



**TÜRKİYE CUMHURİYET
MERKEZ BANKASI**

**Briefing on
July 2016 Inflation Report**

**Murat ÇETİNKAYA
Governor**

**26 July 2016
Ankara**

July 2016 Inflation Report: Main Sections

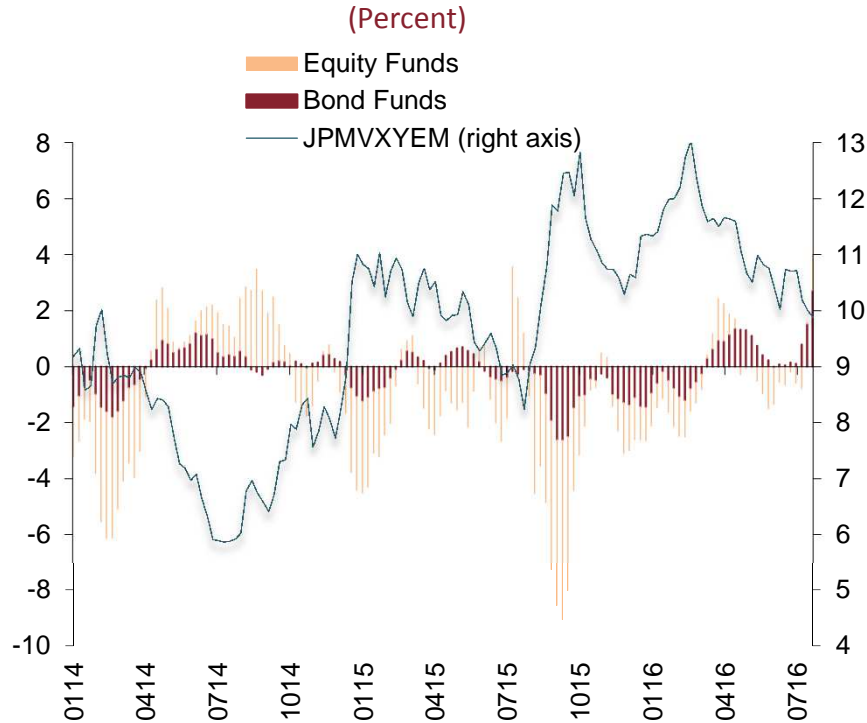
- Overview
- International Economic Developments
- Inflation Developments
- Supply and Demand Developments
- Financial Markets and Financial Intermediation
- Public Finance
- Medium Term Projections

July 2016 Inflation Report: Boxes

- Importance of Food Prices in Controlling Inflation
- Effects of Tourism Developments on Current Account, Growth and Employment
- The Impact of the Minimum Wage Increase on the Labor Markets: Early Review
- The Welfare Impact of Reducing the Completion Duration of Public Investment Projects
- Firm Size, Imported Intermediate Goods and Export Behavior
- Monetary Policy, Lending and Deposit Rates: A General Overview and Recent Developments

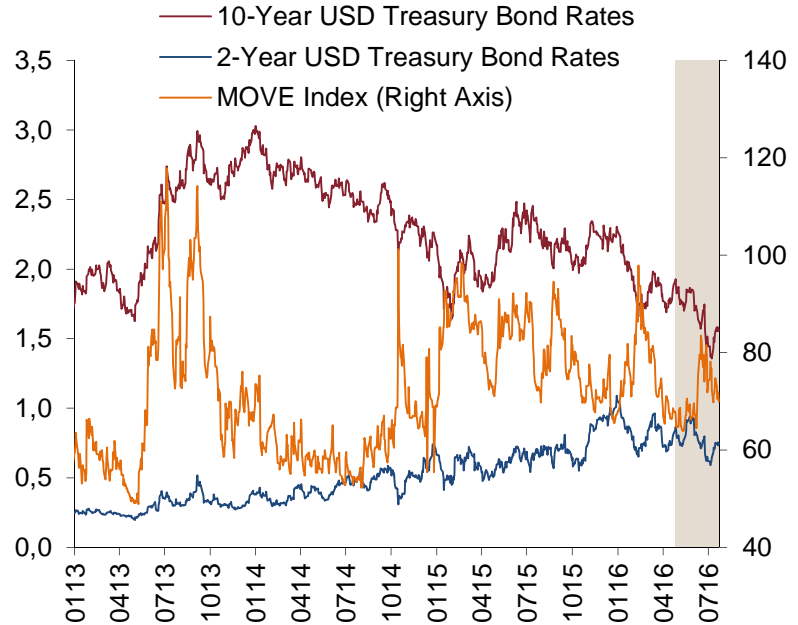
Global Uncertainties and Portfolio Flows

Portfolio Flows to Emerging Economies (4-Week Moving Average, Billion USD) and Currency Volatility Index (JPMVXYEM)



Source: EPFR, Bloomberg.

US Treasury Bond Rate (Percent) and Interest Rate Volatility Index (MOVE Index, Basis Points)



Source: Bloomberg.

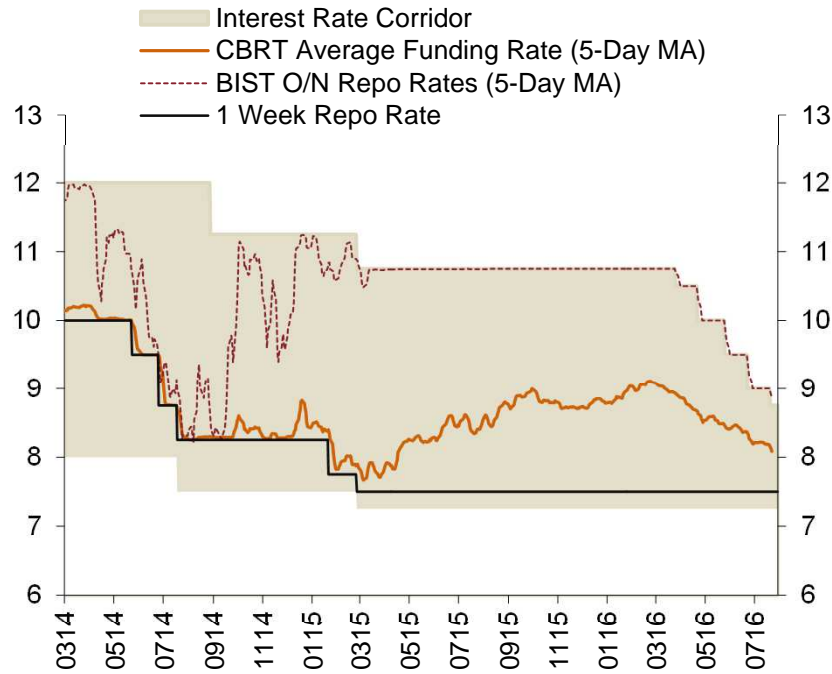
- More recently, record-low long-term interest rates of advanced economies have driven portfolio flows into emerging market bonds.

Monetary Policy and Financial Stability

Monetary Policy

CBRT Rates and BIST Interbank O/N Repo Rates

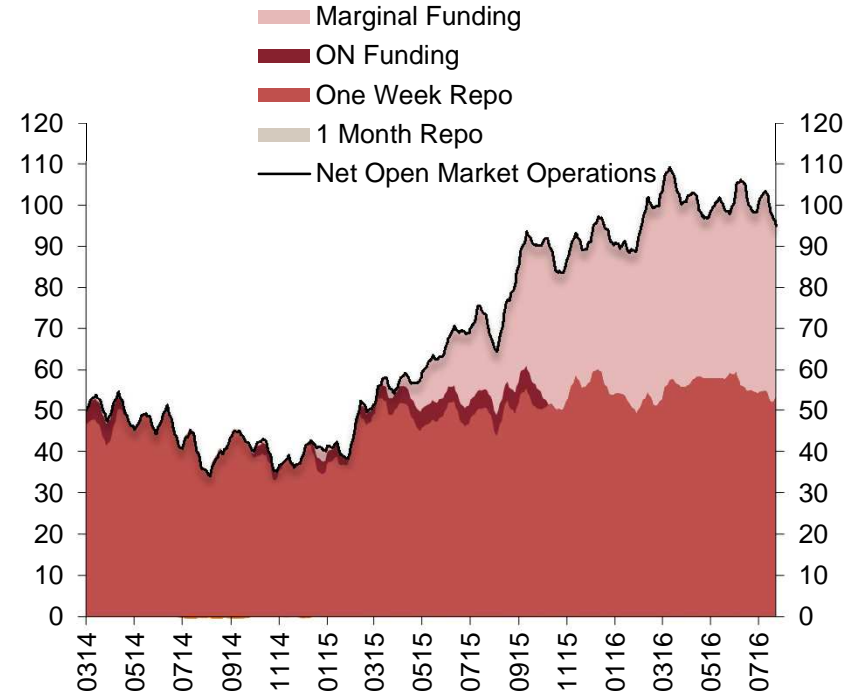
(Percent)



Source: BIST, CBRT.

CBRT Funding*

(2-Week Moving Average, Billion TL)



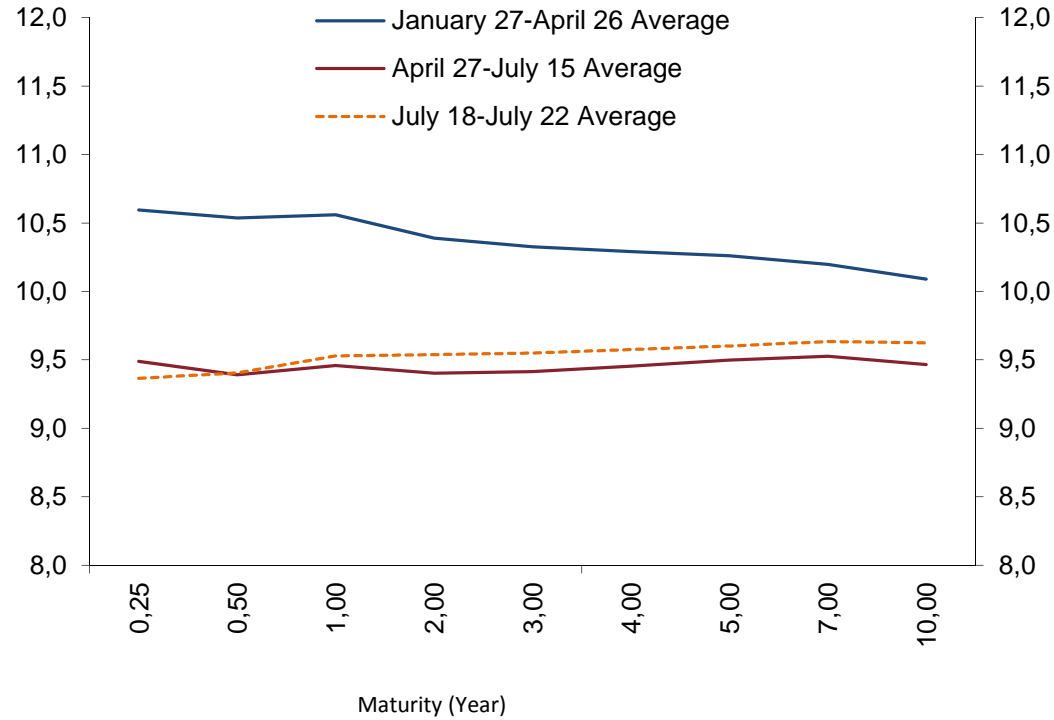
*Marginal funding is O/N funding quoted at the upper limit of the corridor.

Source: BIST, CBRT.

➡ CBRT took measured steps towards simplification of monetary policy framework.

Monetary Conditions

Yield Curve on Cross Currency Swaps
(Percent)

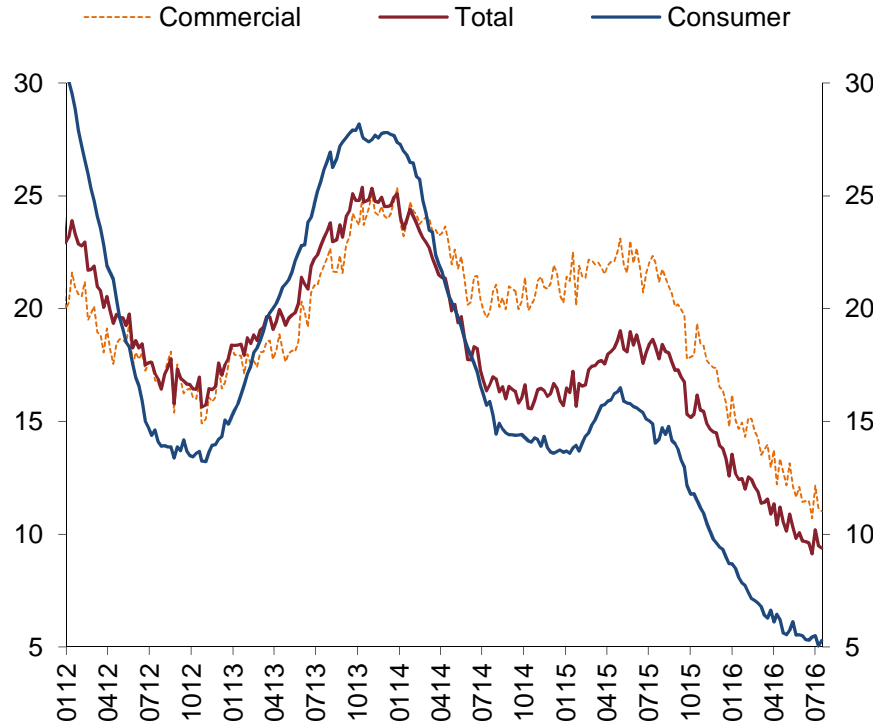


Source: Bloomberg.

- More recently, some of the gains from the yield curve were lost due to domestic uncertainty.

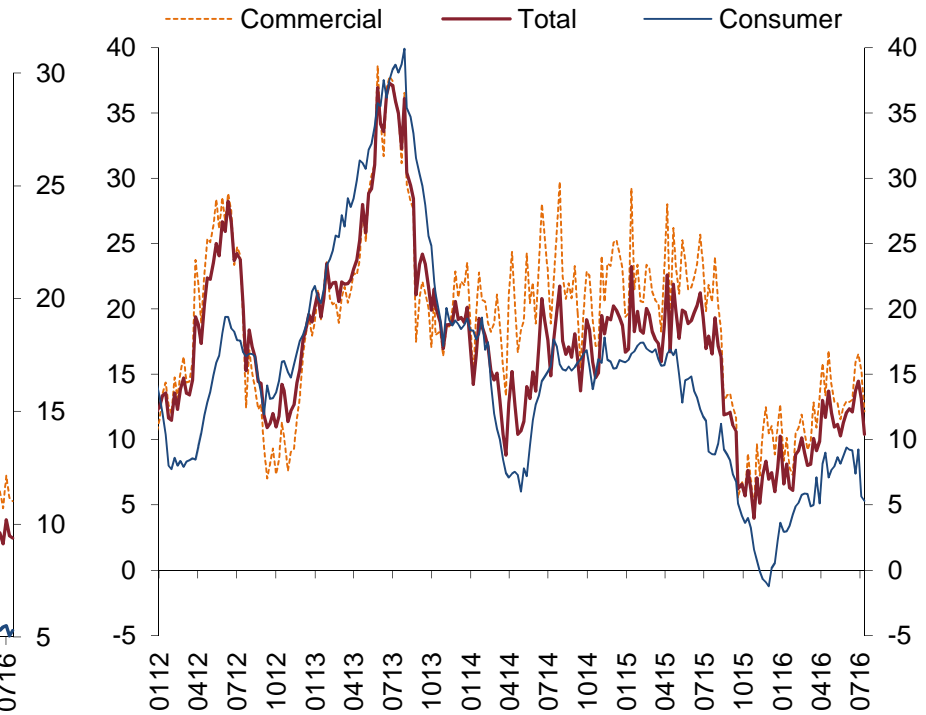
Financial Stability

Annual Credit Growth Rates
(Adjusted for Exchange Rate, Percent)



Source: CBRT.

Annualized Credit Growth Rates
(Adjusted for Exchange Rate, 13-Week Moving Average, Percent)



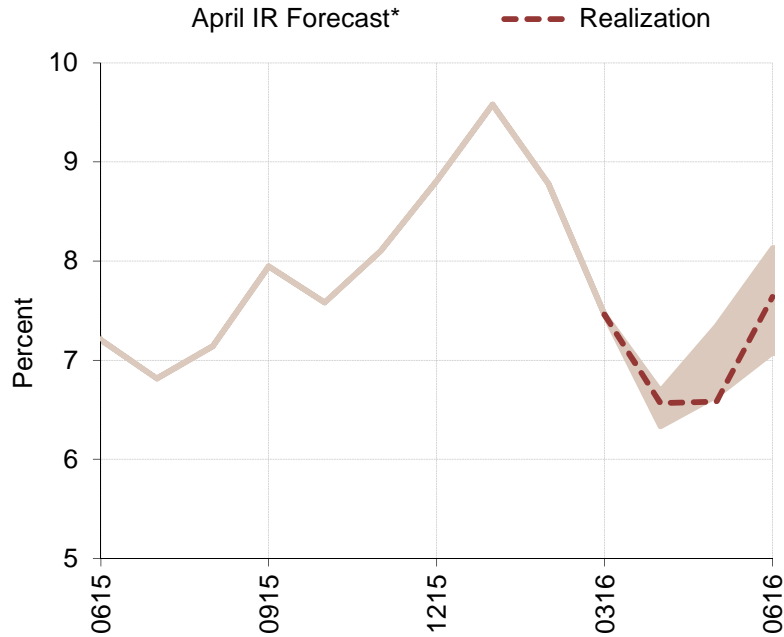
Source: CBRT.

- In the second quarter of 2016, credit growth rates are still below the previous year's averages.

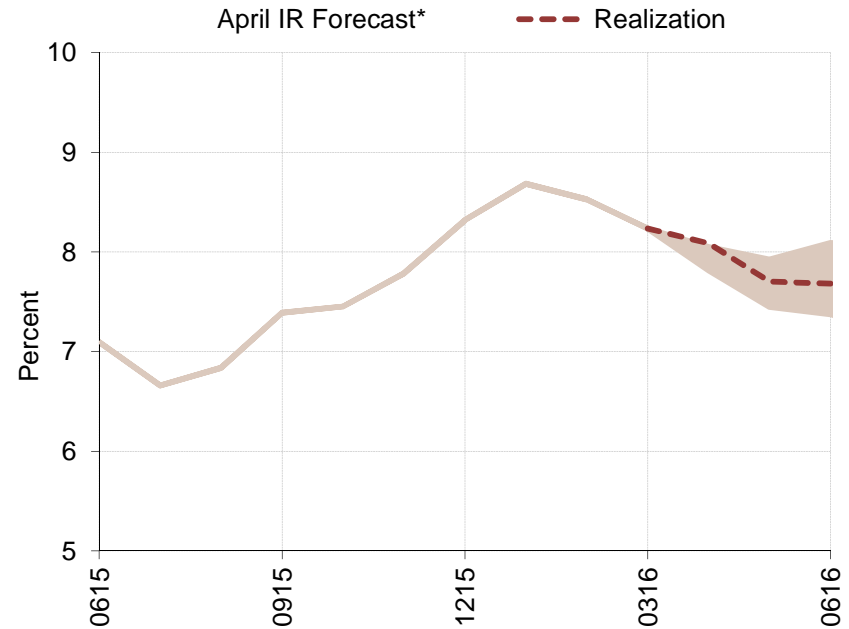
Macroeconomic Developments and Main Assumptions

April 2016 Inflation Report Forecasts and Realizations

April 2016 Inflation Forecasts and Realizations
(Percent)



April 2016 Inflation Forecasts and Realizations Excluding Unprocessed Food and Tobacco
(Percent)



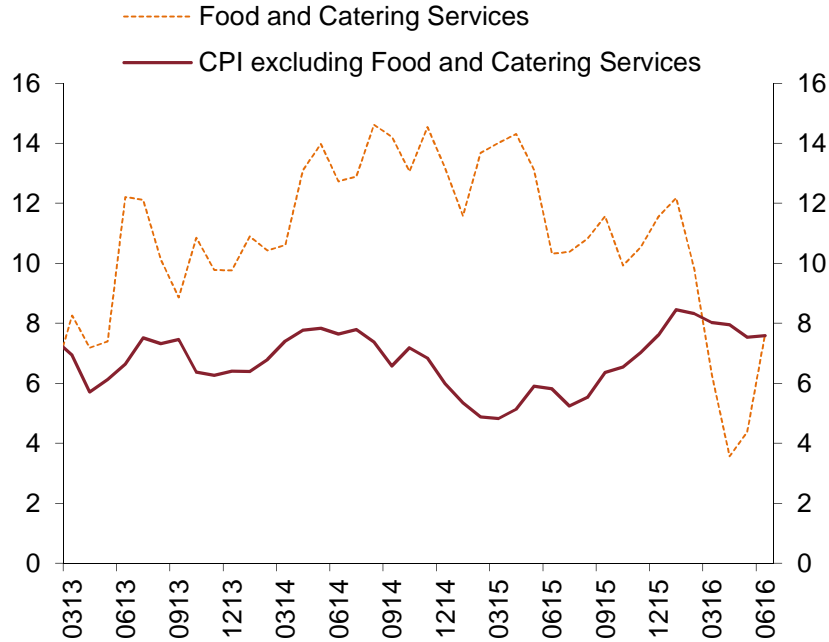
* Shaded region indicates the 70 percent confidence interval for the forecast.
Source: TURKSTAT, CBRT.

- Inflation was up in food and energy but down across core items in the second quarter of 2016.

Inflation

Food and Non-Food Prices

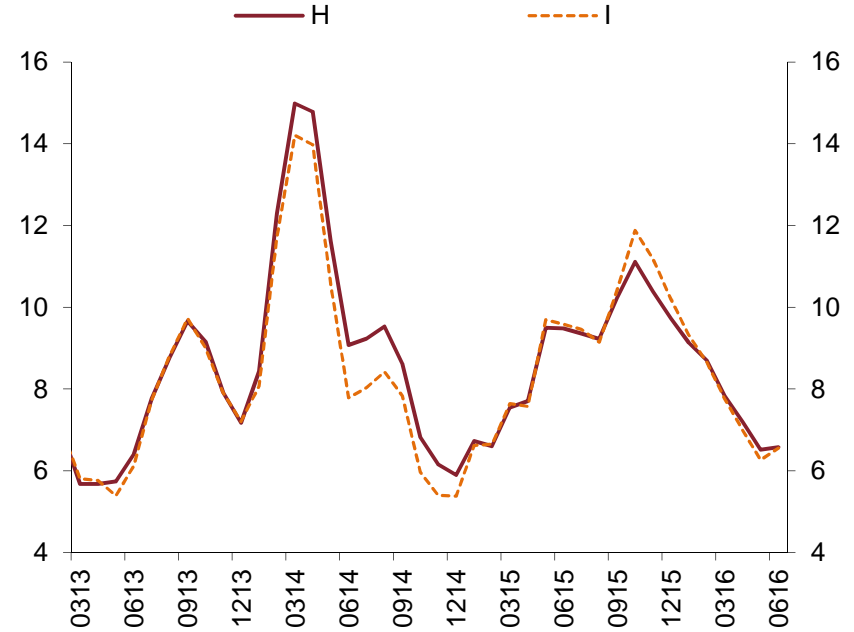
(Annual Percent Change)



Source: TURKSTAT, CBRT.

Core Inflation Indicators H and I

(Seasonally Adjusted, Annualized 3 Month Average, Annual Percentage Change)



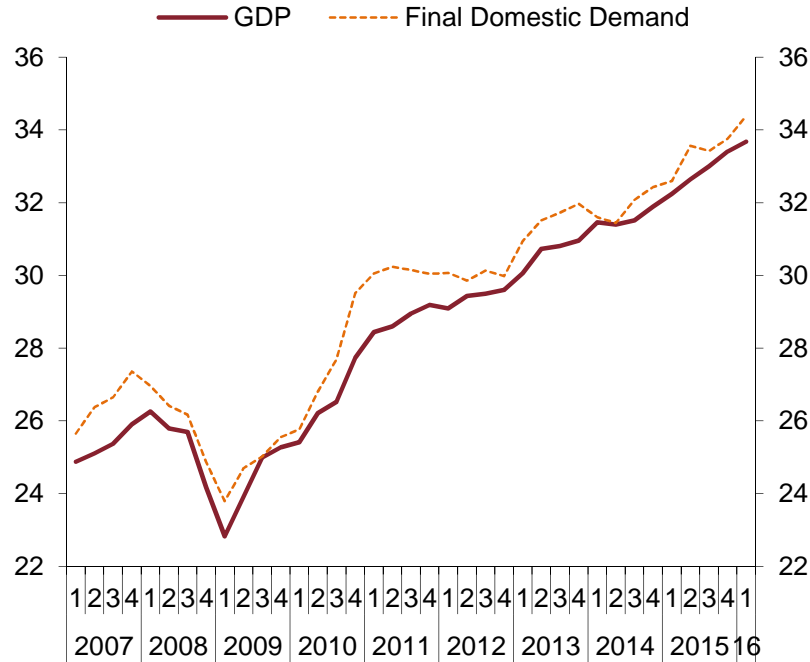
Source: TURKSTAT, CBRT.

- The underlying core inflation indicators continued to slow thanks to prices of services in the second quarter of 2016.

Aggregate Demand Developments

GDP and Final Domestic Demand

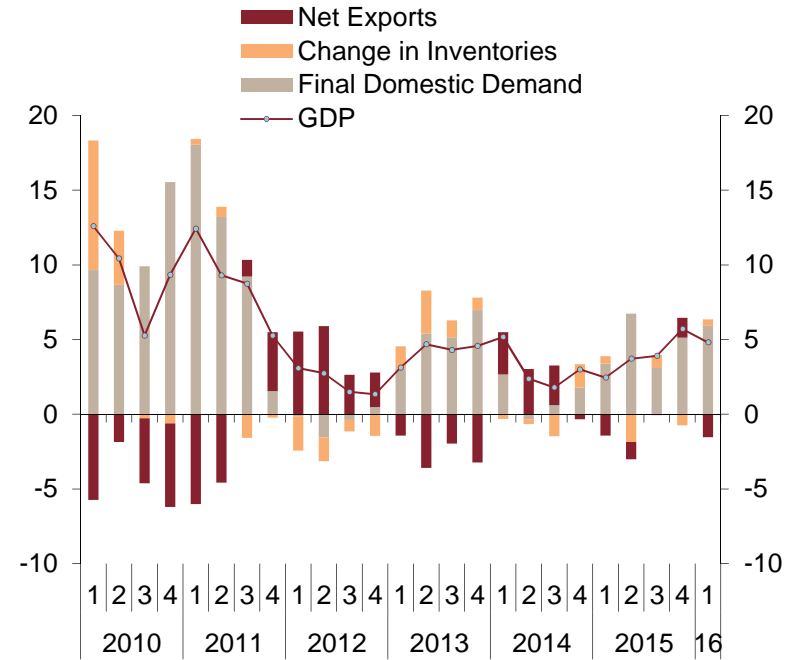
(Real, Seasonally Adjusted, Billion TL)



Source: TURKSTAT.

Contribution of Demand Components to Year-on-Year GDP Growth

(Percentage Point)



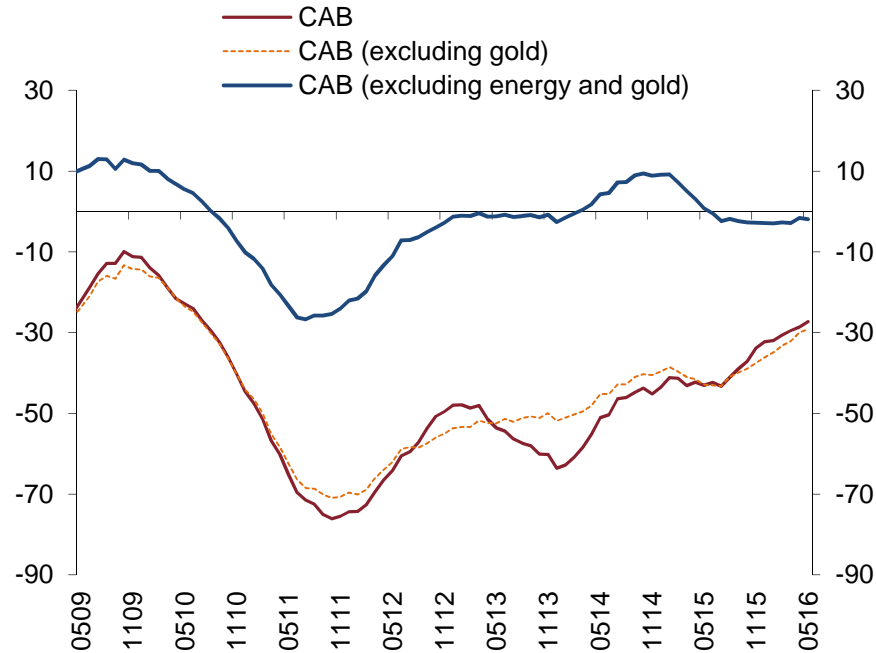
Source: TURKSTAT.

➤ Economic activity continues to display a moderate and stable course of growth.

External Balance

Current Account Balance (CAB)

(12-Month Cumulative, Billion USD)

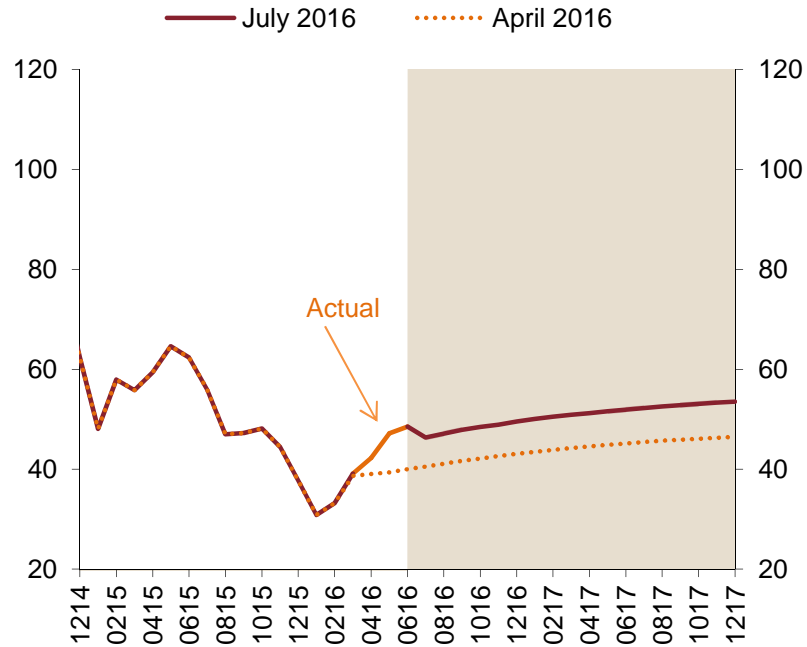


Source: TURKSTAT , CBRT.

- Despite the course of domestic demand on demand composition, amid the ongoing macroprudential measures and the low course of commodity prices, the current account balance is expected to improve further in 2016.

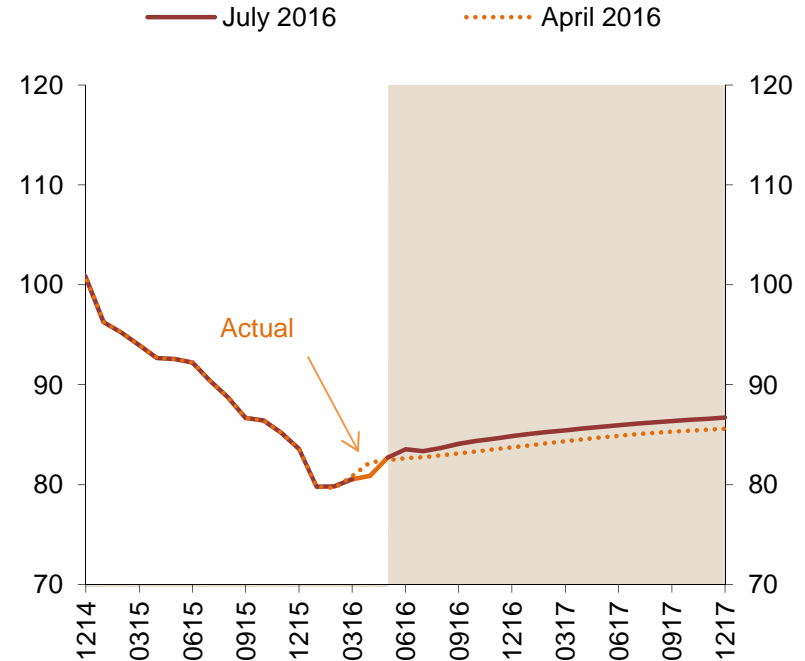
Oil and Import Prices

Oil Prices*
(USD/barrel)



* Shaded area indicates the forecast horizon.
Source: Bloomberg, CBRT.

Import Prices*
(USD, 2010=100)



* Shaded area indicates the forecast horizon.
Source: TURKSTAT, CBRT.

- Assumptions both for crude oil prices and USD-denominated import prices were revised upwards.

Revisions in Assumptions

		April 2016	July 2016
Output Gap	2016 Q1	-0,5	-0,5
	2016 Q2	0,1	-0,2
Food Prices (Year-end Percent Change)	2016	9,0	8,0
	2017	8,0	8,0
Import Prices (Average Annual Percent Change, USD)	2016	-8,9	-8,5
	2017	3,2	4,0
Oil Prices (Average, USD)	2016	40	44
	2017	45	52
Export-Weighted Global Production Index (Average Annual Percent Change)	2016	1,8	1,7
	2017	2,0	1,8

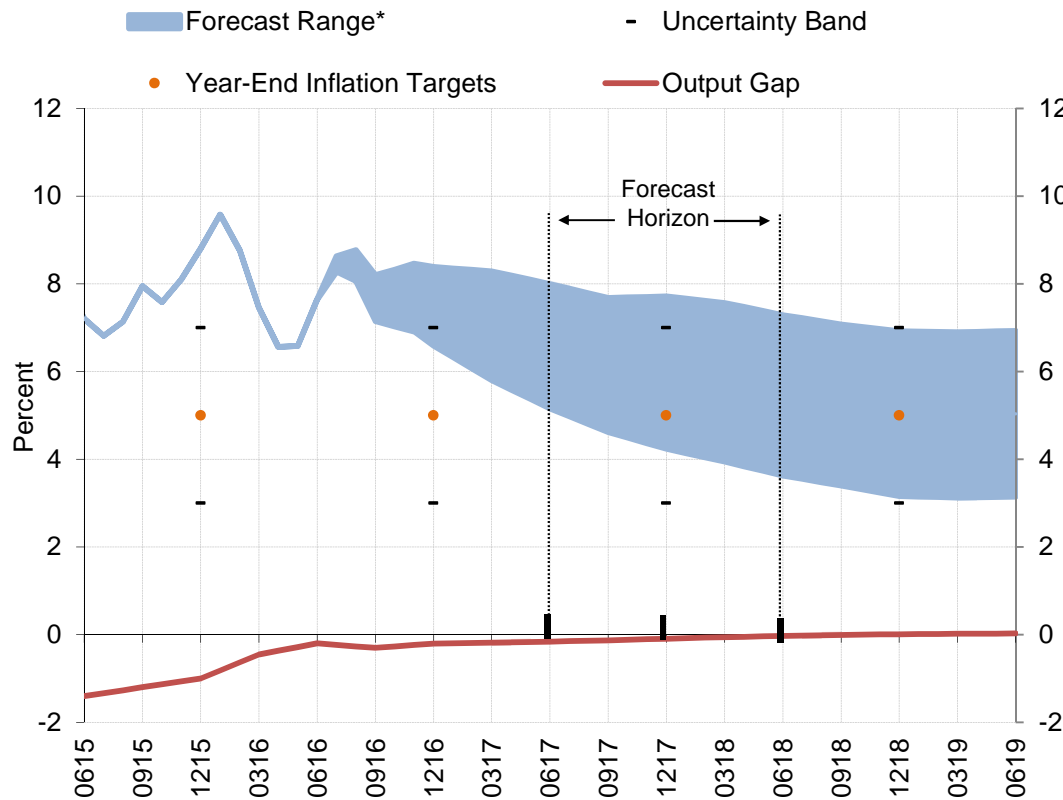
➤ The assumption for food price inflation was revised downwards.

Monetary Policy Stance

- Given a decisive policy stance that focuses on bringing inflation down, the 5-percent target is expected to be achieved gradually;
- Inflation is likely to stabilize around 5 percent as of 2018 after falling to 7.5 percent in 2016 and to 6 percent in 2017.

Inflation Outlook

Inflation and Output Gap Forecasts



Accordingly, inflation is expected to

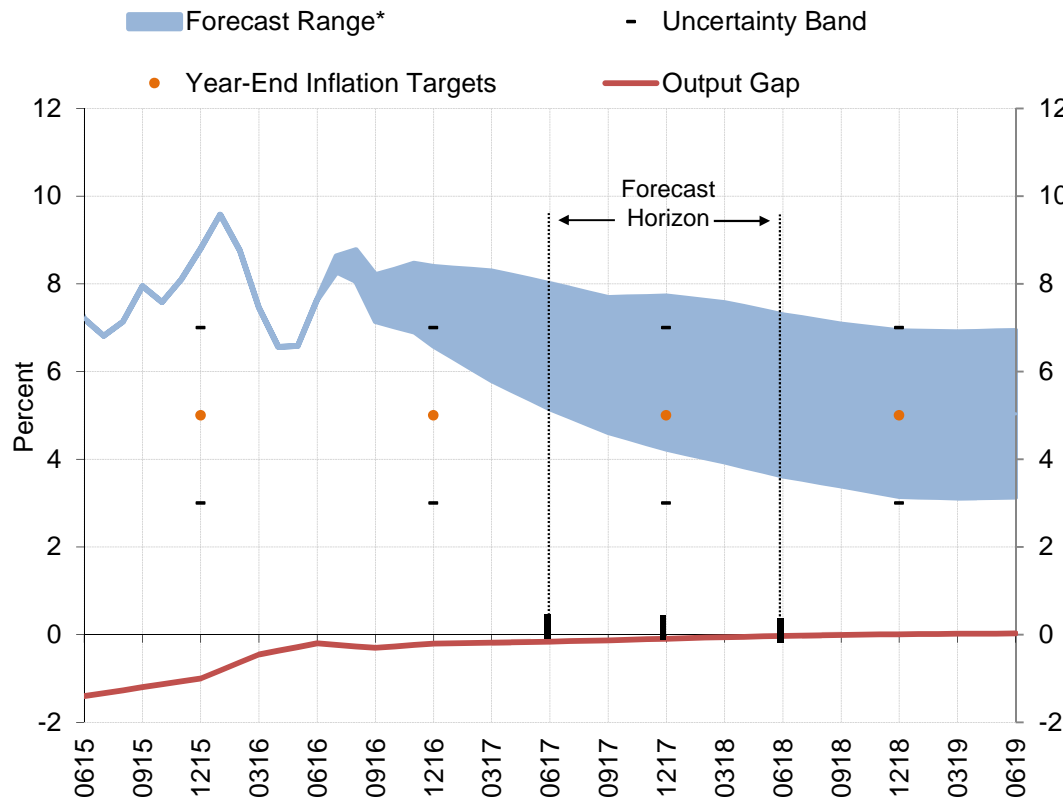
- be between 6.6 % and 8.4 % (mid-point of 7.5 %) by the end of 2016,
- be between 4.3 % and 7.7 % (mid-point of 6 %) by the end of 2017,
- stabilize at 5 % in the medium term

with 70 percent probability.

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

Inflation Outlook

Inflation and Output Gap Forecasts



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

- The pass-through to inflation from TL-denominated import will be restricted.
- The recent upward movements in unprocessed food prices and adjustments in tobacco prices will push inflation remarkably upwards in July.
- Food prices are projected to see a downward correction in the upcoming period.
- Core inflation is likely to hover more modestly across the year compared to the previous reporting period.

Joint Efforts Since April 2016 Inflation Report

Efforts of the Food Committee

- Concrete policy proposals were produced by handling products one by one, the prices of which create notable volatility in CPI. Regarding this, items with high weight in inflation were given priority.
 - measures taken by the Ministry of Food, Agriculture and Livestock on red meat prices
- Structural issues like licensed warehousing, specialized commodity exchanges, agricultural subsidies, producer organizations and data collection and compilation are also handled
 - revision of the Wholesale Market Law is under construction

Structural Issues

- With a view to preparing the infrastructure to investigate structural issues, “Structural Economic Research Unit” was established under the CBRT.
- Efforts to enhance institutional infrastructure to compile regional information on corporate sector developments and the pricing behaviors have gained momentum.
- CBRT has been paying regular visits to corporate sector firms in various cities of our country to report the cyclical evaluations regarding the firms’ activities and expectations and deliberating towards detecting structural problems on a sectoral basis.

Communication Policy

- Technical talks will be hold with investors and analysts.
- Regular meetings will be held with investors in financial centers abroad.
- Meetings will be held to facilitate exchange of views with industrial and trade chambers and other corporate sector representatives.
- Periodic meetings will be held with the representatives of the press agencies and the economic media.
- Monthly meetings currently held with banks' economists will be held when deemed necessary depending on the declining need following new practices.



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