



**TÜRKİYE CUMHURİYET
MERKEZ BANKASI**

THE ECONOMIC OUTLOOK AND MONETARY POLICY

April 03, 2014

London

Overview: Inflation and Monetary Policy

- Retail loan growth continues to slow down in response to the tight monetary policy stance, recent macroprudential measures, and weak capital flows.
- The impact of monetary tightening on inflation will be observed with some lag. Meanwhile, inflation is expected to increase until June, partly reflecting the base effects.
- Exports will support growth while private final domestic demand will lose momentum in the forthcoming period.
- The current account deficit will improve substantially in 2014.

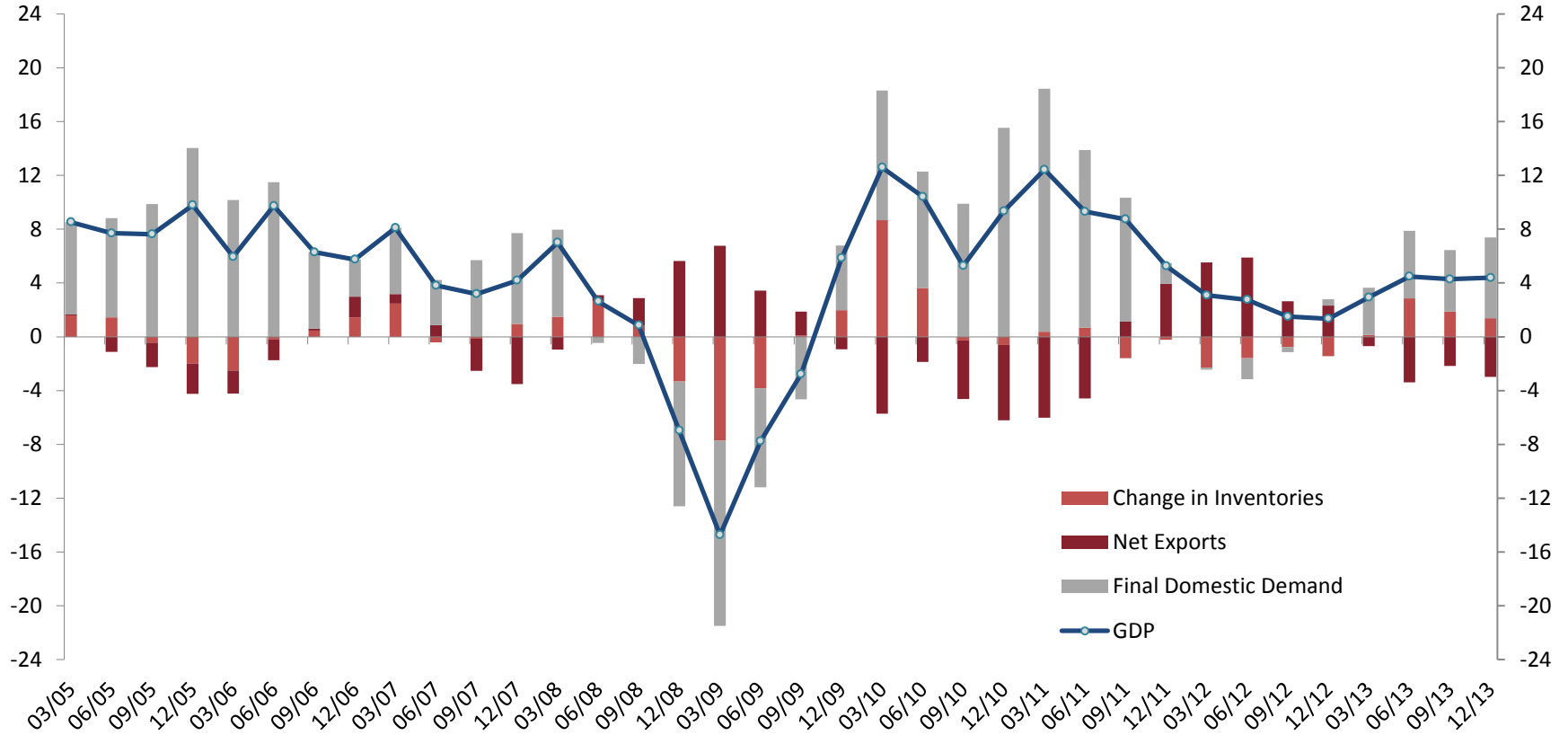
Outline

- I. Growth
- II. External Balance
- III. Inflation
- IV. Monetary Policy

GROWTH

Economic activity continued to expand throughout 2013.

Contribution to Annual GDP Growth (Percentage Points)

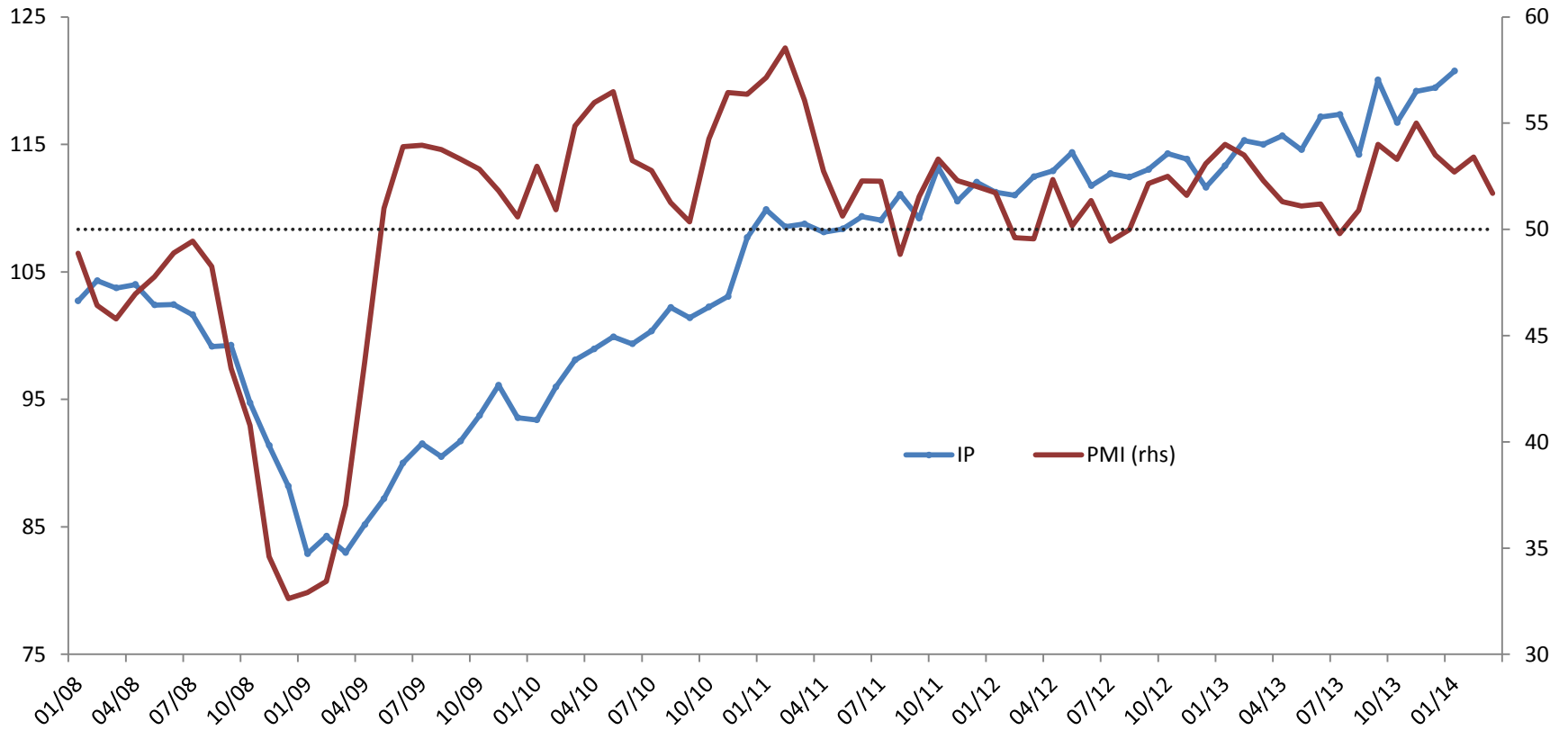


Source: TURKSTAT.

Last Observation: 2013Q4

Leading indicators imply the continuation of moderate growth in 2014 Q1.

Industrial Production (IP) and PMI Indices (Seasonally Adjusted)



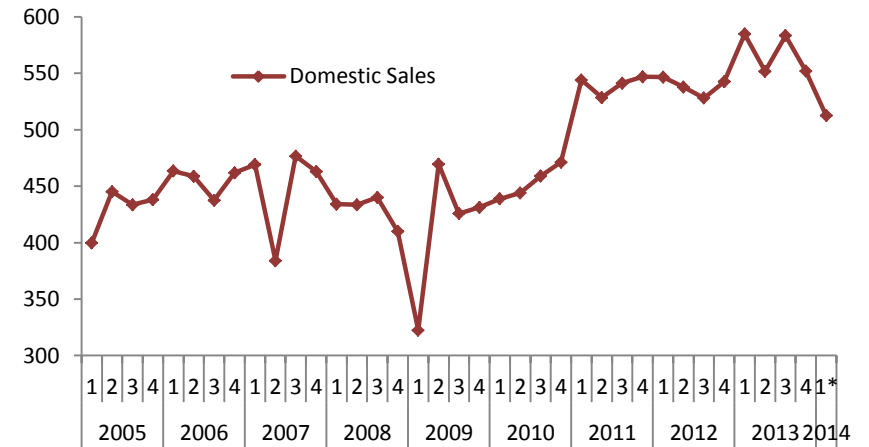
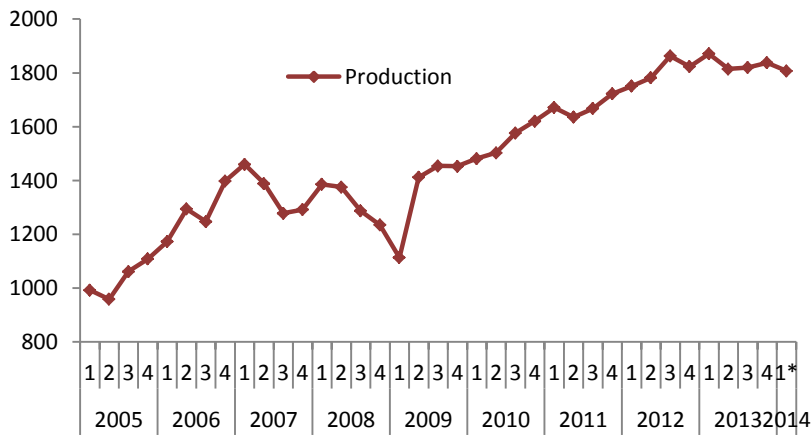
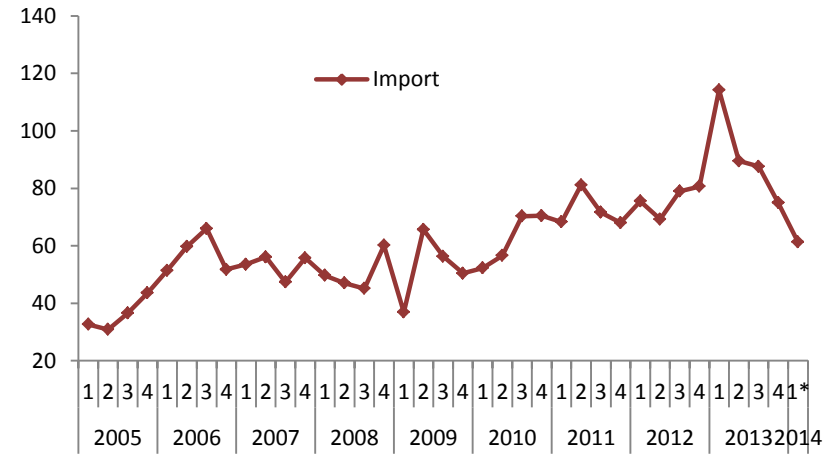
Source: Markit, TURKSTAT.

Last Observation : March 2014 for PMI,
January 2014 for Industrial Production

Resilience of production can be largely attributed to export growth, as demonstrated by recent white goods data.

White Goods

(Seasonally Adjusted, Thousands)



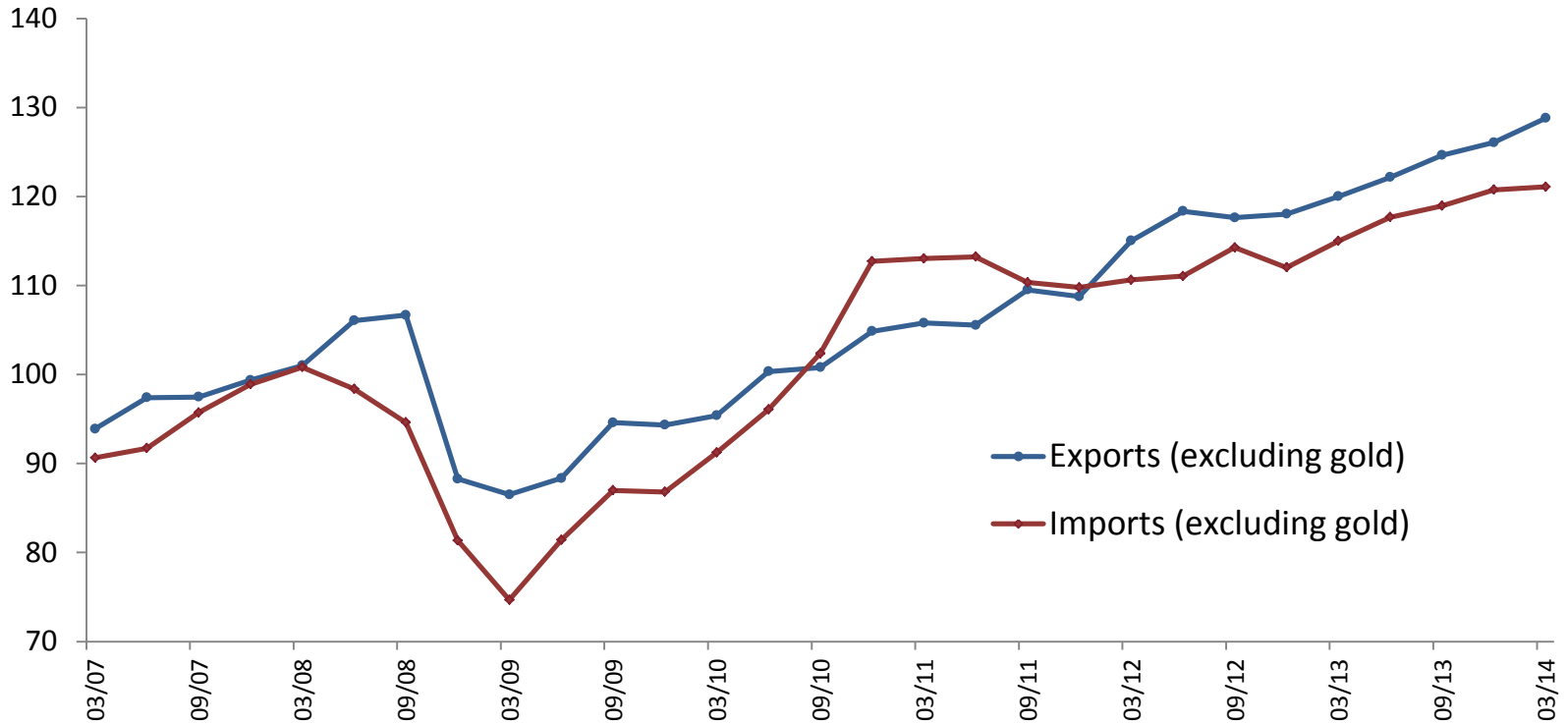
Source: TURKBESD, CBRT.

Last Observation: 2013Q4.

*Figures for the first quarter of 2014 are January and February values.

Exports have been rising while imports have been slowing down due to weak domestic demand.

Exports and Imports
(Excluding Gold, Seasonally Adjusted, 2010=100)



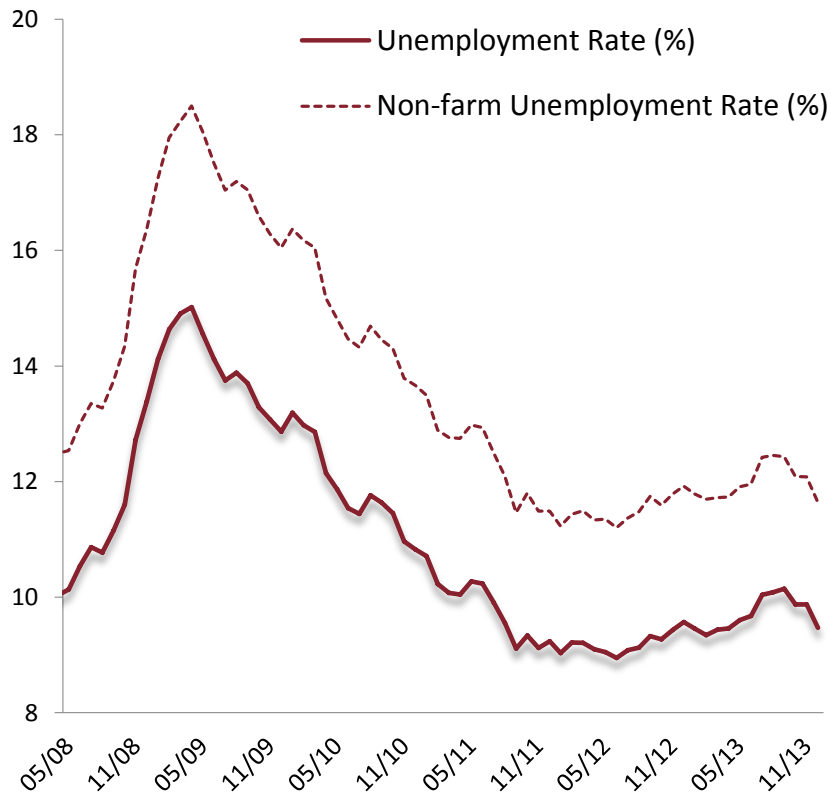
Source: TURKSTAT, CBRT.

Last Observation: 2013Q4.

*Figures for the first quarter of 2014 are January values.

Employment growth and labor participation have recovered recently.

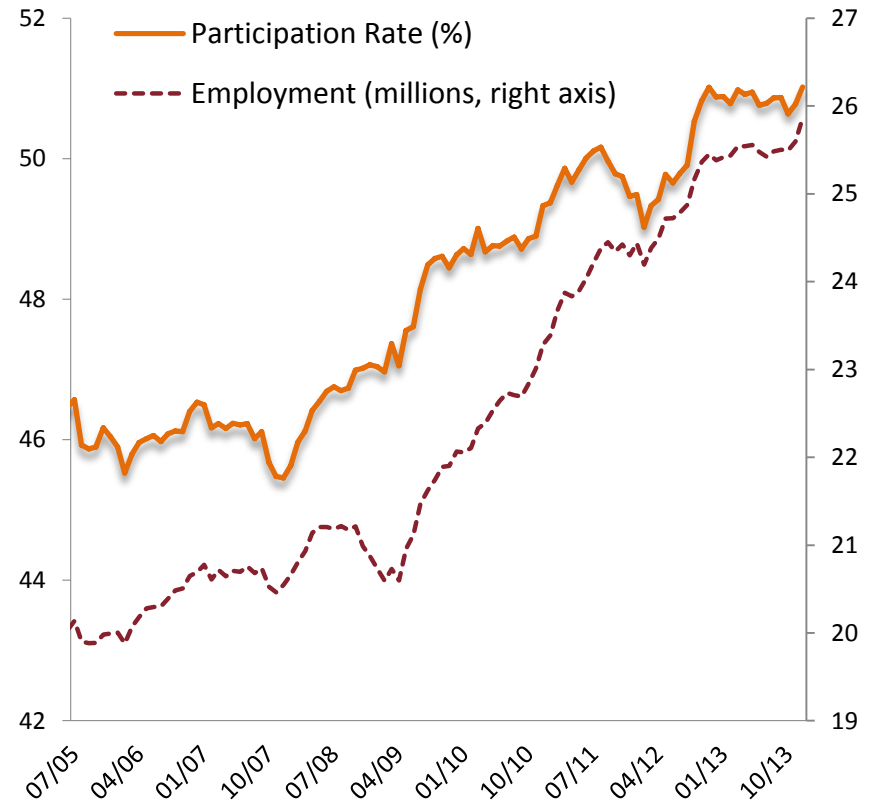
Unemployment Rate (Seasonally Adjusted, Percent)



Source: TURKSTAT, Household Labor Force Survey, CBRT.

Last Observation: December 2013.

Employment and Participation Rate (Seasonally Adjusted, Million People)

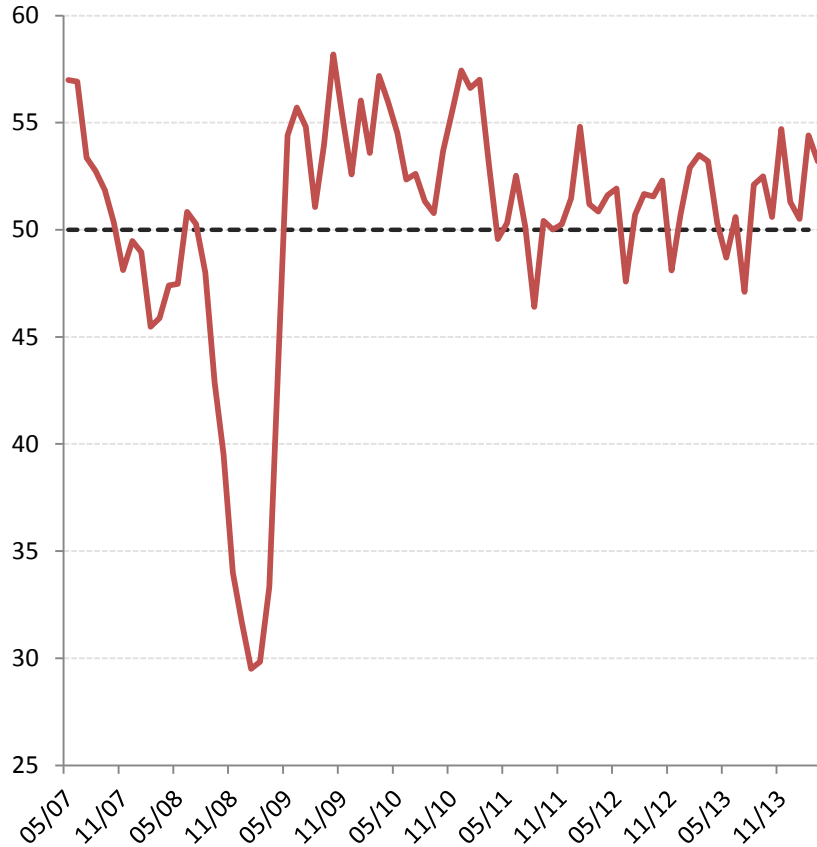


Source: TURKSTAT, Household Labor Force Survey, CBRT.

Last Observation: December 2013.

Exports are seen to support growth and rebalancing,

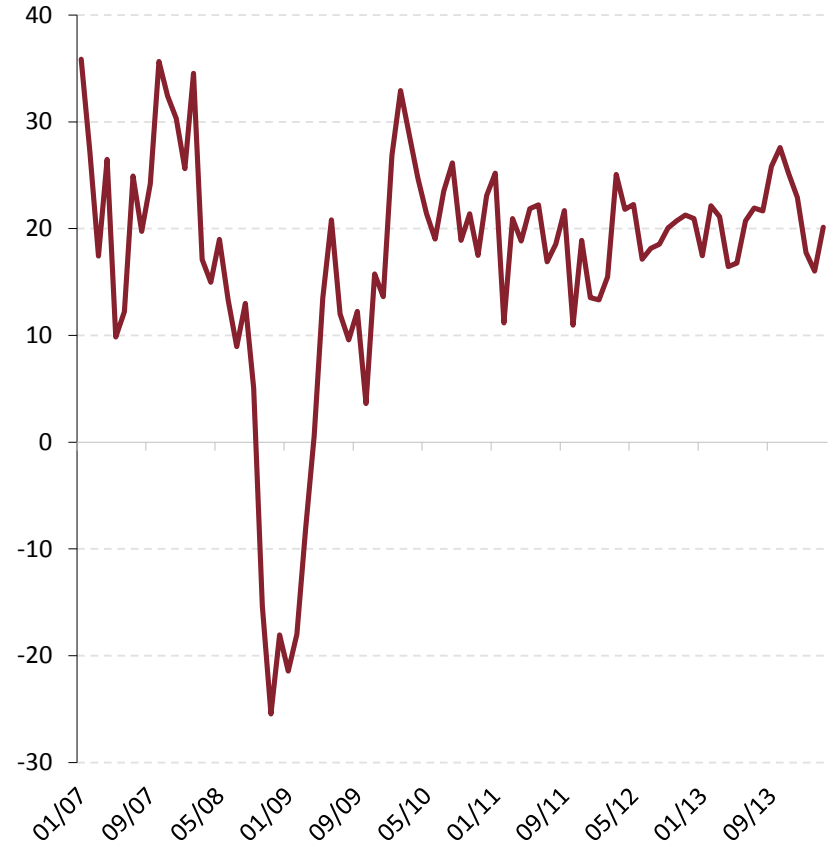
PMI Export Orders (Seasonally Adjusted)



Source: Markit.

Last Observation: March 2014.

Expectation of New Export Orders * (Seasonally Adjusted)



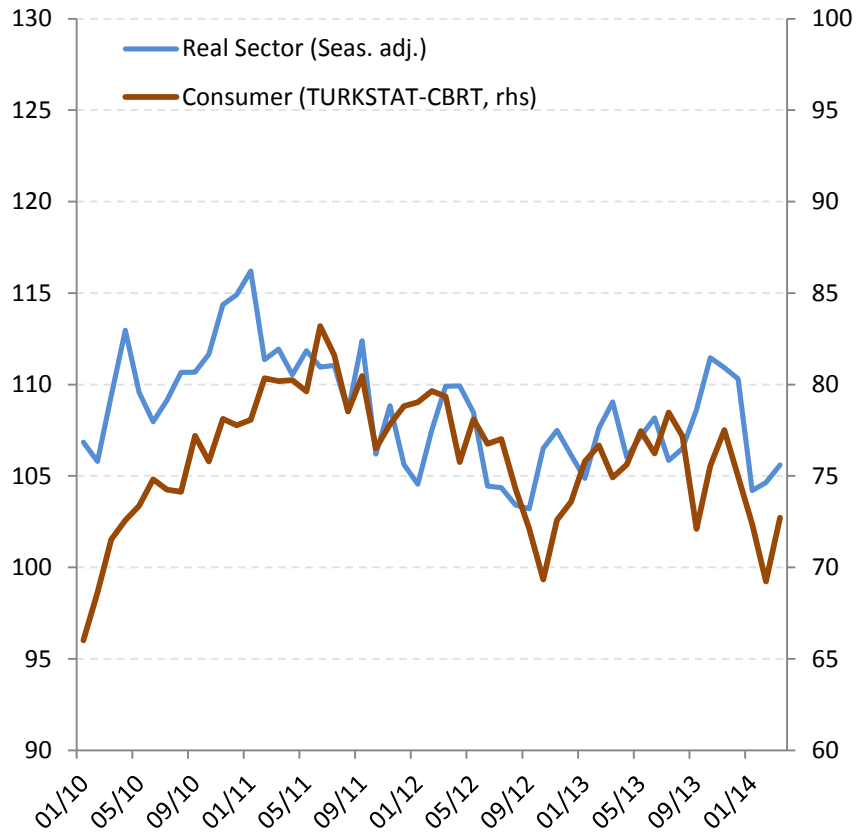
Source: TURKSTAT, CBRT.

Last Observation: March 2014.

*Business Tendency Survey: Expectation of new export orders over the next three months (increase-decrease)

while domestic demand growth will be moderate in the forthcoming period.

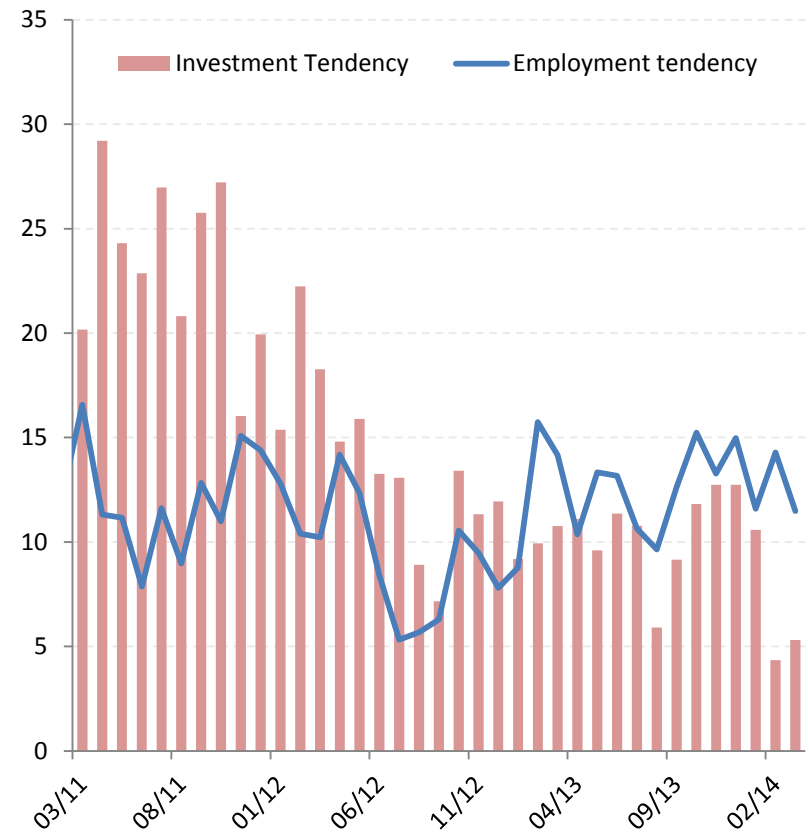
Consumer and Real Sector Confidence Indices



Source: TURKSTAT, CBRT.

Last Observation: March 2014.

Investment and Employment Prospects (Seasonally Adjusted)



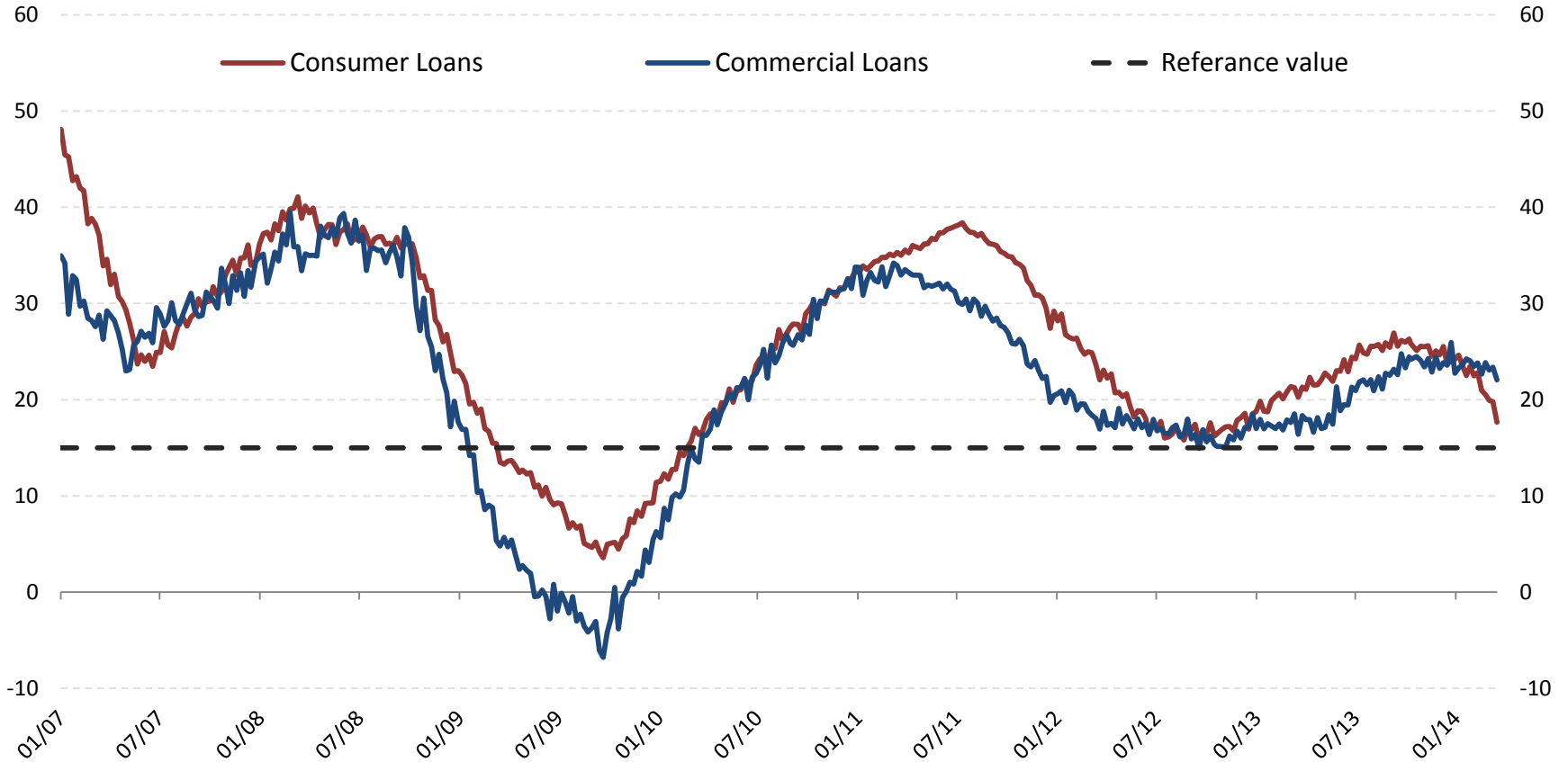
Source: CBRT.

Last Observation: March 2014.
Business Tendency Survey

EXTERNAL BALANCE

Loan growth rates are approaching the reference value of 15%.

Consumer* and Commercial Loans** (YoY Growth, Percent)



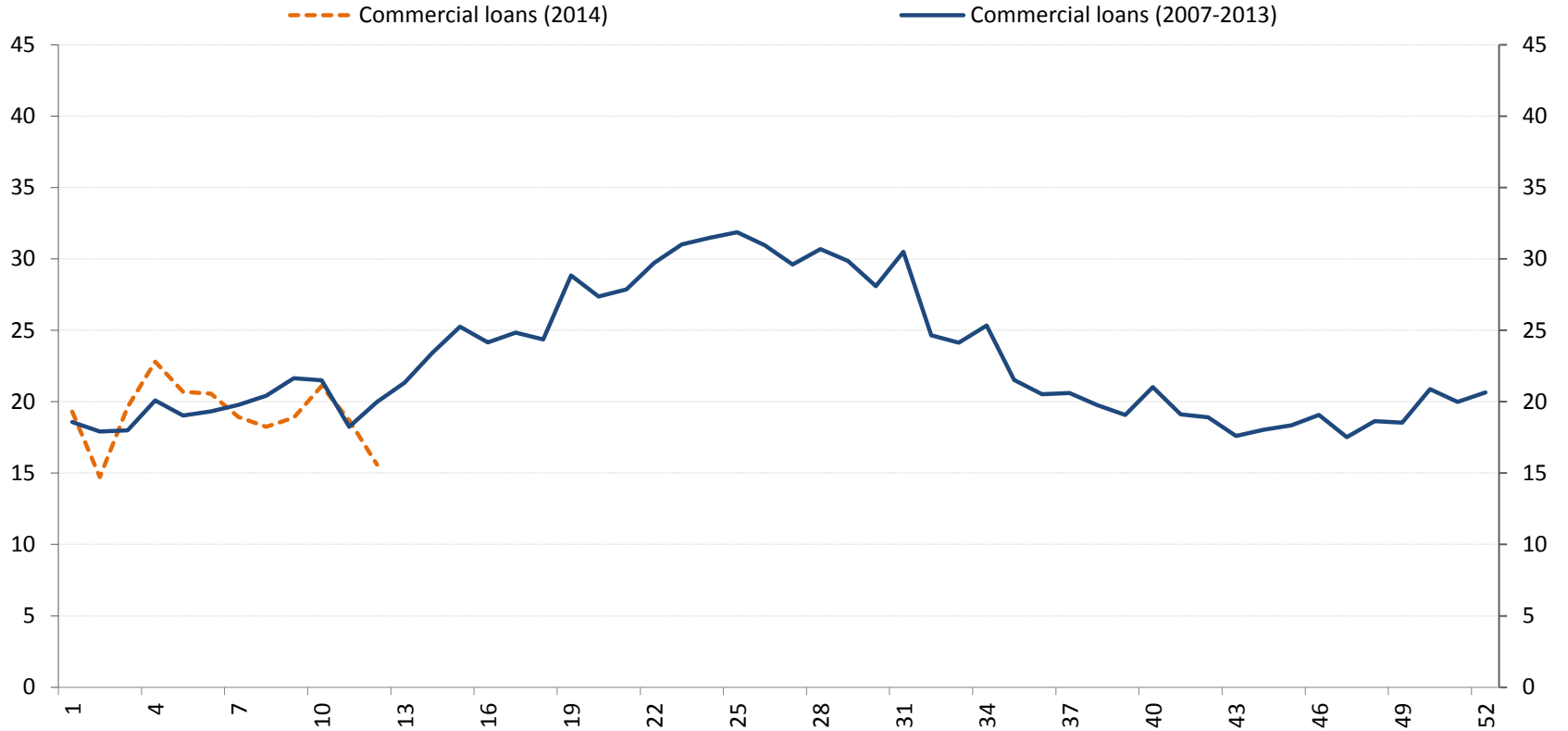
Source: CBRT.

* Including credit cards.
**Total banking sector (including participation banks, excluding nonperforming loans)
Last Observation: 21 March 2014

Commercial loan growth is close to the long-term average.

Commercial Loan* Growth Rates

(13-Week Moving Average**, Exchange Rate Adjusted, Annualized, Percent)



Source: CBRT.

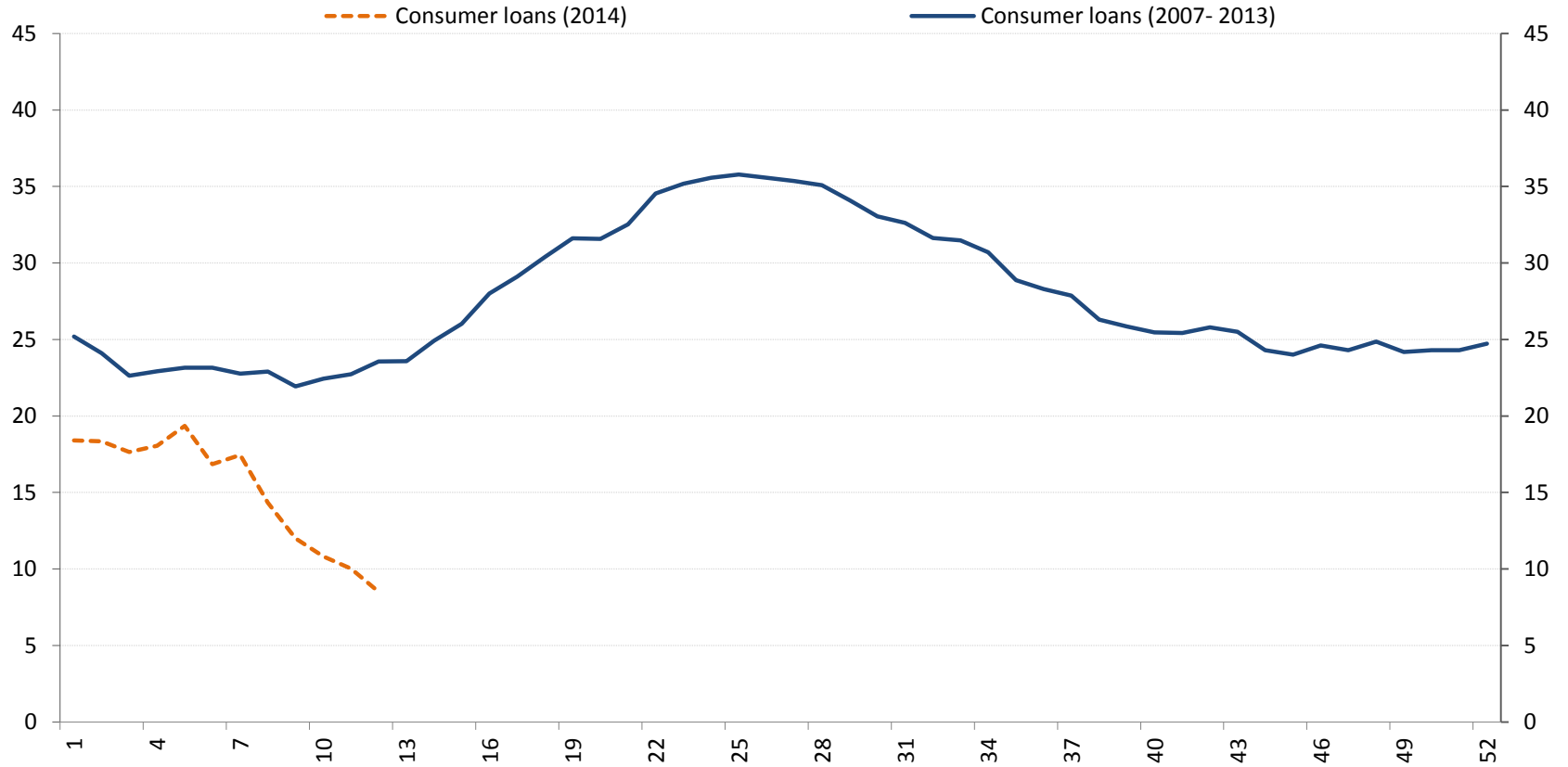
*Total banking sector (including participation banks, excluding nonperforming loans)

**The annual growth rate of credit stock is calculated as the 52nd power of 13-week moving average of weekly growth rate.

Last Observation: 21 March 2014

Slowdown is more pronounced in consumer loans.

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



Source: CBRT.

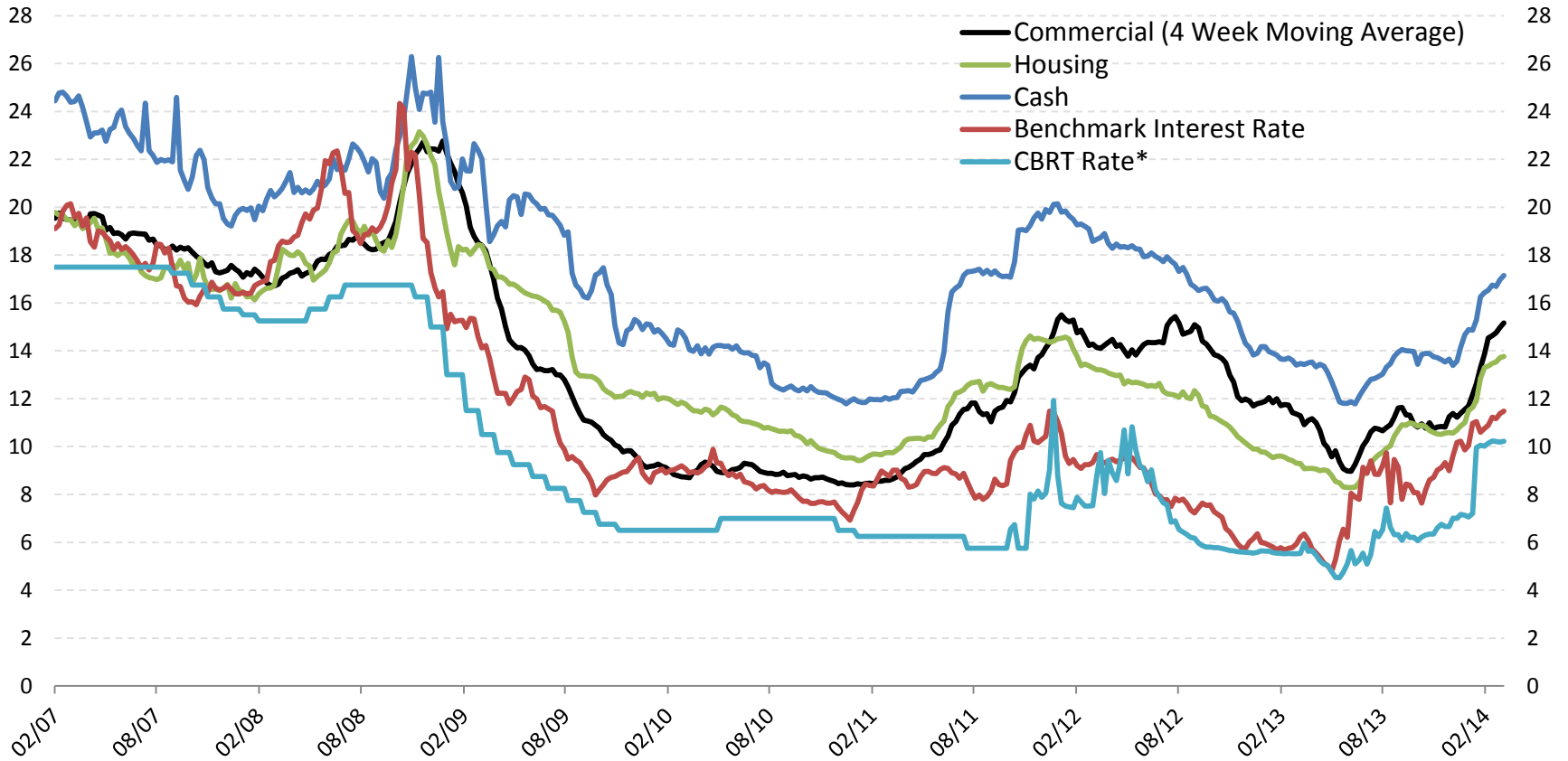
*Total banking sector (including participation banks, excluding nonperforming loans)

**The annual growth rate of credit stock is calculated as the 52nd power of 13-week moving average of weekly growth rate.

Last Observation: 21 March 2014

Lending rates have adjusted gradually,

Lending Rates and Benchmark Interest Rate (Percent)



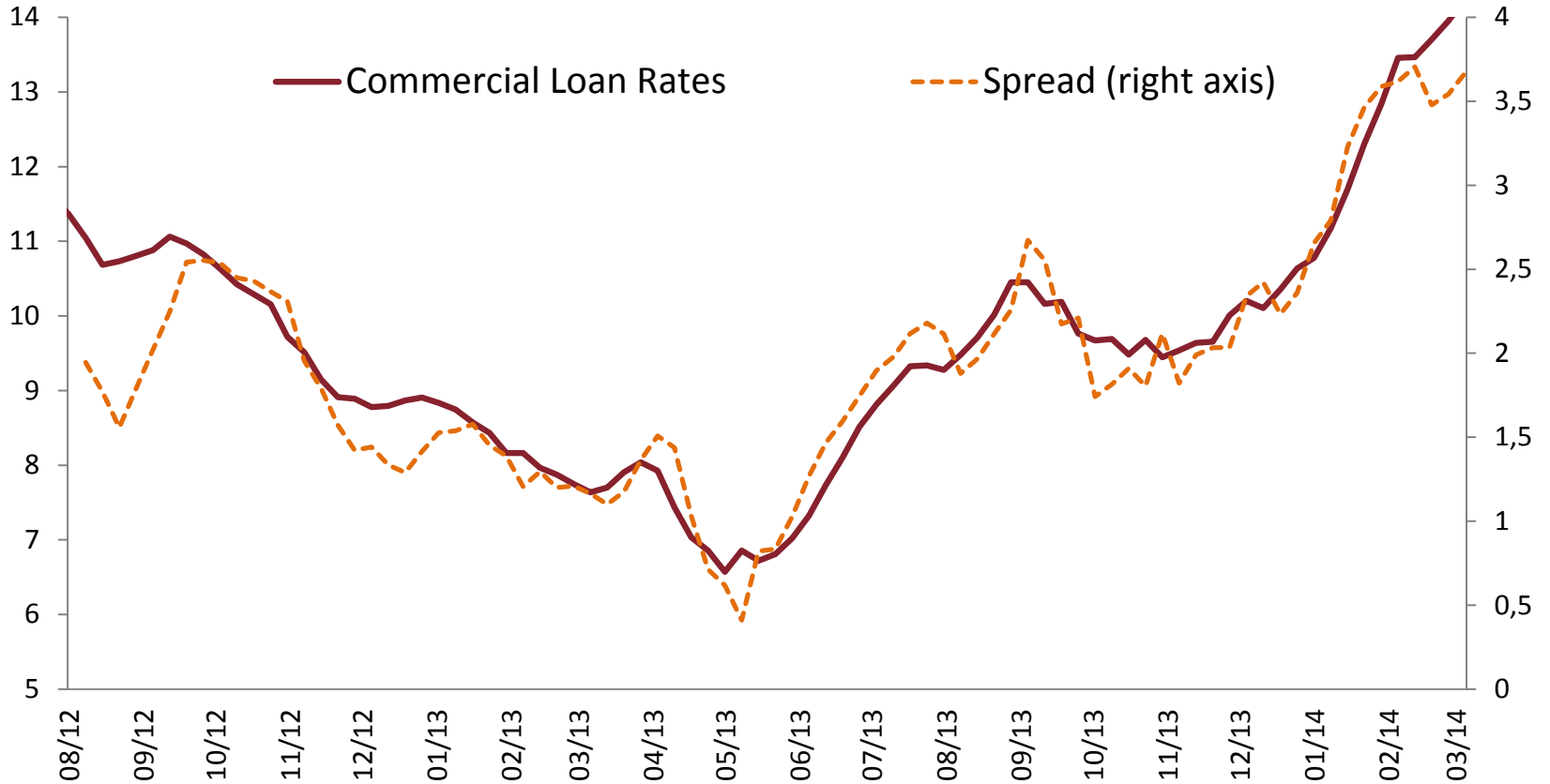
Source: CBRT.

*Central Bank borrowing rate before 10.20.2011, average funding rate thereafter.

Last Observation: 21 March 2014

loan-deposit spread, as well.

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



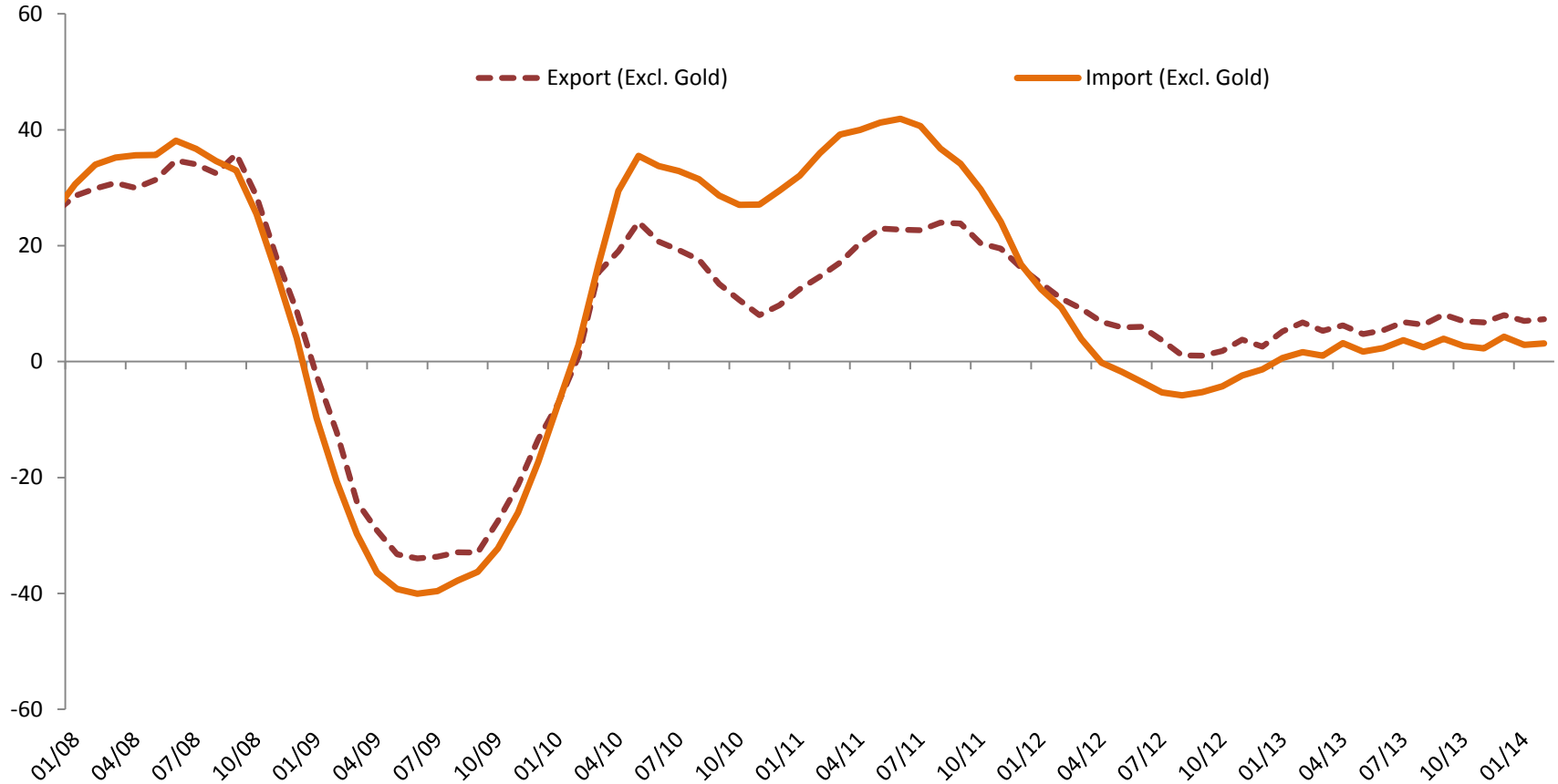
Last Data: February 28, 2014.

Source: CBRT.

Commercial loan rates exclude corporate overdraft account rates and corporate credit card rates.

Exports continue to grow faster than imports.

Exports and Imports (Nominal y-o-y % change, 6-month MA)



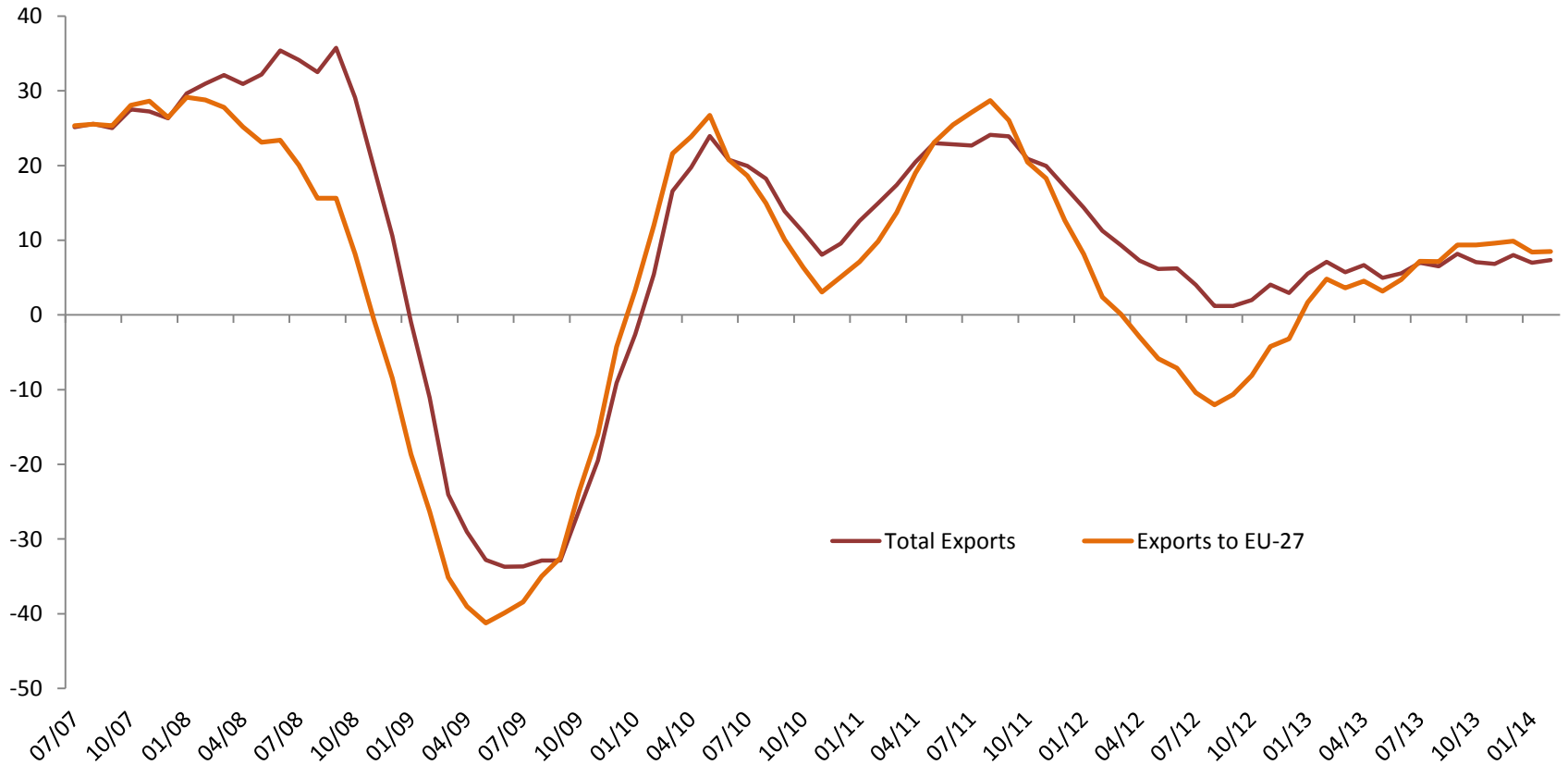
Source: TURKSTAT.

Last Observation: February 2014.

Export growth tracks the European recovery quite closely.

Exports

(Excluding gold, nominal, y-o-y % change, 6-month MA)

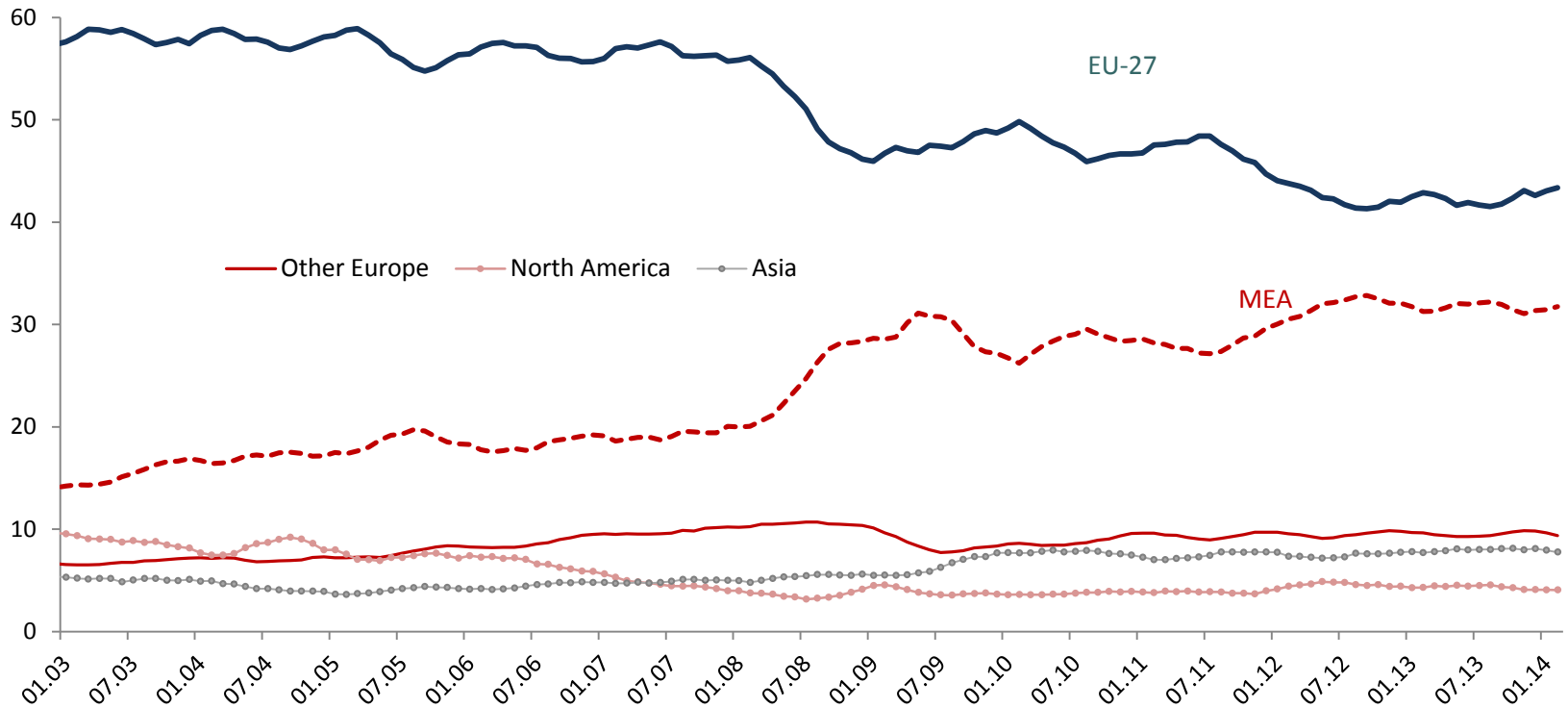


Source: TURKSTAT.

Last Observation: February 2014.

Recovery in the EU economy is reflected in market shares of Turkey.

Exports Market Share (Excluding gold, 6-month cumulative, percent)

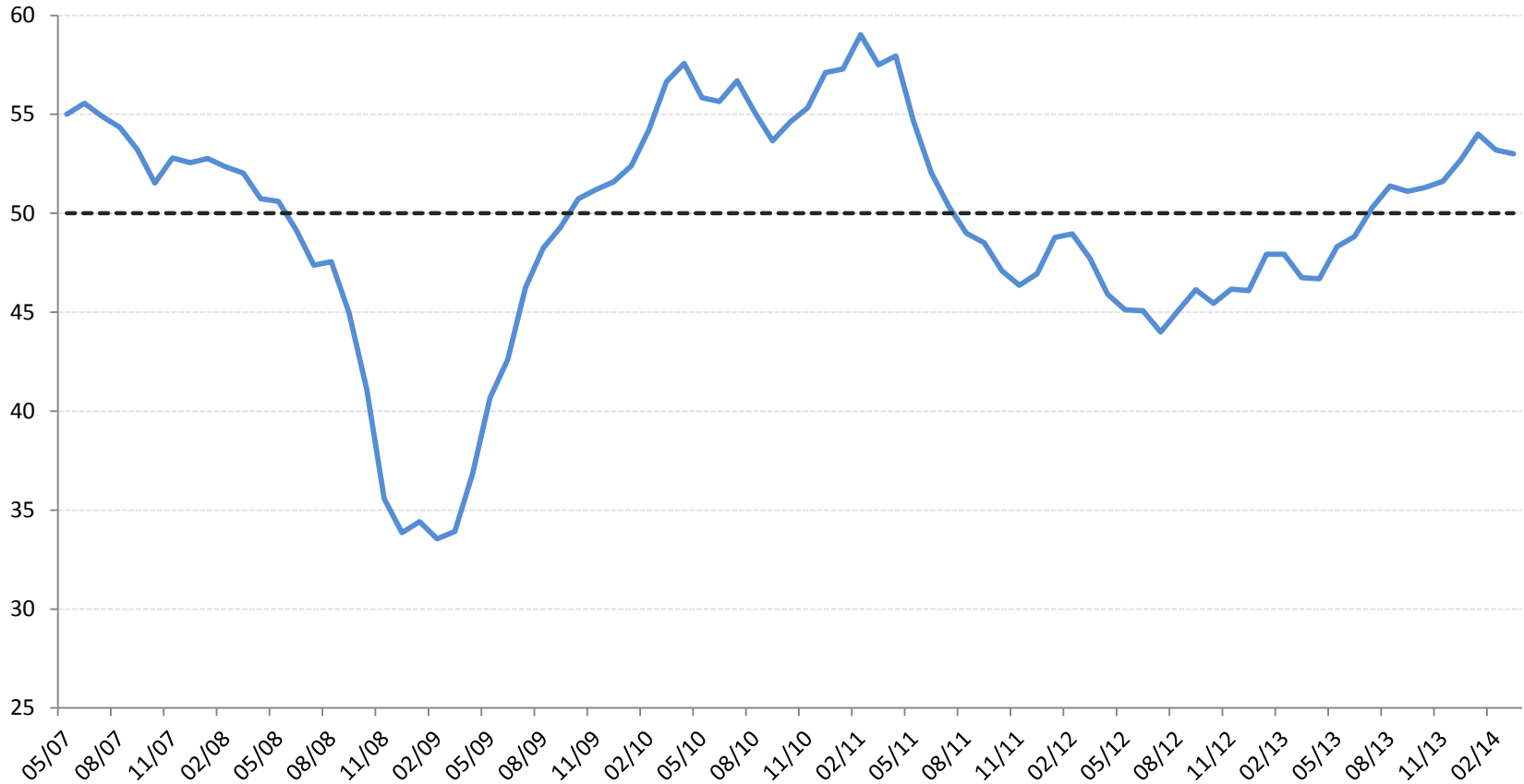


Source: TURKSTAT.

Last Observation: February 2014.

Leading indicators suggest that the recovery in the euro area will continue.

Euro Area Manufacturing PMI (Seasonally Adjusted)

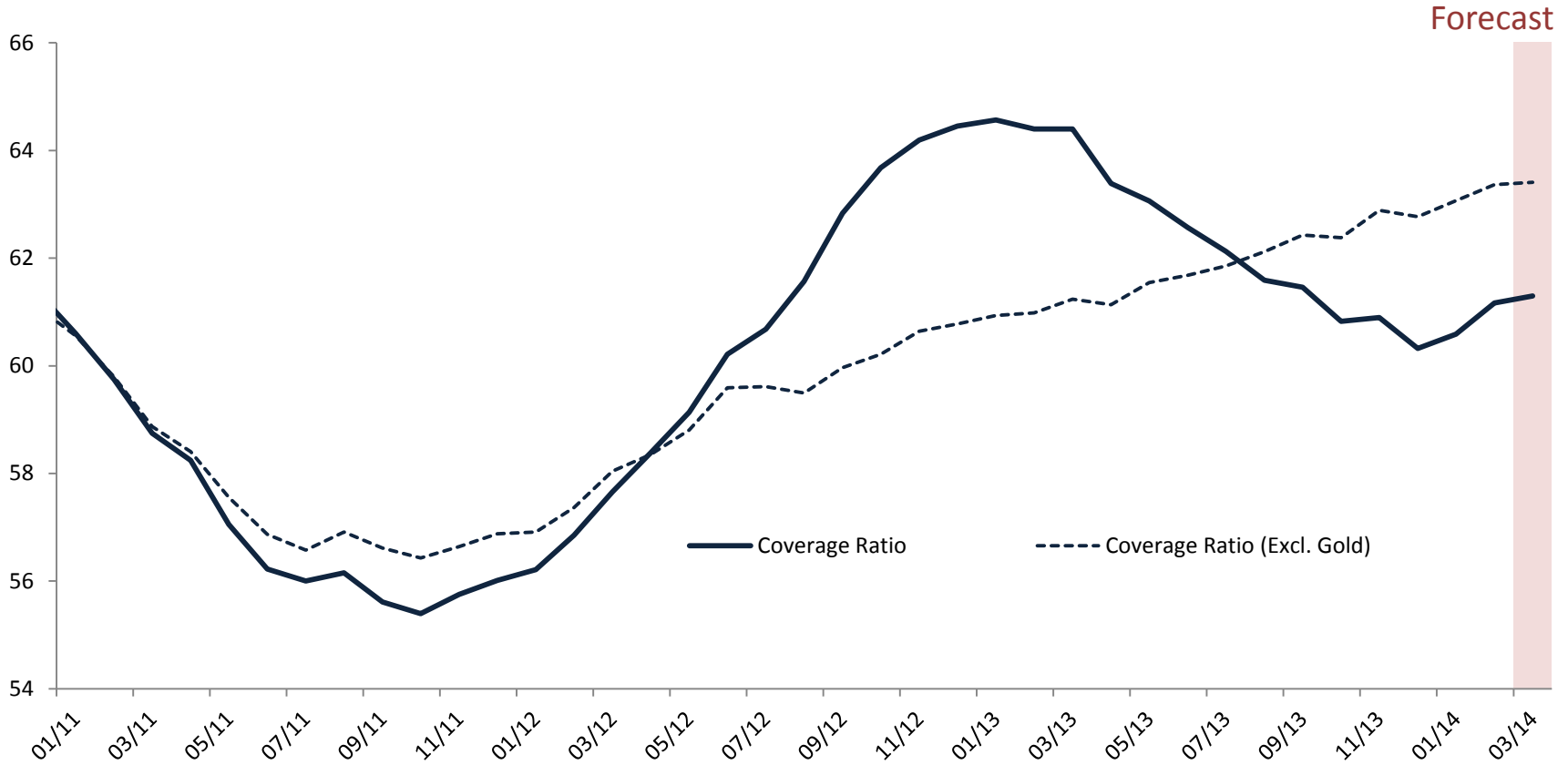


Source: Markit.

Last Observation: March 2014

The uptrend in the export/import coverage ratio is expected to continue.

Export/Import Coverage Ratio* (12-Month Rolling **, Percent)



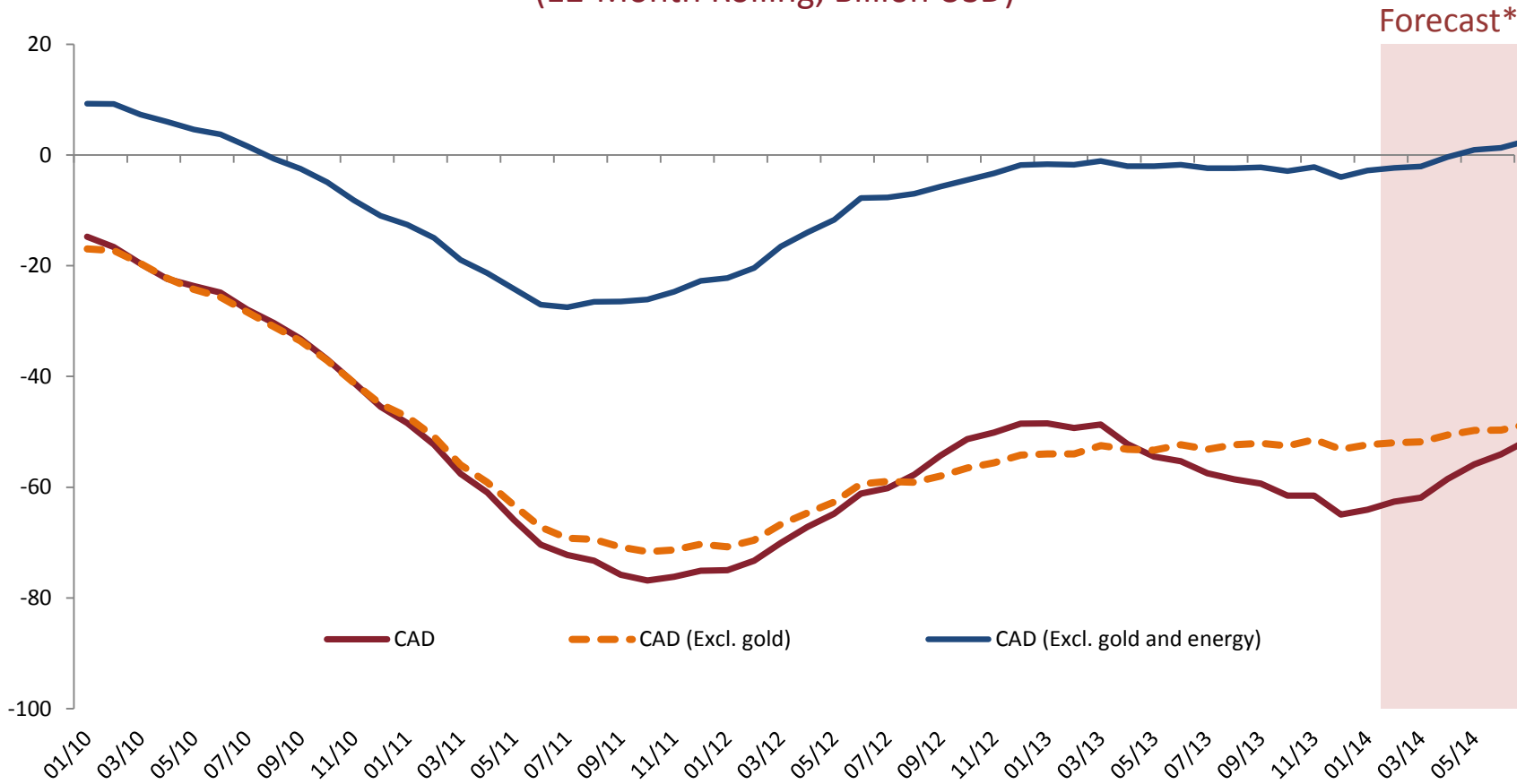
Source: TURKSAT, CRT.

* March data is forecast value.

** 12-month cumulative exports /12-month cumulative imports

A significant improvement is expected in the current account deficit in 2014.

Current Account Deficit
(12-Month Rolling, Billion USD)



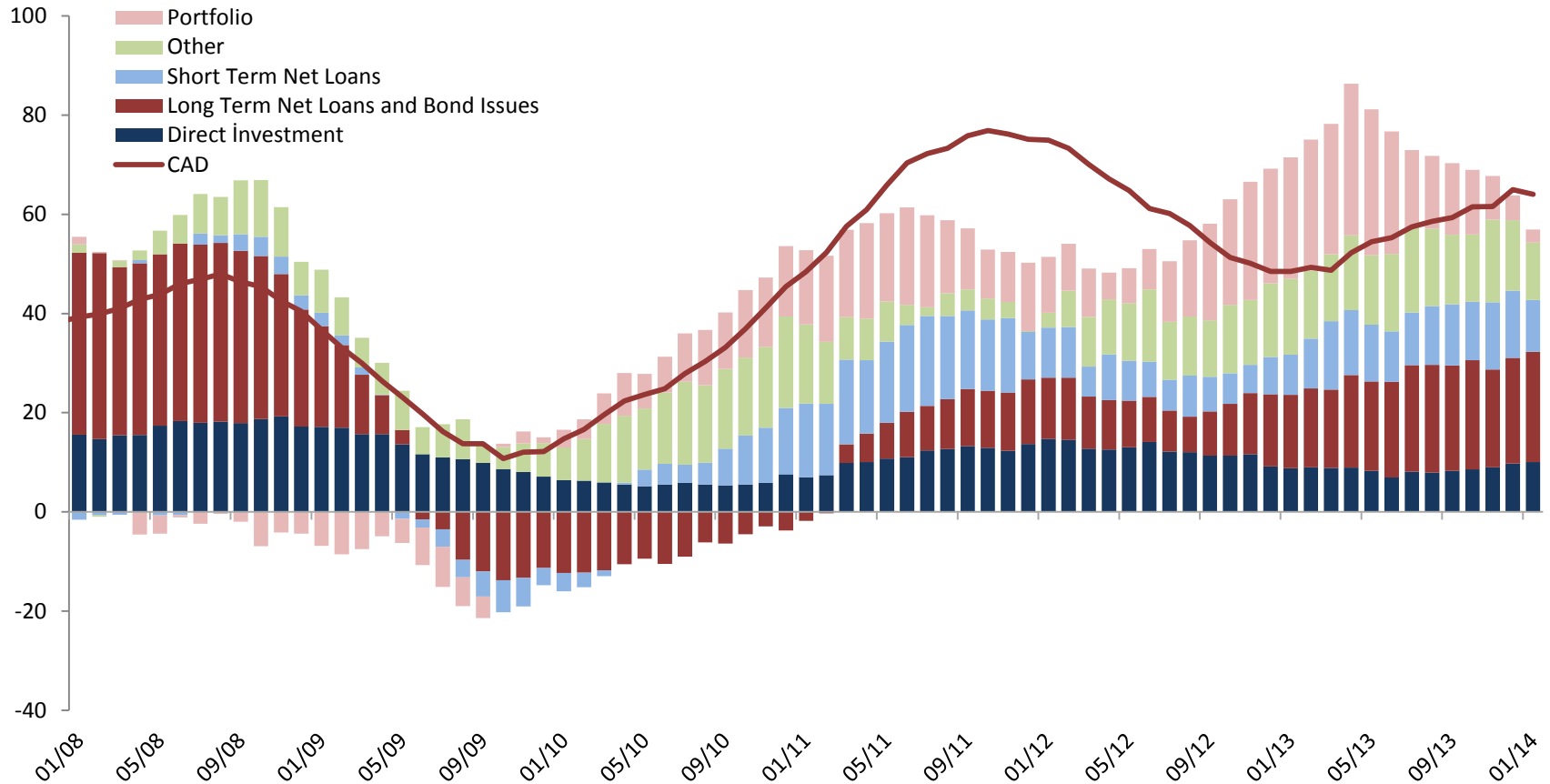
Source: CBRT.

Last Observation: January 2014.

*Forecasts are based on the 2014 GDP growth projection of Medium Term Plan (MTP).

The current account deficit is mainly financed by long term loans and bond issues.

Current Account Deficit Financing Sources (12-Month Cumulative, Billion USD)

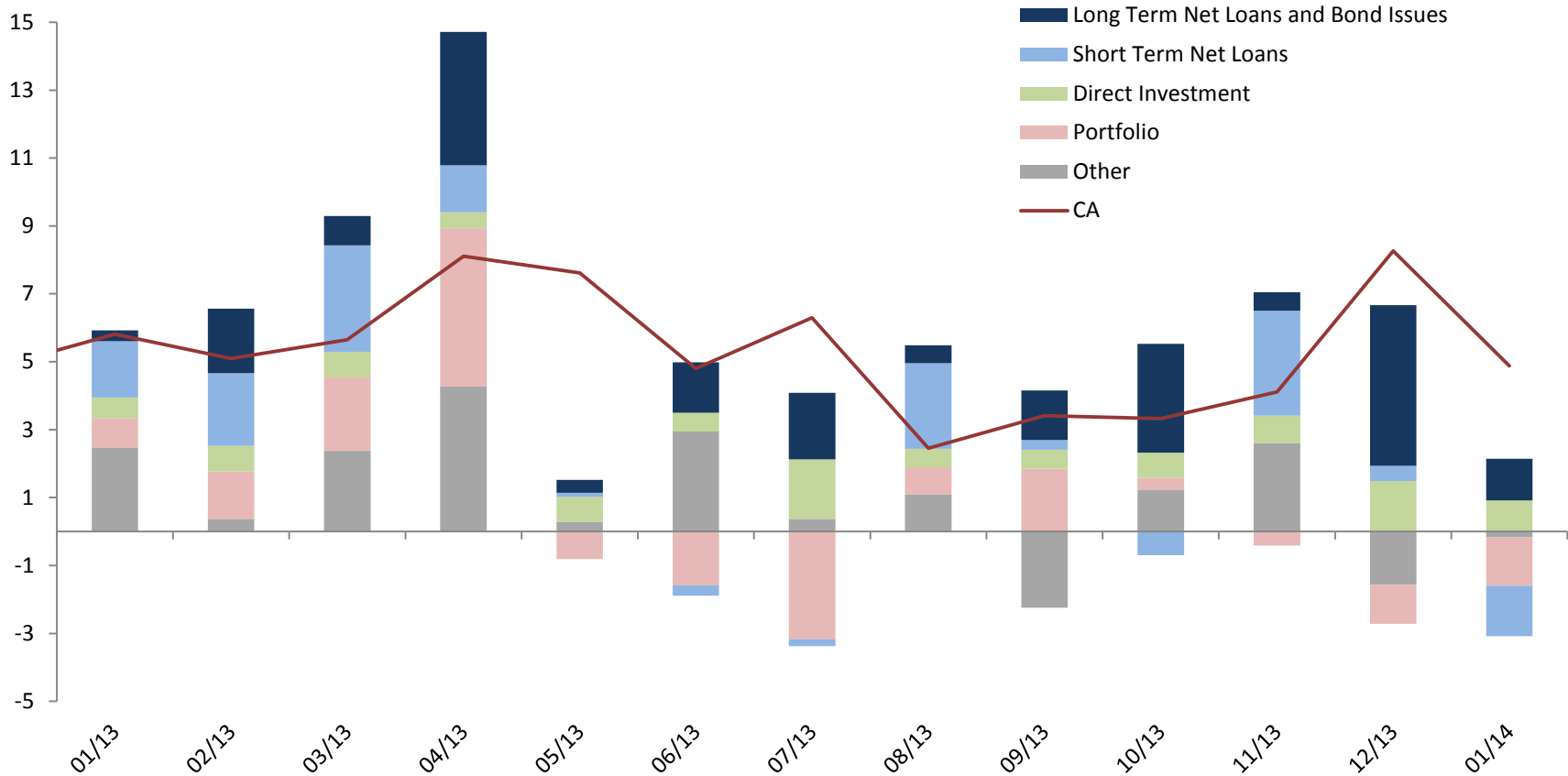


Source:CBRT.

Last Observation: January 2014

Long-term loan flows are stable while portfolio flows are volatile.

Current Account Deficit Financing Sources (Monthly, Billion USD)

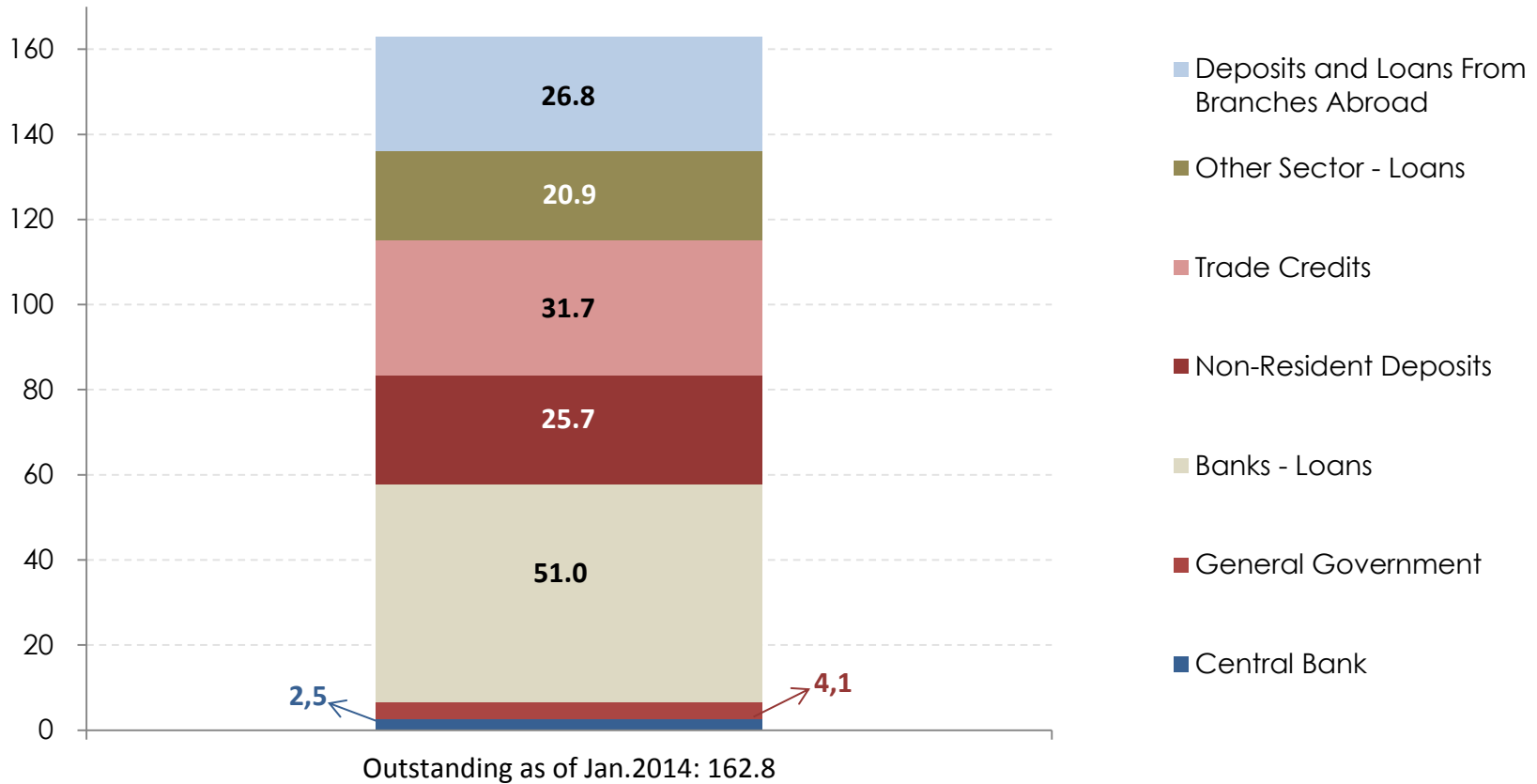


Source: CBRT

Last Observation: January 2014

Short term external debt of the official sector is negligible.

External Debt Stock Maturing in One Year* (Billion USD)



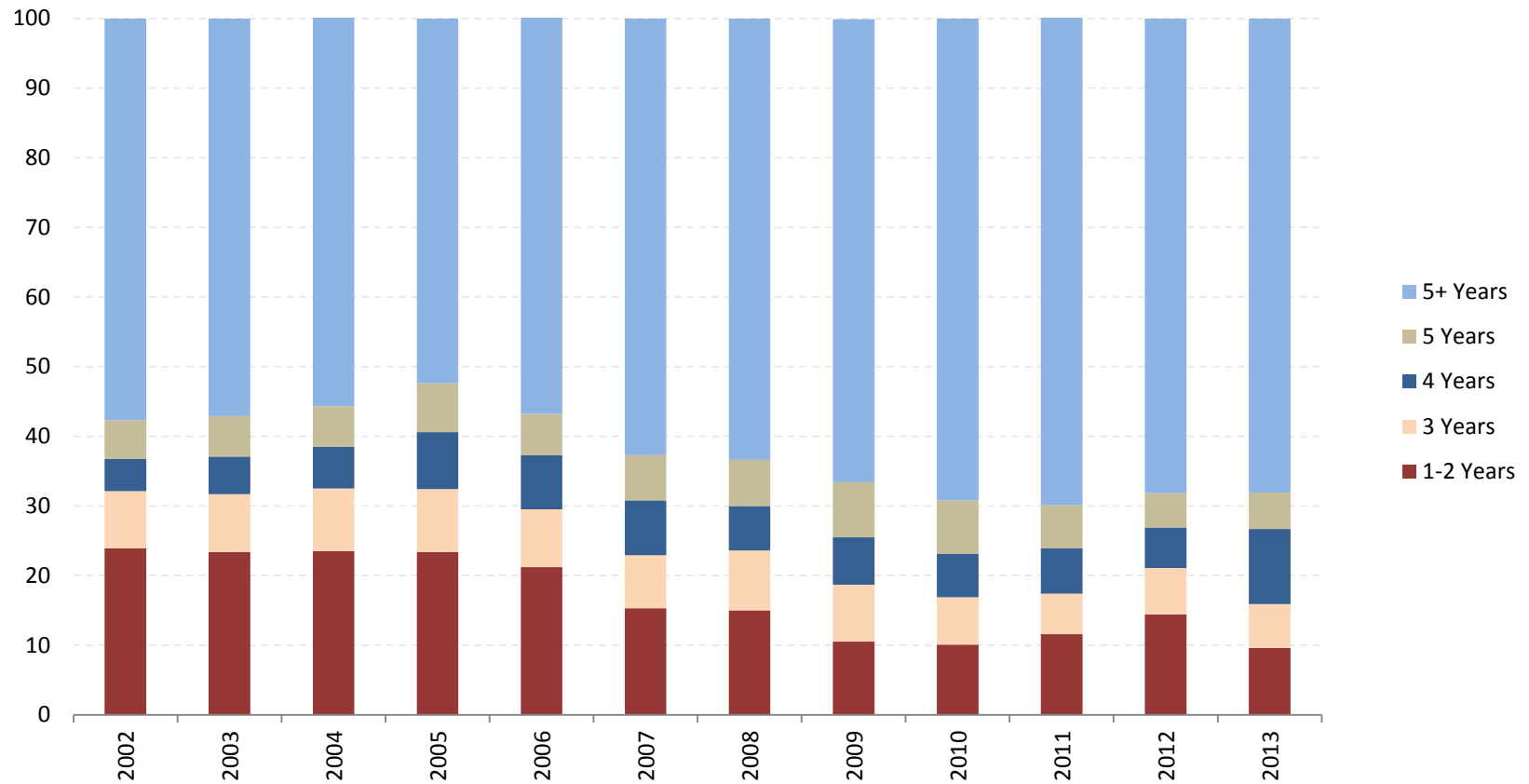
Source: CBRT.

*External debt maturing within 1 year or less regardless of the original maturity.

Last Observation: March 06, 2014.

The external debt maturity of firms is long and still improving.

Real Sector External Debt Maturity (Percent)



Source: CBRT.

Roll-over risks of private sector are minimal.

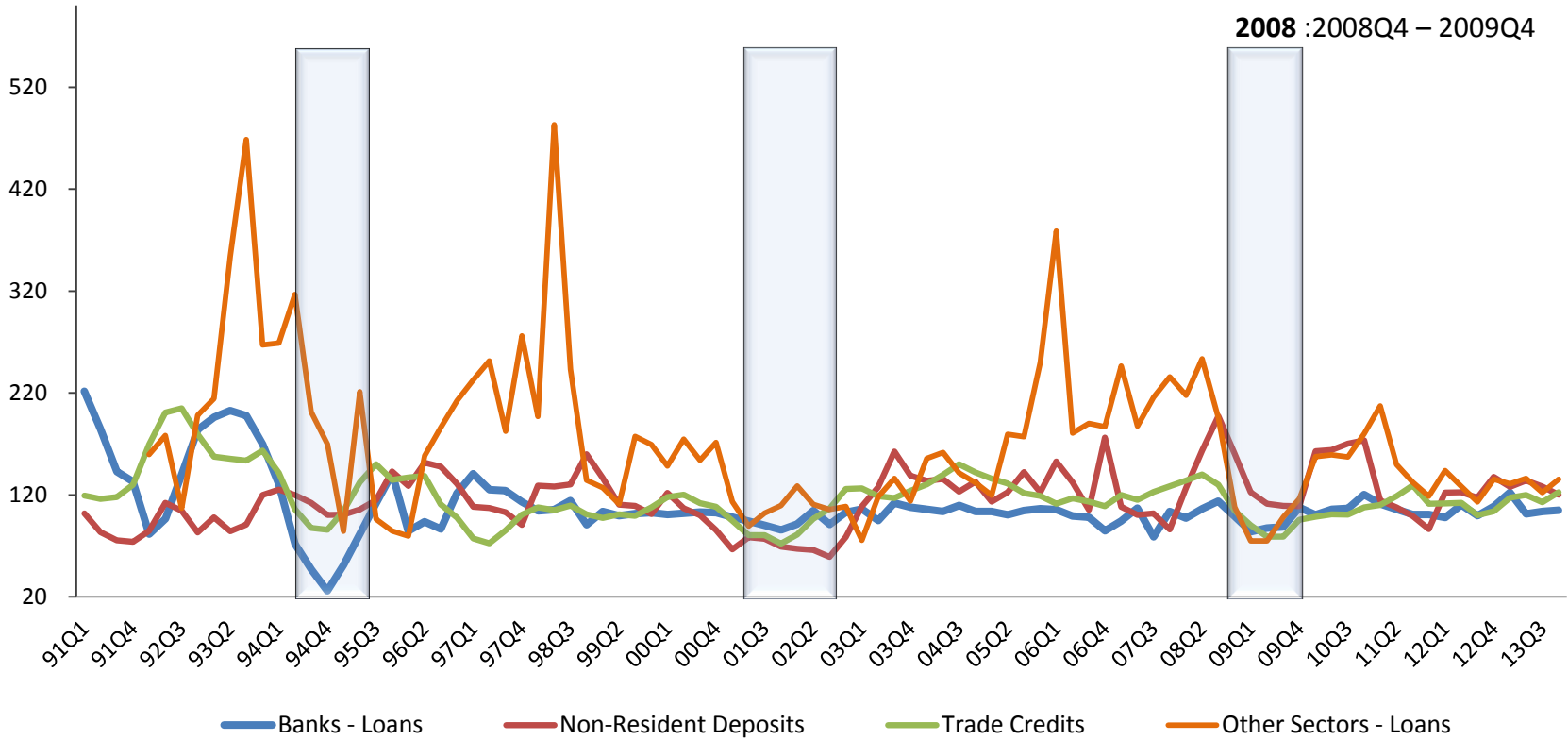
Roll-over Ratios of External Debt

Crisis Periods

1994 :1994Q2 – 1995Q2

2001 :2001Q2 – 2002Q3

2008 :2008Q4 – 2009Q4

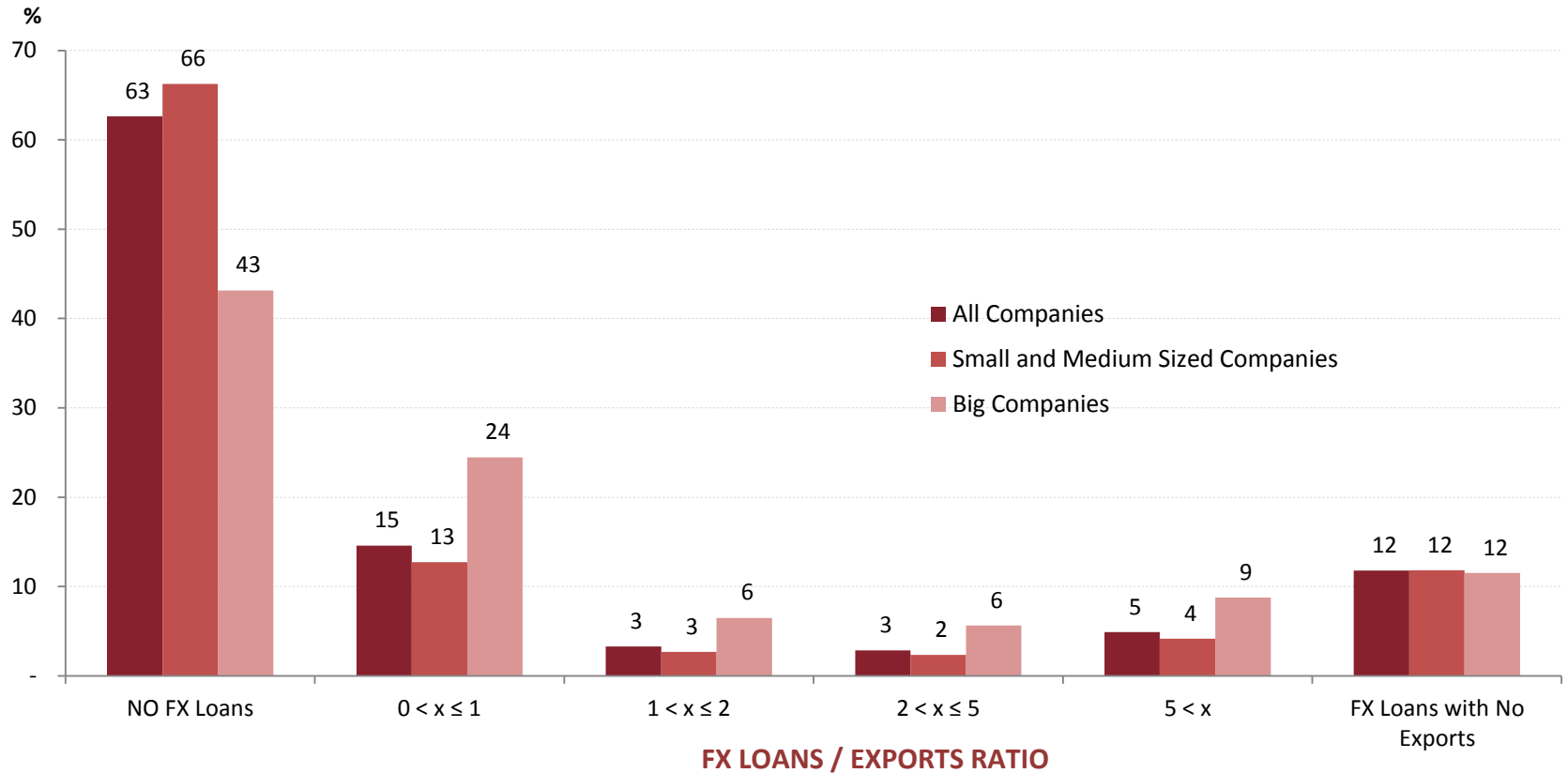


Source: CBRT.

Last Observation: 2013Q4.

Majority of firms have no currency risk.

Distribution of Firms with Different FX Loans/Exports Ratios



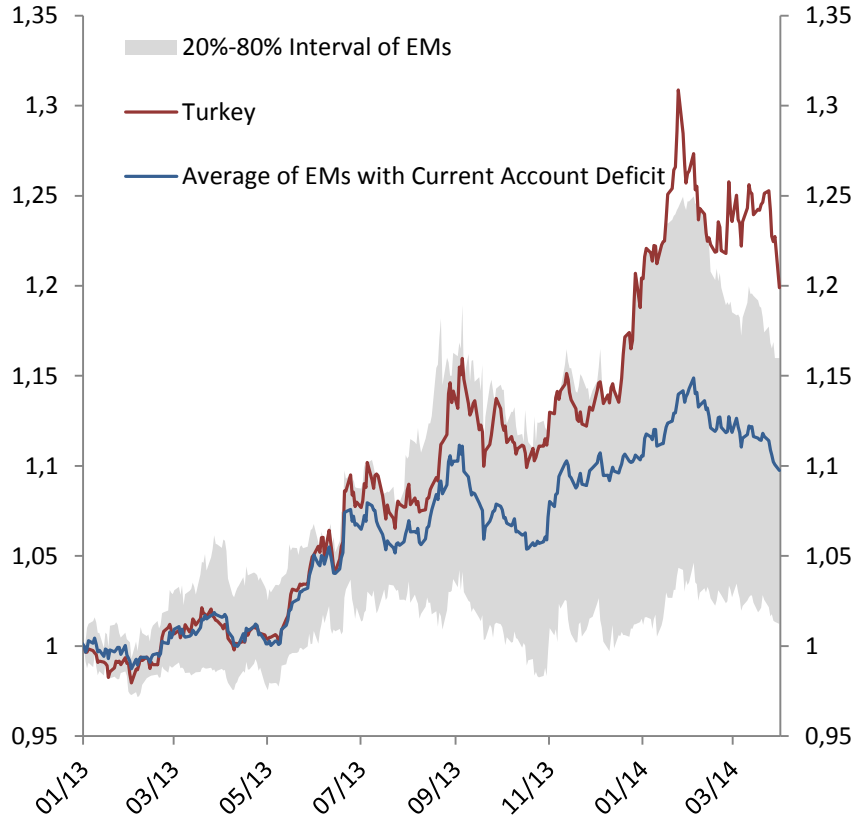
Figures show the percentage of firms with different FX loans to Exports ratio (x).
 Total net sales of all firms in the sample is 71 percent of GDP in 2012
 Number of firms is 9468.

Source: CBRT, Company Accounts Data Set. Date: 31.08.2013.

INFLATION

Both nominal and real exchange rates have depreciated significantly since May 2013.

TL and Other Emerging Market Currencies vs USD
(01.01.2013=1)

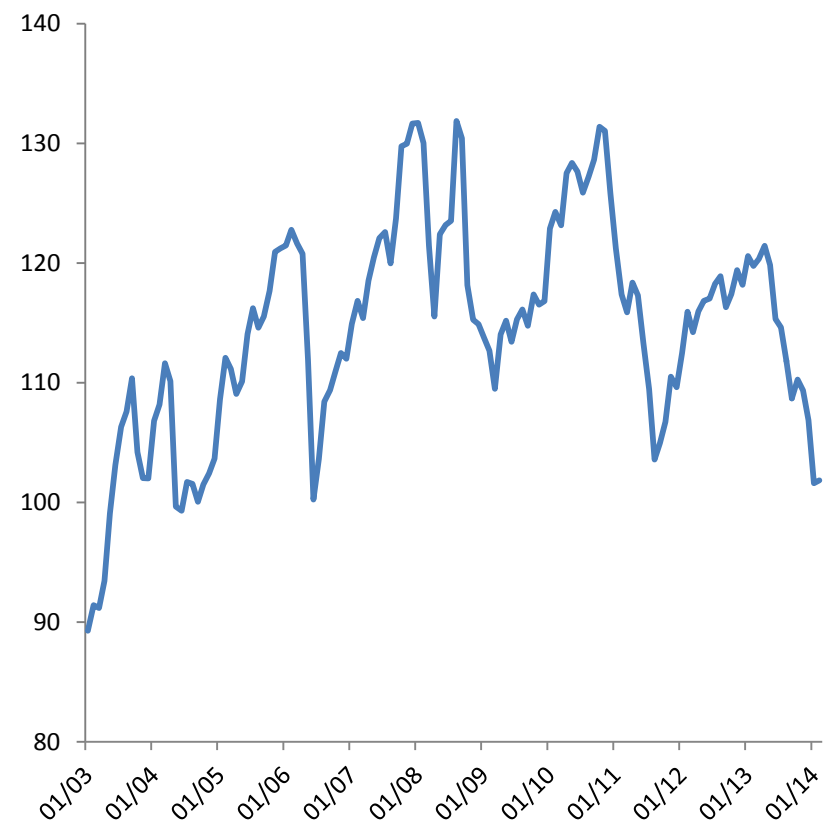


Last Observation: March 31, 2014.

Emerging economies include Brazil, Chile, Colombia, Czech Republic, Hungary, India, Indonesia, Israel, Malaysia, Mexico, Philippines, Poland, Romania, South Africa, South Korea and Thailand.

Source: Bloomberg.

Real Effective Exchange Rates
(2003=100)

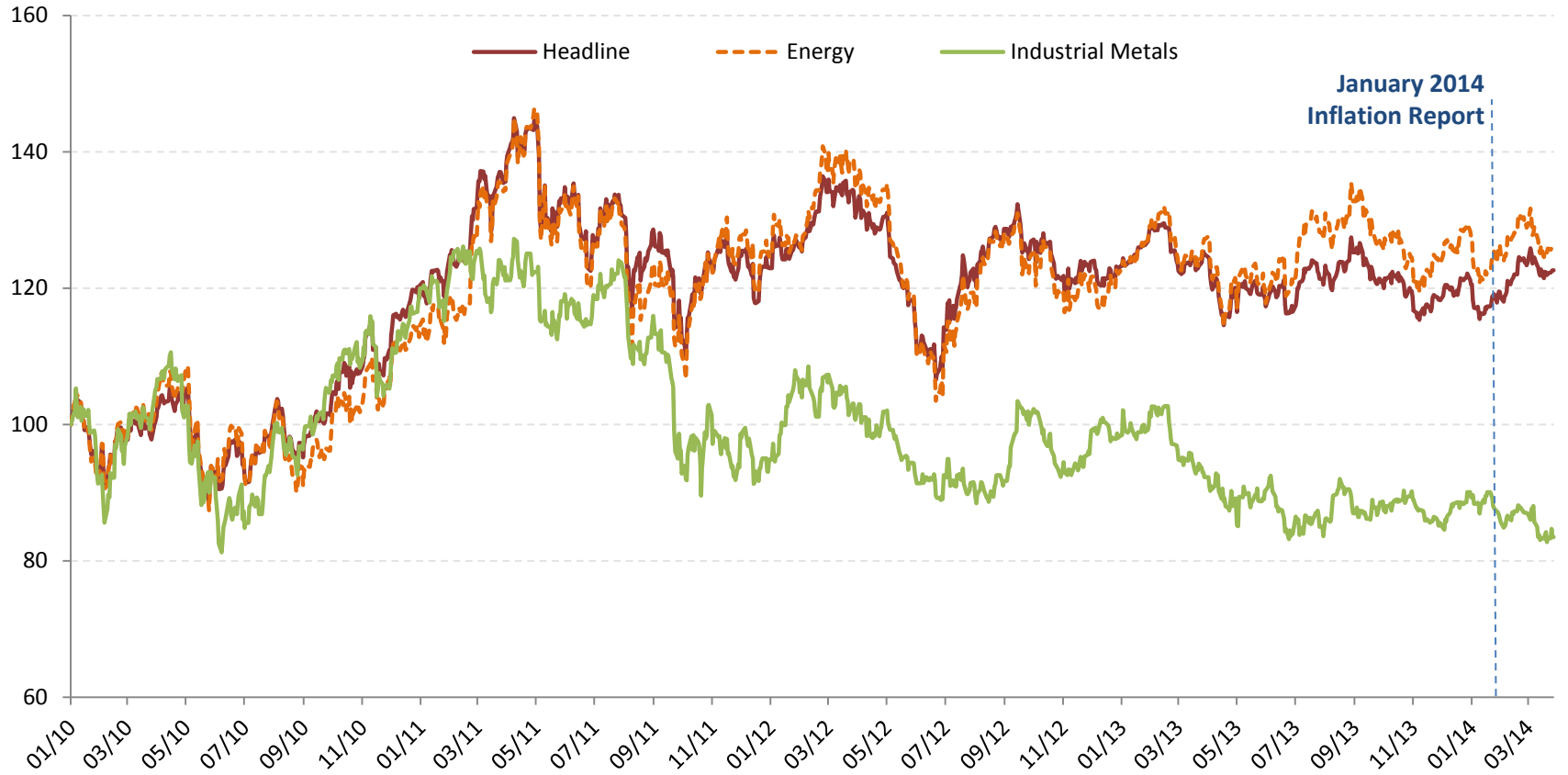


Source: CBRT.

Last Observation: February 2014

There is no significant inflationary pressure from commodity prices.

S&P GS Indices

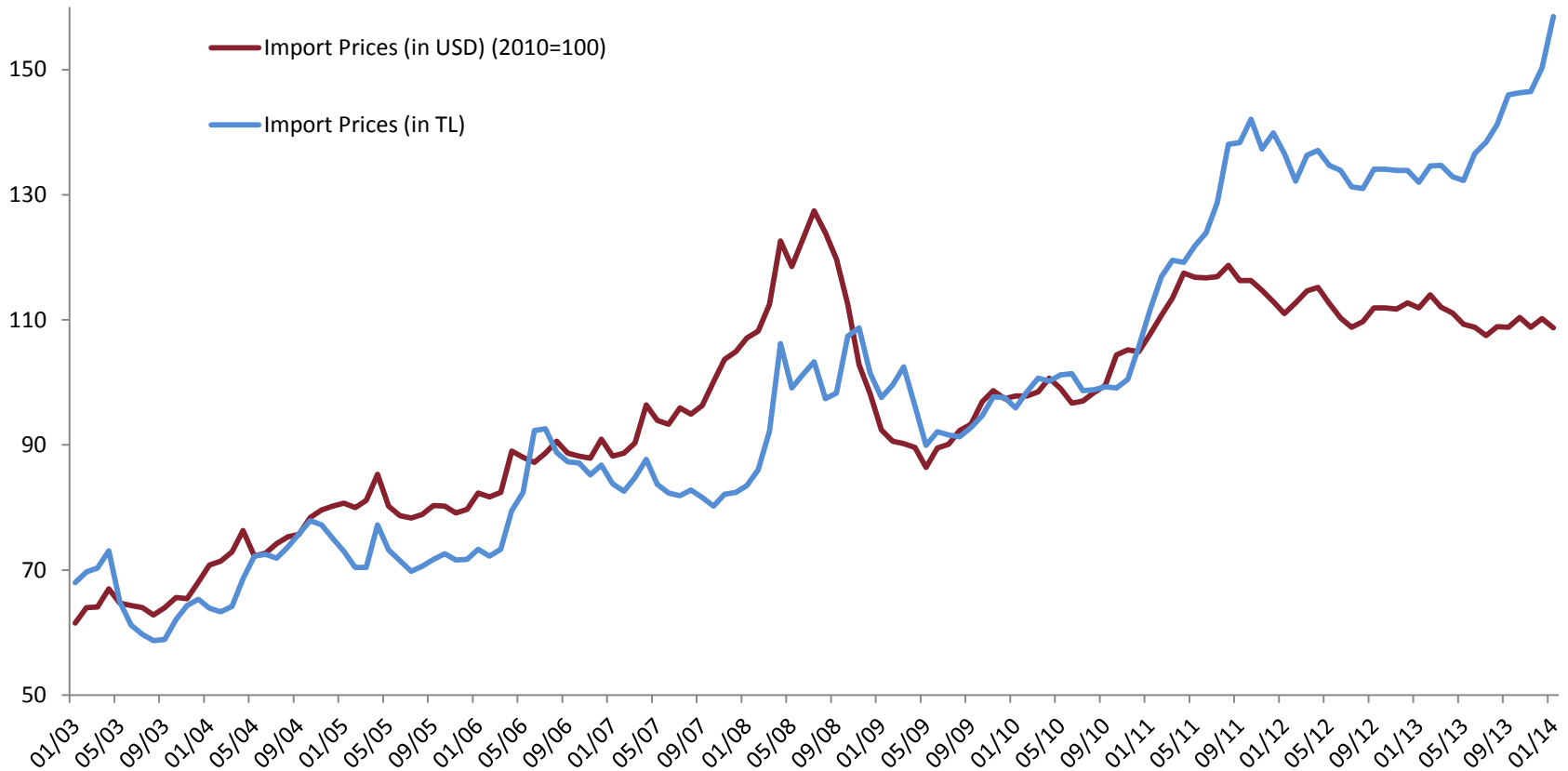


Source: Bloomberg.

Last Observation: : 27 March 2014.

Exchange rate pass-through remains to be the main driver of inflation.

Import-Export Prices (2010=100)

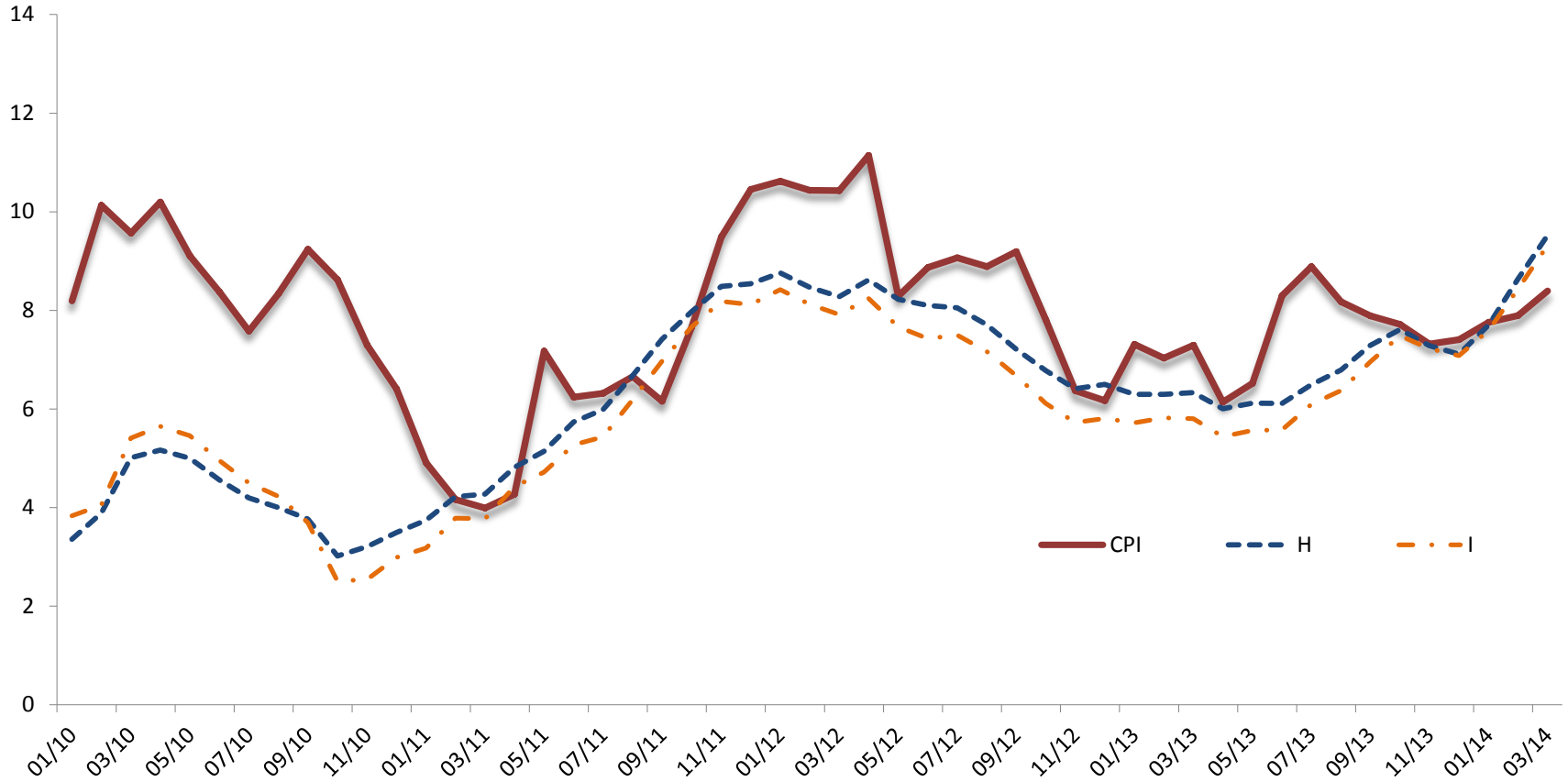


Source: TURKSTAT, CBRT.

Last Observation: January 2014.

Exchange rate pass-through is also visible in core indicators.

CPI, H and I Index (Annual Percentage Change)

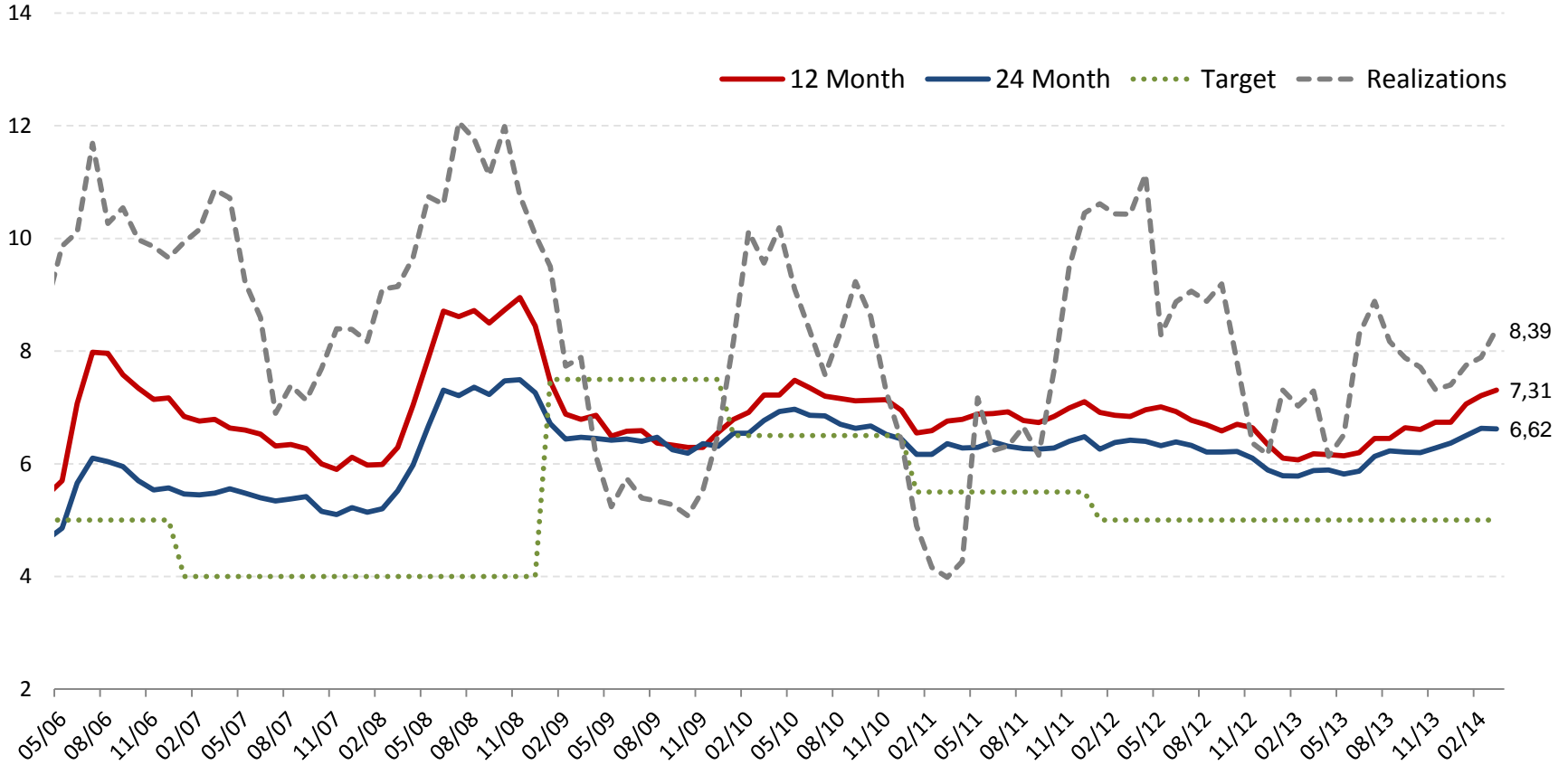


Source: TURKSTAT.

Last Observation: March 2014.

Deterioration in inflation expectations is limited in longer terms.

12 and 24 Months CPI Expectations* and Realizations (Percent)

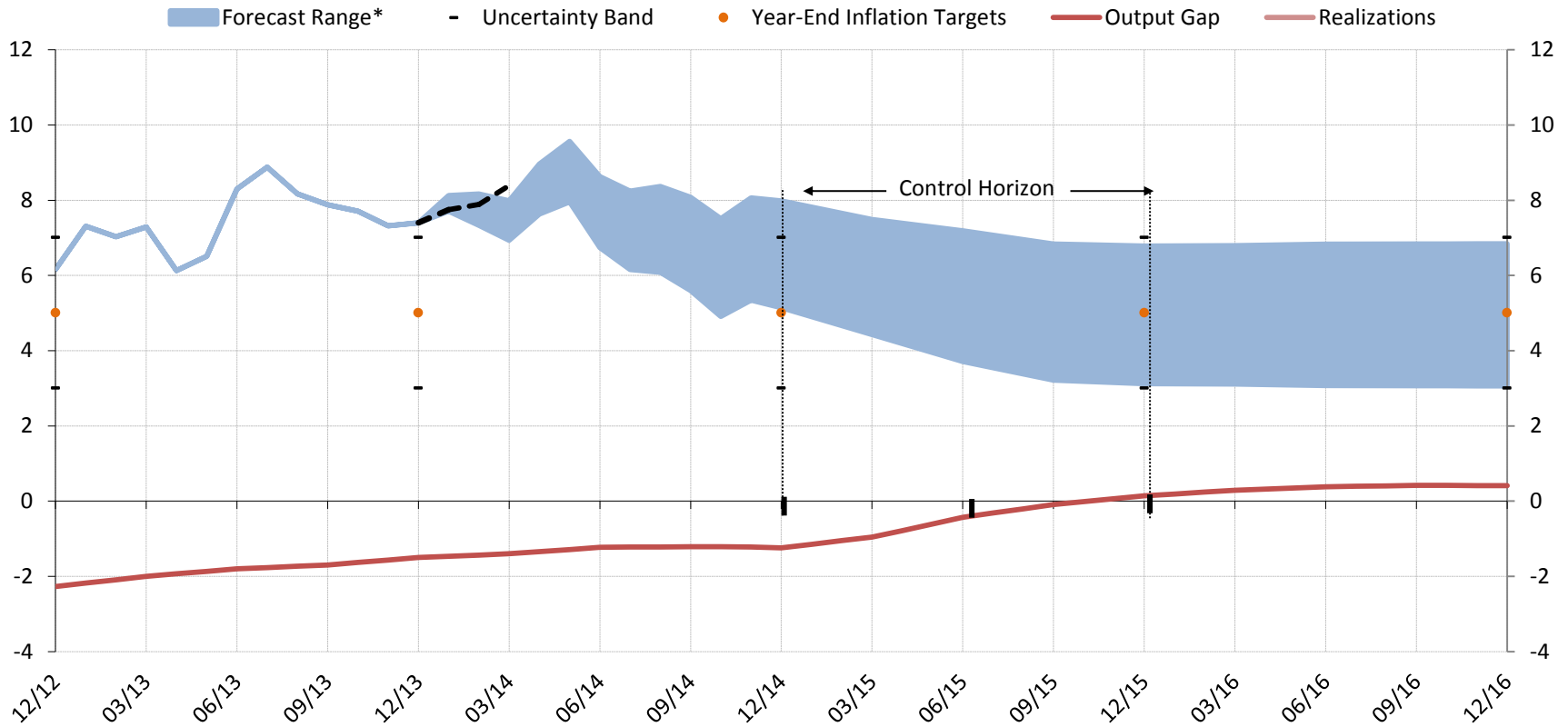


Source: TURKSTAT, CBRT.

*CBRT Expectation Survey.
Last Observation: March 2014

Inflation is expected to increase until June, partly reflecting base effects.

Inflation Report Forecast (Percent)



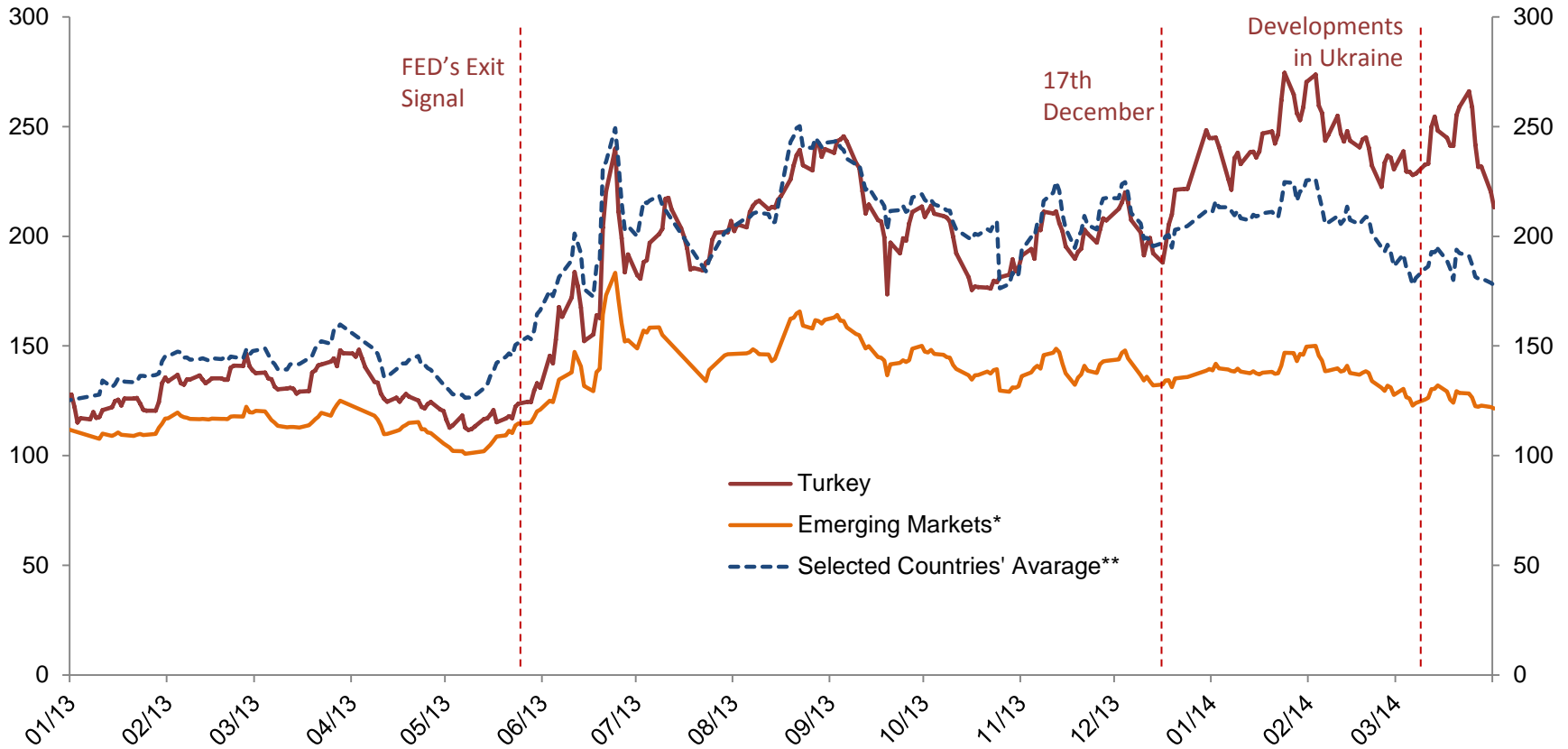
* Shaded region indicates the 70 percent confidence interval for the forecast

Last Observation: March 2014.

MONETARY POLICY

Recent developments had an additional impact on Turkey's risk premia.

CDS Prices (Countries with Current Account Deficit)



Source: Bloomberg, CBRT.

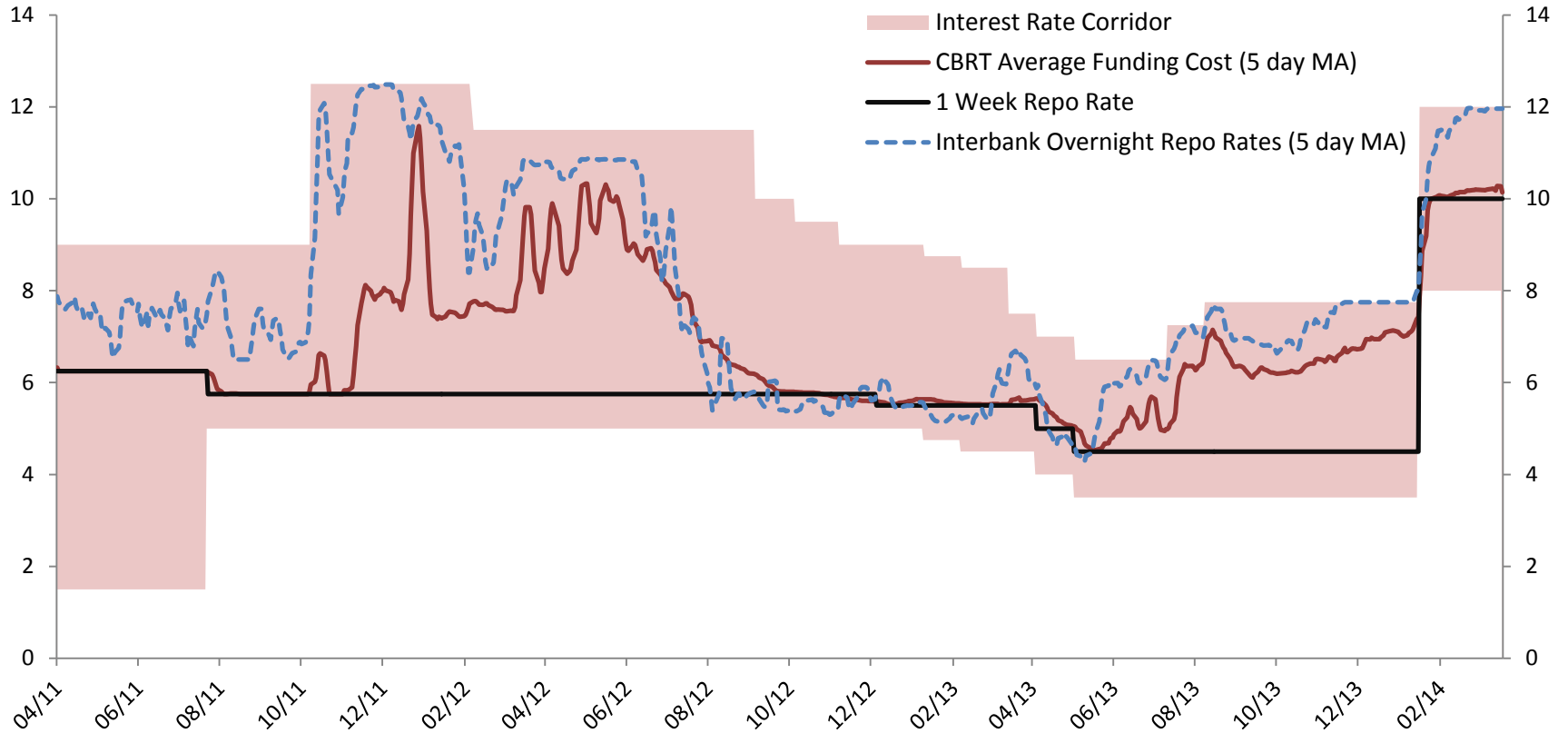
*Brazil, Colombia, Chile, Czech R., Hungary, Indonesia, Mexico, Poland, Romania and S. Africa.

** Brazil, Indonesia and S. Africa.

Last Observation: 01 April 2014

The Central Bank implemented a strong and frontloaded monetary tightening at the interim meeting of January 28, 2014.

Monetary Policy Interest Rates (Percent)

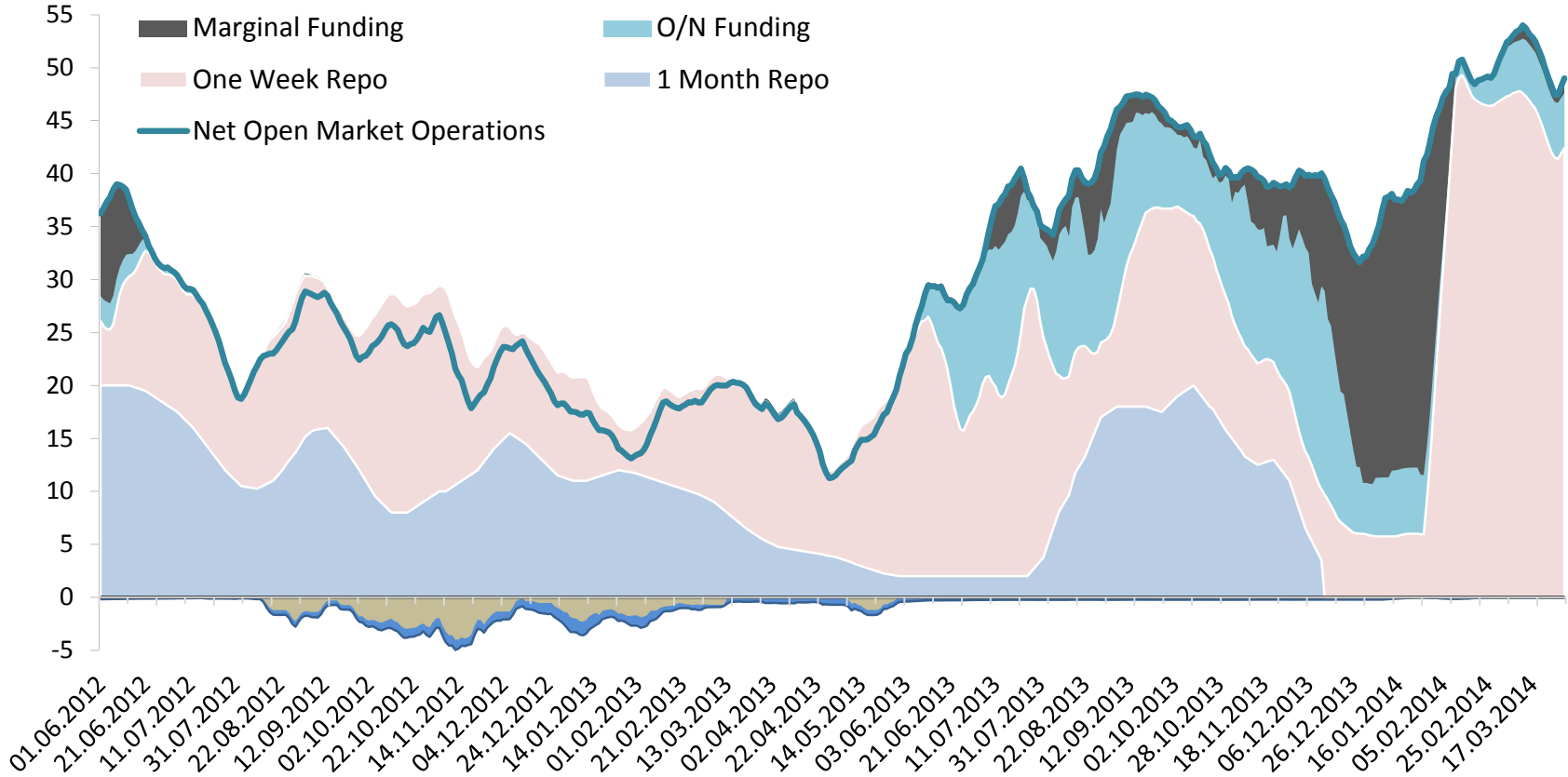


Source: CBRT.

Last Observation: 01 April 2014

Funding composition was shifted to one week maturity.

Composition of CBRT Funding (2 Week Moving Average, Billion TL)

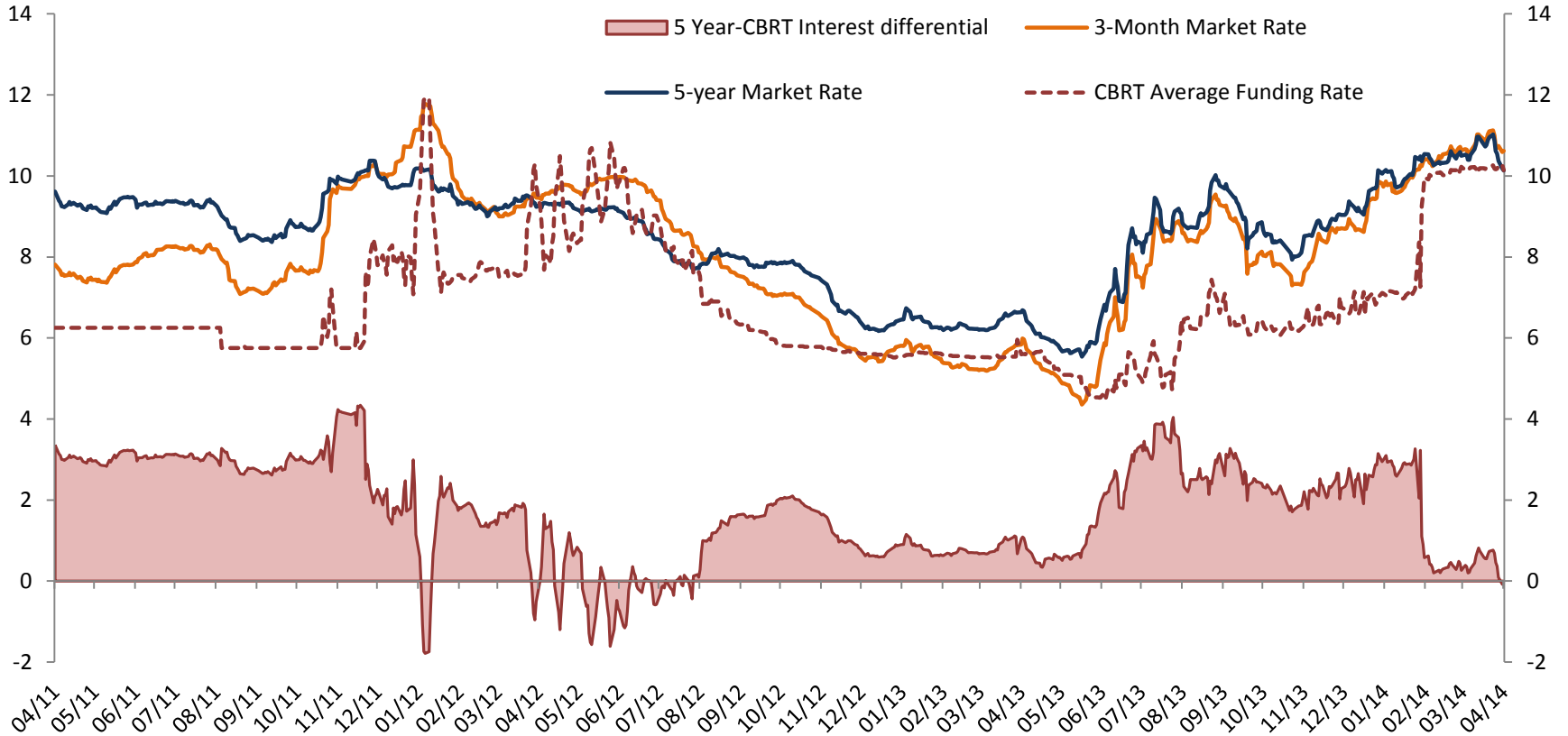


Source: CBRT

Last observation: 31 March 2014

Yield curve has flattened after the January tightening.

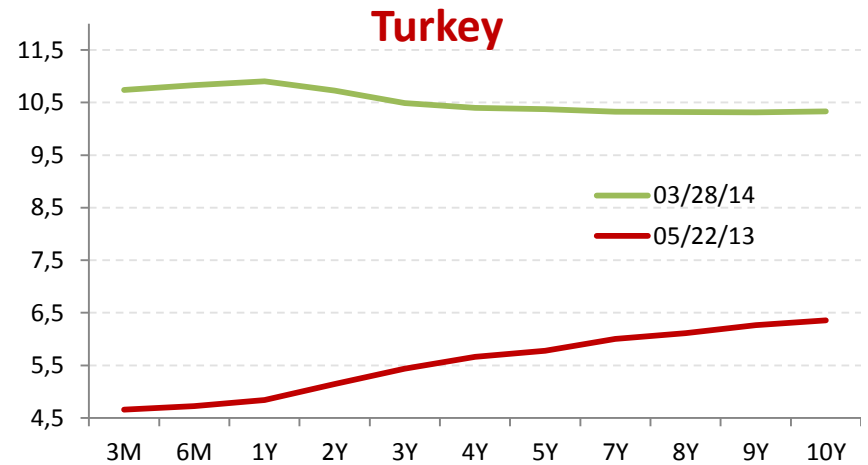
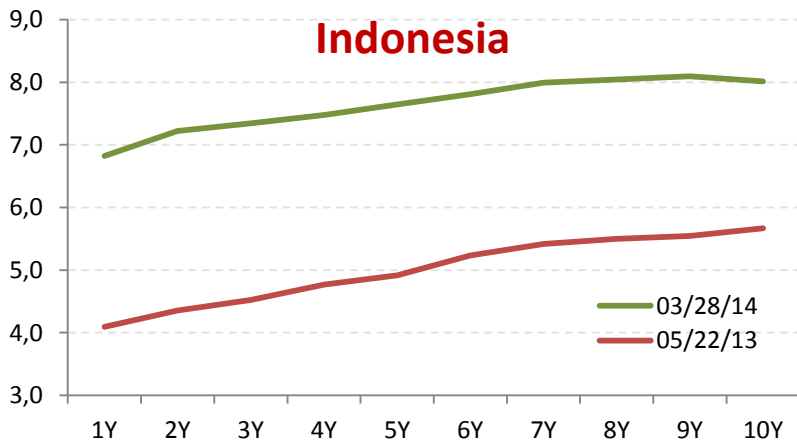
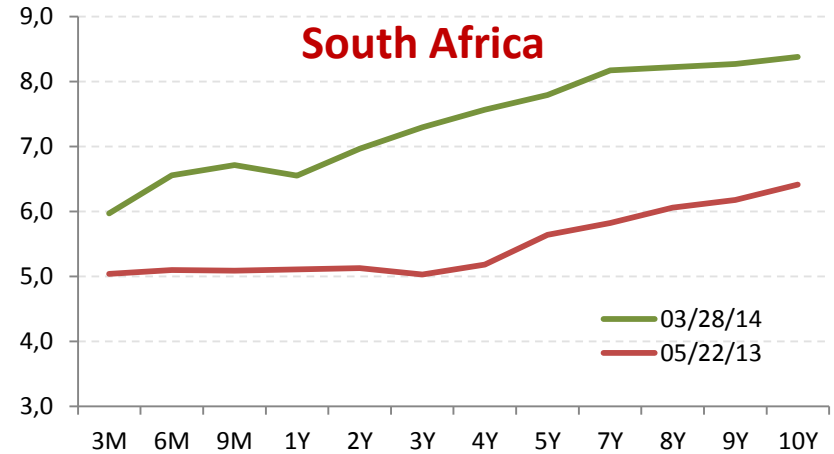
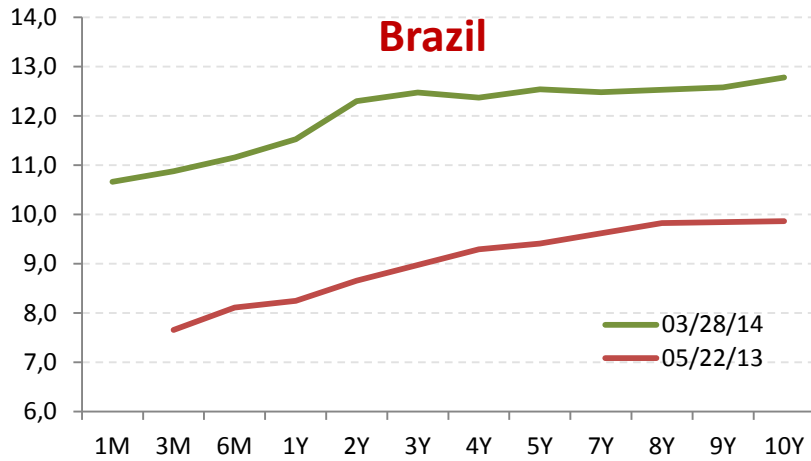
Policy Rate and Funding Rate (Percent)



Source: CBRT, Bloomberg.

Last observation: 01 April 2014

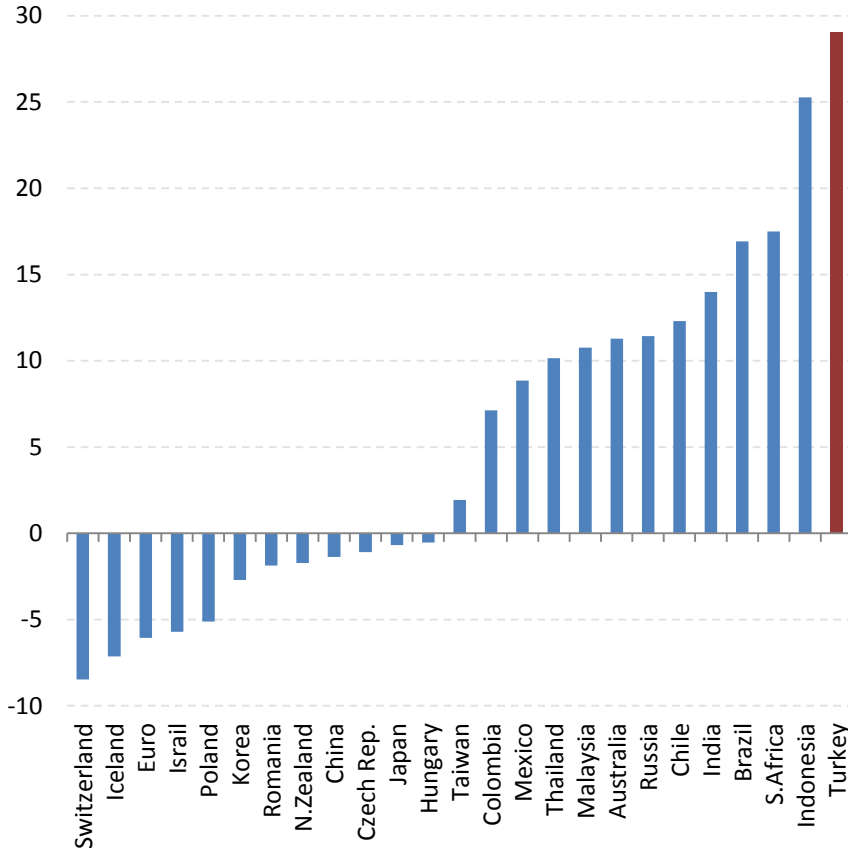
Yield curve is flatter in Turkey due to tight monetary policy.



Source: Bloomberg.

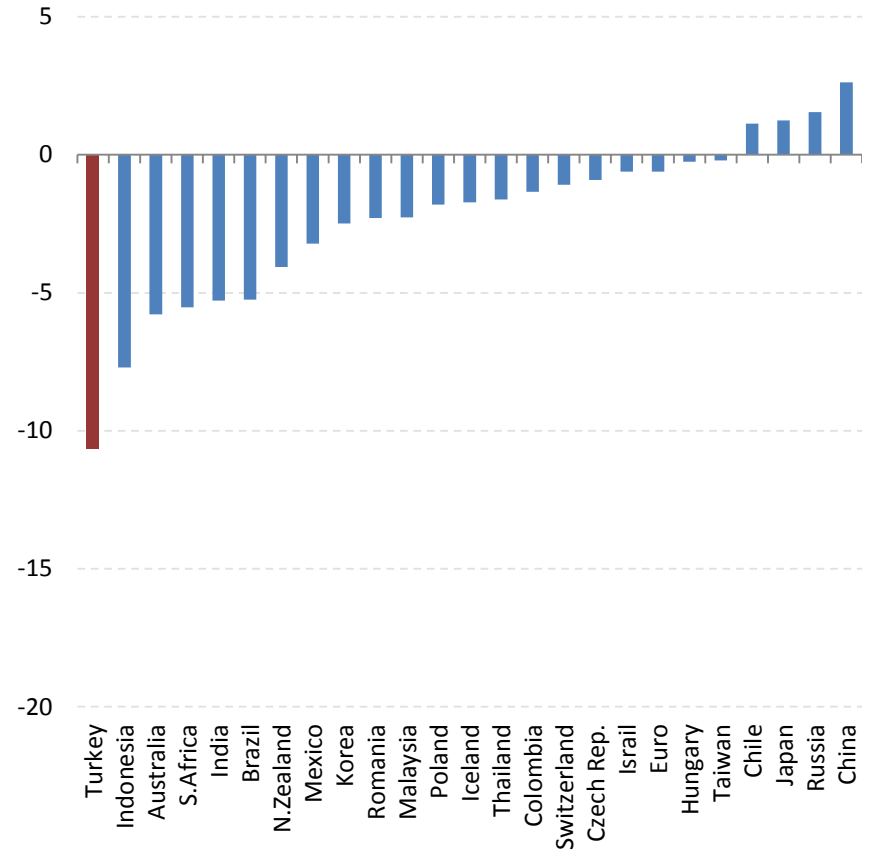
Depreciation trend of TL reversed after the monetary tightening.

22.05.2013-27.01.2014



Source: Bloomberg.

27.01.2014-02.04.2014



Source: Bloomberg.

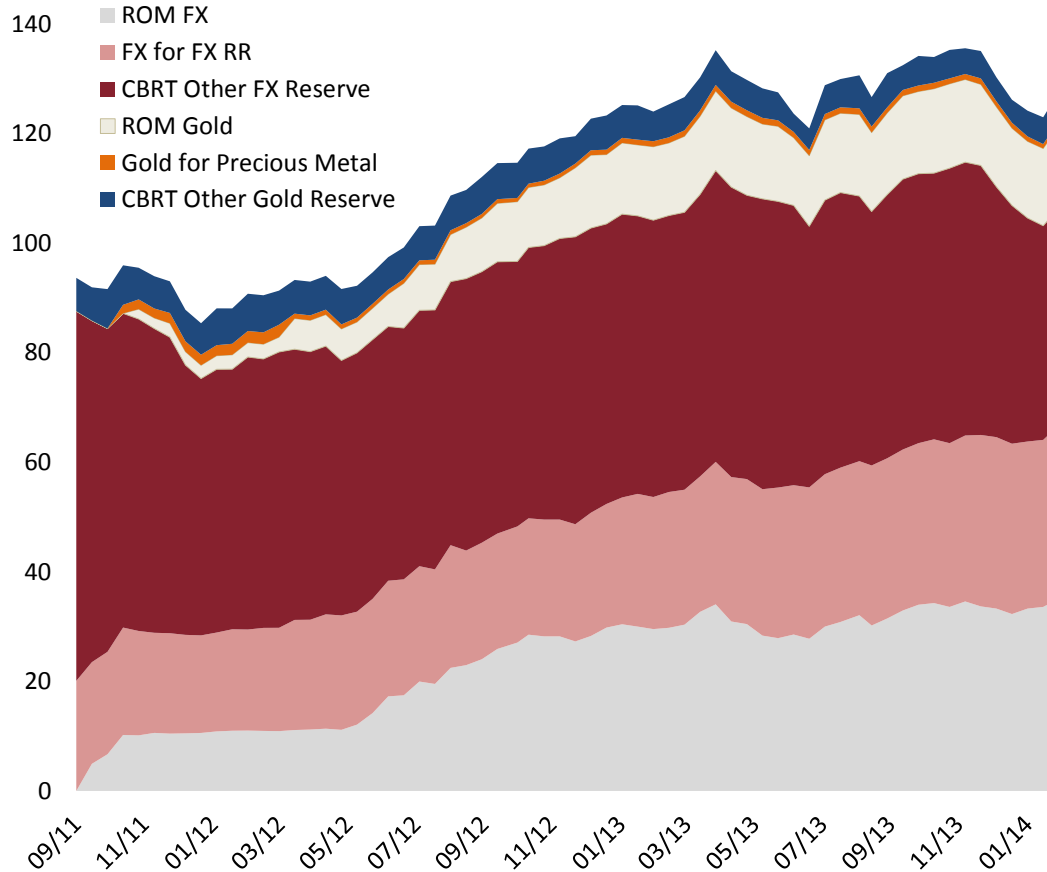
Monetary tightening had a visible impact on the currency.



Source: Bloomberg, CBRT.

FX reserves have been used against the excess volatility.

(Billion USD)



Source: CBRT.

	FX Sales (-)	Export Credit (+)
August 2013	1,95	1,19
September 2013	1,86	1,15
October 2013	0,84	1,07
November 2013	1,44	1,70
December 2013	4,67	1,02
January 2014*	5,75	0,57
February 2014	1,00	0,30
March 2014	1,05	0,48
ROM FX		34,9
FX Required Reserves		31,9
Total		66,8

*Includes the direct currency intervention of January 2014.

The Macroprudential Dimension

(Summary of the MPC minutes, March 2014)

- The Central Bank may utilize reserve requirements, reserve option mechanism and liquidity policies against the risk of a slowdown in the economic activity, if needed.
- Remuneration of Turkish lira reserve requirements could be considered at a future date if deemed necessary, in the context of the normalization of monetary policy.
- The remuneration decision will be measured and limited.

Overview: Inflation and Monetary Policy

- Retail loan growth continues to slow down in response to the tight monetary policy stance, recent macroprudential measures, and weak capital flows.
- The impact of monetary tightening on inflation will be observed with some lag. Meanwhile, inflation is expected to increase until June, partly reflecting the base effects.
- Exports will support growth while private final domestic demand will lose momentum in the forthcoming period.
- The current account deficit will improve substantially in 2014.



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