



CENTRAL BANK OF TURKEY

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November 30, 2009



Holistic Approach to Economic Stability

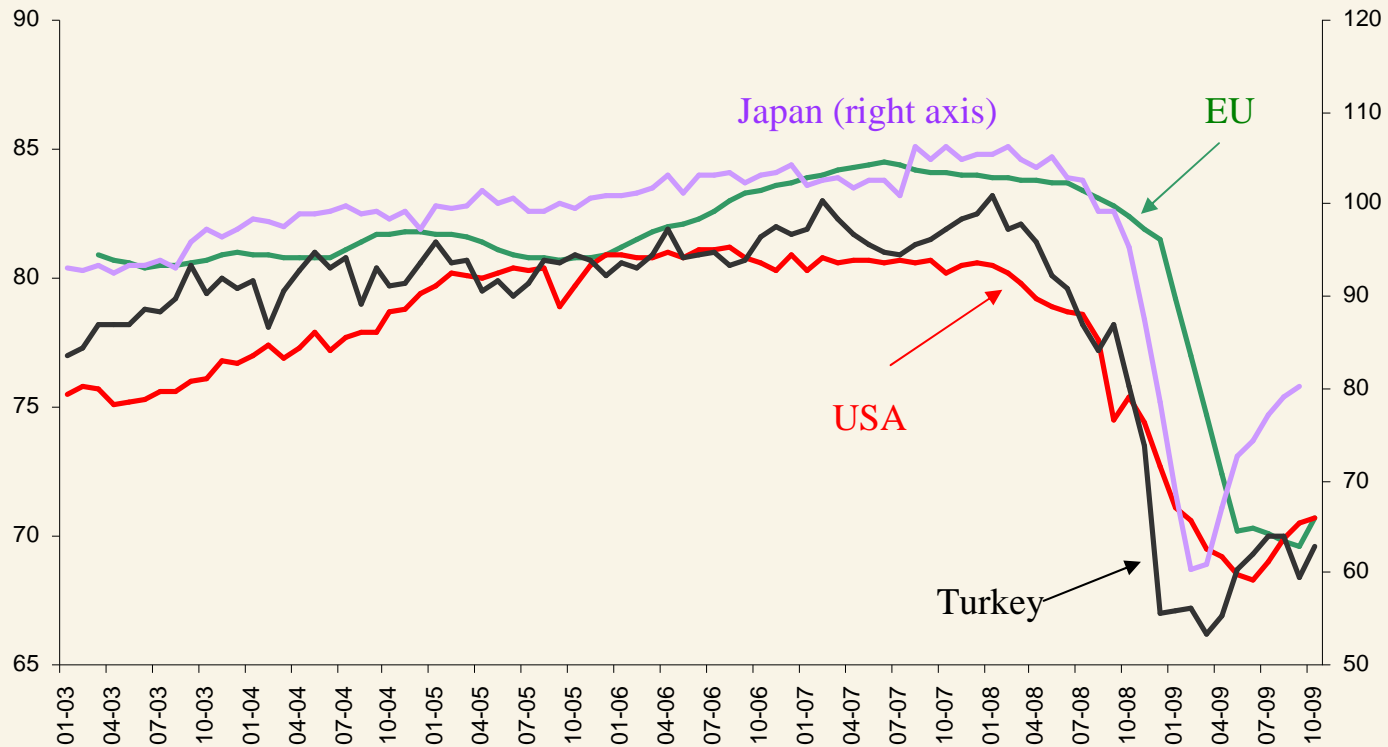
- I. Price Stability**
- II. Financial Stability**
- III. Sustainable Growth**



Current Situation - 1

Industrial Capacity Utilization

(Jan 2003 – Oct 2009, SA, percent)



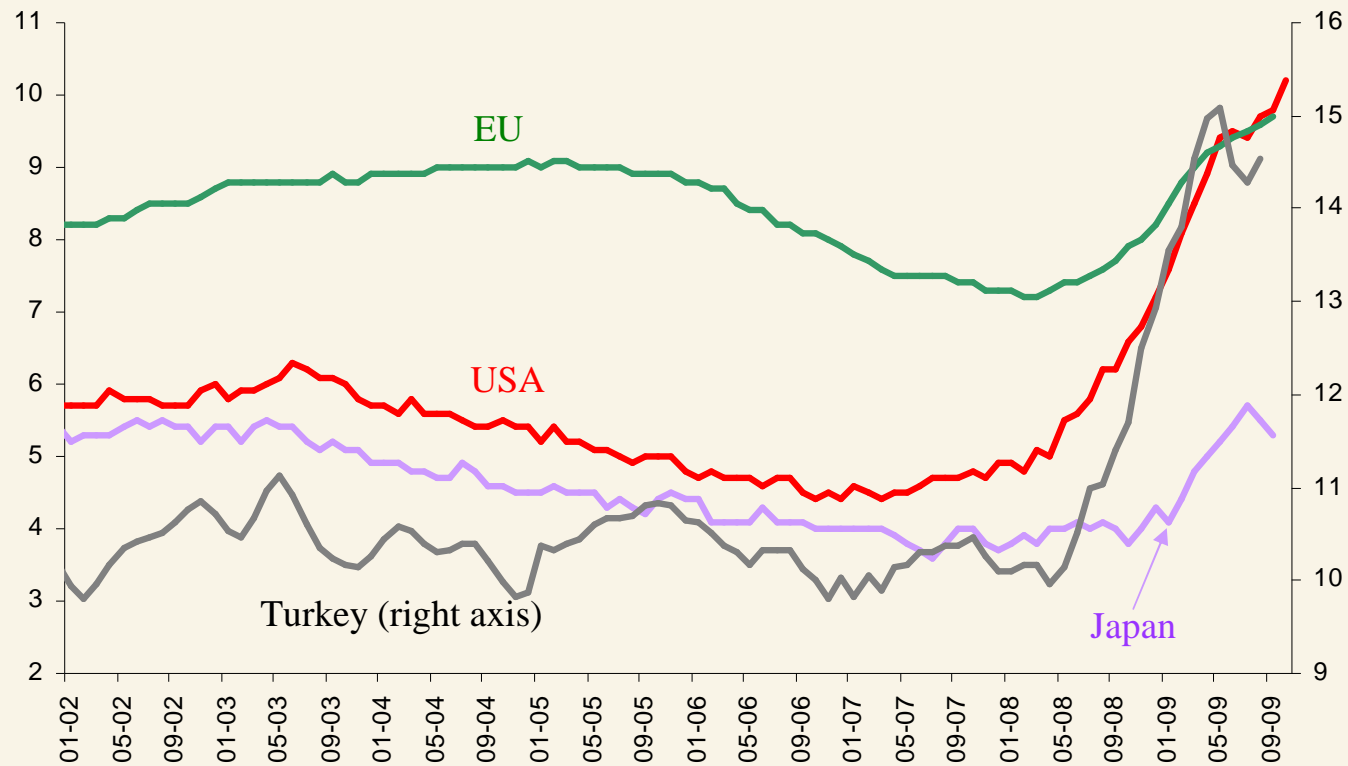
Source: Bloomberg, TURKSTAT, CBT



Current Situation - 2

Unemployment Rates

(Jan 2002 – Oct 2009, SA, percent)

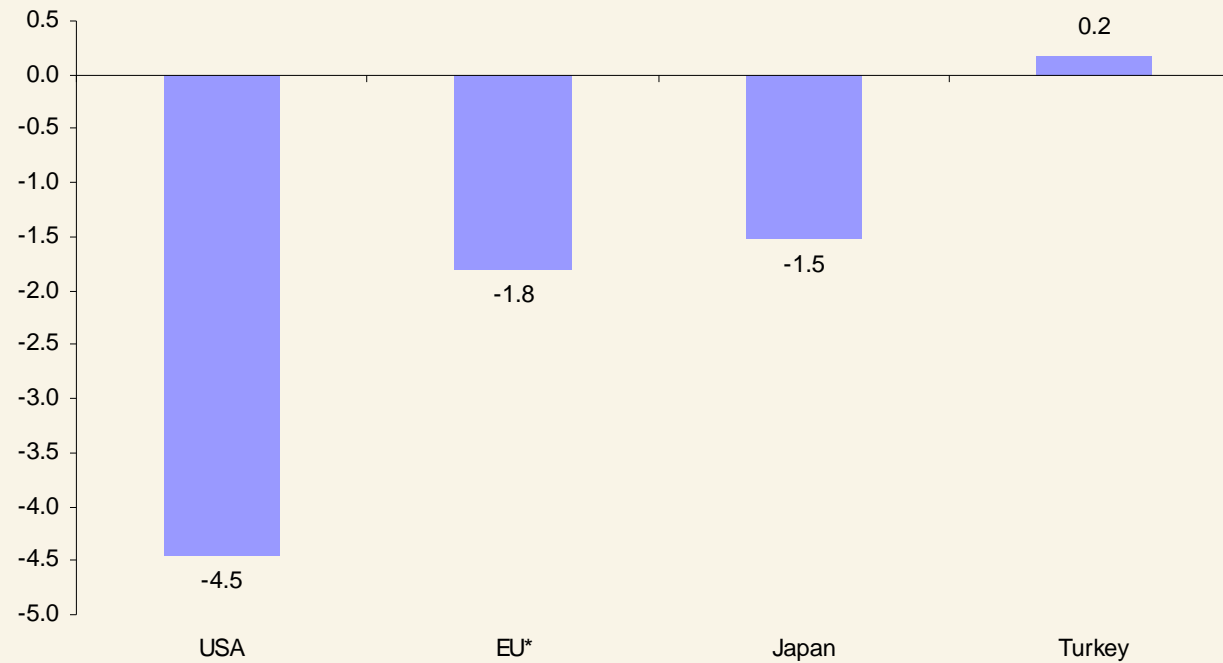


Source: Bloomberg, CBT



Current Situation - 3

Change in Employment
(Sep 2008 - Sep 2009, percent)



Source: Bloomberg, TURKSTAT, CBT

* Change between 2008 1.H and 2009 1.H



Analysis: Consumption Expenditure

- Permanent Income Hypothesis (Friedman 57, Hall 78):

$$y_p^e \downarrow \Rightarrow C \downarrow$$

- Borrowing Constraints and Wealth Effects (Carroll 92, 97; Deaton 91)

$$W_t \downarrow \Rightarrow C \downarrow$$

- Precautionary Saving Hypothesis (Carroll et al 99)

$$u \uparrow \Rightarrow C \downarrow$$

- Counter-cyclical Monetary Policy:

$$r \downarrow \Rightarrow y_p^e \uparrow \quad W \uparrow \quad u \downarrow$$

y_p^e : Expected Income u : Unemployment
 C : Consumption r : Nominal interest rate
 W : Wealth



Analysis: Labor Demand

$$(1+r)\frac{w}{p} = F_L(\bar{K}, L)$$

r : Interest rate

F_L : Marginal productivity of Labor

w : Nominal wages

L : Labor

p : Nominal price level

K : Capital

- Fuerst (1992)



Causes of Deviation from Economic Stability

During booming periods, excessively loose

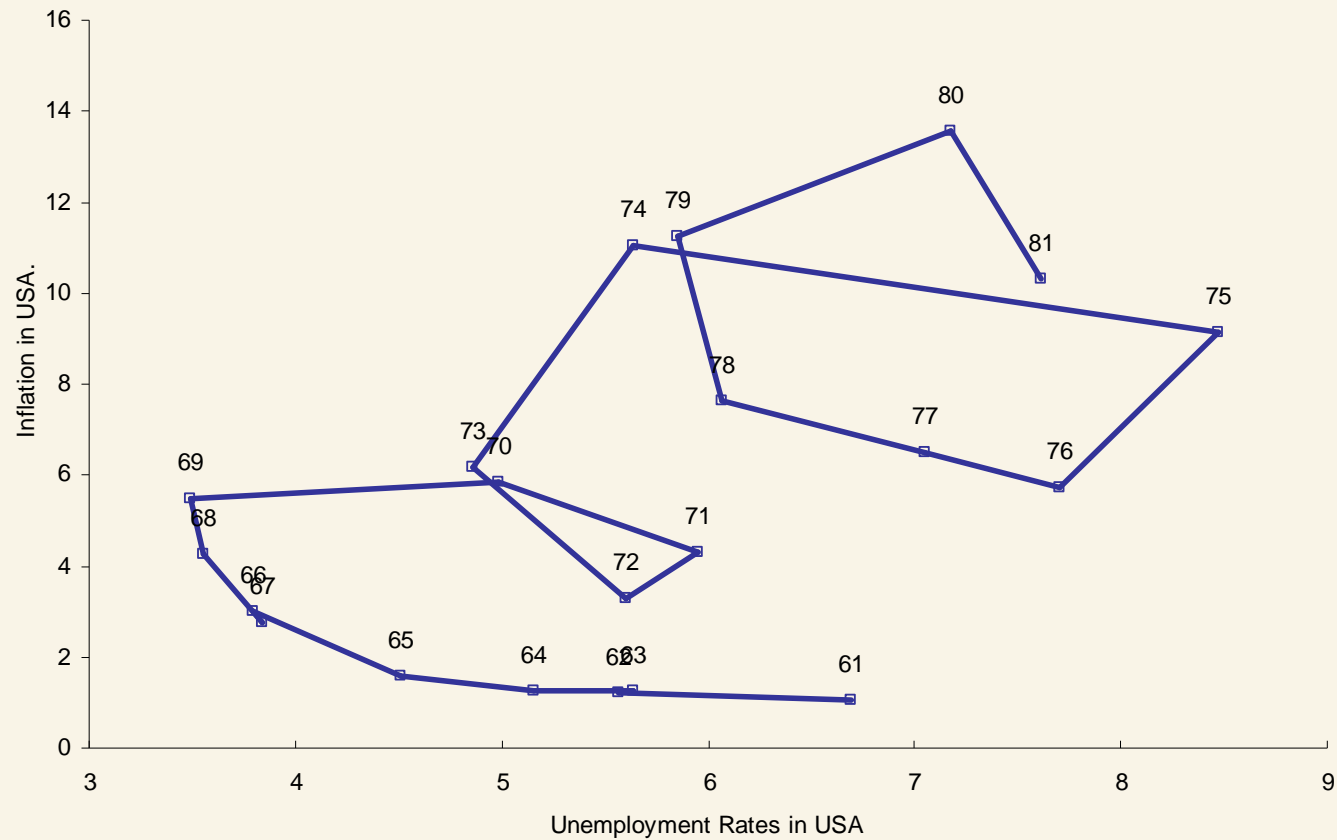
- ✓ **Monetary Policies**
- ✓ **Fiscal Policies**
- ✓ **Financial Sector Policies**



Deviation from Stability - I: Inflation

Excessively Loose Monetary Policy : USA during 1970s

Philips Curve in USA (1961-1981)



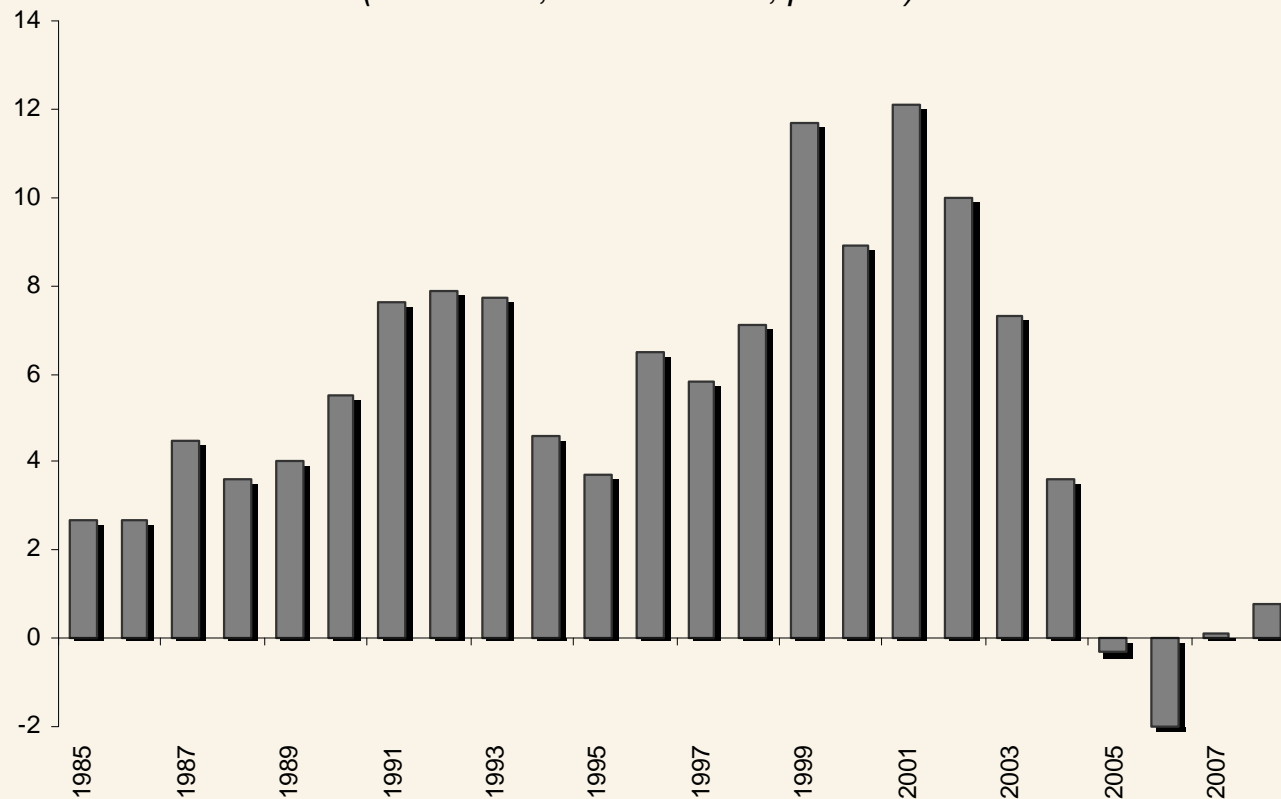
Source: FED, CBT



Deviation from Stability - II: Public Debt

Excessively Loose Fiscal Policy: Turkey during 1990s

Public Sector Borrowing Requirements
(1985-2008, ratio to GDP, percent)



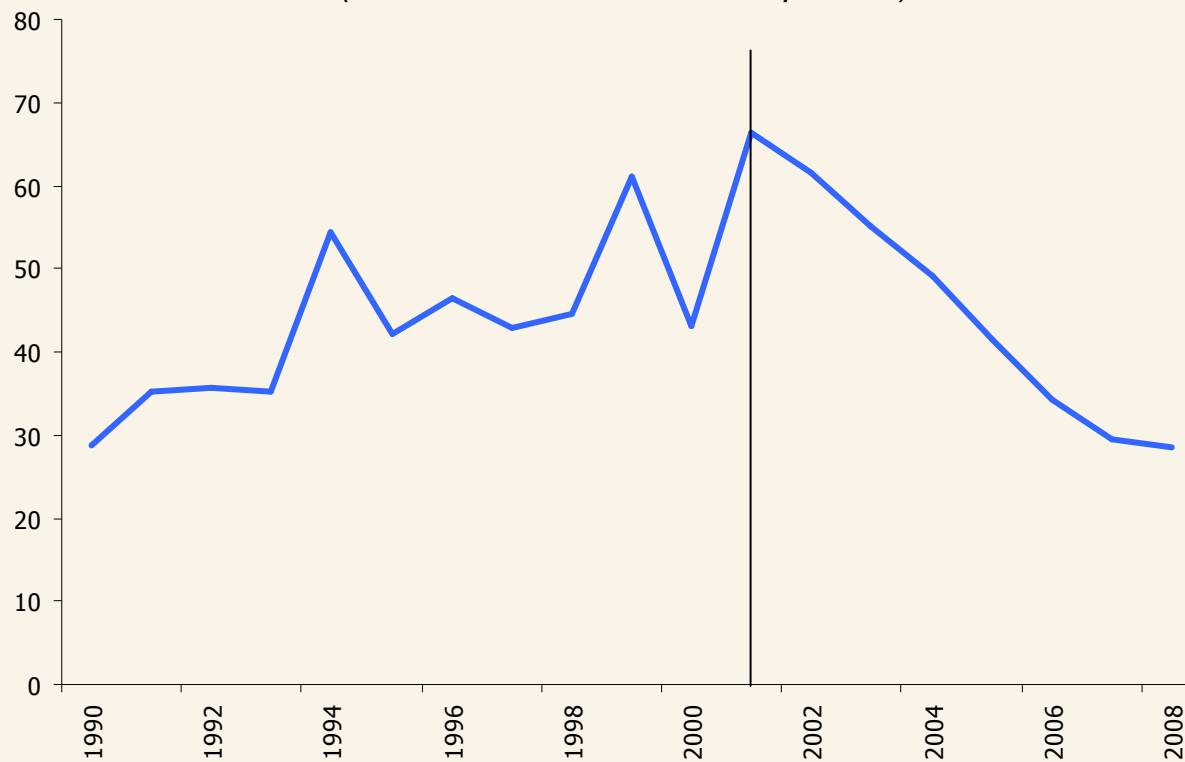
Source: Treasury, CBT



Deviation from Stability - II: Public Debt

Excessively Loose Fiscal Policy: Turkey during the 1990s

Net Debt of the Public Sector
(1990 – 2008, ratio to GDP, percent)



Source: Treasury, CBT

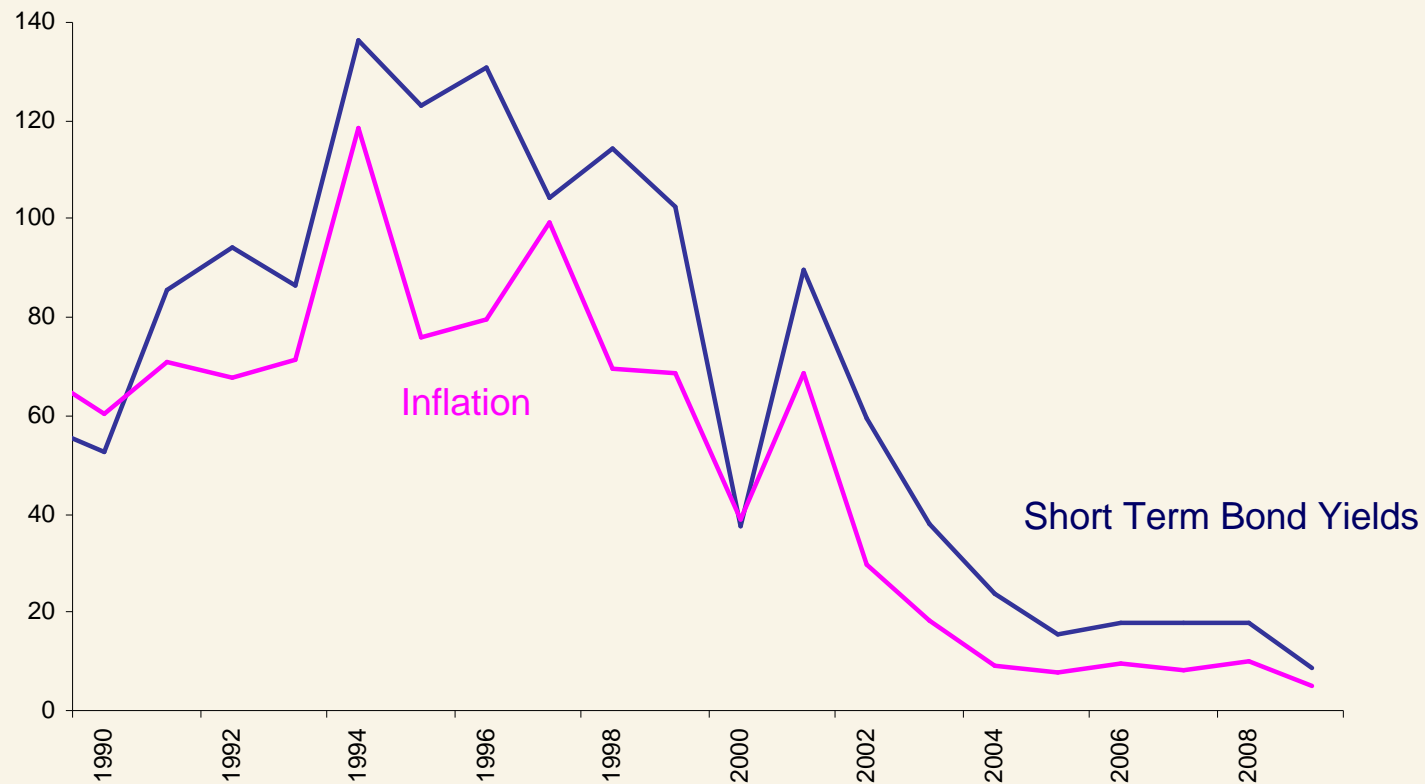


Deviation from Stability - II: Public Debt

Excessively Loose Fiscal Policy: Turkey during the 1990s

Inflation and Interest Rates in Turkey

(1990 – 2009*, compound, percentage)



Source: Treasury, CBT

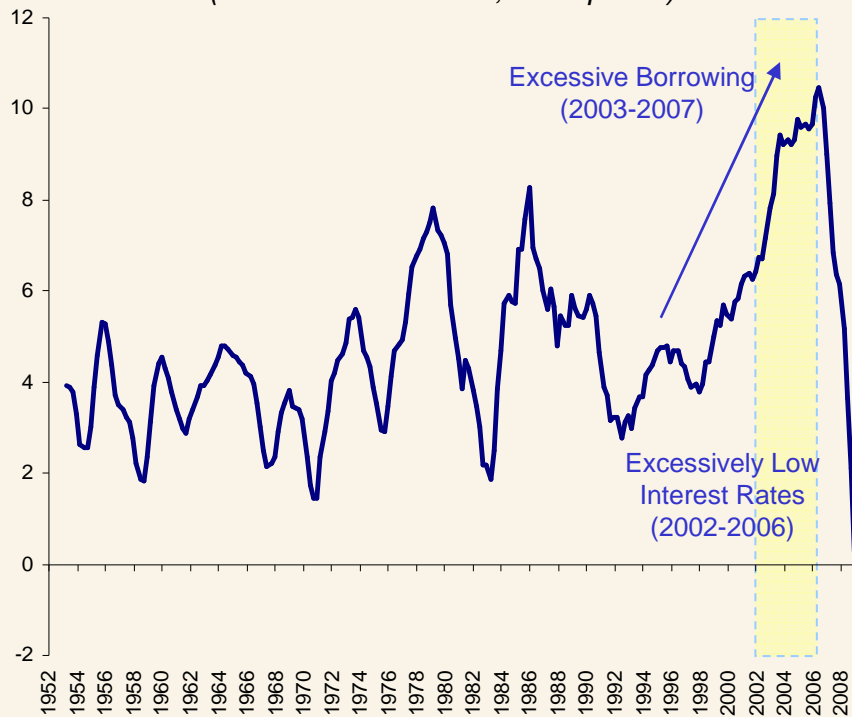
* As of October 2009



Deviation from Stability - III: Financial Sector Policies

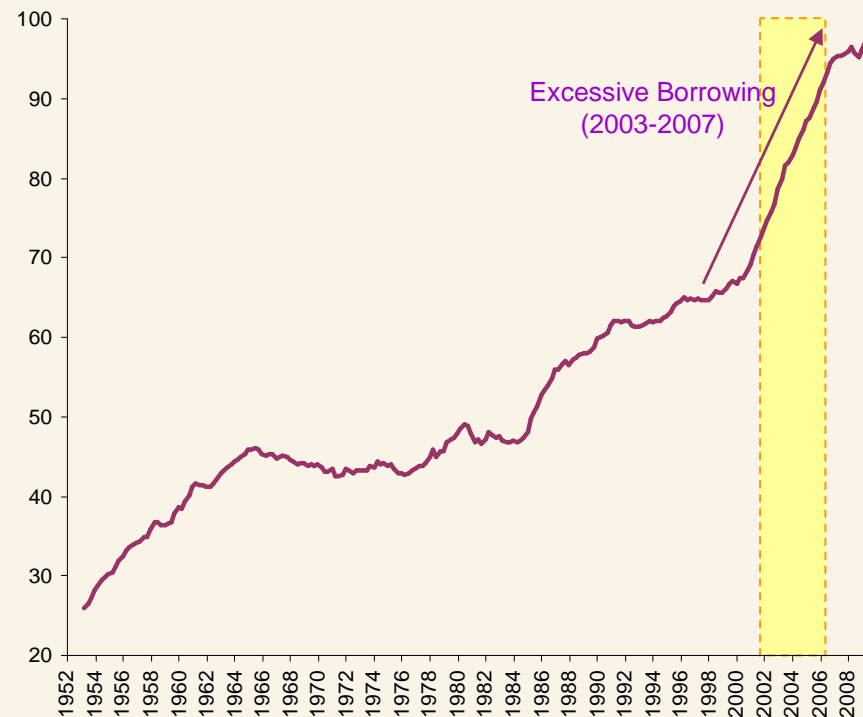
Excessively Loose Financial Sector Policies: USA during 2000s

The ratio of the annual change in US Household Indebtedness to GDP
(Mar 1952 – Jun 2009, basis points)



Source: Bloomberg, CBT

US Household Indebtedness Ratio
(Mar 1952 – Jun 2009, ratio to GDP)

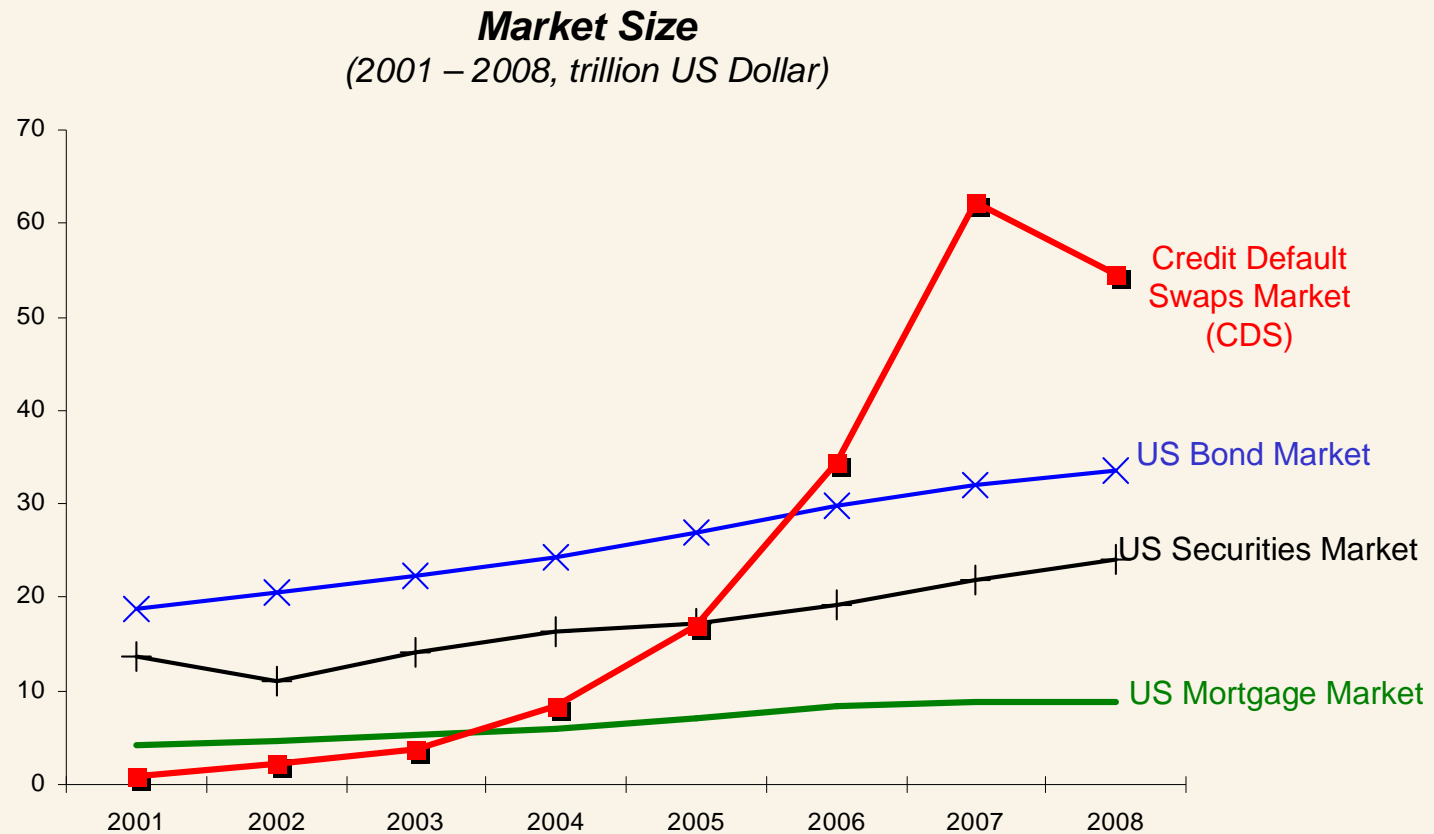


Source: Bloomberg, CBT



Deviation from Stability - III: Financial Sector Policies

Excessively Loose Financial Sector Policies: USA during 2000s



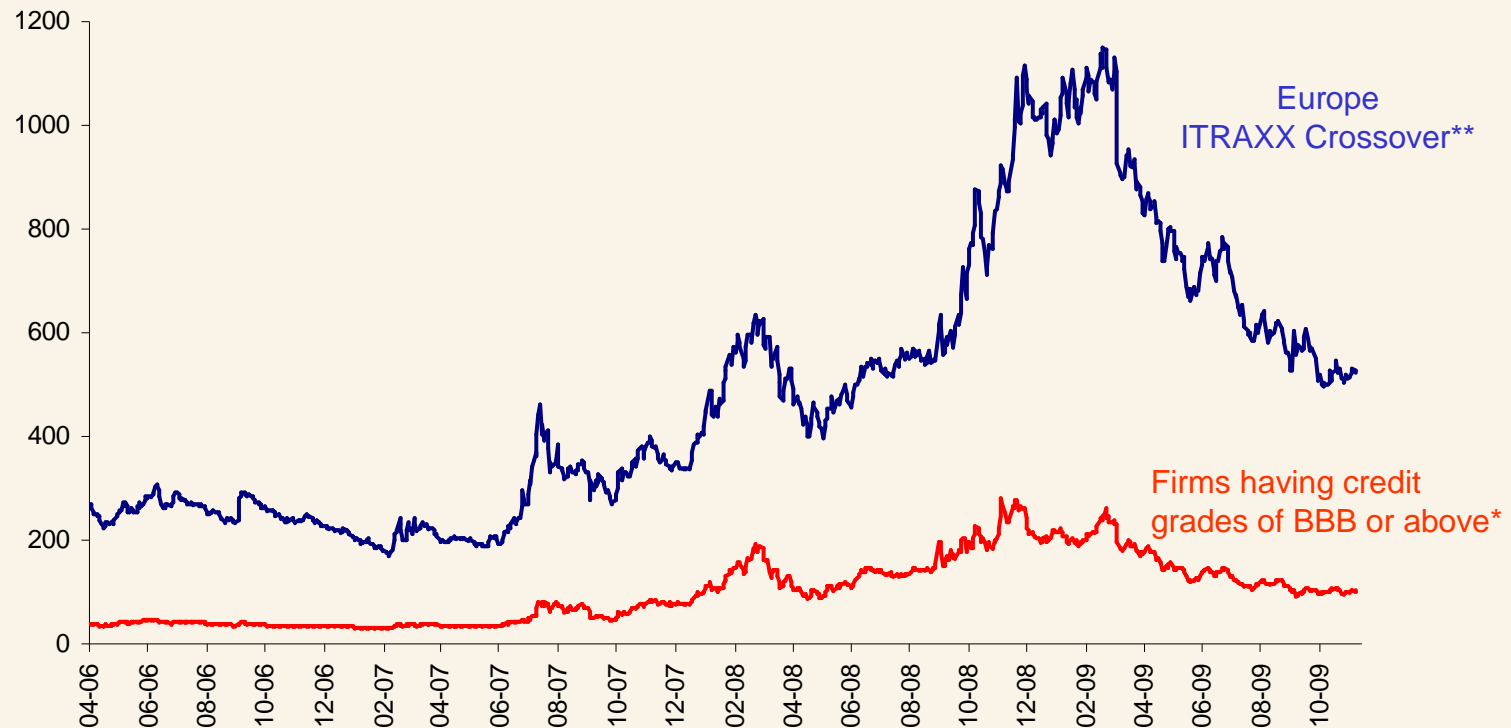
Source: ISDA, WFE, SIFMA



Deviation from Stability - III: Financial Sector Policies

Excessively loose financial sector policies ended up with the crisis

Credit Default Swap (CDS) Premiums
(Jan 2004 - Nov 2009, basis points)



* Firms with investment grade (BBB or above) in North America

** Index was derived from the CDS indexes of the most liquid assets in the European Markets

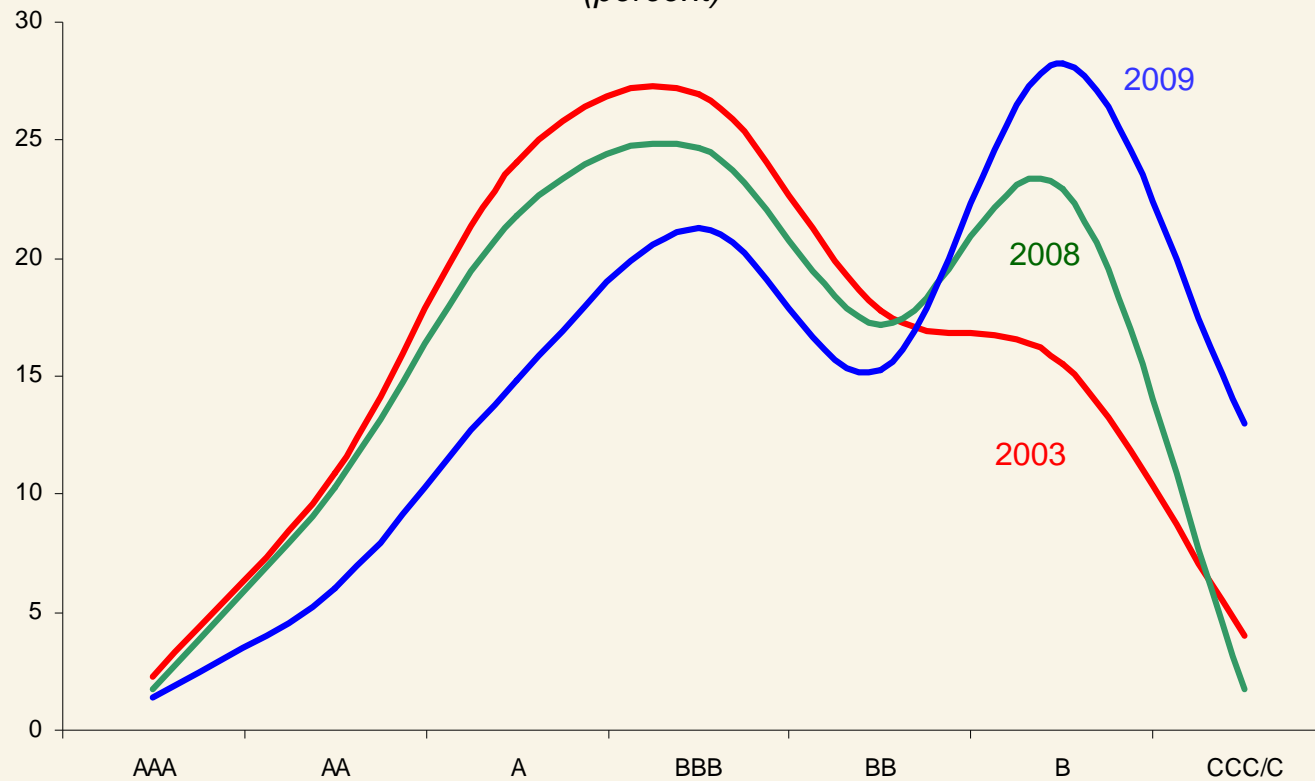
Source: JP Morgan, Bloomberg, CBT



Deviation from Stability - III: Financial Sector Policies

Excessively loose financial sector policies ended up with the crisis

Distribution of USA Firms by Credit Ratings
(percent)



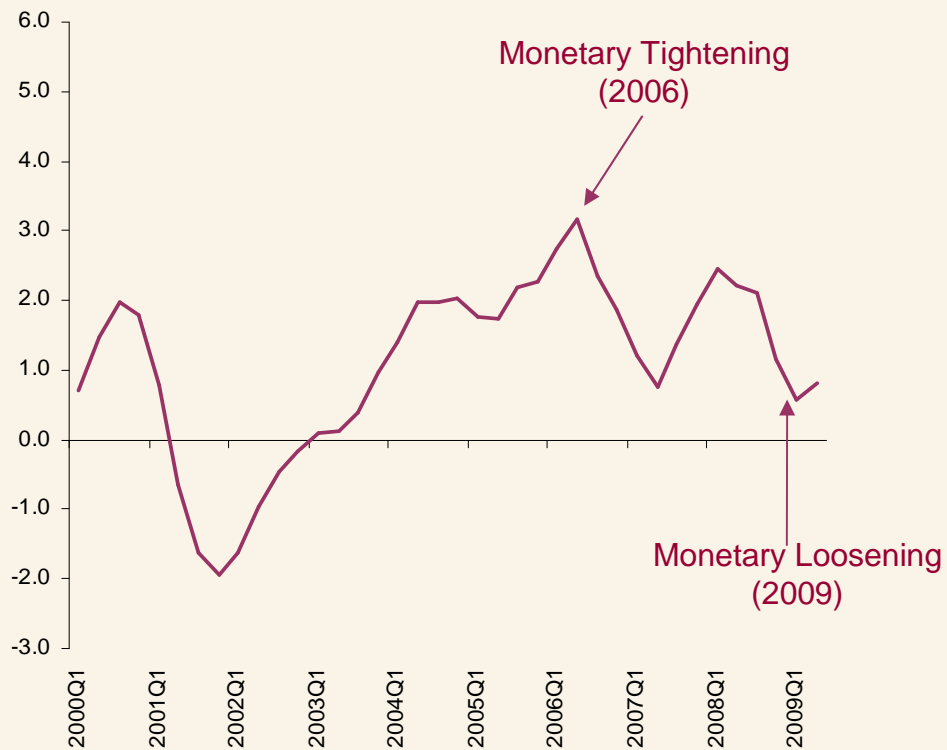
Source: Bloomberg, CBT



Countercyclical Monetary Policy in Turkey – I

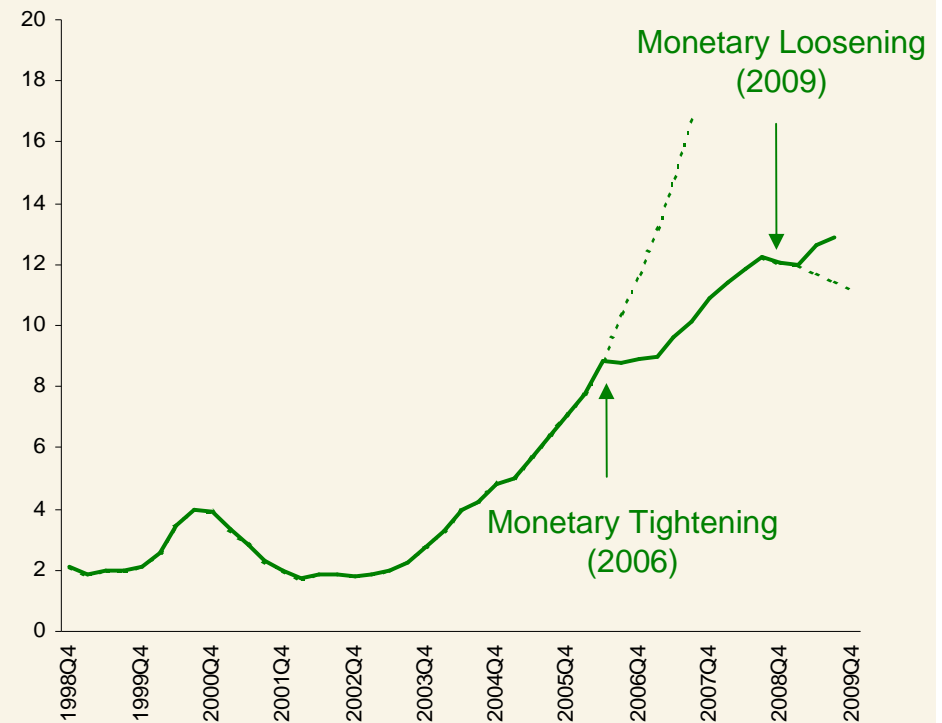
Household indebtedness in Turkey has increased moderately due to tight monetary and fiscal policies

The ratio of the annual change in Turkey Household Indebtedness to GDP
(2000 Q1 –2009 Q2 basis points)



Source: TURKSTAT, CBT

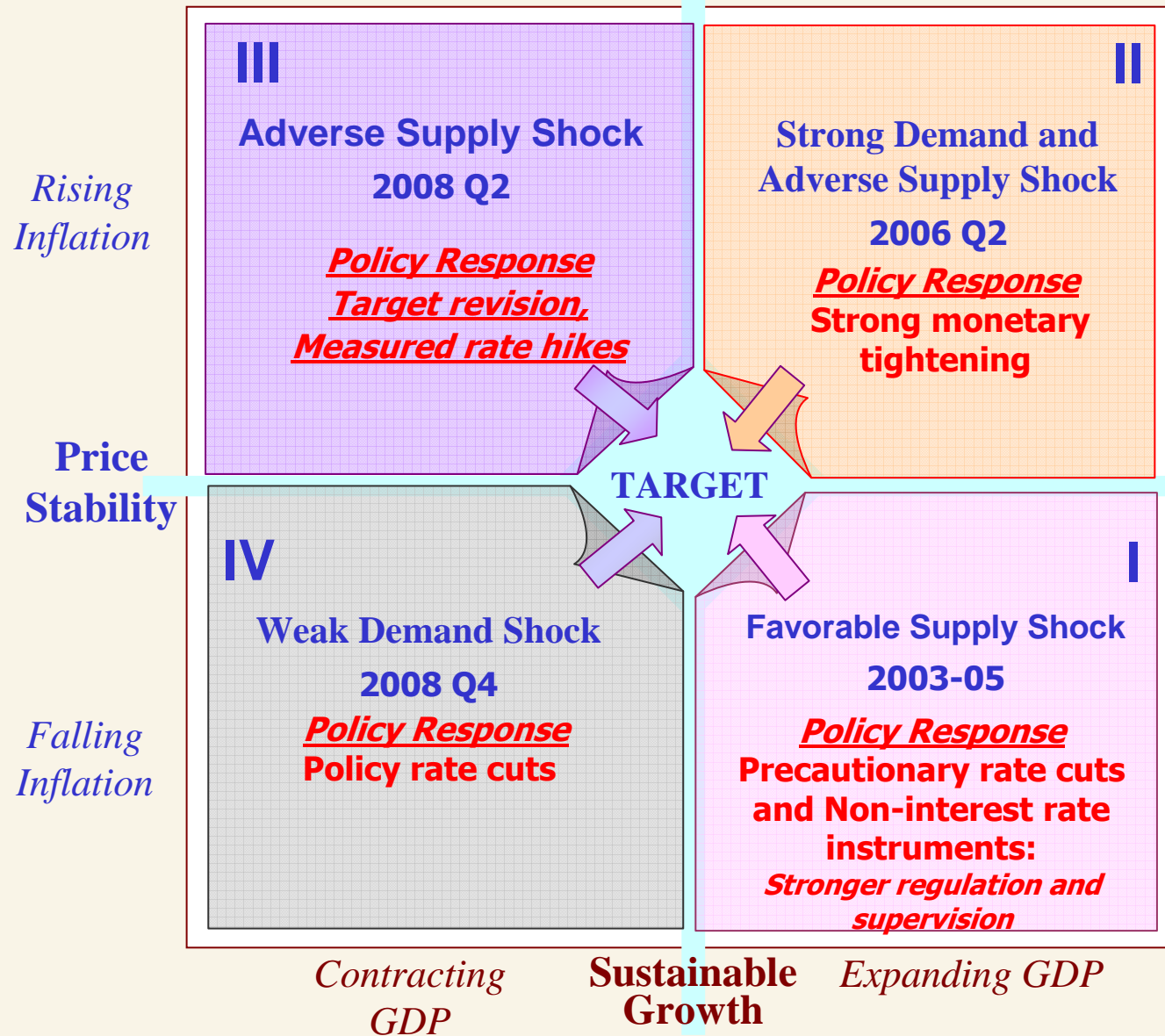
Household Indebtedness Ratio in Turkey
(1998 Q4 –2009 Q2, ratio to GDP)



Source: TURKSTAT, CBT



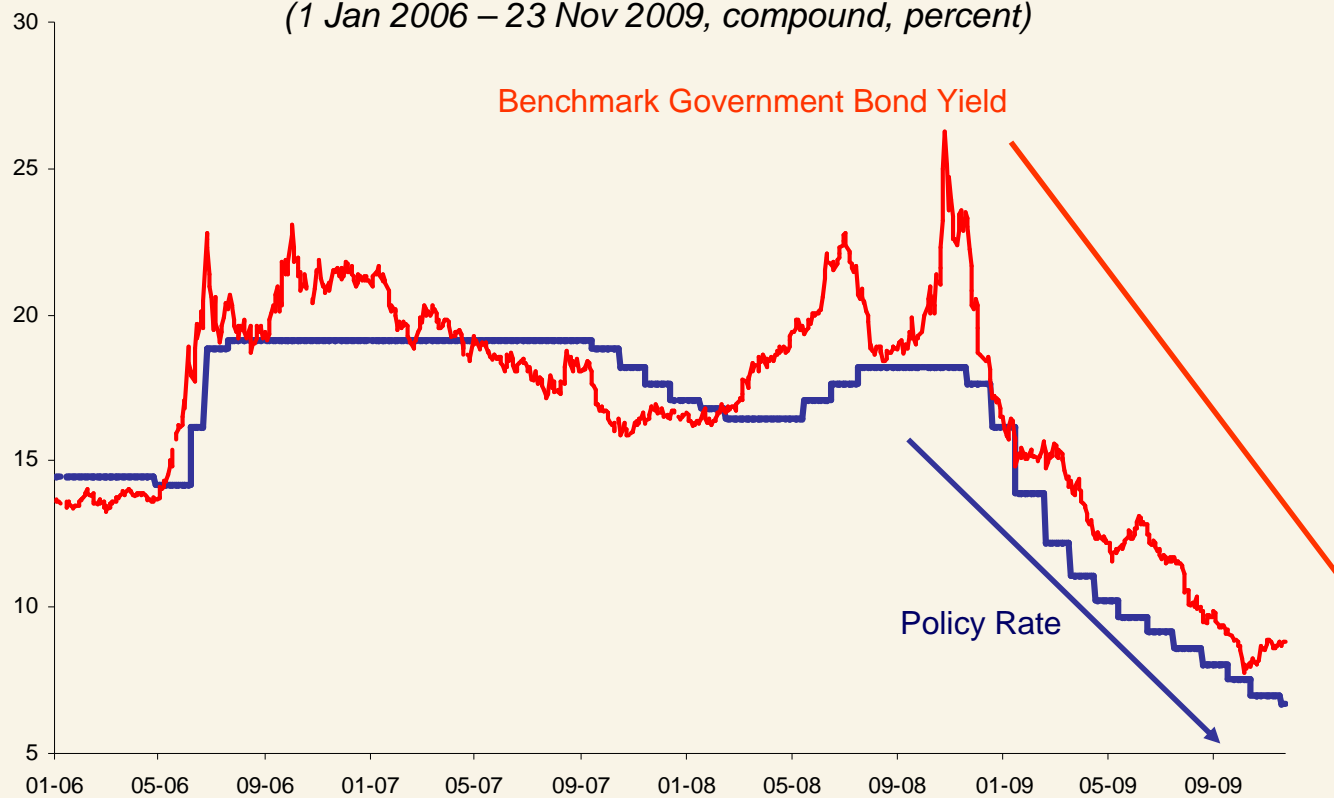
Countercyclical Monetary Policy in Turkey – II





Countercyclical Monetary Policy in Turkey - III

**CBT Policy Rate and
Benchmark Government Securities Interest Rate**
(1 Jan 2006 – 23 Nov 2009, compound, percent)



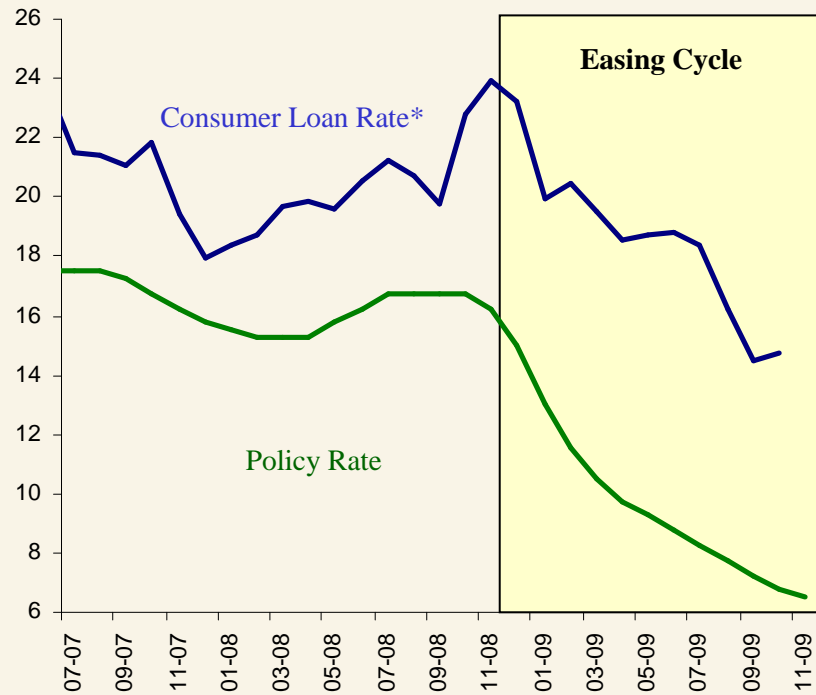
Source: BRSA, CBT



Countercyclical Monetary Policy in Turkey - IV

Interest Rates

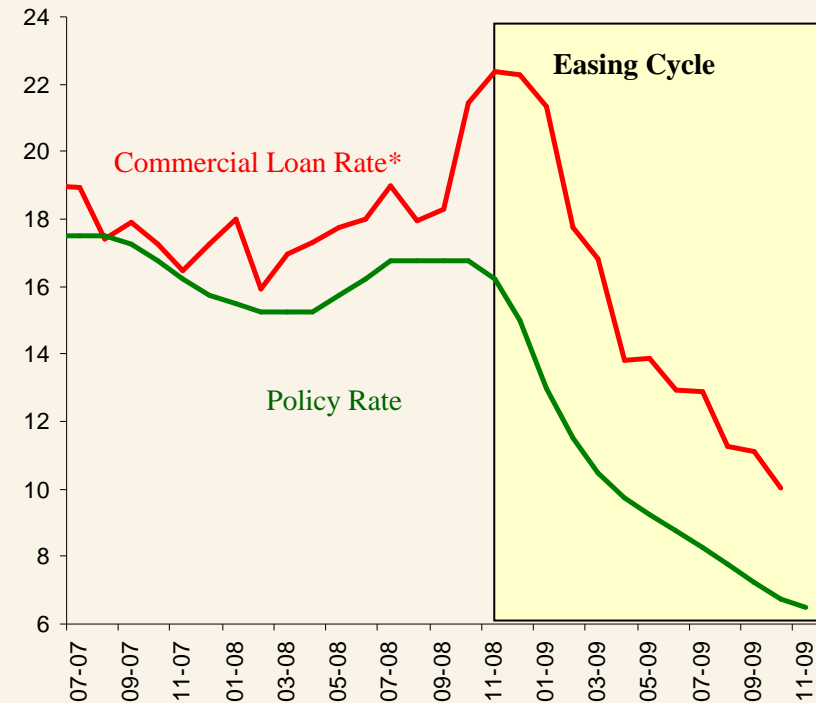
(Apr 2007 – Nov 2009, compound percent)



* Weighted Average, Flow
Source: CBT

Interest Rates

(Apr 2007 – Nov 2009, compound percent)

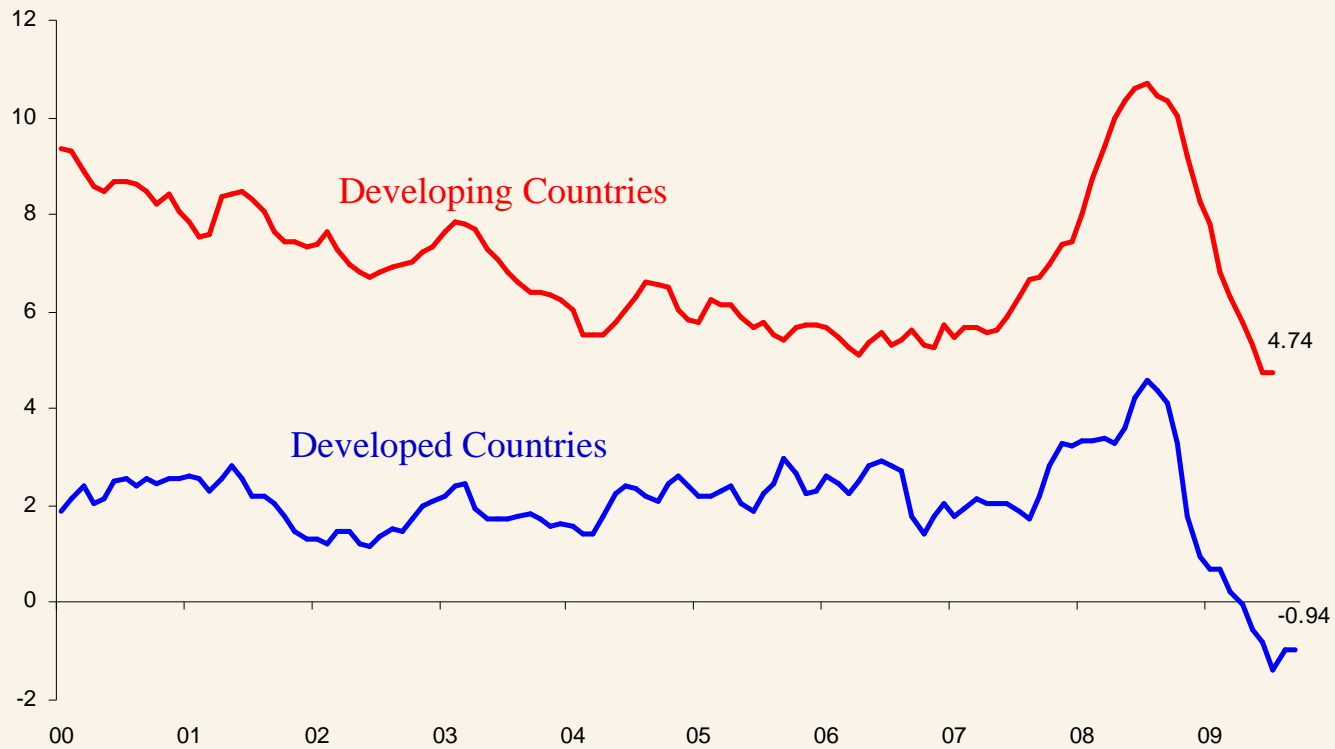


* Weighted Average, Flow
Source: CBT



Inflation Developments

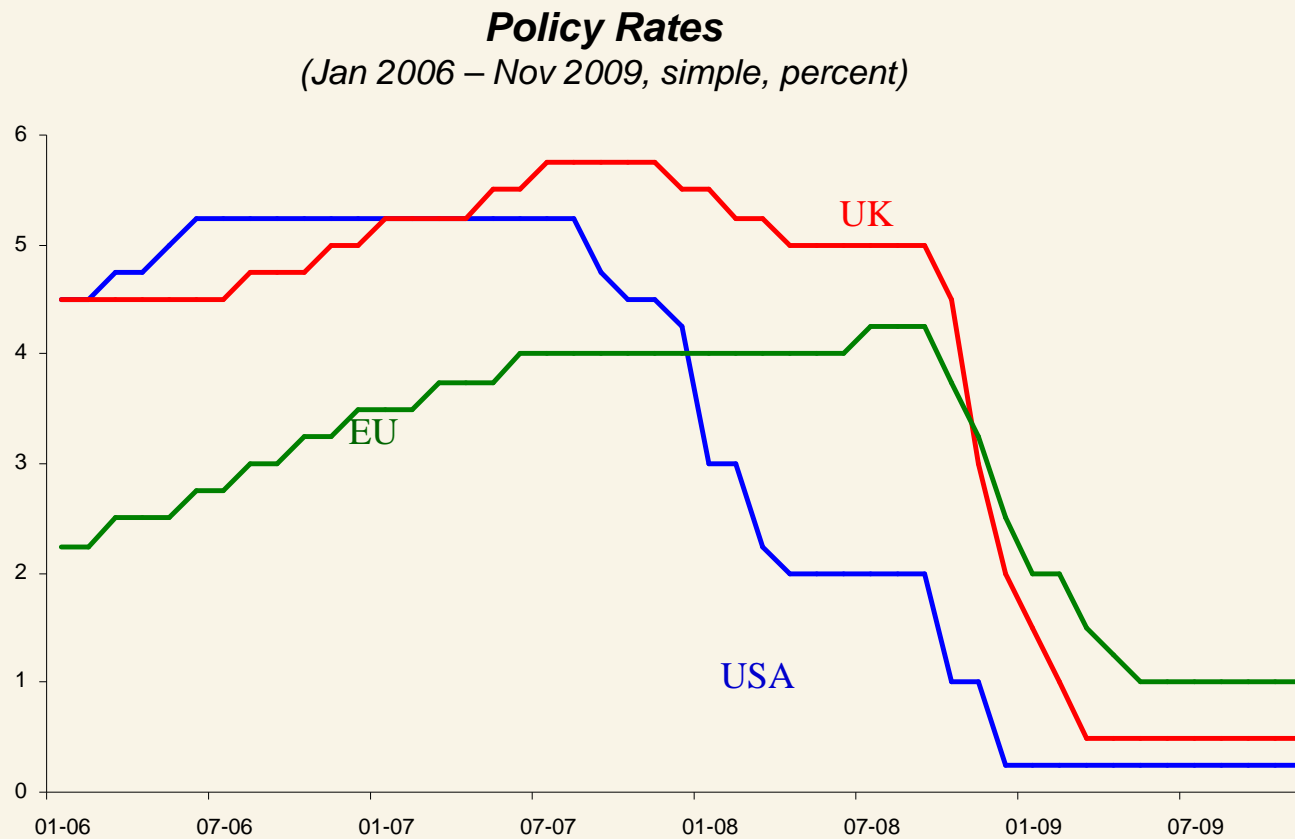
Inflation Developments
(Jan 2000 – Oct 2009, annual percentage change)



Source: IMF



World Policy Interest Rates



Source: Central Banks, CBT



Holistic Approach to Economic Stability

Targets

- 1. Price Stability**
- 2. Financial Stability**
- 3. Sustainable Growth**

Tools

- | | |
|-----------------------------------|---------------------------|
| 1. Monetary Policy | (Counter-cyclical) |
| 2. Financial Sector Policy | (Counter-cyclical) |
| 3. Fiscal Policy | (Counter-cyclical) |



Thank You...



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