



TÜRKİYE CUMHURİYET  
MERKEZ BANKASI

# MACROECONOMIC OUTLOOK AND MONETARY POLICY IN TURKEY

February 9, 2017

London

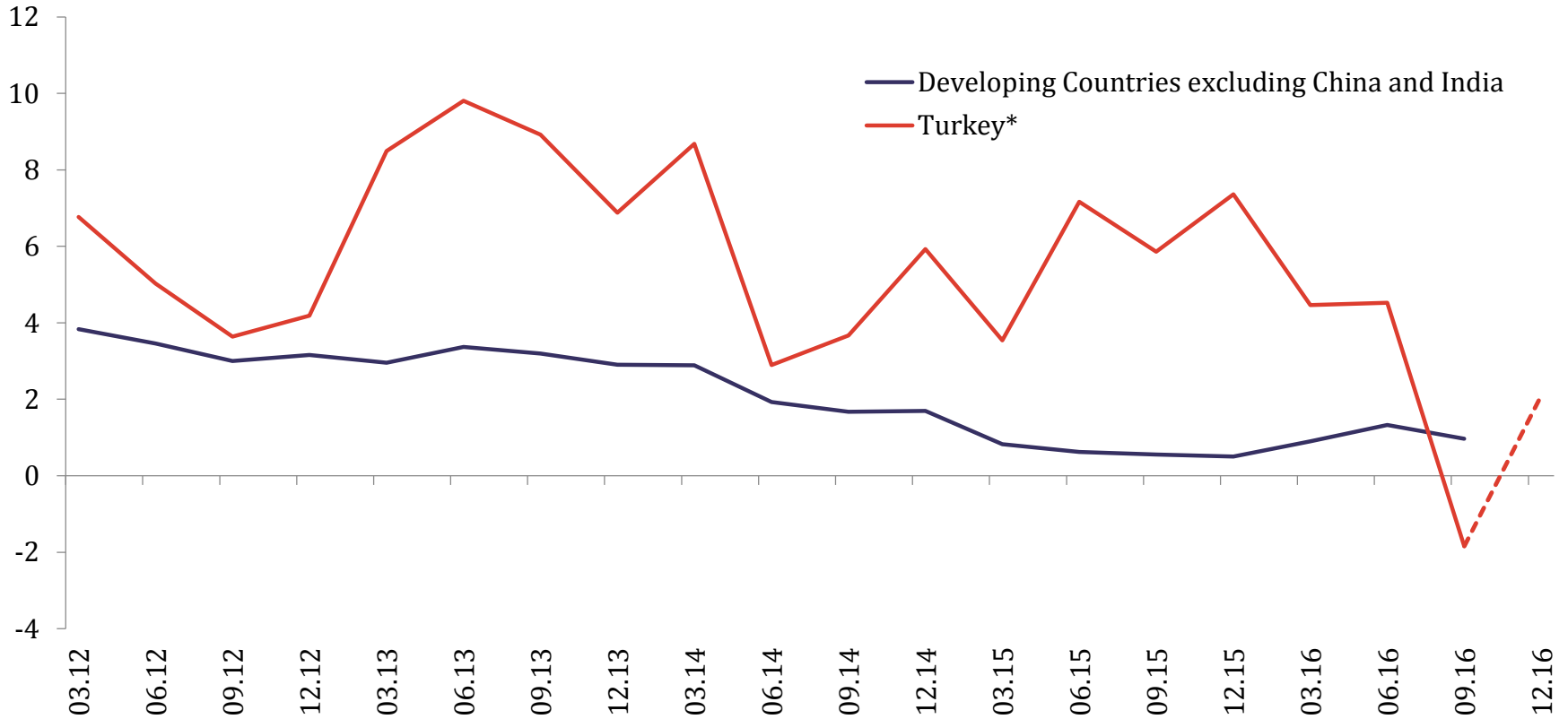
# Outline

- I. Macroeconomic Outlook
- II. Monetary Policy

# Macroeconomic Outlook

# Turkish economic growth has outperformed emerging economies until recently.

**Growth Rates in Turkey and Emerging Economies**  
(Percentage Change, Annual)



\* Forecast for 2016 Q4.

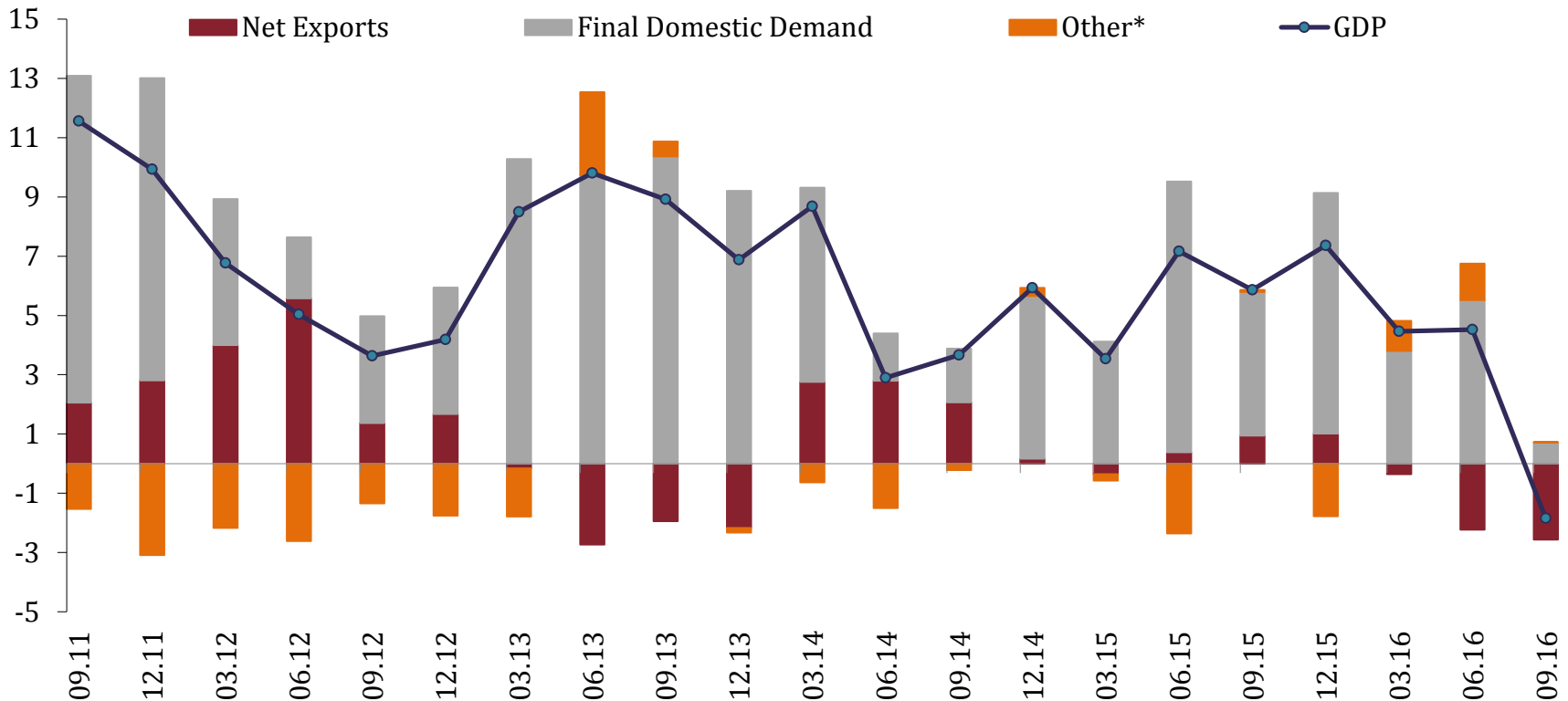
Source: Bloomberg, CBRT.

Last Observation: 2016 Q4

**Developing Countries excluding China and India:** Brazil, Chile, Colombia, Czechia, Hungary, Indonesia, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Romania, Russia, S Africa, Thailand, Turkey, Ukraine.

# Economic activity slowed down in the third quarter due to concurrent domestic and external shocks.

**Growth Rates in Turkey and Emerging Economies**  
(Percentage Change, Annual)



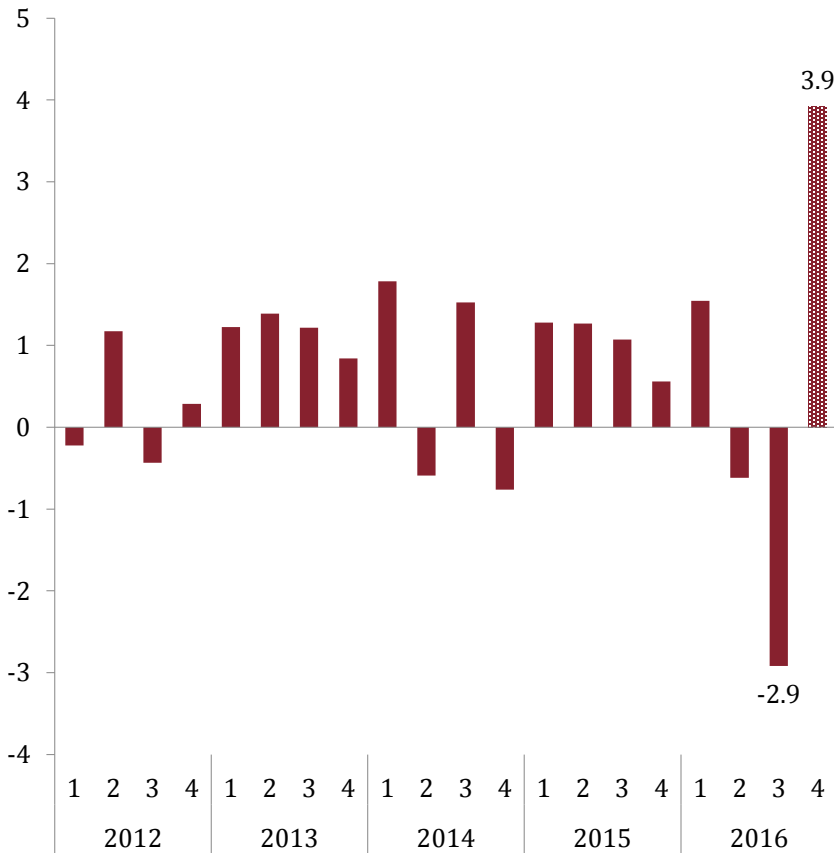
\*Contains stock movements and residual item

Source: TURKSTAT

Last Observation: 2016 Q3

# The contraction in 2016 Q3 proved temporary as production displayed a rebound in Q4.

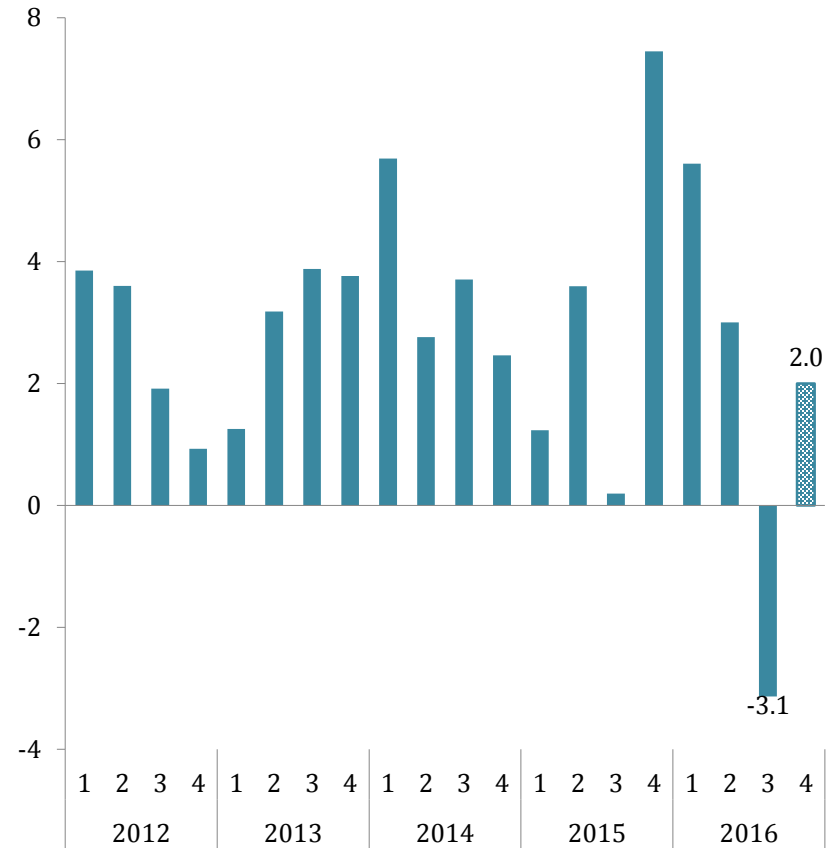
**Industrial Production**  
(QoQ, Seasonally Adjusted)



Source: TURKSTAT, CBRT.

Last Observation: 2016 Q4

**Industrial Production**  
(YoY)

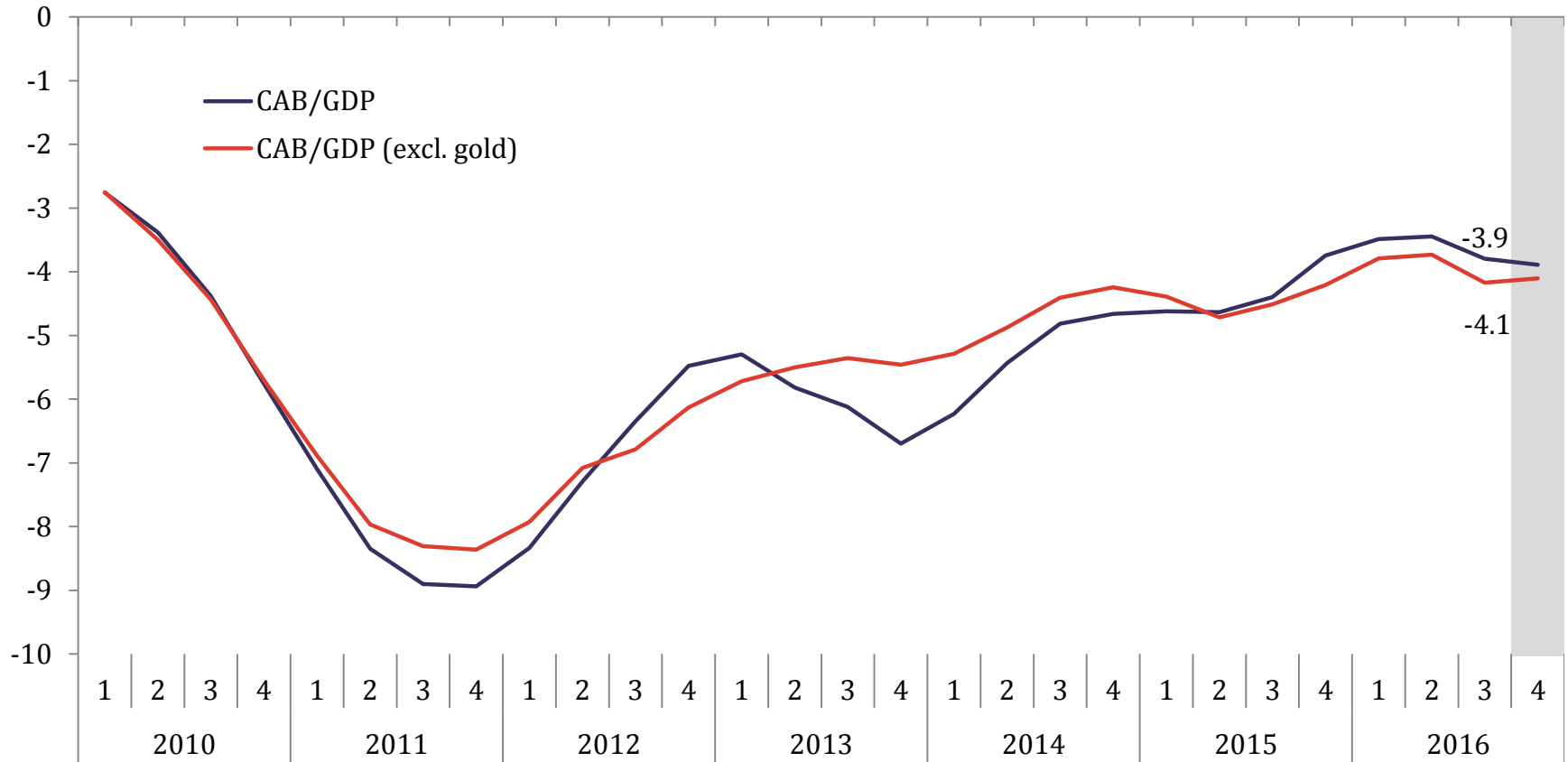


Source: TURKSTAT, CBRT.

Last Observation: 2016 Q4

# Current account balance have posted a marked improvement in recent years.

**Current Account Balance (CAB)**  
(12-Month Cumulative, Percent of GDP)

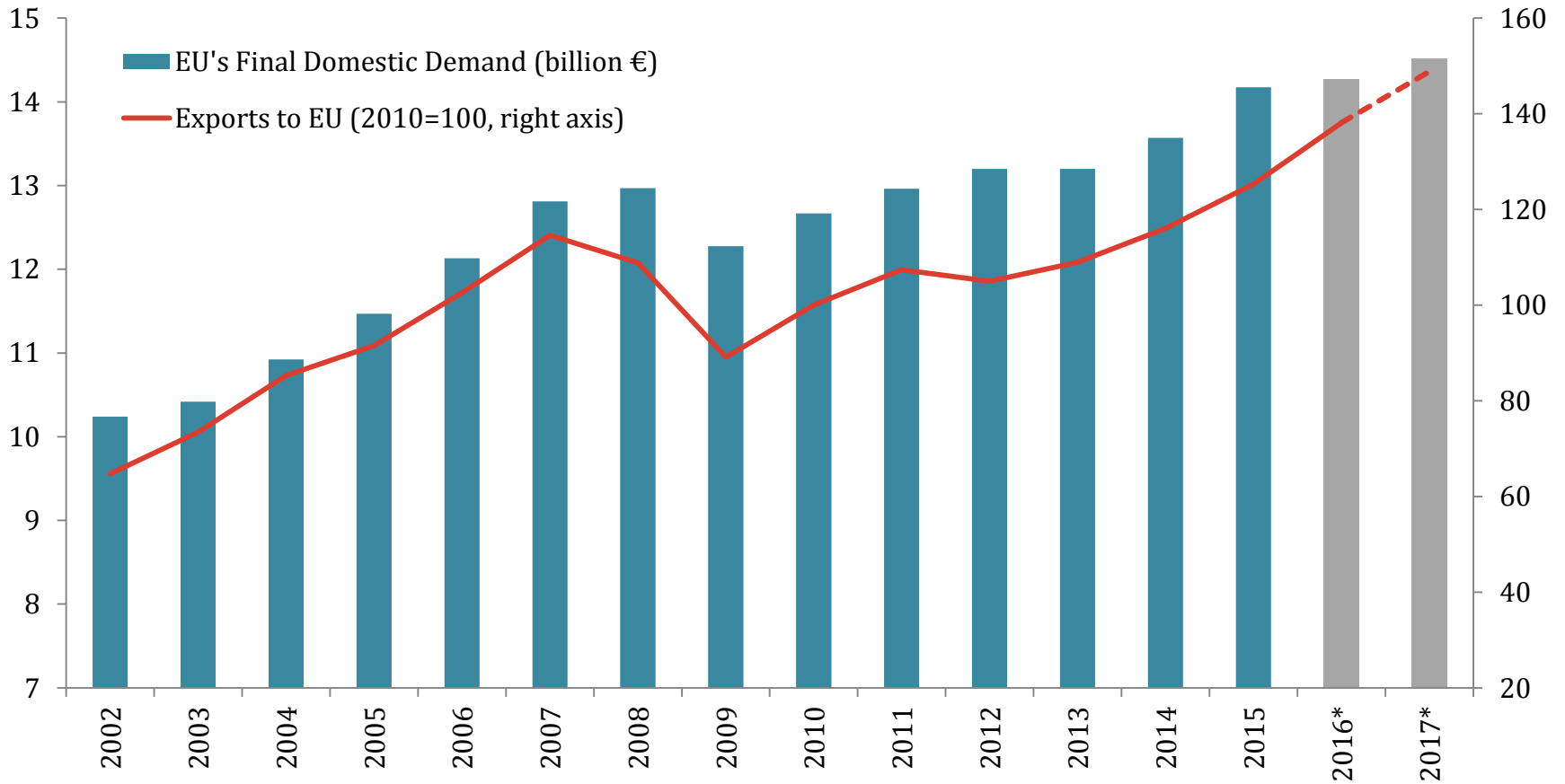


Source: CBRT

Last Observation: 2016 Q3

Demand from the European Union economies will continue to provide significant contribution to export growth.

### Exports to EU and EU's Final Domestic Demand



Source: Eurostat, IHS CBRT

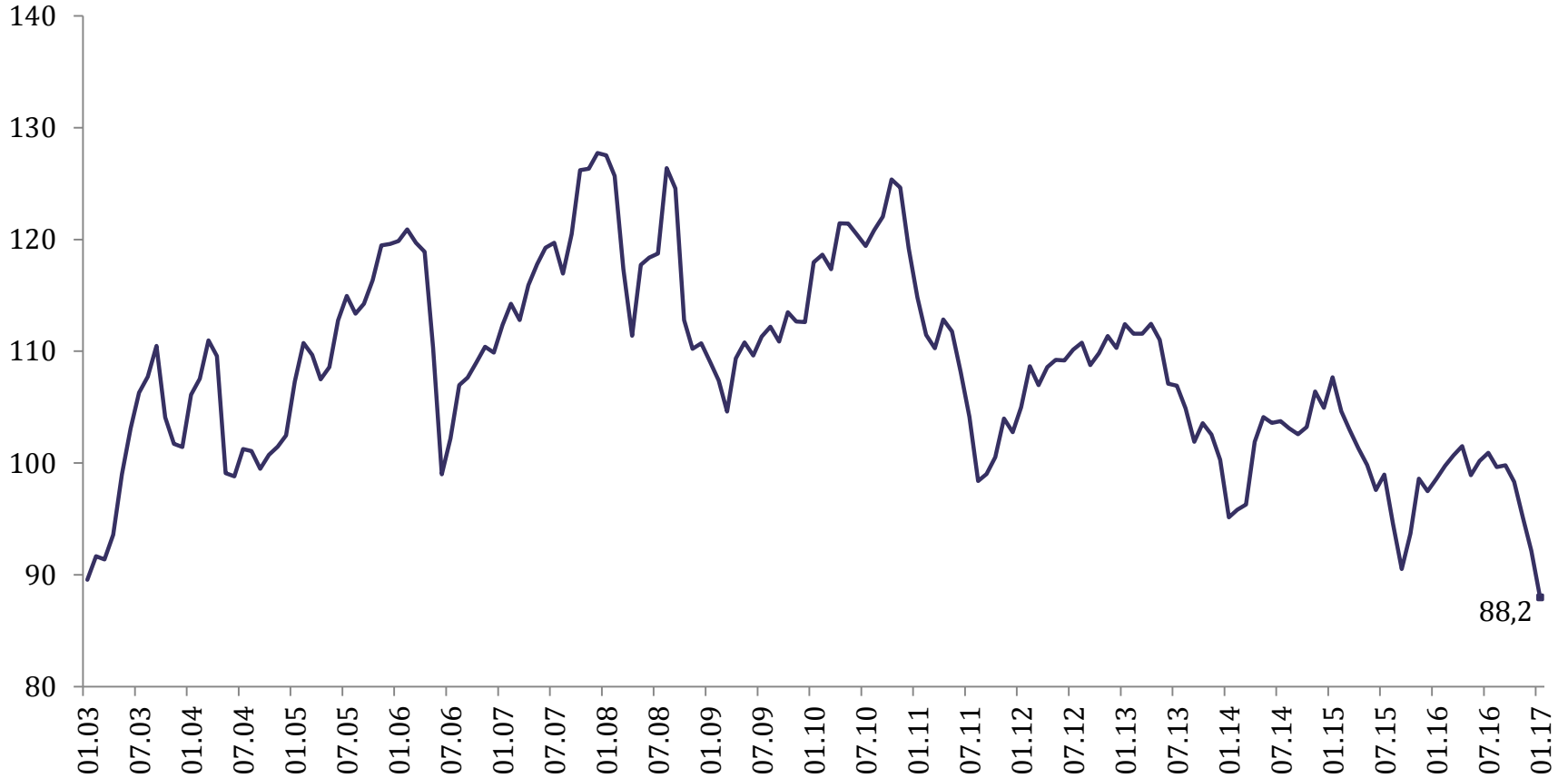
\* Forecast.



Real exchange movements in recent years have boosted the competitiveness of the economy.

### Real Effective Exchange Rate

(CPI Based, 2003=100)

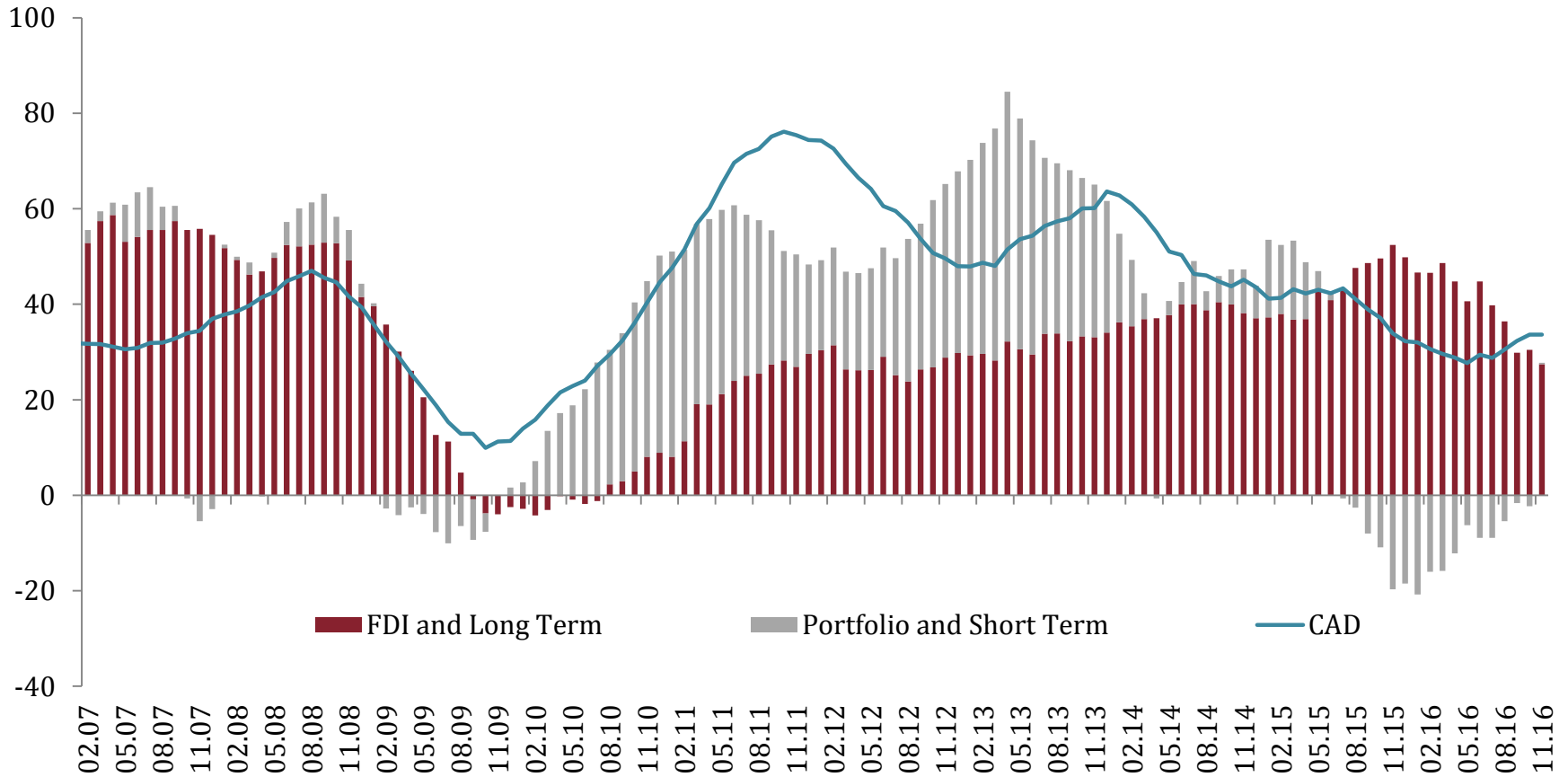


Source: CBRT

Last Observation: January 2017.

# Current account deficit is financed mainly through long term borrowing and FDI flows.

(12 Month Cumulative, Billion USD)



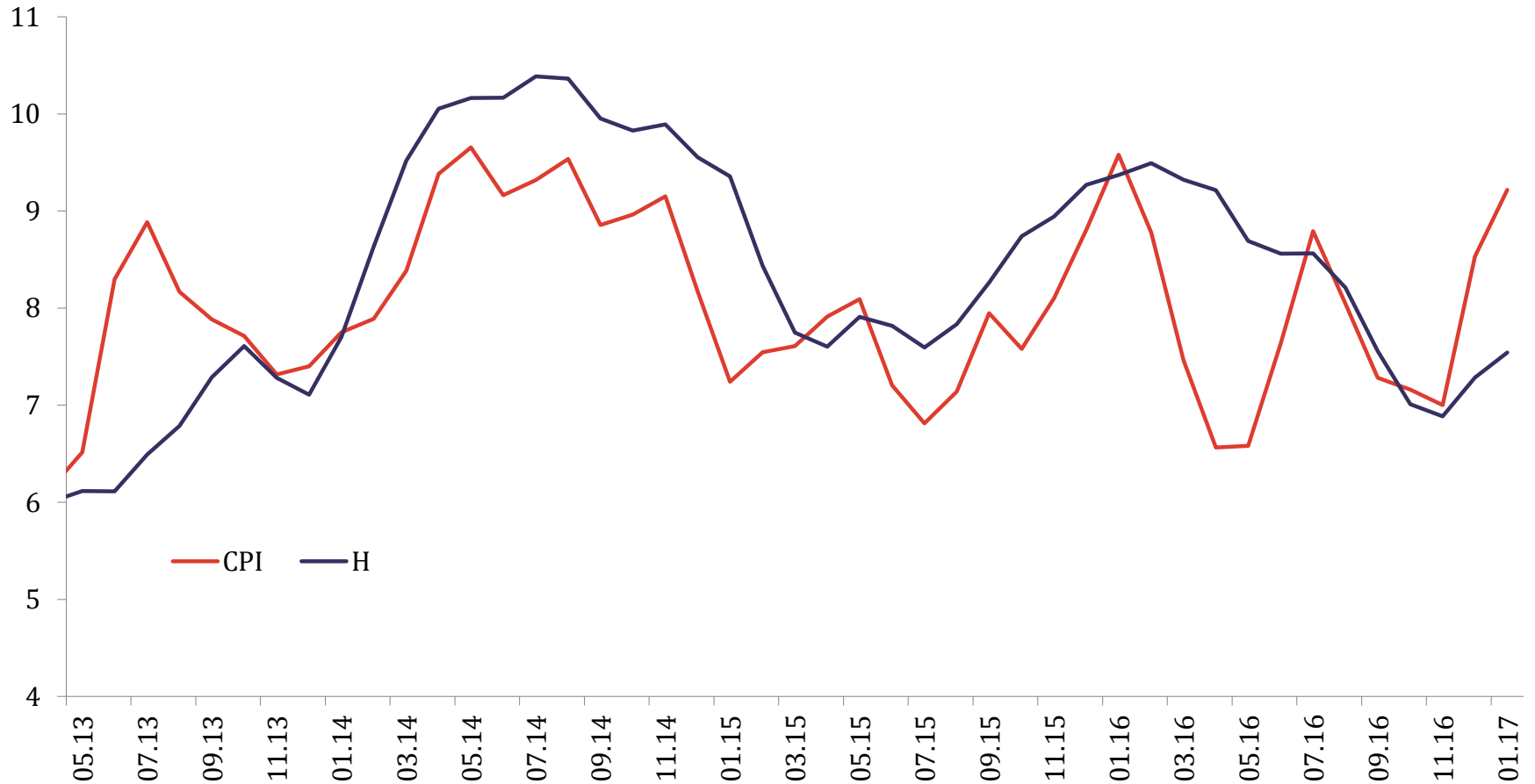
\*Long term inflows are sum of banking and real sectors' long term net credit and bonds issued by banks and the Treasury. Short term capital movements are sum of banking and real sectors' short term net credit and deposits in banks.

Source: CBRT.

Last Observation: November 2016

Recently, CPI inflation has increased due to an upward correction in food prices and the FX pass-through effect.

**Headline CPI and Core Price Indicator**  
(Annual Percentage Change)

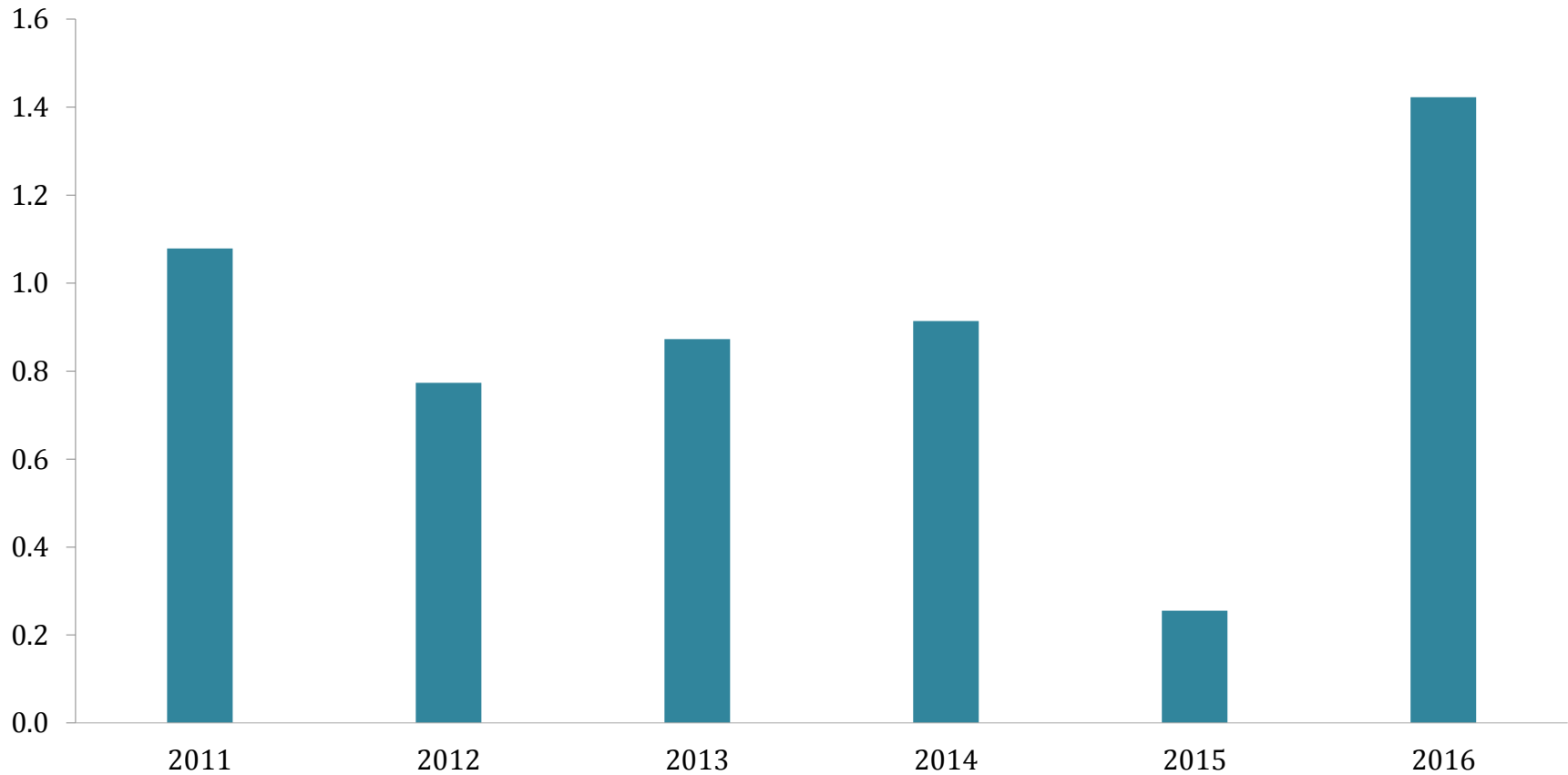


Source: TURKSTAT, CBRT

Last Observation: January 2017

The historically high impact of tax adjustments during the past year is expected to fade away throughout 2017.

### Contribution of Tax Adjustments to Inflation (Percent)

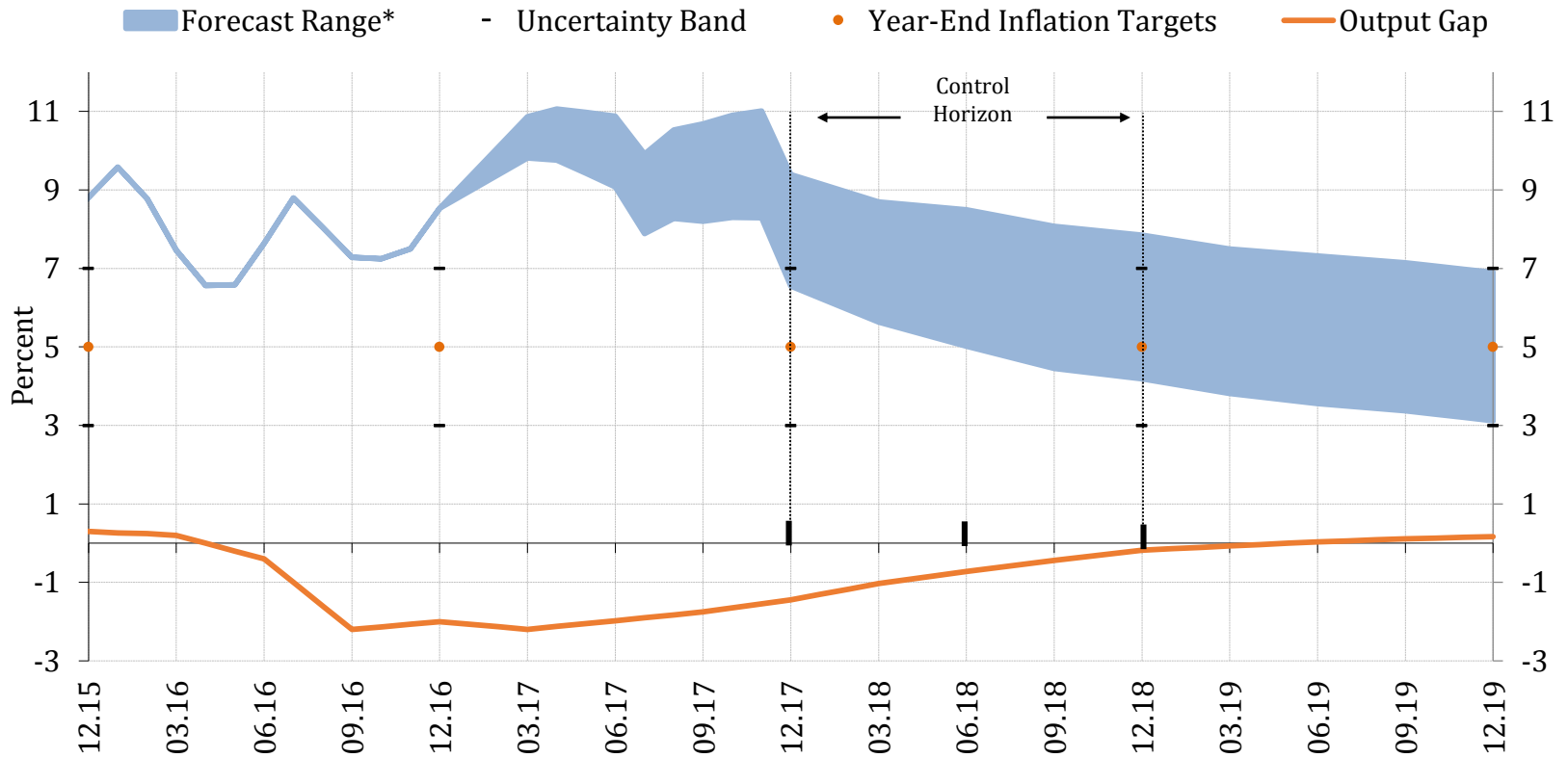


Source: TURKSTAT, CBRT

Last Observation: December 2016

Inflation is projected to further increase in the near term before falling gradually towards 5 percent target by 2019.

### January 2017 Inflation Report Forecasts



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

Source: January 2017 Inflation Report.

# The Policy Response

# Main Policy Strategy

- The CBRT has taken a series of steps to simplify monetary policy throughout 2016.
- However, irrational pricing behavior observed in foreign exchange market as of early January necessitated an alternative approach.
- The response to these unprecedented developments had to be swift, strong, and targeted.
- Accordingly, a comprehensive policy package was designed implemented to address the root cause of the problem.
  - Tighter liquidity conditions
  - Currency swaps

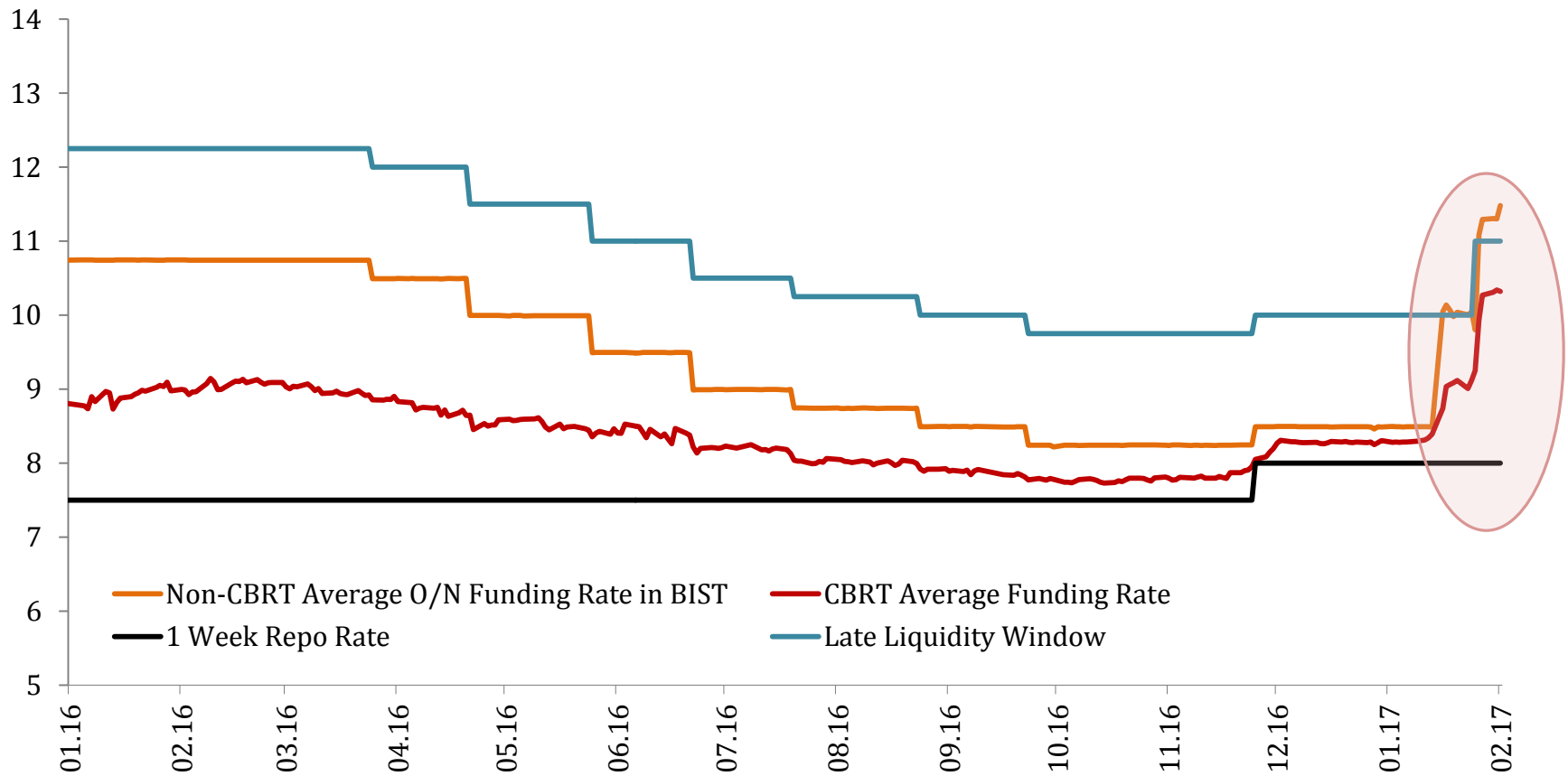
# January MPC Statement

- Aggregate demand developments support disinflation. Yet, excessive fluctuations in exchange rates since the previous meeting have increased the upside risks regarding the inflation outlook.
- Accordingly, the Committee decided to strengthen the monetary tightening in order to contain the deterioration in the inflation outlook.
- The Central Bank will continue to use all available instruments in pursuit of the price stability objective.
- Future monetary policy decisions will be conditional on the inflation outlook.
- Inflation expectations, pricing behavior and other factors affecting inflation will be closely monitored and, if needed, further monetary tightening will be delivered.
- Moreover, necessary liquidity measures will be taken in case of unhealthy pricing behavior in the foreign exchange market that cannot be justified by economic fundamentals.



# The CBRT has significantly tightened monetary policy.

CBRT Interest Rates  
(Percent)

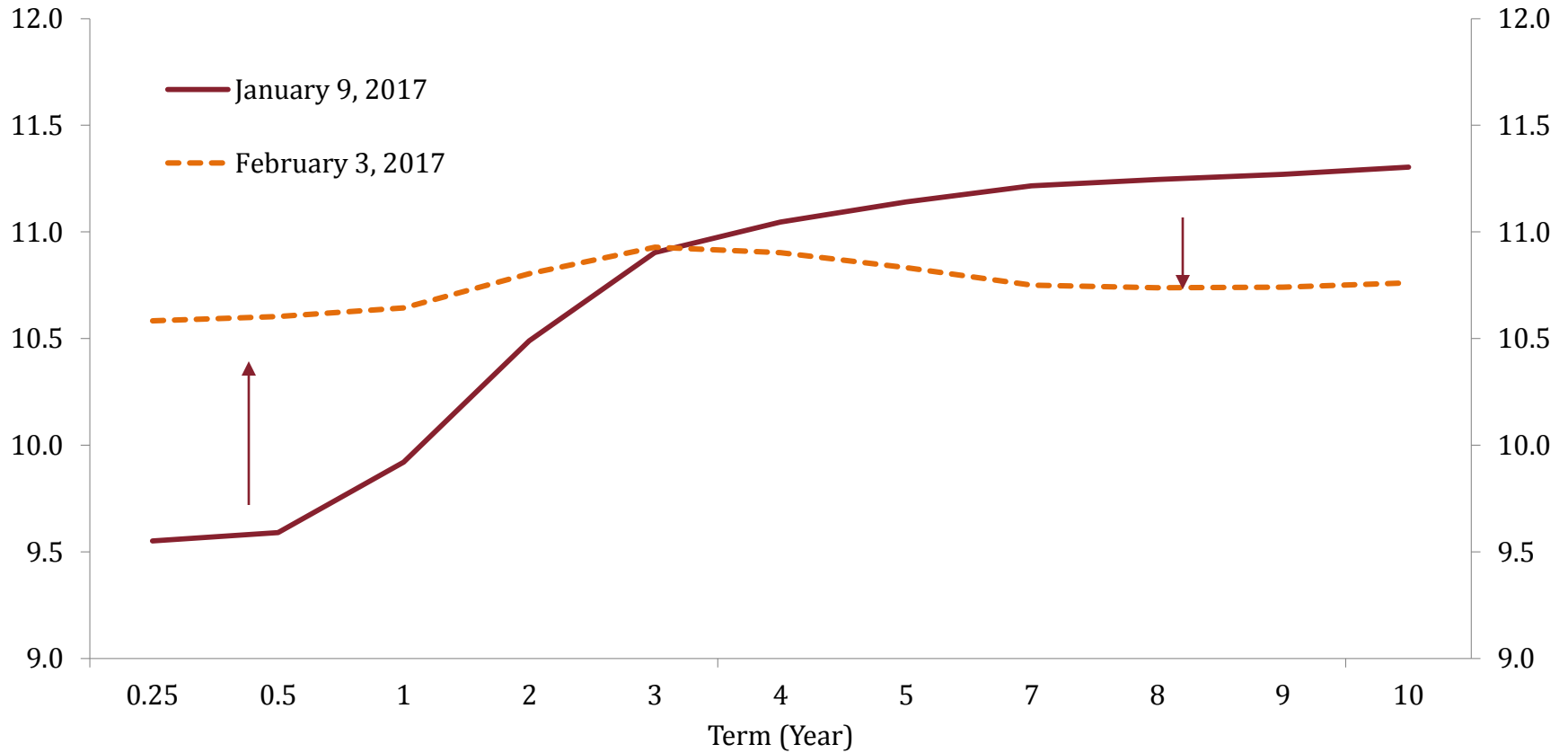


Source: CBRT, BIST

Last Observation: February 01, 2017

The yield curve has flattened after the policy response.

**Yield Curve**  
(Treasuries, Percent)



Source: Bloomberg

Last Observation: February 03, 2017

Monetary tightening is evident in the slope of the yield curve.

### 5 Year-3 Month Differential in Swap Rates

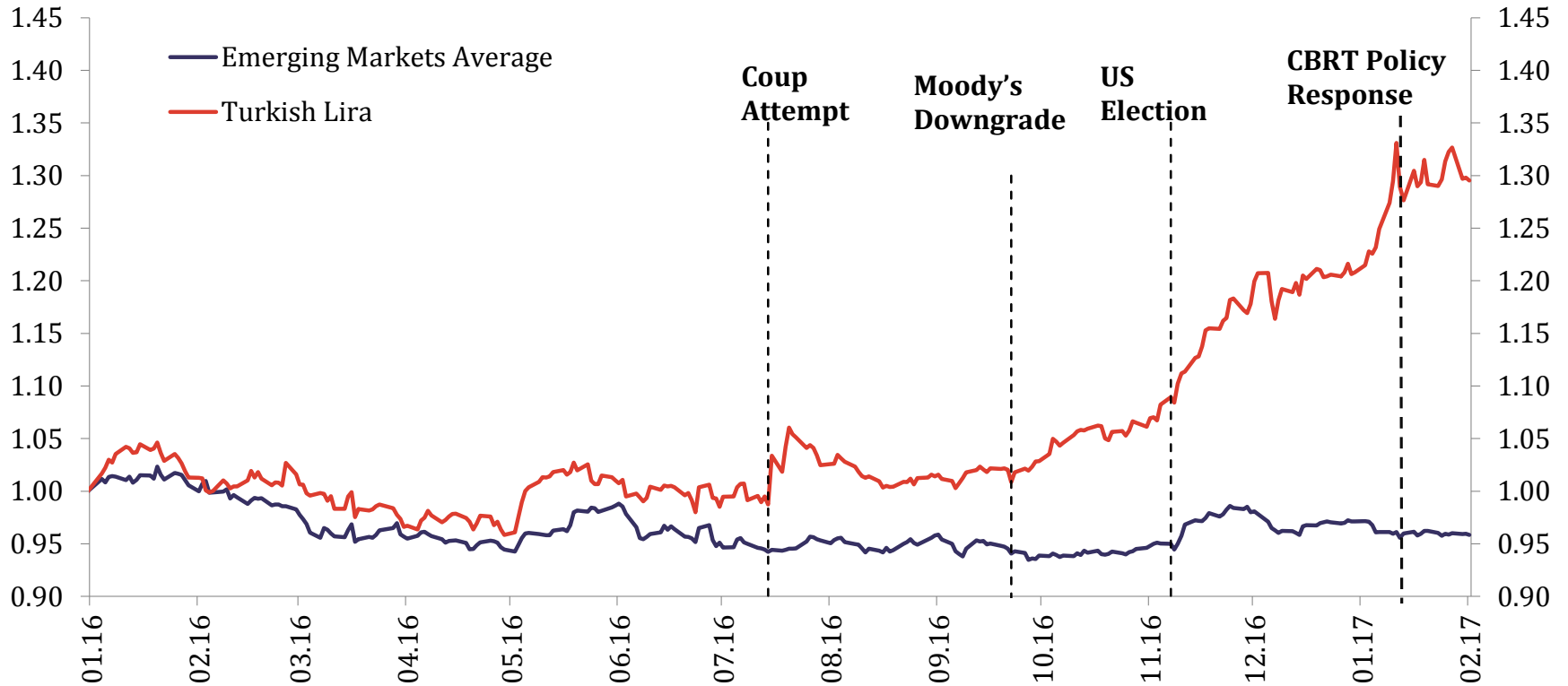


Source: CBRT, Bloomberg

Last Observation: February 03, 2017

Turkish lira, which has depreciated sharply in the second half of 2016, stabilized after the monetary policy response.

TL and EM Currencies Against USD  
(01.01.2016=1)



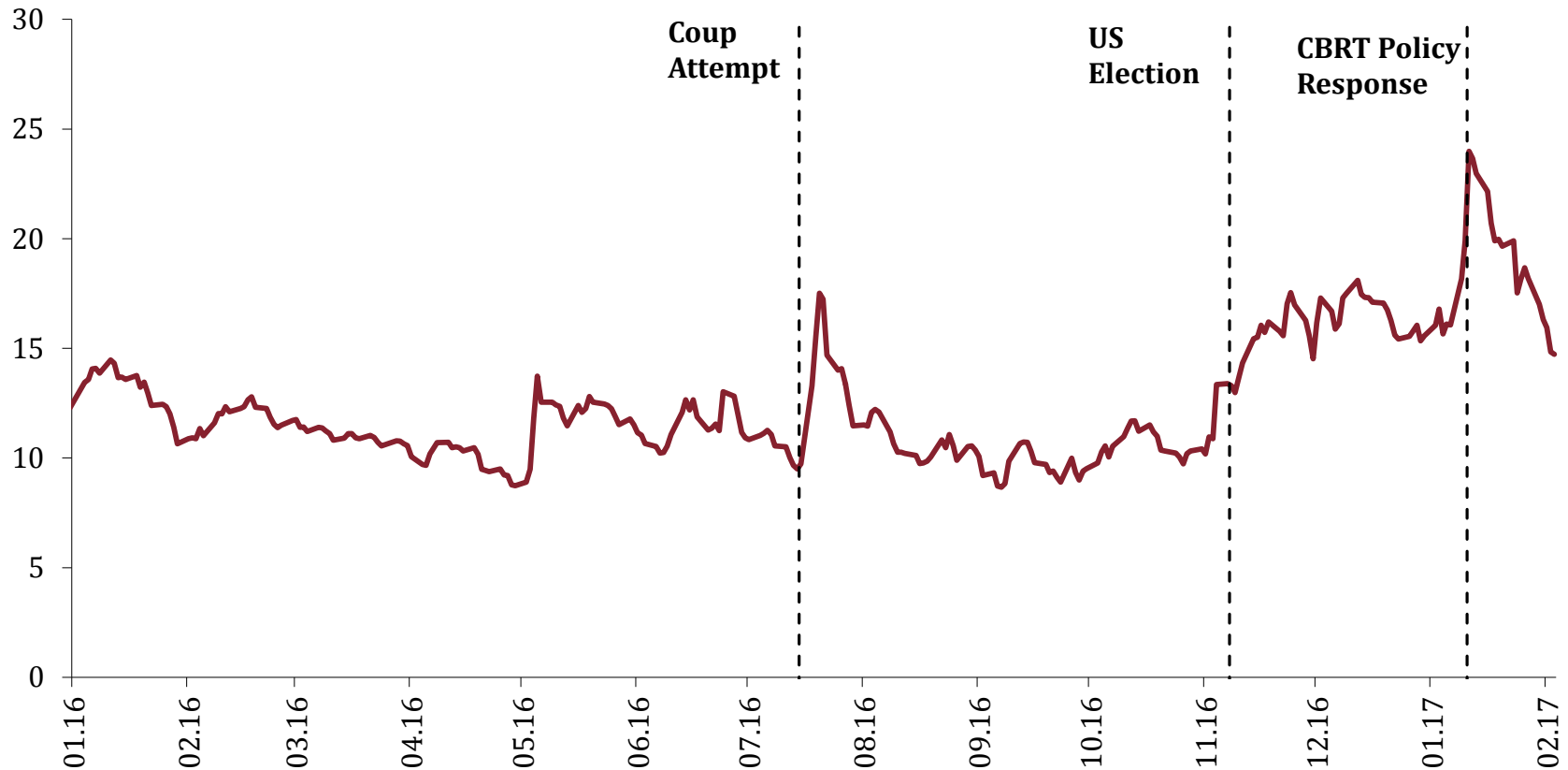
Emerging markets include Brazil, Chile, Colombia, Hungary, Indonesia, Malaysia, Mexico, Philippines, Poland, Romania, S. Africa.

Source: Bloomberg

Last Observation: February 01, 2017

# Currency volatility abated shortly after the policy response.

**Options Implied TL Volatility**  
(1-Month, Percent)



Source: Bloomberg

Last Observation: February 03, 2017

# Overview: Coordinated Policy Response

- Turkish economy proved resilient against concurrent shocks.
- Yet, developments since mid-2016 have led to a slowdown in the economic activity and cost-push based pressures on inflation.
- A coordinated policy mix was adopted to address the trade-offs.
  - The CBRT tightened monetary policy with a price stability objective.
  - The regulatory and government authorities have taken comprehensive measures to support the credit channel.
  - Fiscal and monetary policy coordination has been strengthened.
- These concerted efforts will not only bring inflation gradually towards to the 5 percent target, but also support the economic recovery in the forthcoming period.



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