TÜRKİYE CUMHURİYET
MERKEZ BANKASI

Emerging market economies have become more resilient than you think

Turalay Kenç

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June 2014

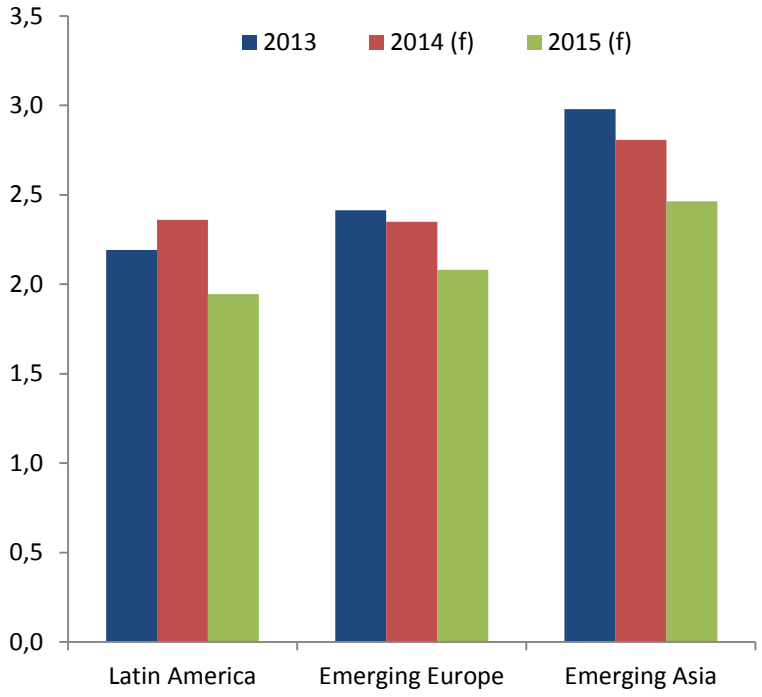
The global financial crisis of 2007-08 highlighted differences between DM and EM economies.

- Differences in economic fundamentals in favour of EM countries
  - ✓ Structural differences
    - Population dynamics
    - Productivity dynamics
    - …
  - ✓ Flow balances
  - ✓ Stock balances
  - ✓ Policy spaces

Flow and Stock Balances of EM Governments

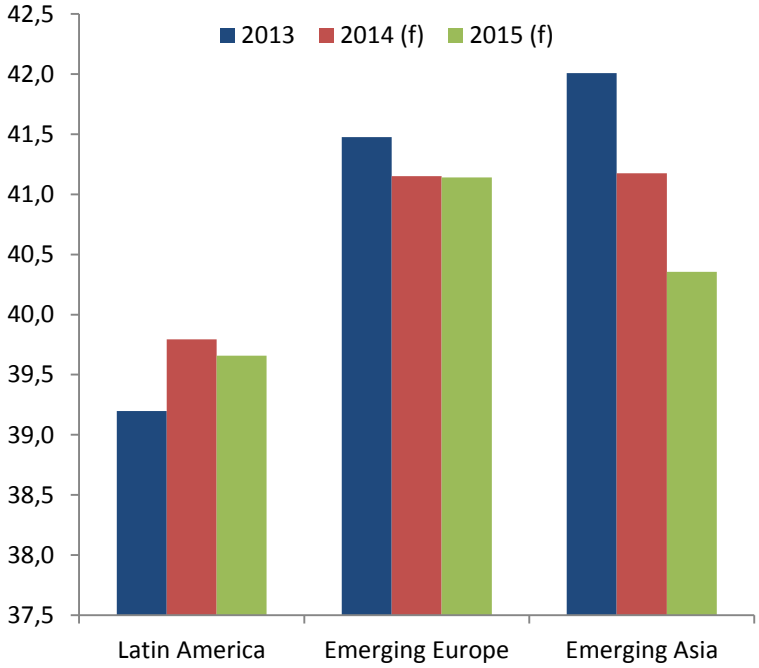
EME Budget Deficits

(% of GDP)



EME General Government Debt

(% of GDP)

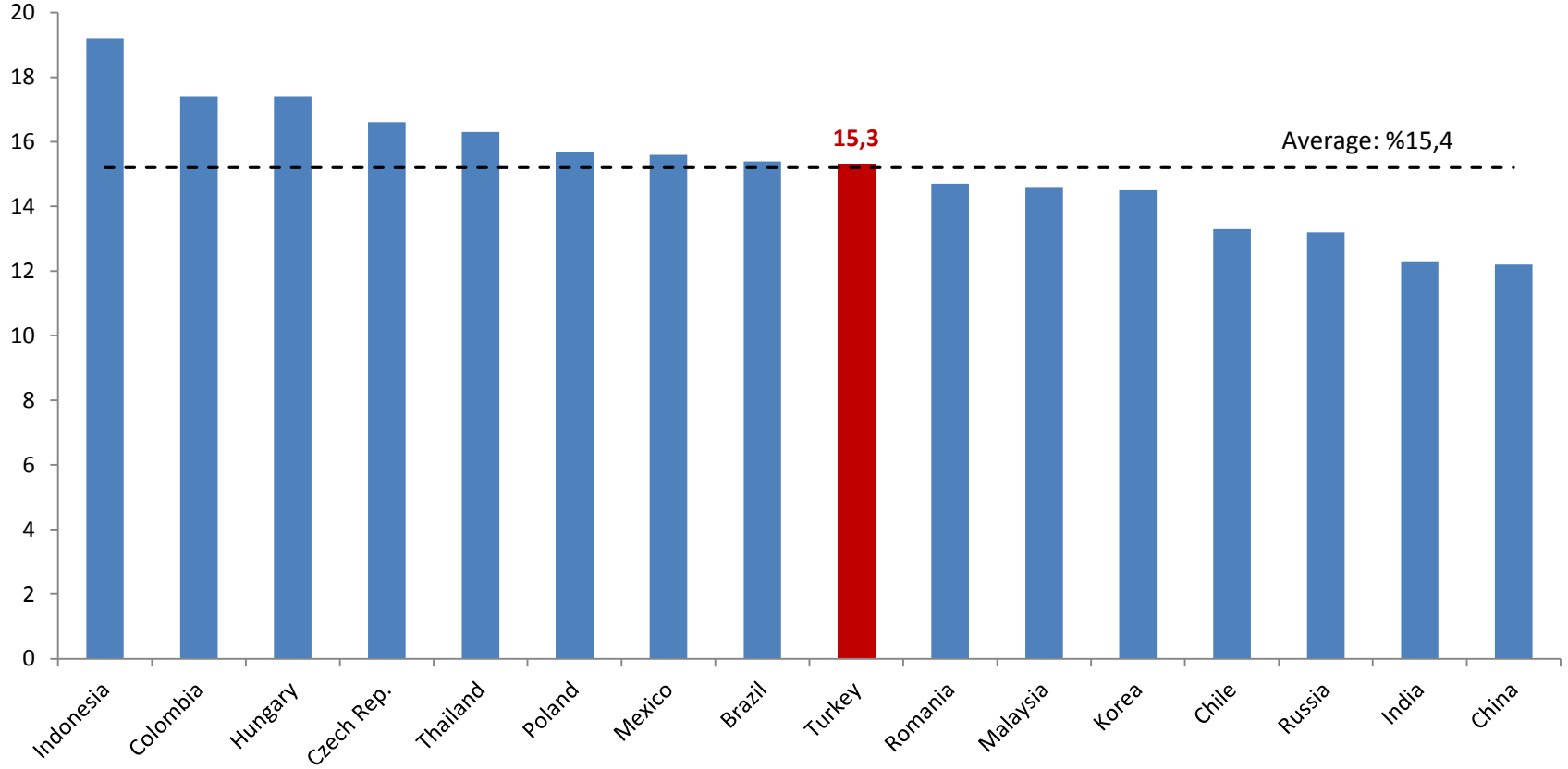


Source: IMF WEO, April 2014

Emerging Asia: Thailand, Indonesia, India, S. Korea, Malaysia
Emerging Europe: Czech Rep., Poland, Hungary, Russia, Ukraine, Turkey, S. Africa
Latin America: Brazil, Mexico, Chile, Peru, Colombia

Strong Banking Sectors in EMEs

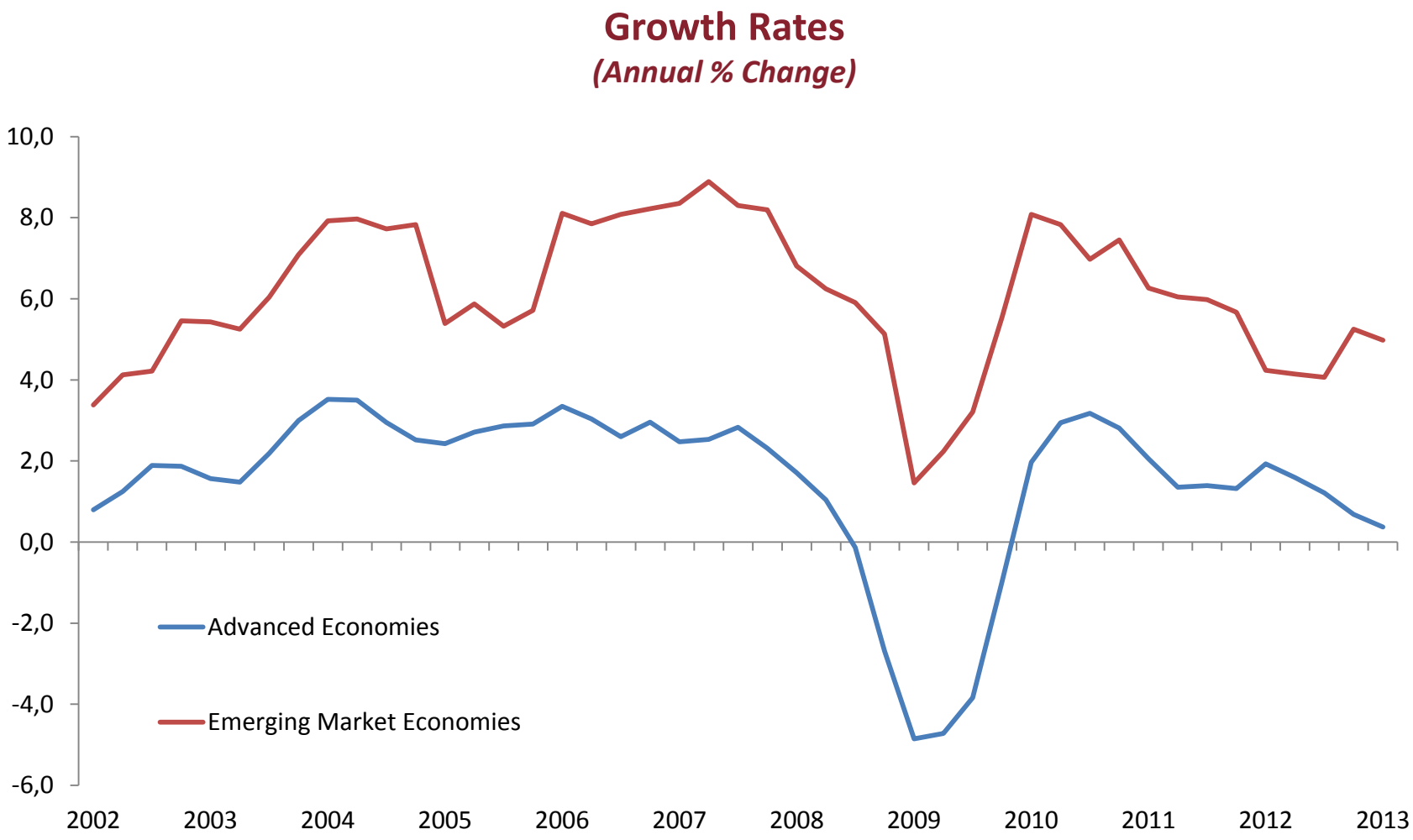
Capital Adequacy Ratio in Emerging Markets
(%, 2013q4)



Source: IMF Financial Soundness Indicators

Thailand, China and Chile as of 2012q4
Russia, Indonesia and Colombia as of 2014q1
Czech Republic as of 2013q3

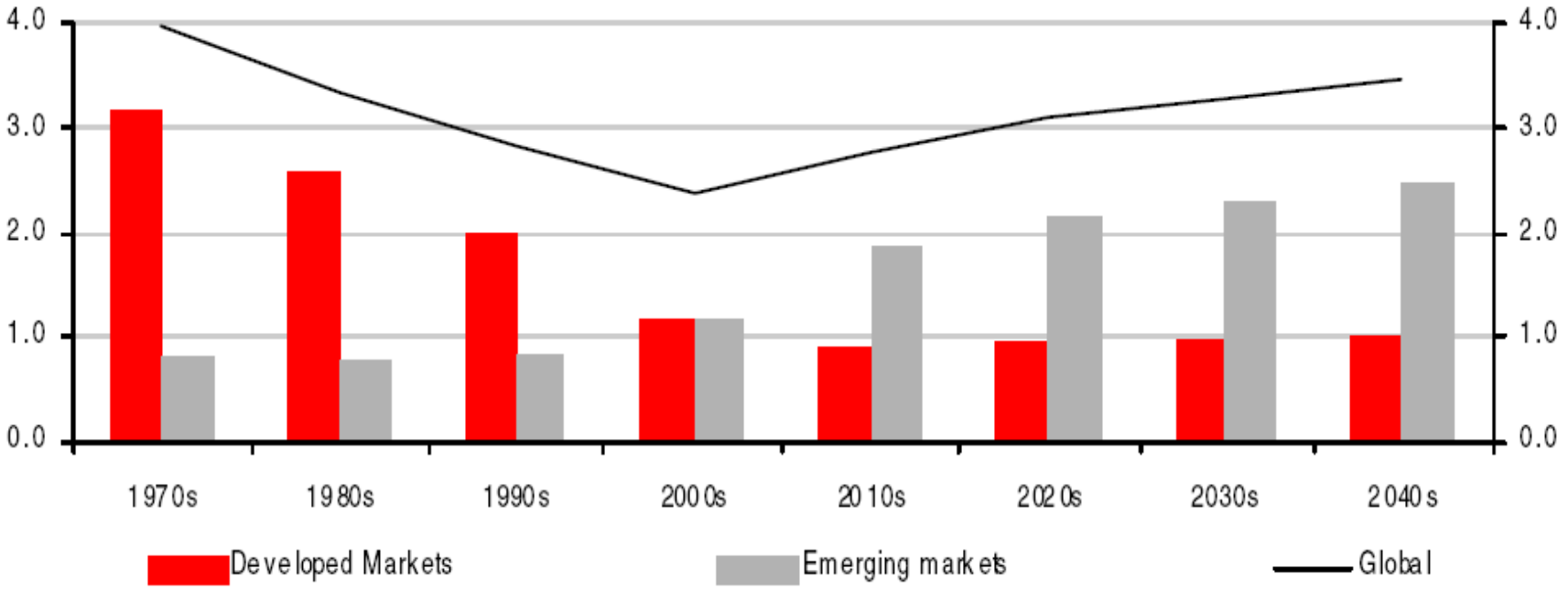
Growth Differential



Source: IFS

Emerging markets will be the main driver of the global growth.

Contributions to Global Growth



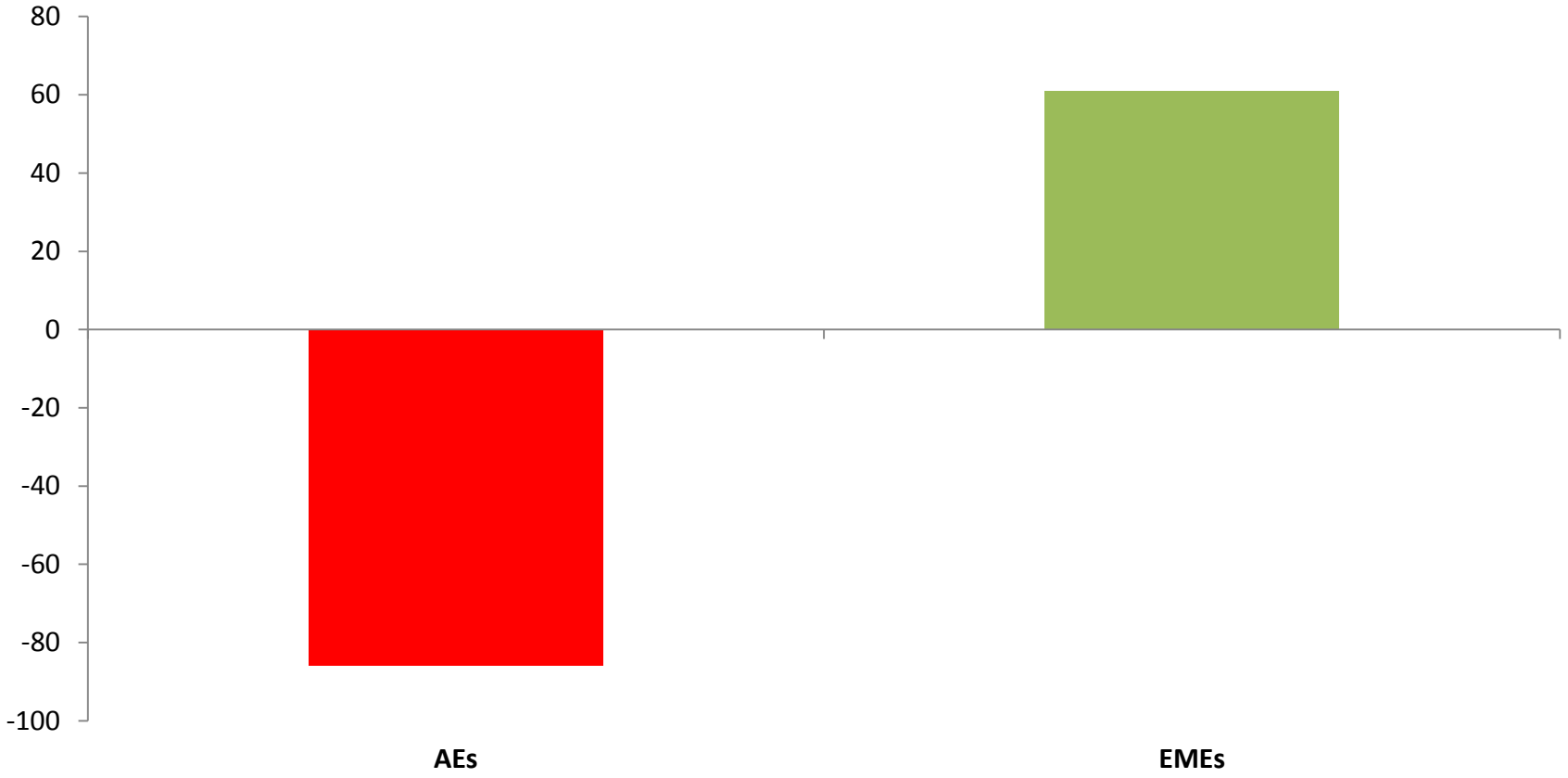
Source: HSBC, World in 2050, January 2012

Financial markets have priced the relative strengths of EM economies

- Strong sovereign credit rating gains for EMEs after the GFC.
- Marked declines in EM risk premia.
- Substantial falls in EM rates as result of not only improved risk premia but also increased policy effectiveness

As riskiness of EMEs declines, their sovereign ratings rise.

Net Number of Rating Changes since 2008 (Increases - Decreases)



Source: Bloomberg

Last Observation: As of May 2014, Moody's, S&P and Fitch Ratings ratings.

The relative strength of EMEs stems from their past crisis lessons

- **In the 1990s and early 2000s many currency, banking and fiscal crises in EMEs due to:**
  - ✓ Premature financial liberalization
    - Capital account liberalization
  - ✓ Imprudent structural and macroeconomic policies
  - ✓ Institutions lacked quality
  - ✓ Ineffective monetary policy
  - ✓ Insufficient safety nets

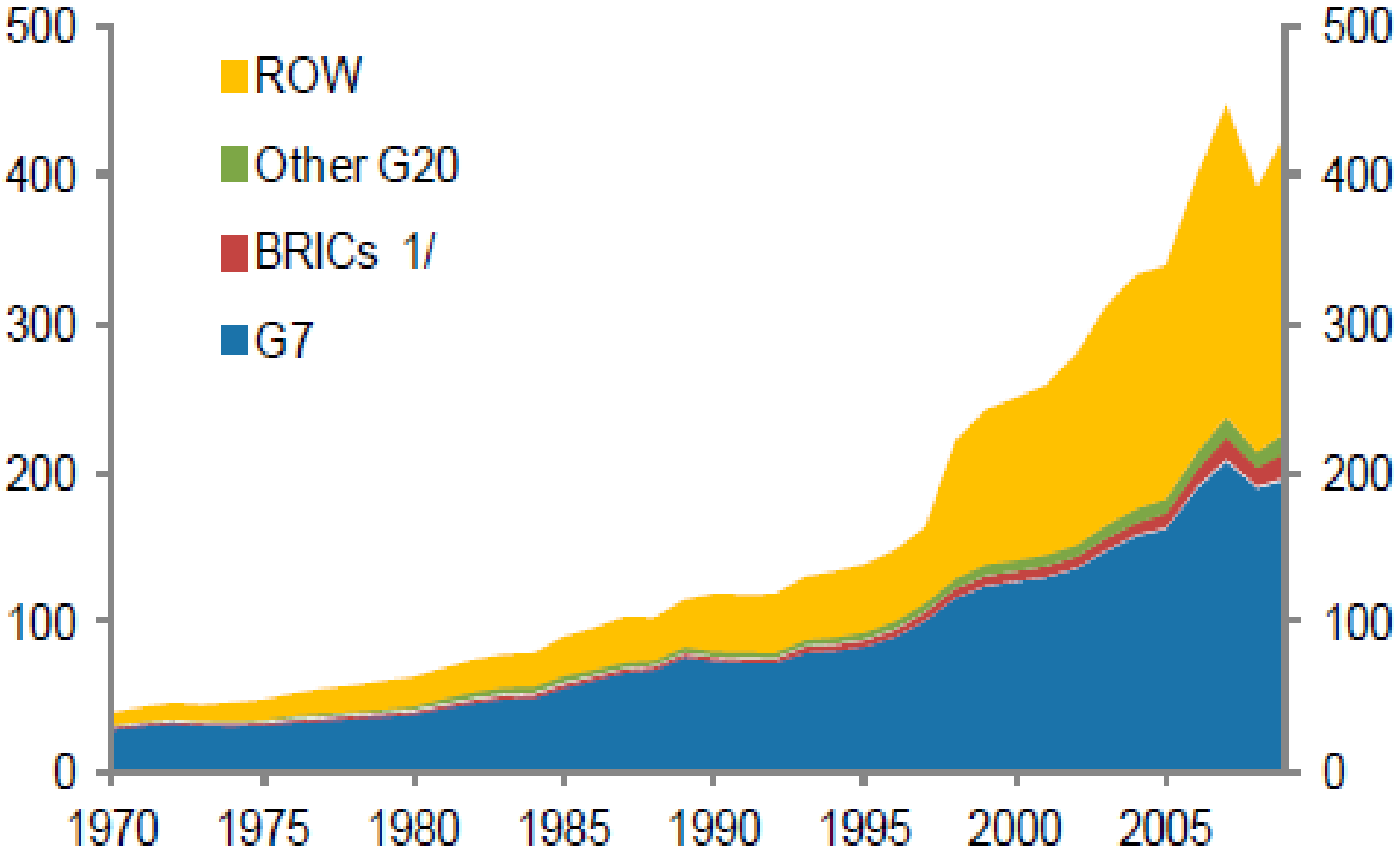
EMEs overhauled governance structures, adopted prudent policies and repaired balance sheets.

- Flexible exchange rate systems
- Prudent monetary, fiscal, financial, micro- and macro-prudential policies
  - ✓ Inflation targeting regimes
- Improved institutional quality
  - ✓ Granting independency to central banks
- Reserves accumulation
- Deepened financial markets

Favourable and unfavourable developments

- Globalization
  - ✓ Significant trade flows
    - Supply chain in production
  - ✓ Strong FDI flows
  - ✓ Declined home bias in asset allocation
- Lowered “original sin”
- Lowered asset dollarization
- But increased liability dollarization
- Unconventional monetary policies of DM CBs
  - ✓ Excessive global liquidity

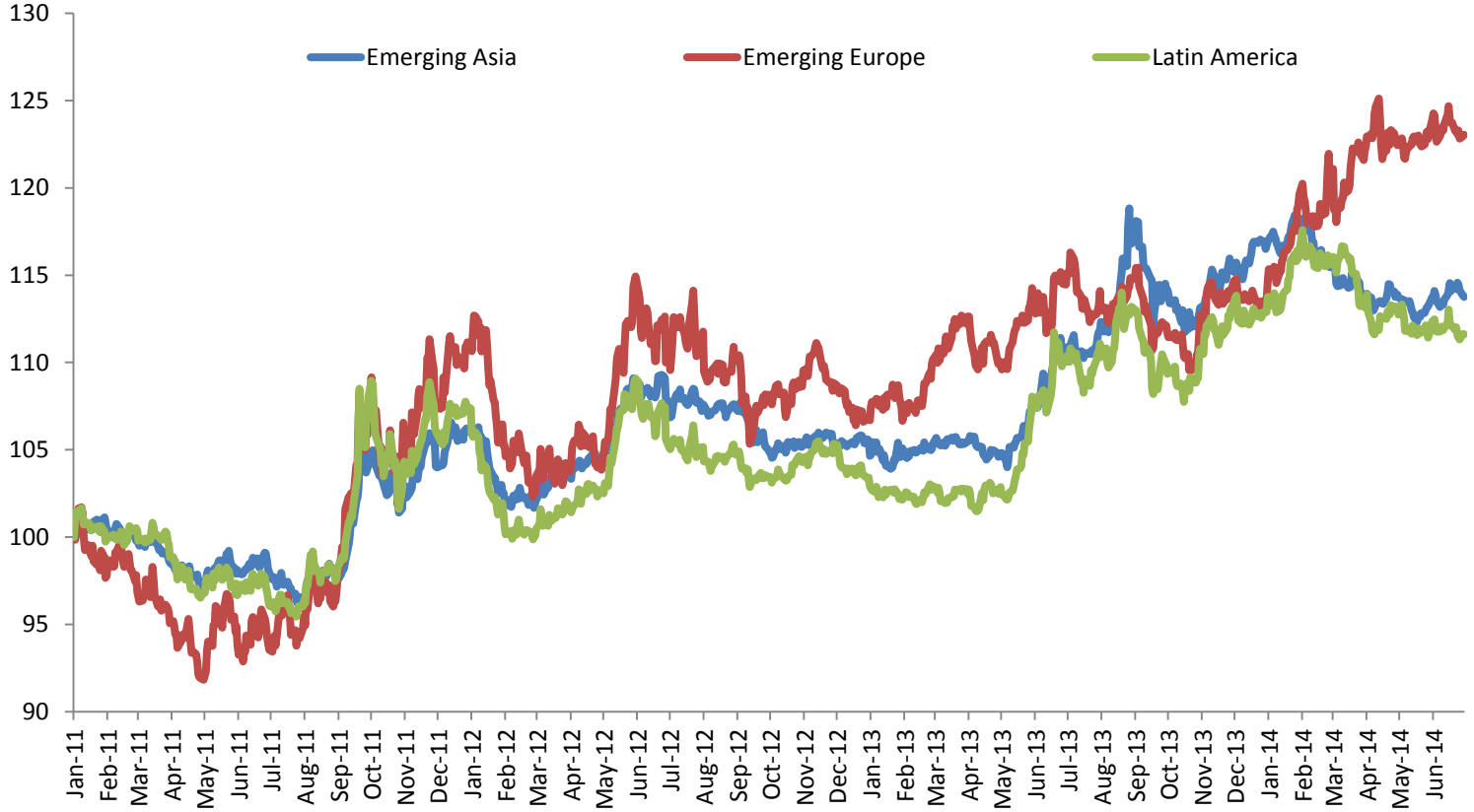
Great External Balances



UMP in DMEs have led to appreciated EM countries.

EM Nominal Exchange Rates

(Against USD, 3 January 2011=100)



Source: Bloomberg

Last Observation: 1 July 2014

Emerging Asia: Thailand, Indonesia, India, S. Korea, Malaysia

Emerging Europe: Czech Rep., Poland, Hungary, Russia, Ukraine, Turkey, S. Africa

Latin America: Brazil, Mexico, Chile, Peru, Colombia

Recent Financial Crises and Turbulences (I).

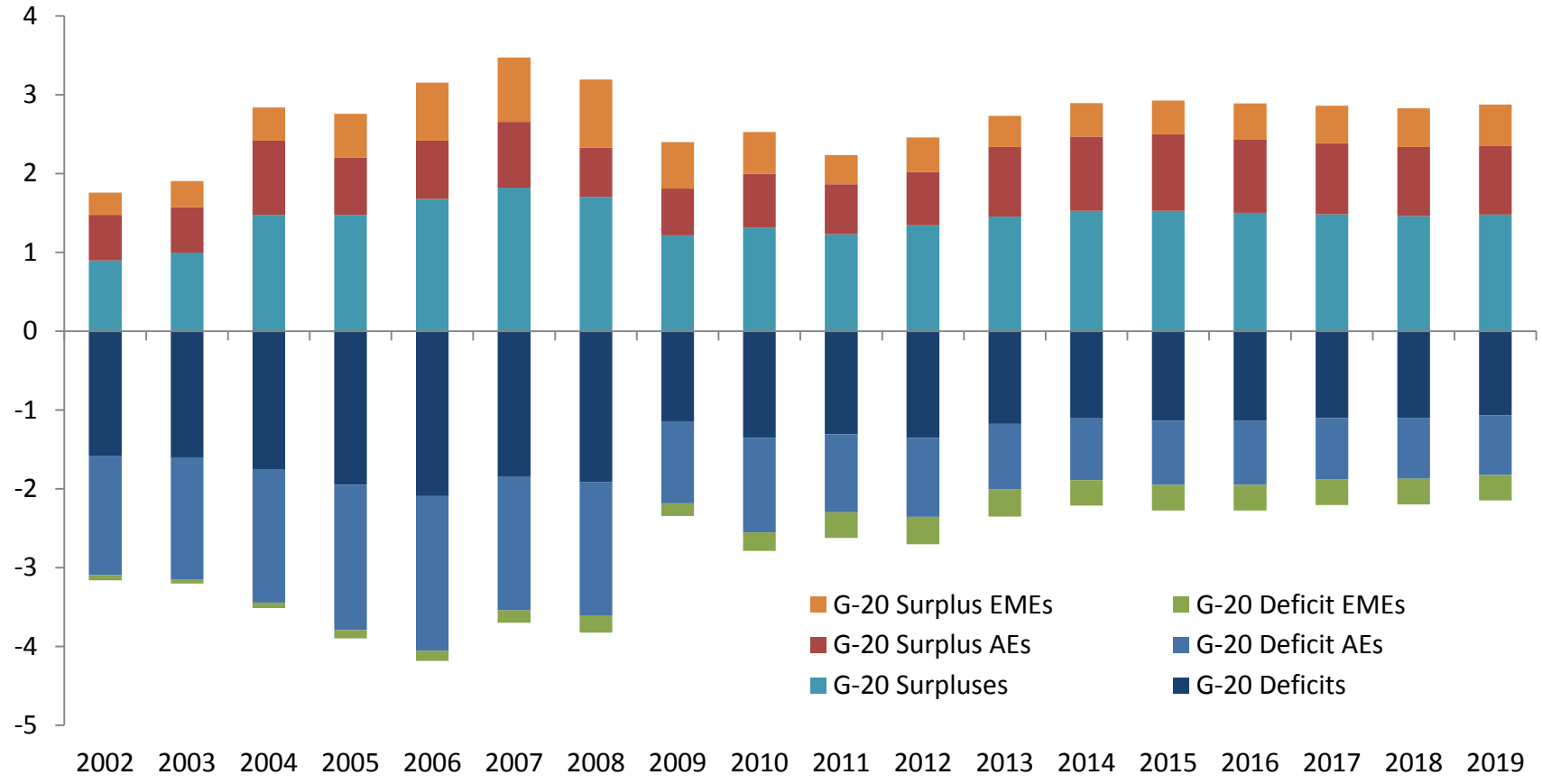
- The recent financial crises and turbulences
  - The global financial crisis of 2007-2008
  - The Eurozone sovereign bond crisis of 2011
  - The Fed's tapering of large scale asset purchases of 2013-2014
- Worsened financial conditions for EMEs
  - ✓ Depreciated currencies
  - ✓ Widened sovereign spreads
  - ✓ Increased yields

Recent Financial Crises and Turbulences (II).

- Resilient EM economies and financial institutions
  - ✓ Fundamental problems in global economy
    - Depressed private investment
    - Weak productivity
    - Broken global trade – global growth link
  - ✓ Great rebalancing in favour of DMEs

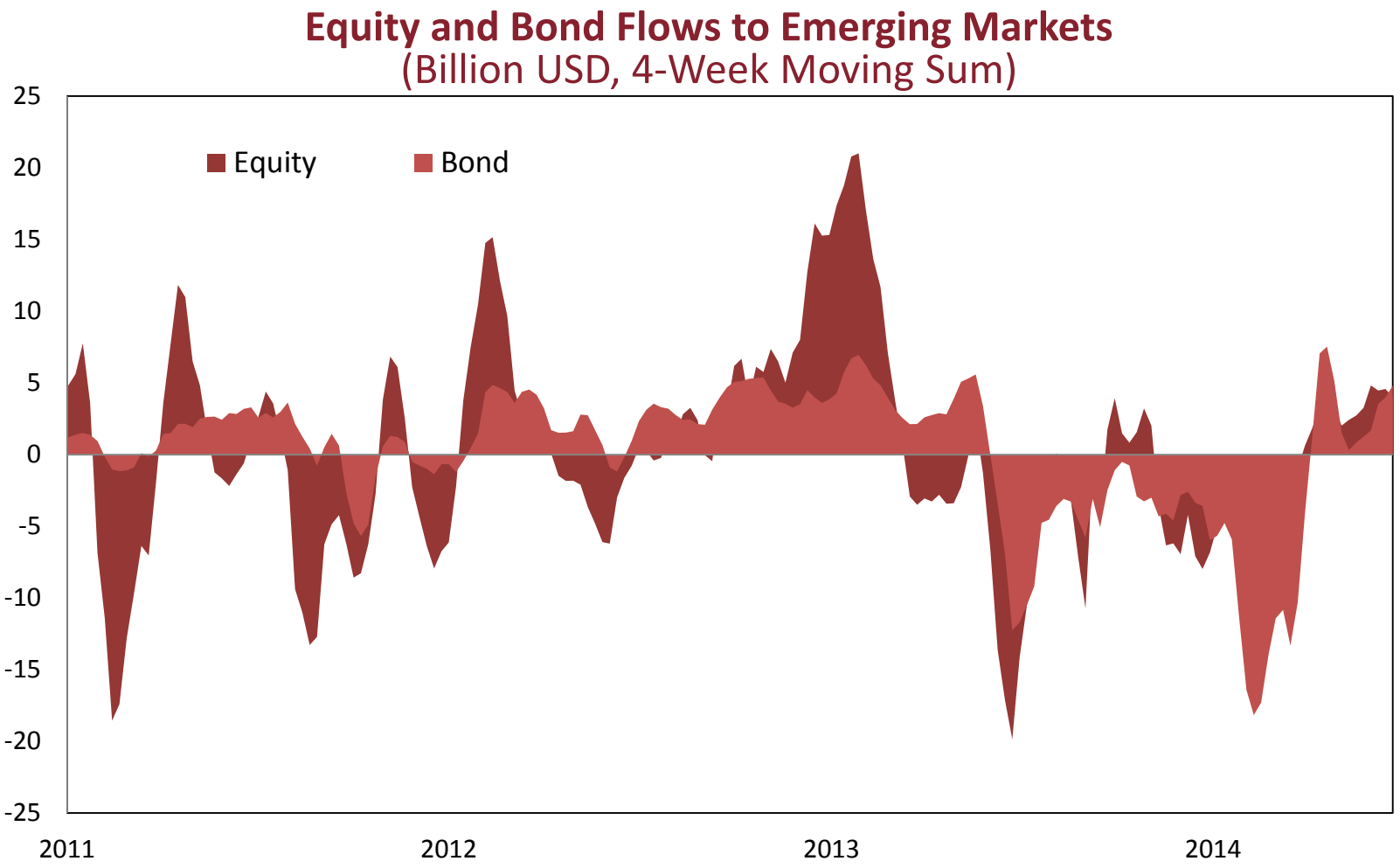
Great Rebalances

Current Account Balances (% World GDP)



Source: IMF WEO April 2014 Database

Volatile Capital Flows

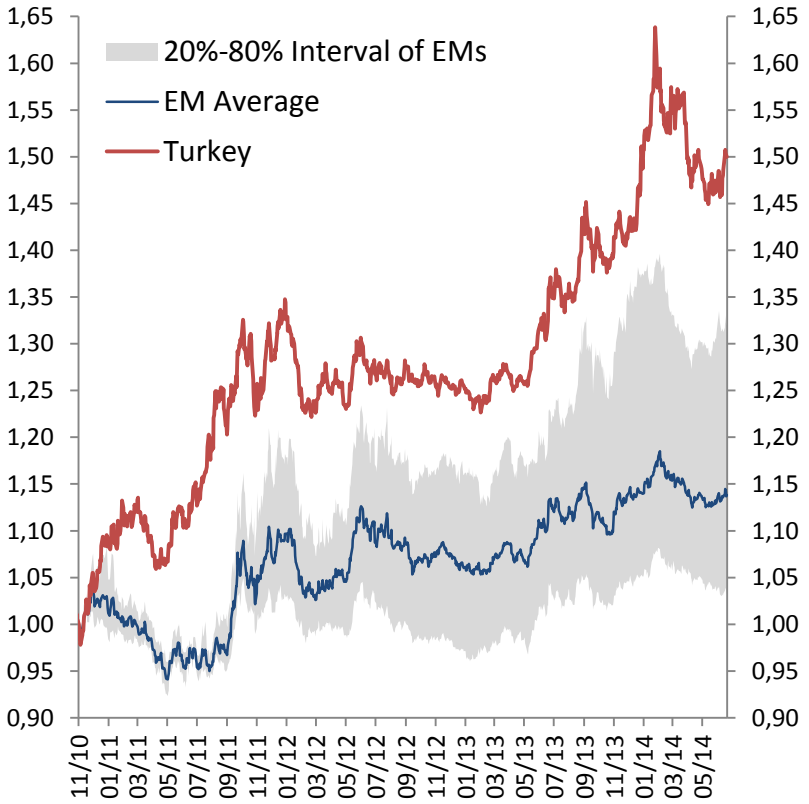


Source: EPFR.

Last Observation: June 25, 2014

Both nominal and real exchange rates have appreciated in recent months.

TL and Other Emerging Market Currencies vs USD (01.11.2010=1)

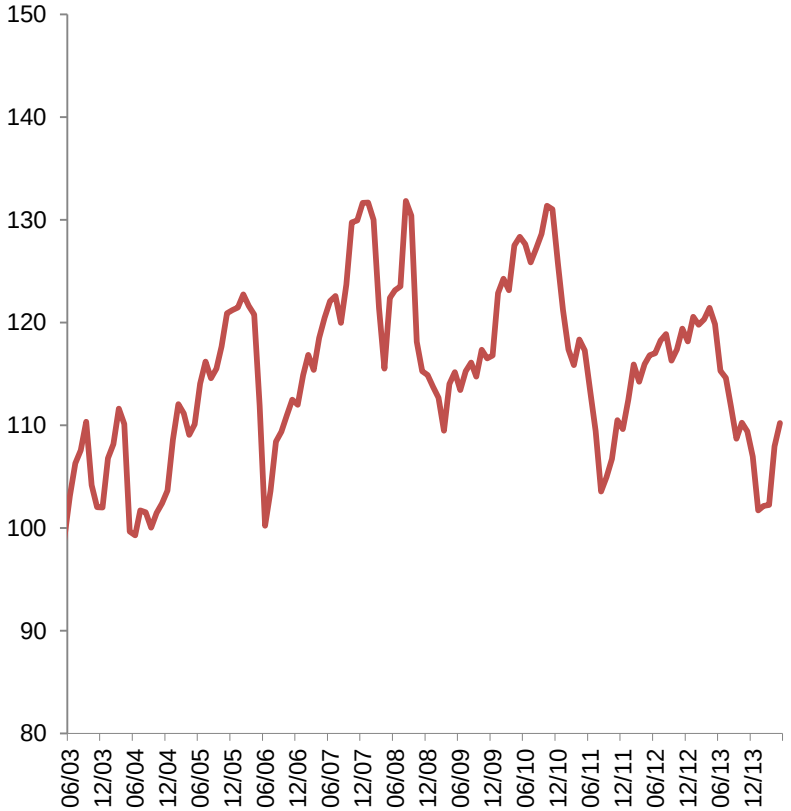


Source: Bloomberg.

Last Observation: June 20, 2014.

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

Real Effective Exchange Rates (2003=100)

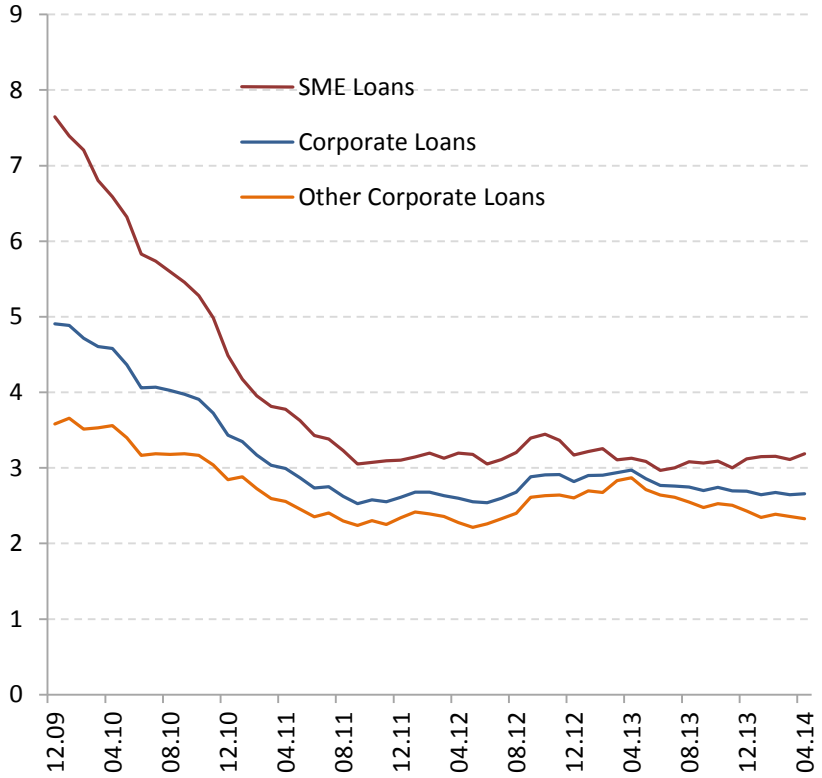


Source: CBRT.

Last Observation: May 2014.

High asset quality – Low non-performing loans (NPL).

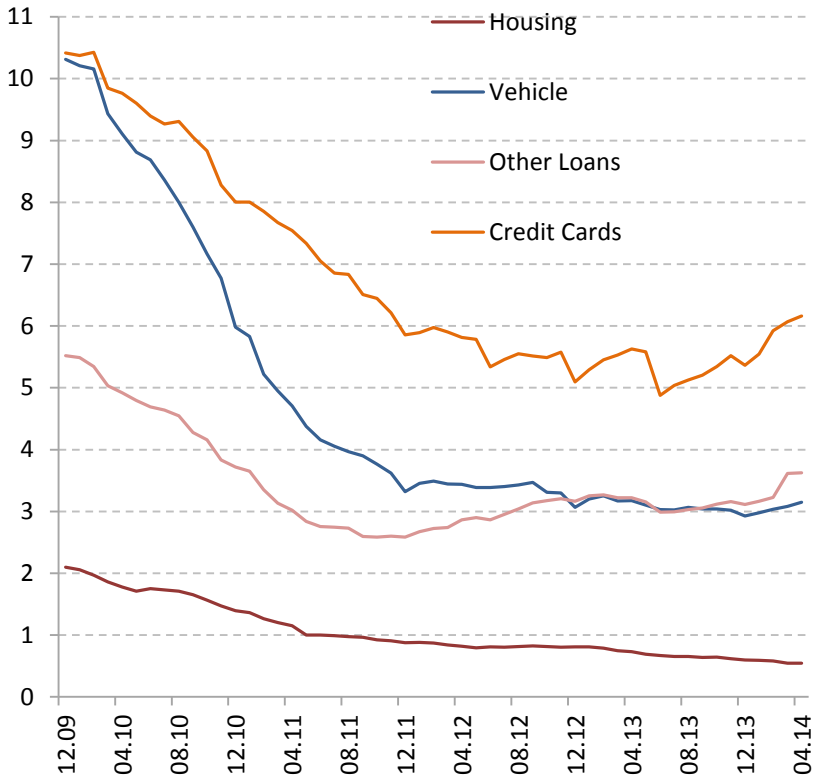
NPL Rates
(Stock data, %)



Source: CBRT.

Last Observation: April 2014

NPL Rates
(Stock data, %)



Source: CBRT.

Last Observation: April 2014

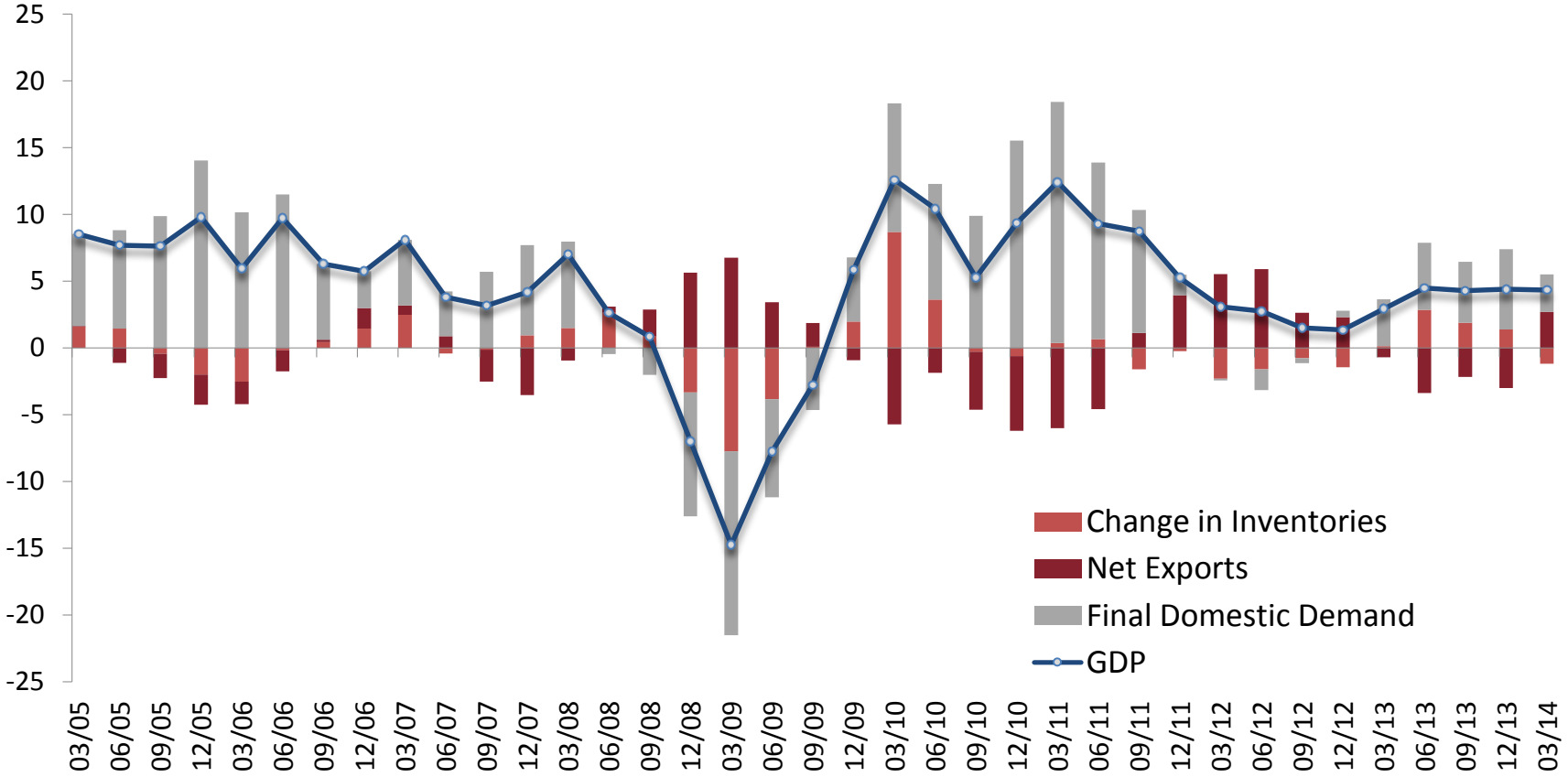
Inflation expectations have stabilized recently.

Source: CBRT.

Last Observation: June 2014.

Economic activity continues to expand around 4% yearly.

Contribution to Annual GDP Growth
(Percentage Points)



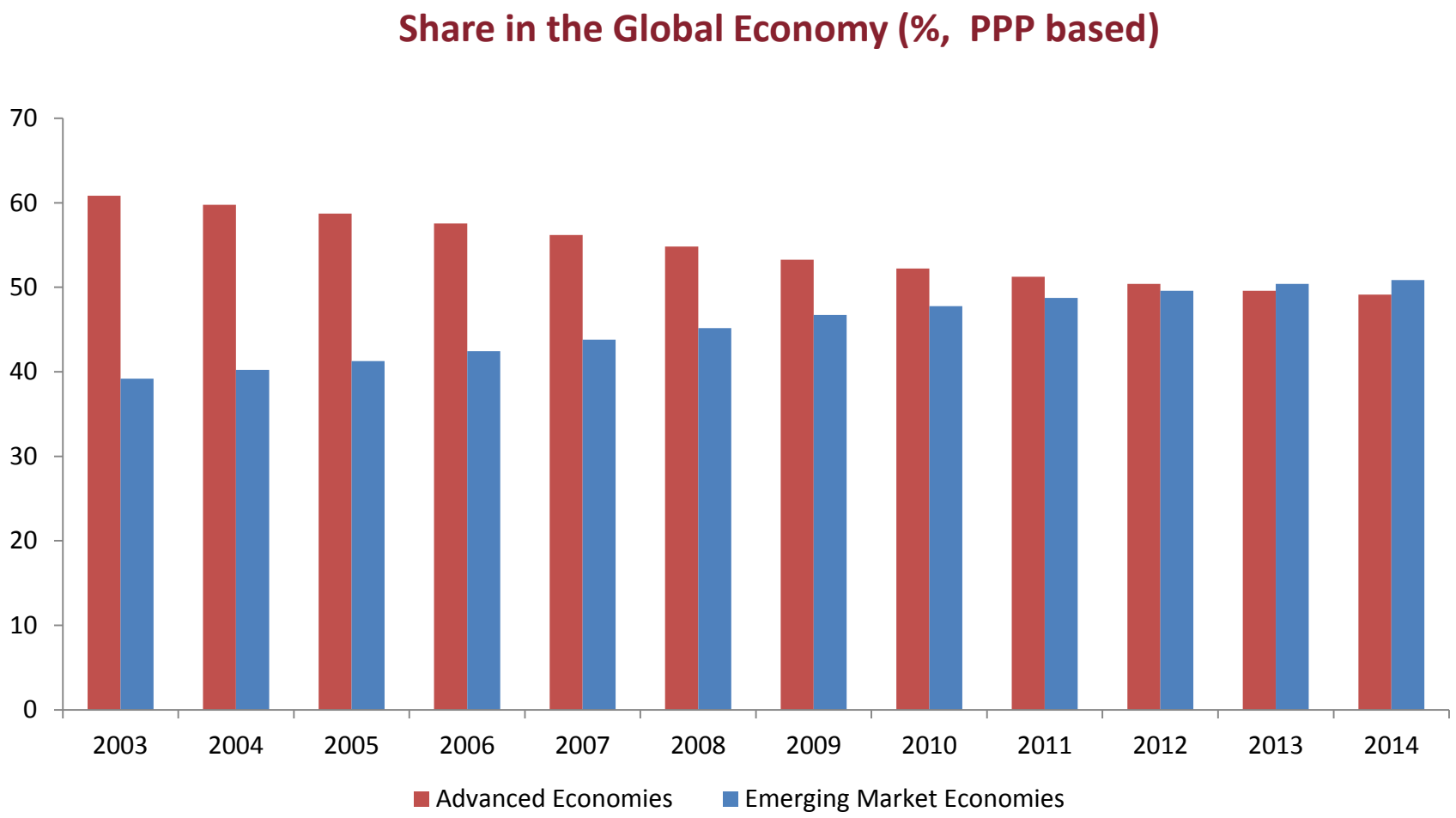
Source: TURKSTAT.

Last Observation: 2014Q1.

Further improvements are welcome though.

- Lower external funding requirements
- Lower inflation
- Deepened financial markets

Great change in the global economy



Source: IMF WEO April 2014 Database
Last Observation: 2014

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