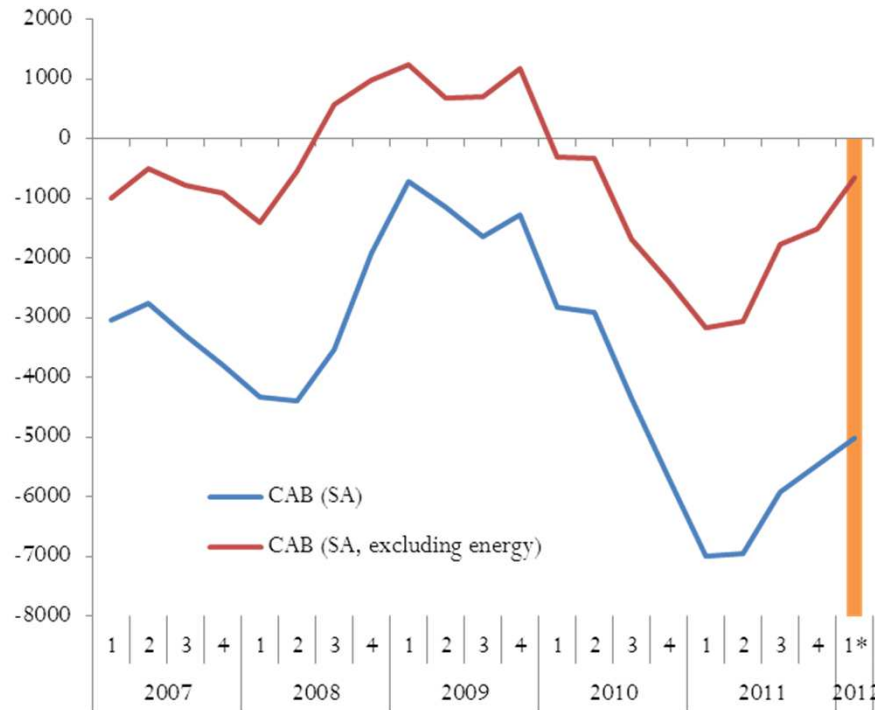


Source: TurkStat, CBRT.

\*Estimate for q1 2012.

## Soft landing is on the way in CAB

**Current Account Balance (CAB)**  
(Seasonally Adjusted, Quarterly Average,  
Million USD)



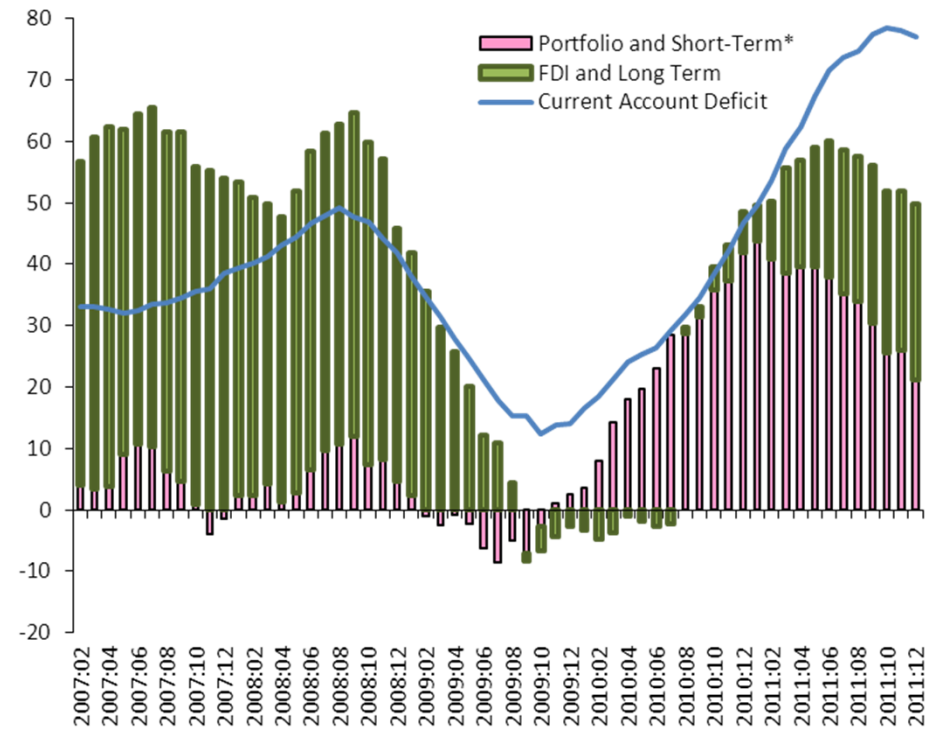
Source: TurkStat, CBRT.

\*Forecast.

Latest Observations: q4 2011

## The share of long term financing started to exceed short term

**Composition of Capital Flows**  
(12-months Cumulative, Billions USD)



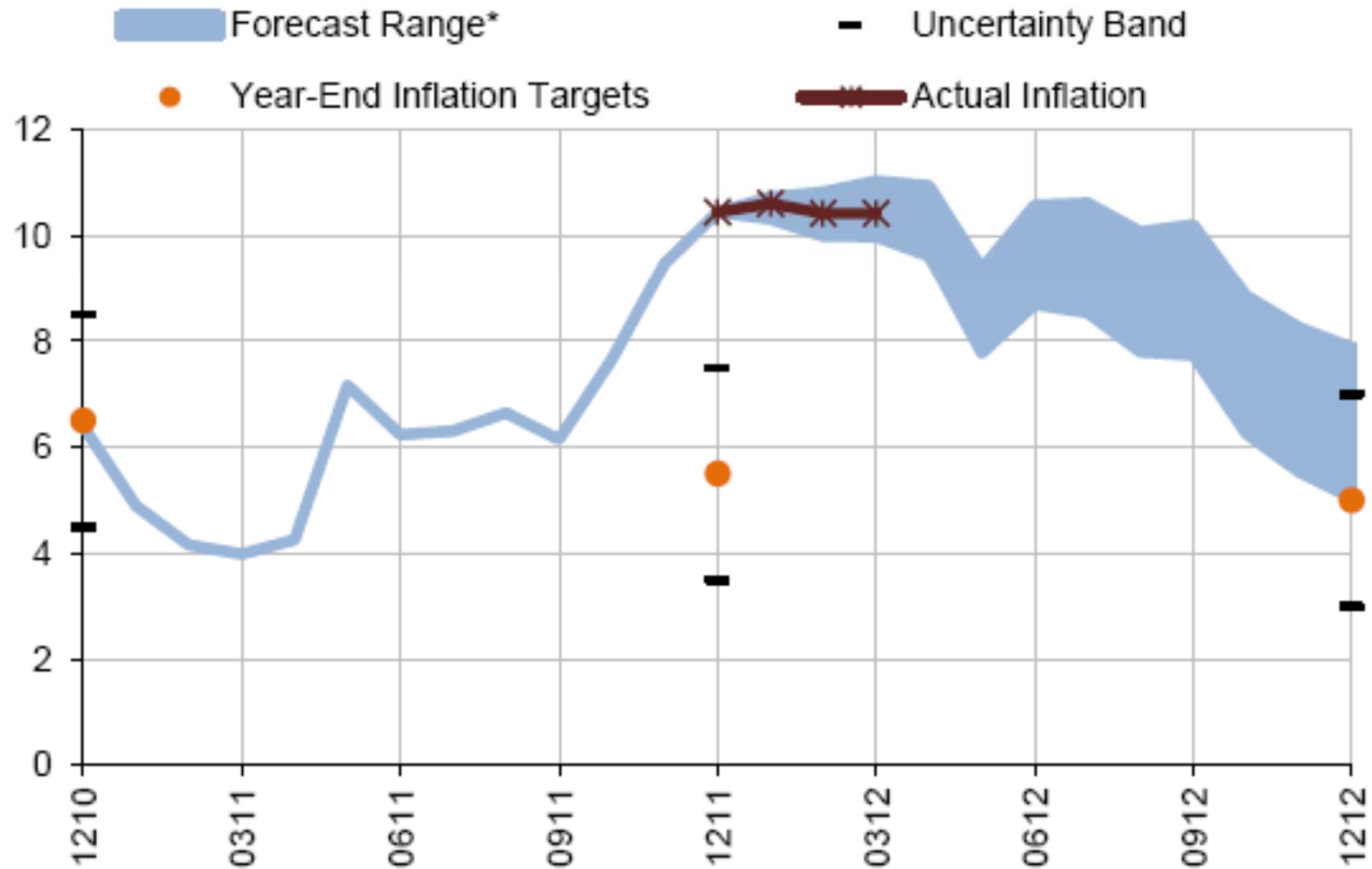
\*Portfolio and Short-Term: Equities, Domestic government bonds, short-term credits of banks and non-banks and deposits held in banks.

Source: CBRT

Latest Observation : December 2011.

# Inflation Surged...

January 2012 Inflation Forecasts and Realizations (Percent)



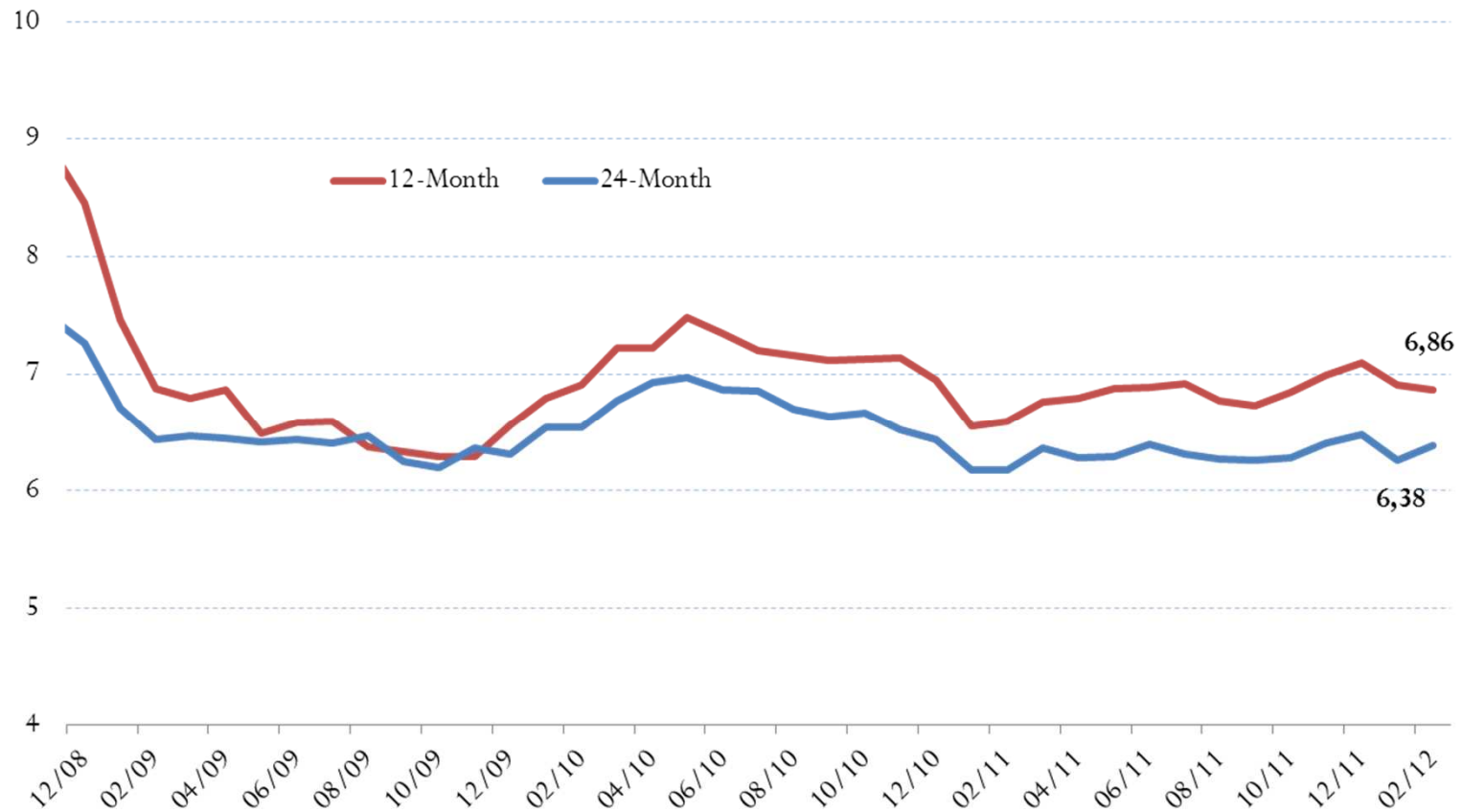
\* Shaded region indicates the 70 percent confidence interval for the forecast.

Latest observations: February 2012



## ... But inflation expectations are well anchored

### *Inflation Expectations\**



Source: CBRT.

\*CBRT Survey of Expectations, second survey period results.

Latest Observations: February 2012

- Post crisis dynamics emphasized the importance of financial stability and led the central banks towards implementation of unconventional policies.
- CBRT is implementing a new policy strategy in order to limit the macro financial risks.
- This new policy mix, has proved to be successful in rebalancing domestic and external demand, without damaging inflation expectations.
- Annual inflation will remain high for a while due to the cumulative effects of foreign exchange movements. With the gradual elimination of these effects, inflation is expected to converge to the 5 percent target in mid-2013.



TÜRKİYE CUMHURİYET  
MERKEZ BANKASI

# **Turkish Monetary Policy Experience with the Recent Financial Crisis**

4 May 2012

Istanbul