TÜRKİYE CUMHURİYET
MERKEZ BANKASI

THE RISING ROLE OF THE EMERGING MARKETS IN THE WORLD ECONOMY: THE CASE OF TURKEY

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Outline

I. The Rising Role of the Emerging Markets in the World Economy

II. A Short Development History of Turkey

III. Current Challenges

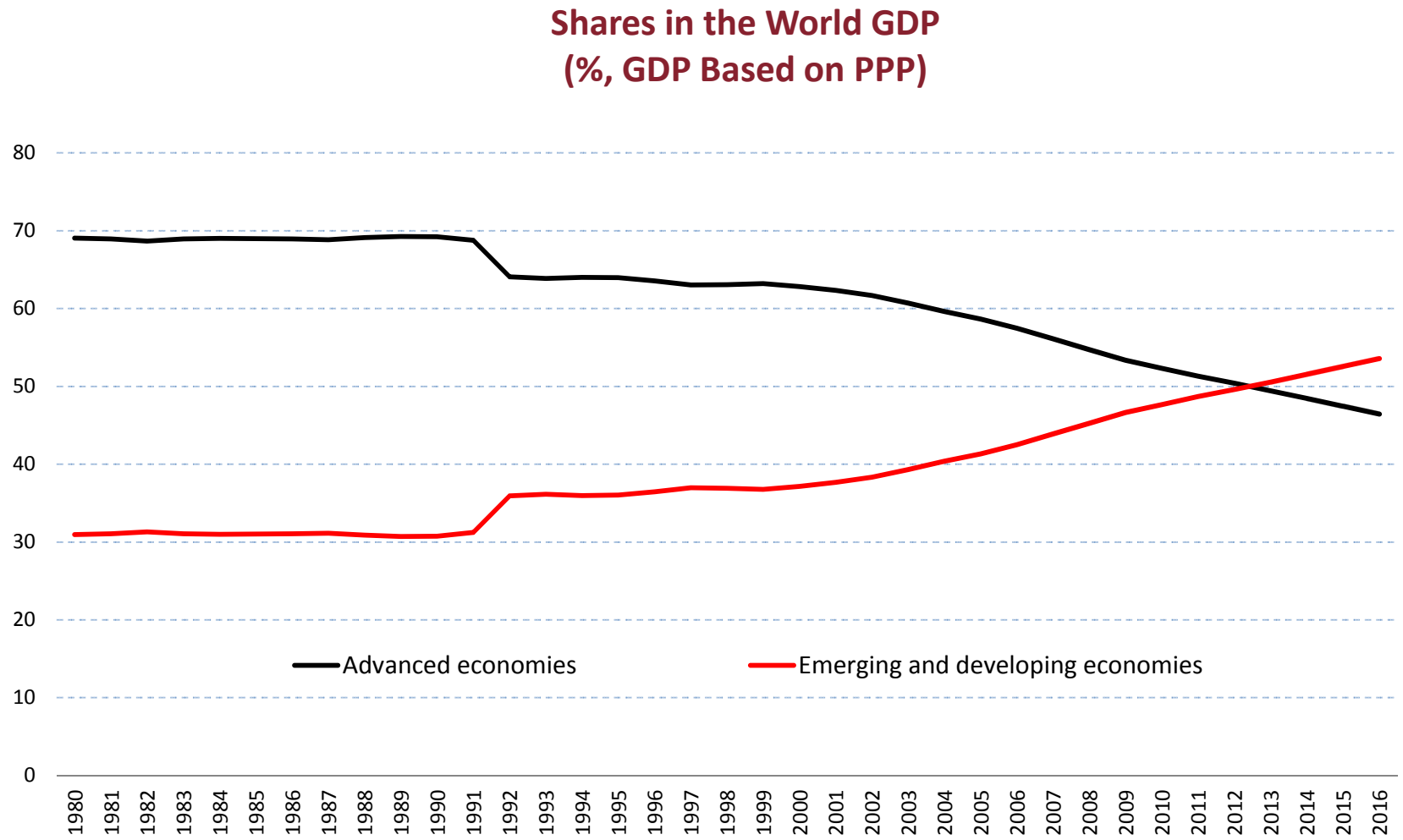
IV. Conclusion

THE RISING ROLE OF THE EMERGING MARKETS IN THE WORLD ECONOMY

EMEs vs AEs

- Growth prospects and rates in EMEs are higher than that of AEs
- Unemployment rates in G7 exceed that of EMEs
- Stock balances (public debt/GDP etc.) in EMEs are much better than that of AEs
- Average market risk spread on AEs now exceeds that on EMEs

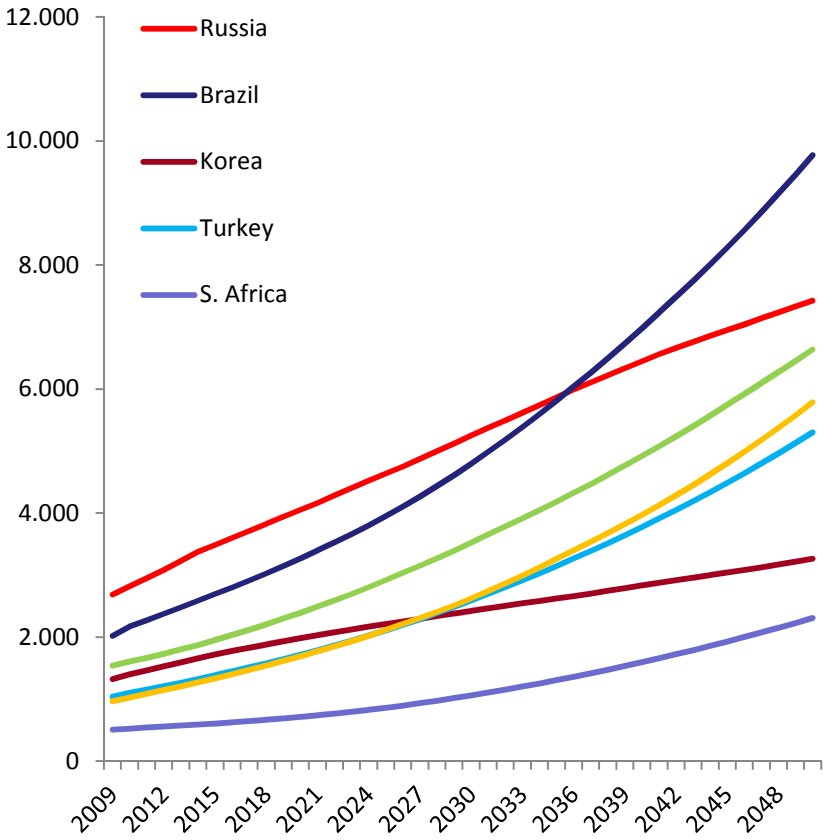
Shares of emerging and developing economies in the world GDP has been increasing…

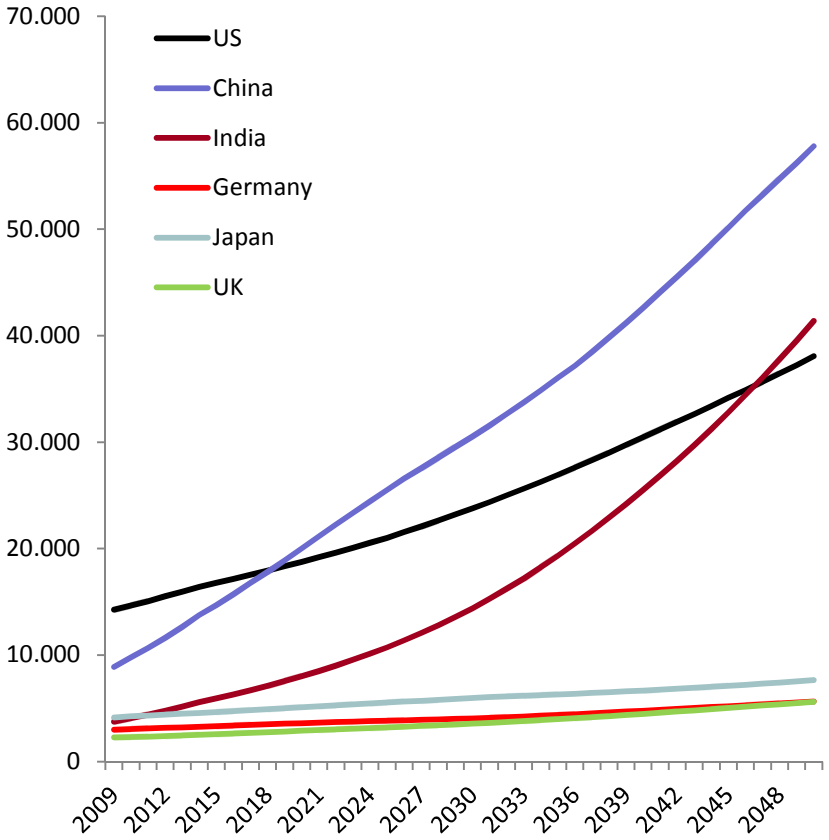


Source: HSBC, World in 2050, January 2012

Some of the emerging markets will grow faster...

PPP Converted GDP Projections
(constant 2009 dollar, $bn)

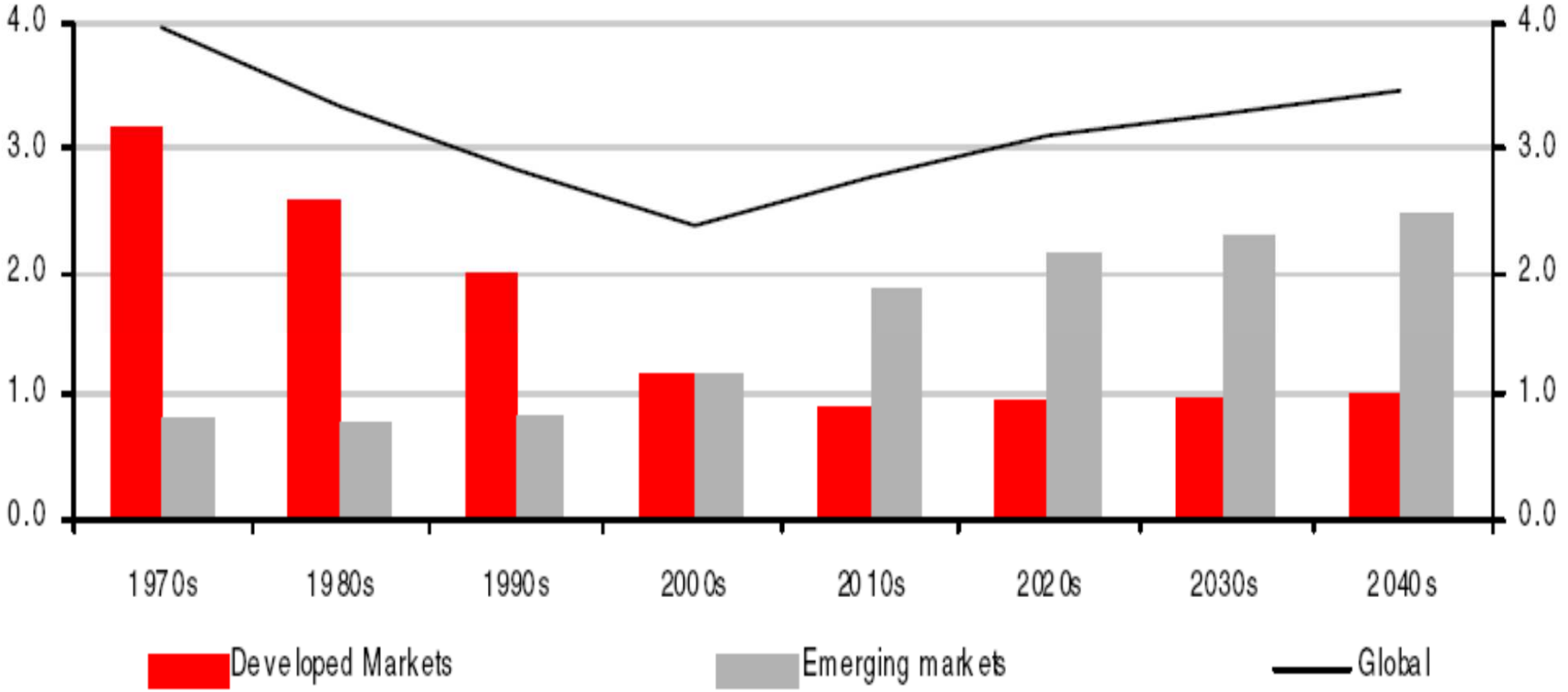




Source: PWC, The World in 2050, January 2011

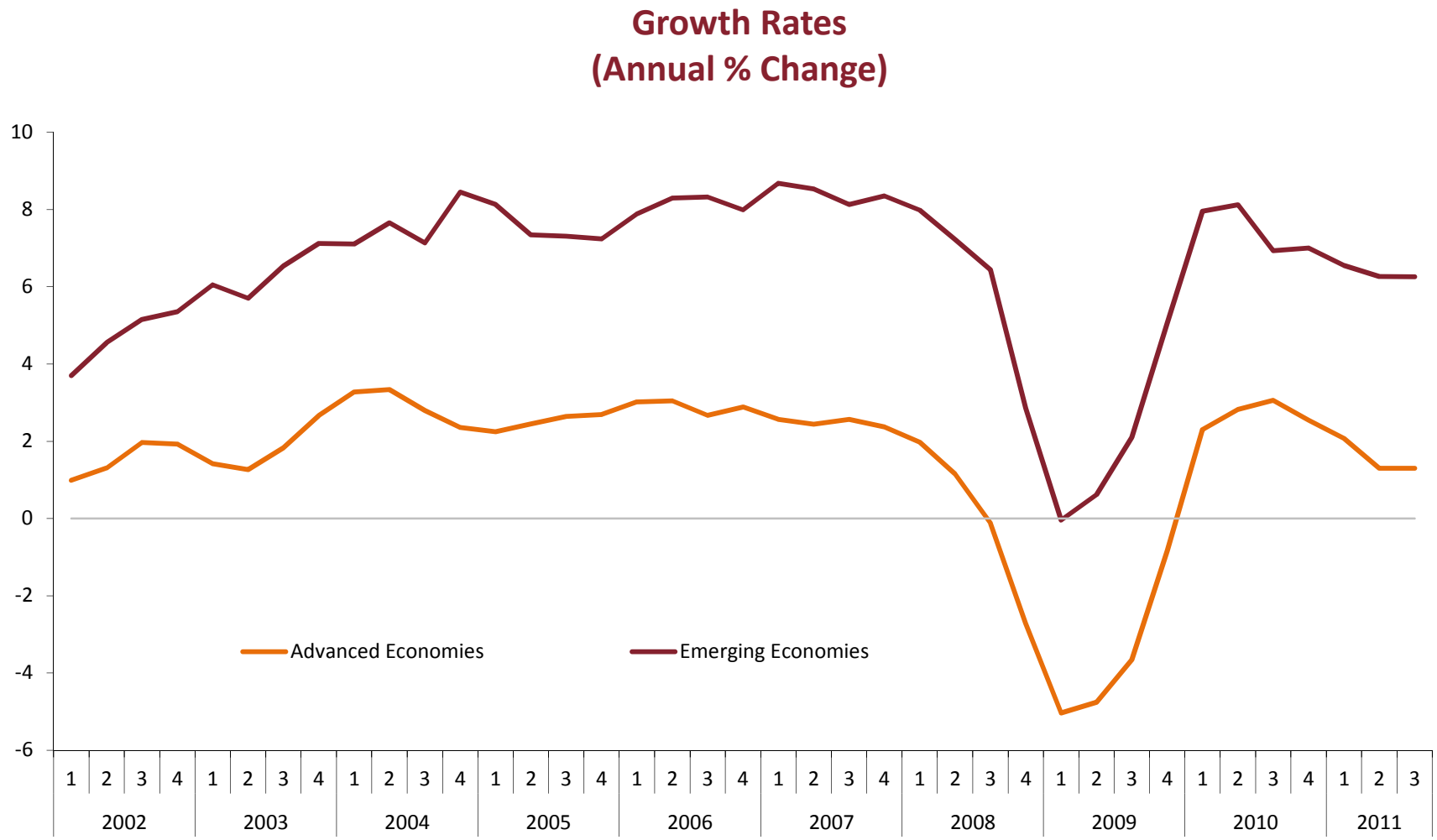
Emerging markets will be the main driver of the global growth.

Contributions to Global Growth



Source: HSBC, World in 2050, January 2012

The latest growth differential.



Source: Bloomberg, CBRT

Turkey is expected to go up in the economic league ranking by 6 steps in 40 years.

The Economic League in 2050

		Size of Economy in			Income Per Capita			
		2010*	2050*	Change in Rank	2010**	Rank	2050**	Rank
1	China	3511	25334	2	2579	63	17759	54
2	U.S.	11548	22270	-1	36354	6	55134	8
3	India	960	8165	5	790	88	5060	86
4	Japan	5008	6429	-2	39435	3	63244	4
5	Germany	2058	3714	-1	25083	18	52683	10
6	U.K.	1711	3576	-1	27646	11	49412	14
7	Brazil	921	2960	2	4711	52	13547	61
8	Mexico	688	2810	5	6217	42	21793	47
9	France	1496	2750	-3	23881	20	40643	21
10	Canada	892	2287	0	26335	15	51485	12
11	Italy	1124	2194	-4	18701	23	38445	23
12	Turkey	385	2149	6	5088	49	22063	46
13	South Korea	798	2056	-2	16463	25	46657	17
14	Spain	711	1954	-2	15699	26	38111	24
15	Russia	412	1878	2	2934	58	16174	56
16	Philippines	112	1688	27	1215	83	10893	72
17	Indonesia	274	1502	4	1178	85	5215	85
18	Australia	565	1480	-4	26244	16	51523	11
19	Argentina	428	1477	-2	10517	33	29001	38
20	Egypt	160	1165	15	3002	57	8996	76

* Billion with constant (2000) U.S. Dollar
** With constant (2000) U.S. Dollar

Source: HSBC, World in 2050, January 2012

A SHORT DEVELOPMENT HISTORY OF TURKEY

A short development history of Turkey

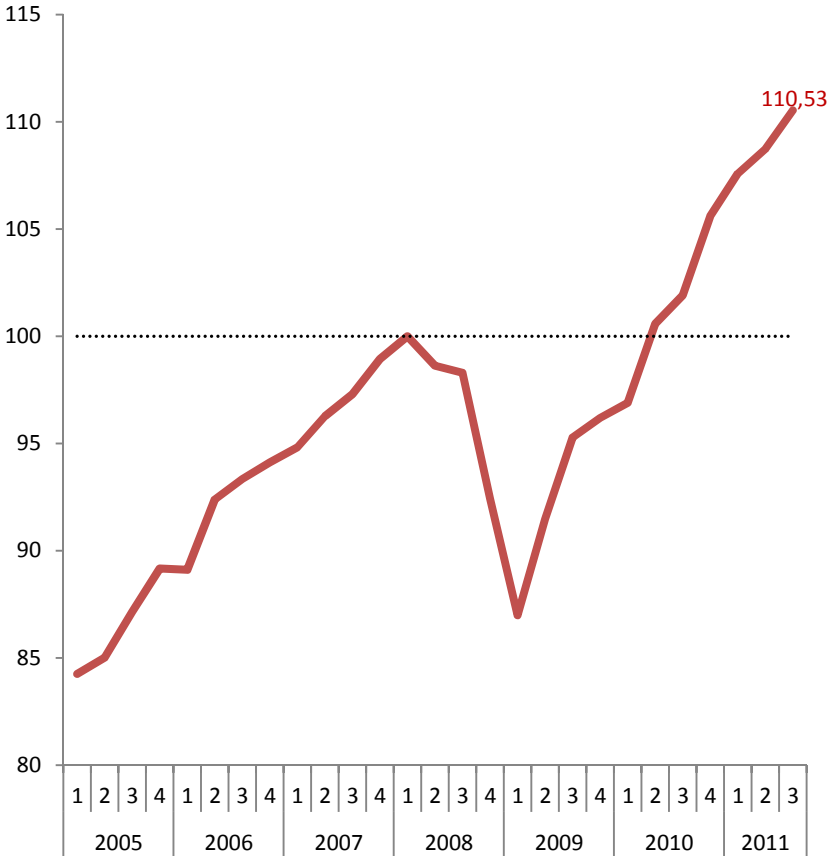
Income, Investments and Savings in Turkey

	1980-89	1990-99	2000-10
GDP per Capita (US dollars)	2,276	3,812	8,749
GDP per Capita (US dollars) in PPP	4,114	7,166	11,641
GDP Growth (%)	4.1	4.0	4.2
Gross Fixed Investment (% of GDP)	21.6	24.2	19.4
Public (% of GDP)	8.8	6.2	5.0
Private (% of GDP)	12.8	18.0	14.4
Savings (% of GDP)	19.7	23.8	16.3
Public (% of GDP)	4.9	-0.5	-0.8
Private (% of GDP)	14.8	24.3	17.0

Source: T.R. Ministry of Development

Strong growth rates…

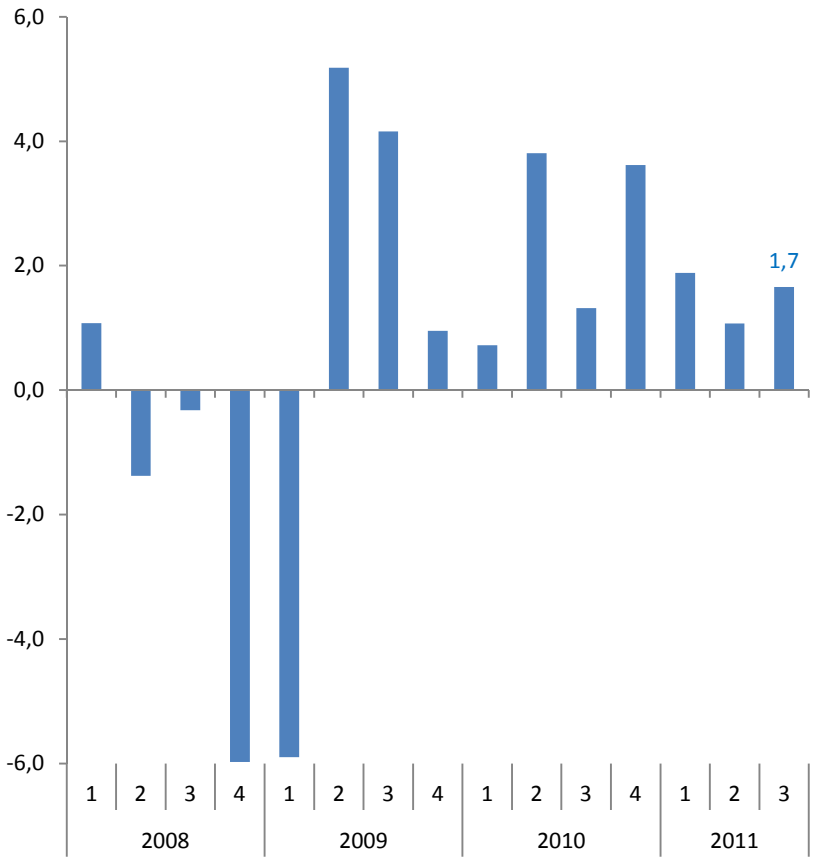
GDP
(2008q1=100, Seasonally Adjusted)



Source: TurkStat, CBRT.

Latest Observation: q3 2011

GDP Growth
(qoq, %)

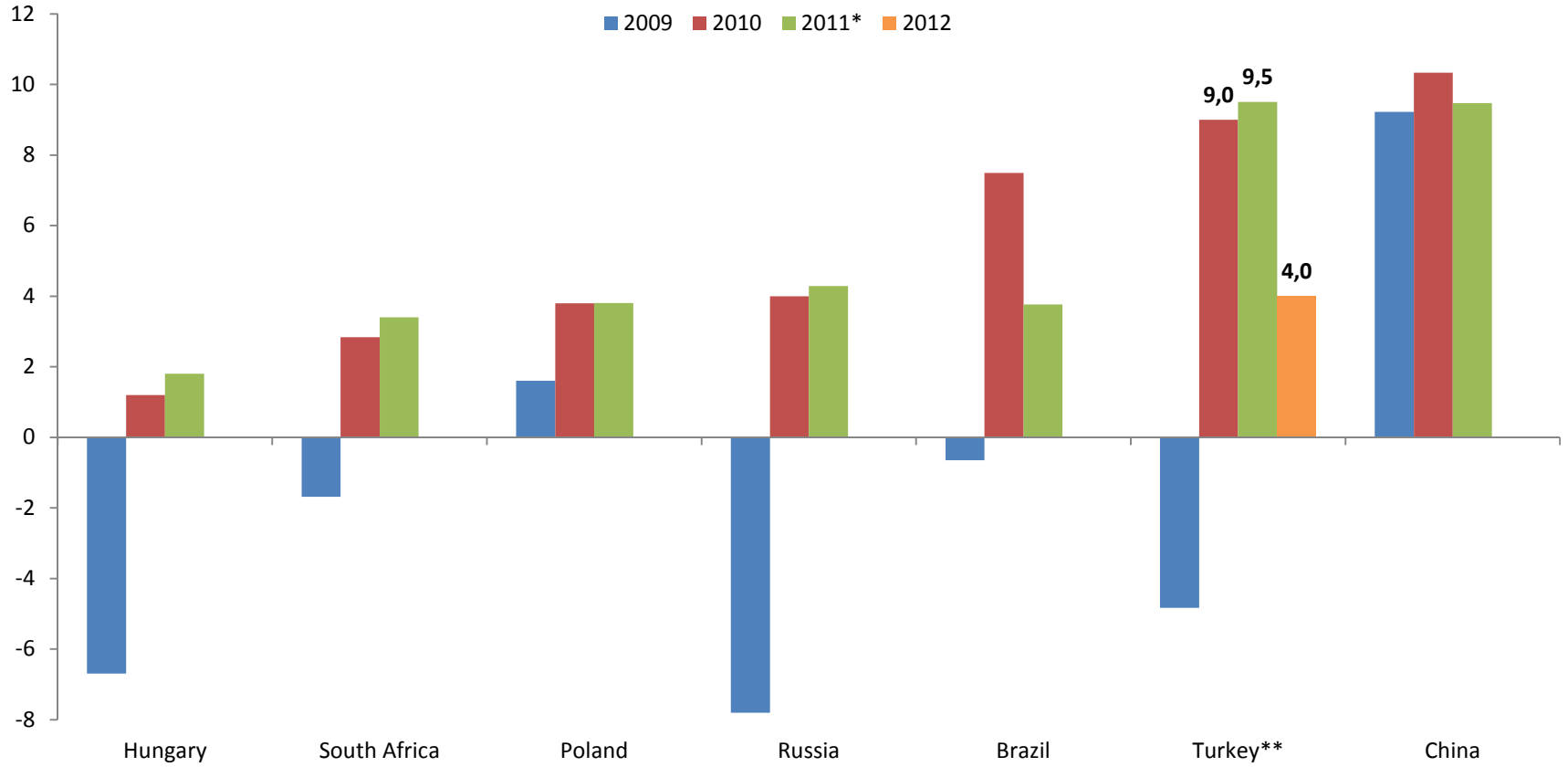


Source: TurkStat, CBRT.

Latest Observation: q3 2011

… compared to selected countries.

GDP Growth of Selected Countries
(Real, Annual, %)



Source: IMF, CBRT.

* IMF Forecast

** 2011 q3 Annualized growth, 2012 growth is Medium Term Program projection.

A short development history of Turkey

External Sector and Foreign Debt

	1980-89	1990-99	2000-10
Foreign Trade Volume (% of GDP)	24.2	23.9	40.6
Foreign Trade Deficit (% of GDP)	-4.4	-4.6	-5.8
Current Account (% of GDP)	-1.6	-0.6	-3.6
Capital Inflows (% of GDP)	1.8	1.7	3.8
FDI (% of GDP)	0.2	0.3	1.4
Portfolio and Others (% of GDP)	0.3	1	2.4
Foreign Debt Stock (% of GDP)	30.0	33.3	43.7
Private Foreign Debt (% of GDP)	5.8	10.9	21.7
Public Foreign Debt (% of GDP)	24.2	22.4	22.0

Source: T.R. Ministry of Development and Undersecretariat of Treasury

A short development history of Turkey

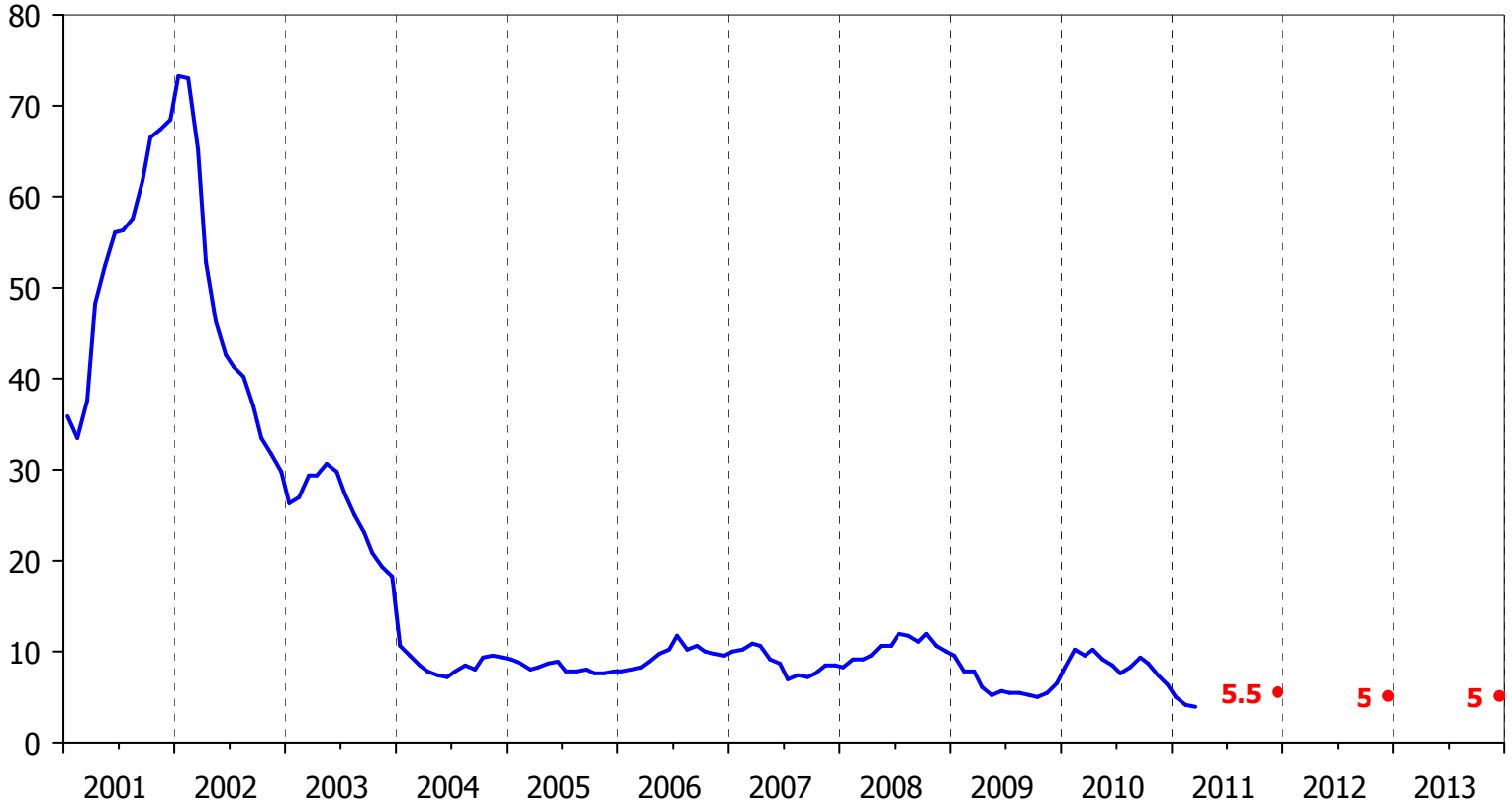
Inflation, Banking and Financial Markets

	1980-89	1990-99	2000-10
CPI (% change)	51	77.4	19.7
Interbank Overnight Interest Rate (%)	38.8	76	37.8
M2 (% of GDP)	13	10.4	21.3
M2Y (% of GDP)	15.3	17.6	35
Deposits (% of GDP)	15.2	24	38.5
Credits (% of GDP)	15	17	21.5
Transaction Volume in ISE (% of GDP)	185.7	15990	42199

Source: T.R. Ministry of Development, Central Bank of Turkey

In the last decade inflation continued to decline.

Inflation Realizations
(%, red dots are the year-end inflation targets)



Source: CBRT.

A short development history of Turkey

Budget Balance and Public Debt

	1980-89	1990-99	2000-10
PSBR (% of GDP)	3.8	6.8	4.4
Consolidated Budget Balance (% of GDP)	-2	-4.7	-5.6
Consolidated Budget Interest Payments (% of GDP)	1.5	5.6	9.2
Public Debt (% of GDP)	36.2	37.4	57.9
Domestic Debt	12	15	35.9
Foreign Debt	24.2	22.4	22

Source: T.R. Ministry of Development

A short development history of Turkey

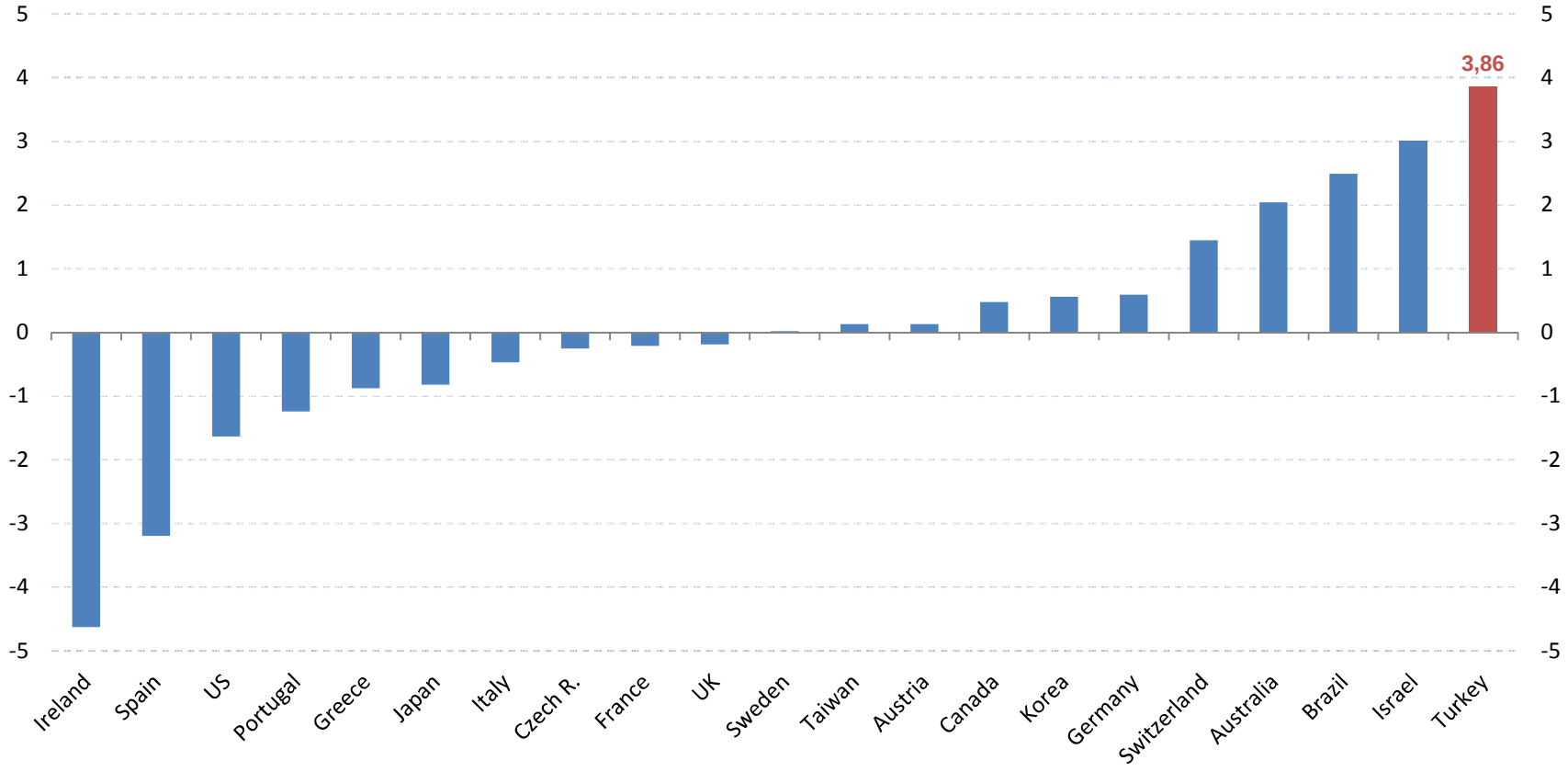
Labour Market Developments

	1980-89	1990-99	2000-10
Unemployment Rate	8.2	8.3	10.6
Labour Force (1000)	16,554	20,064	22,765
Real Labour Cost (% change)			
Worker	-	11.2	0.6
Public	-	9.9	0.1
Private	-	11.0	1.1
Civil Servant	-	17.5	1.0
Minimum Wage			

Source: T.R. Ministry of Development

Turkey is one of the leading countries in job creation.

Average Annual Employment Growth*
(Percent, 2007-2010)

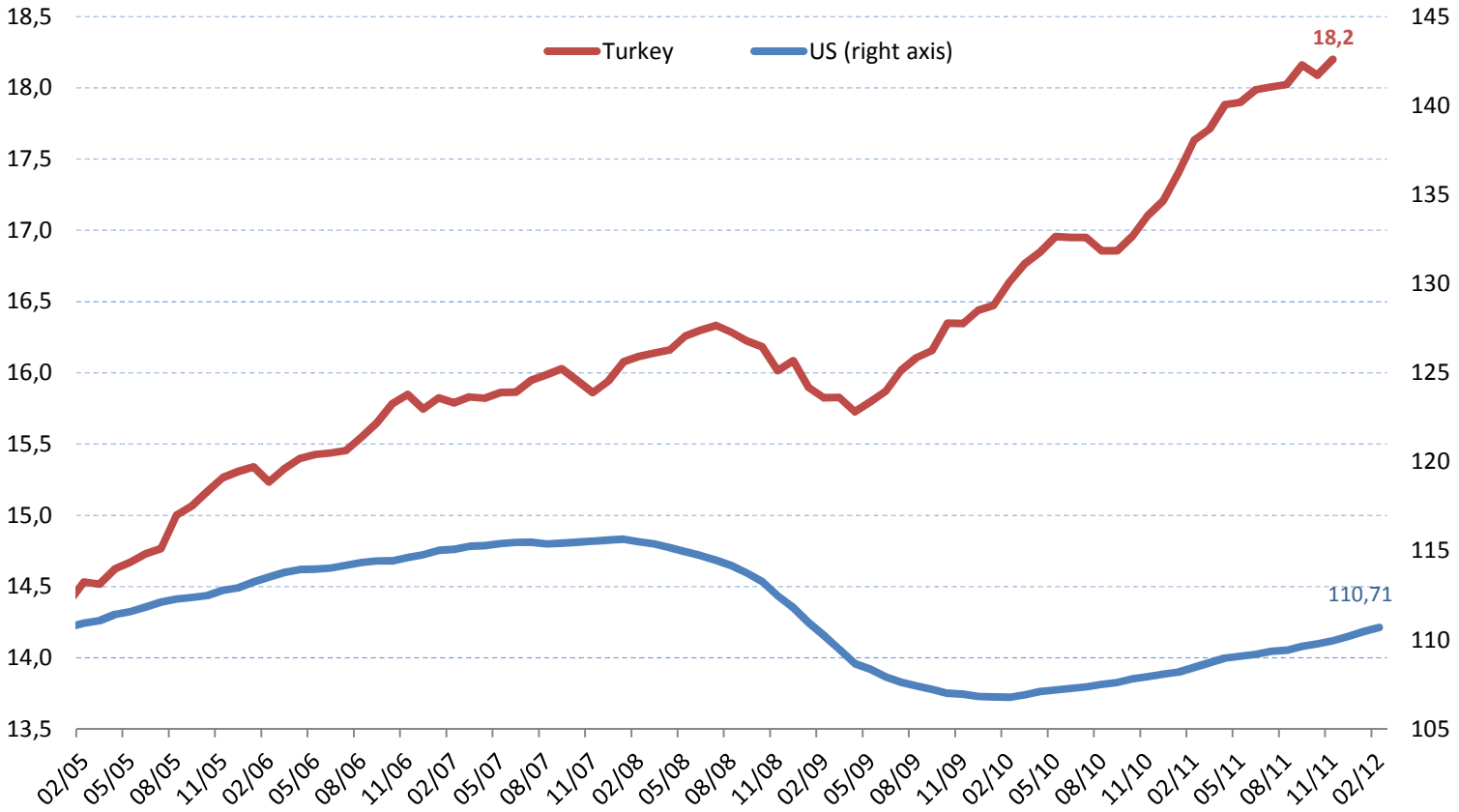


Source: IMF WEO, ILO, TURKSTAT, CBRT.

*Difference of natural logs

Growth in total employment and …

Total Employment
(Seasonally Adjusted, Non-Agricultural, Million People)

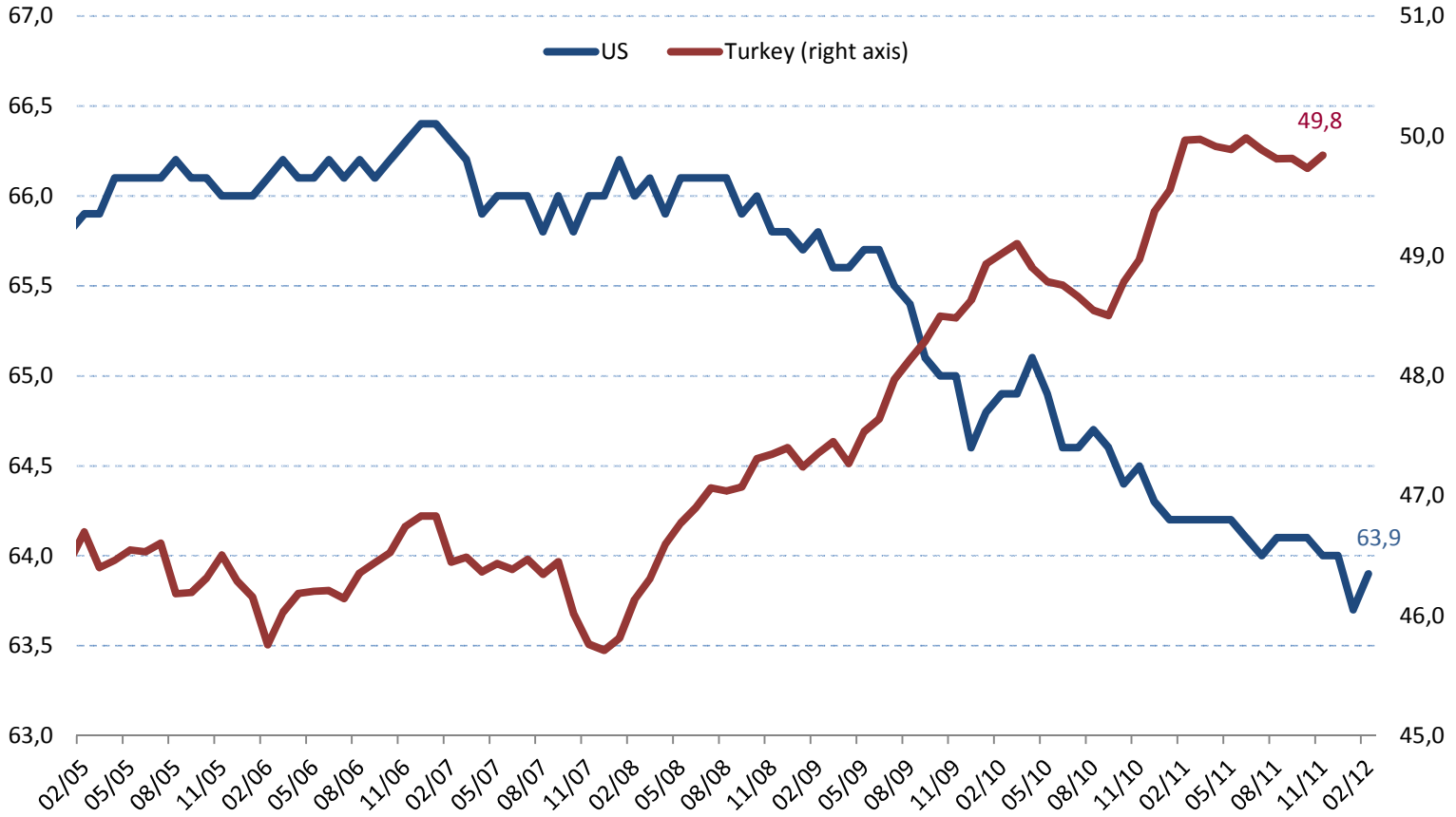


Source: TurkStat, ADM, CBRT.

Latest Observations: November 2011 for Turkey , February 2012 for US.

...labor market participation rate have better outlook in Turkey compared with the US.

Labor Market Participation Rate
(Seasonally Adjusted, Percent)

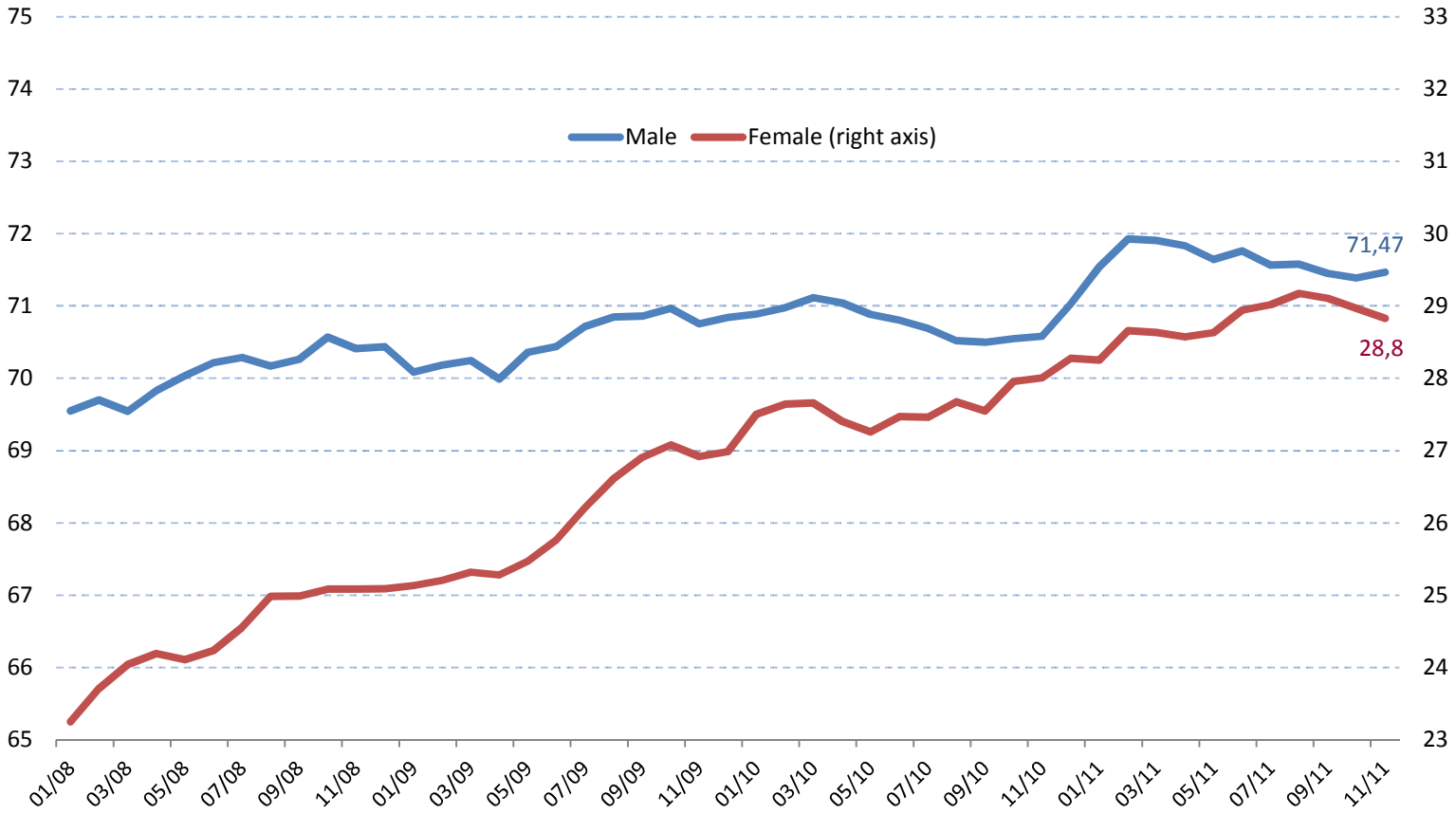


Source: TURKSTAT, BLS, CBRT.

Latest Observations: November 2011 for Turkey , February 2012 for US.

Female participation rate in Turkey continues to increase.

Male and Female Participation Rates in Turkey
(Seasonally Adjusted, Percent)

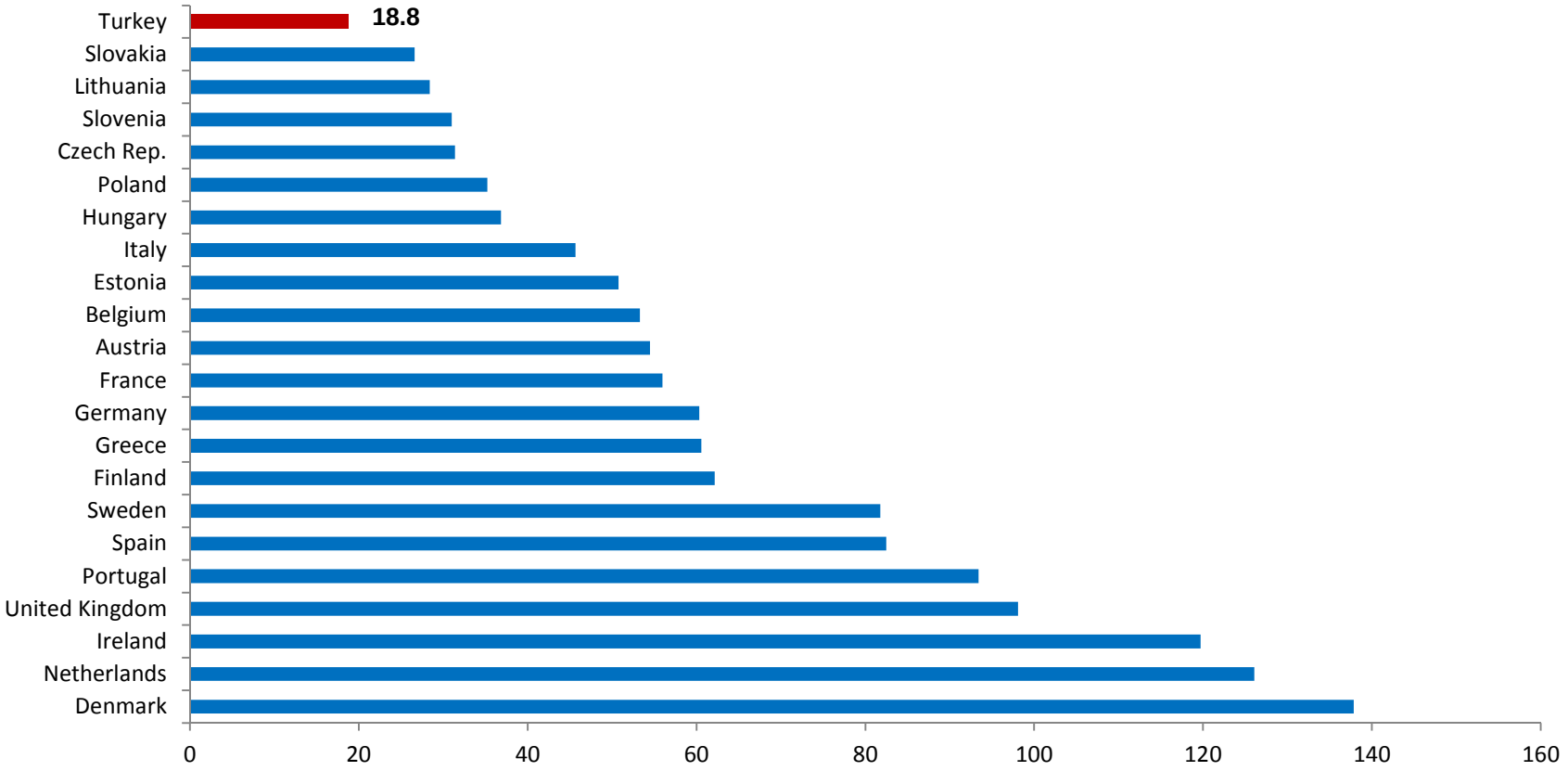


Source: TurkStat, CBRT.

Latest Observations: November 2011.

Strong stock balances

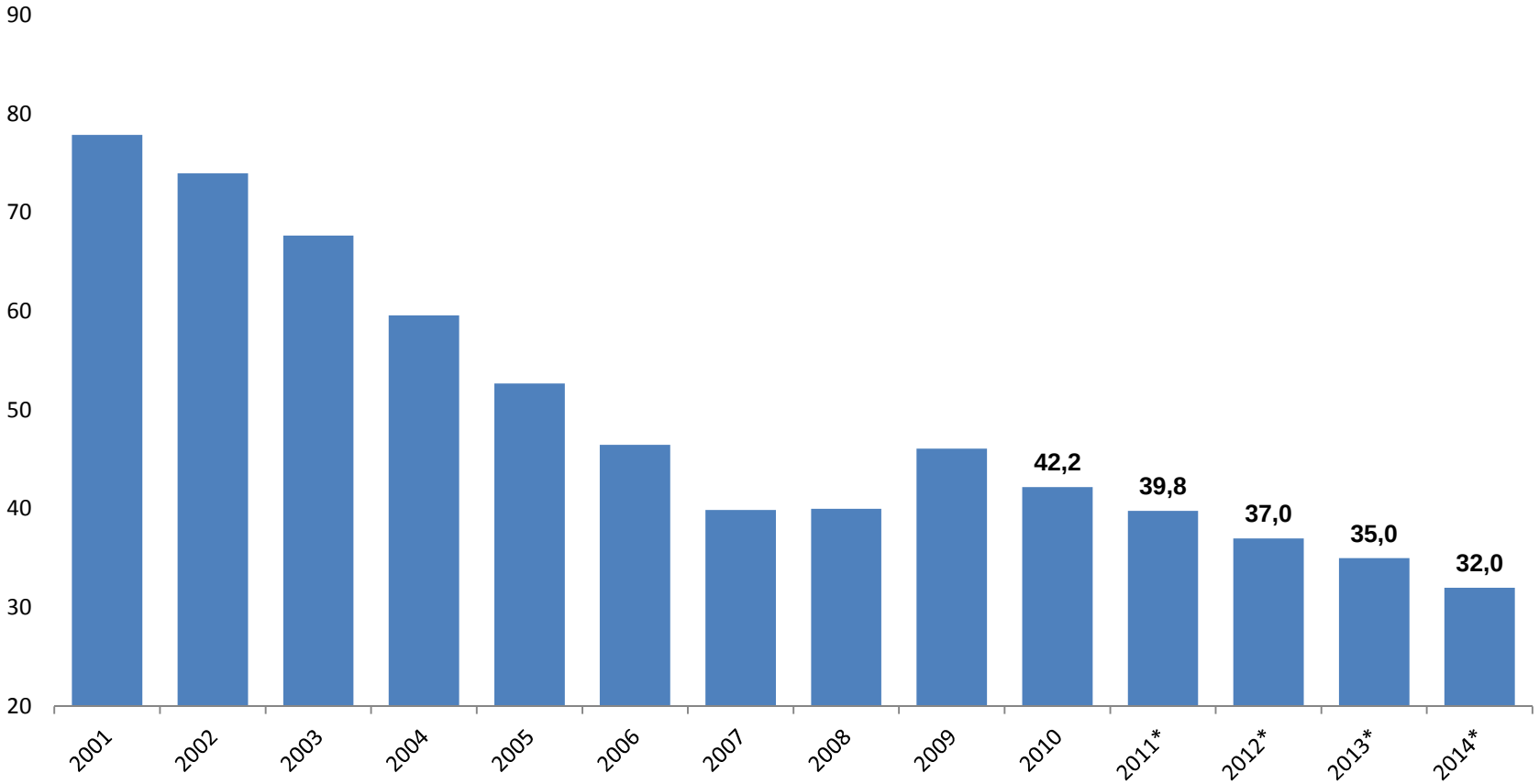
Household Liabilities
(% GDP, 2011q2)



Source: ECB, CBRT.

Strong stock balances

Government Debt Stock
(% GDP)

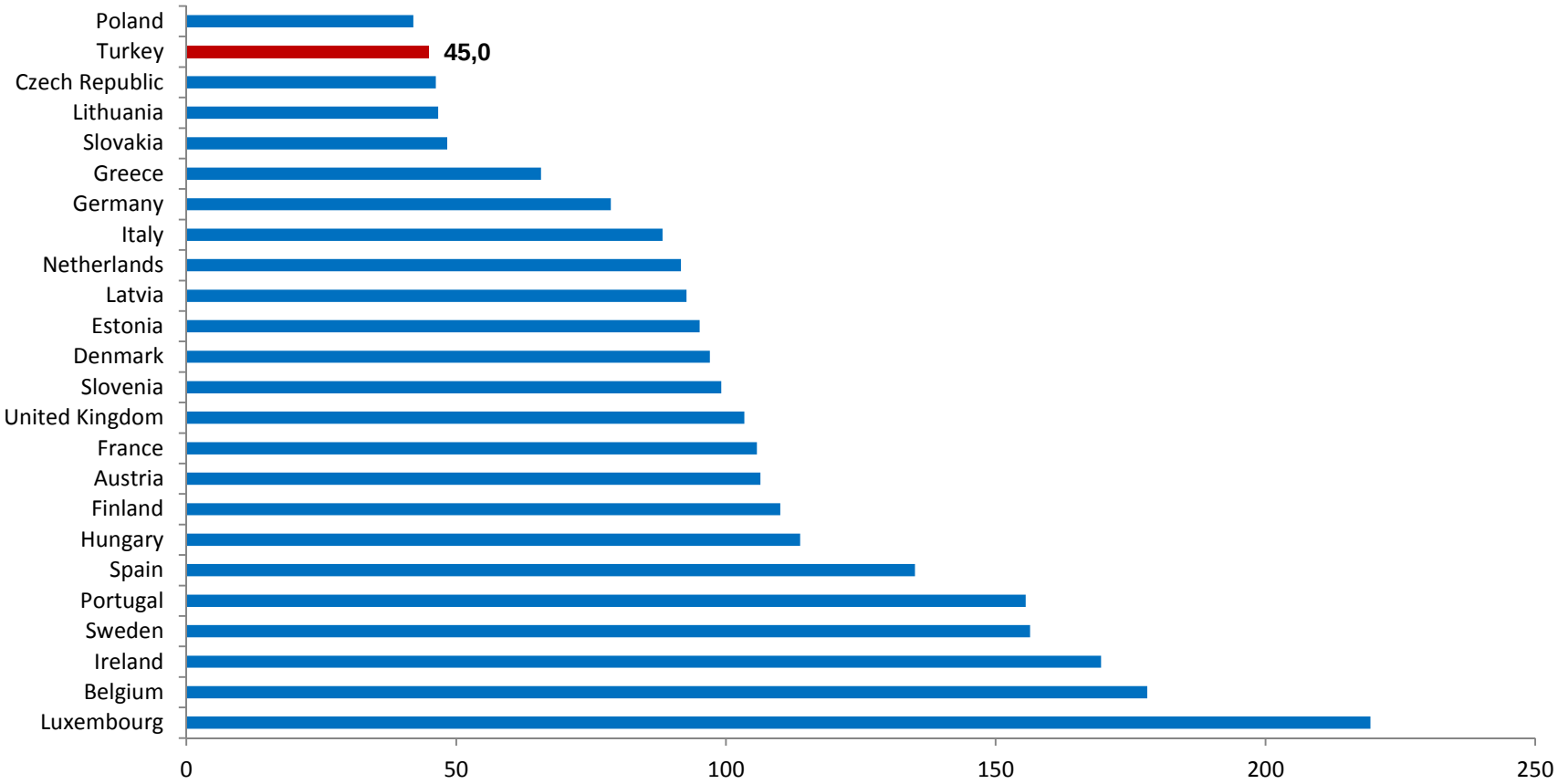


Source: TurkStat, CBRT.

*Medium Term Program projections.

Strong stock balances

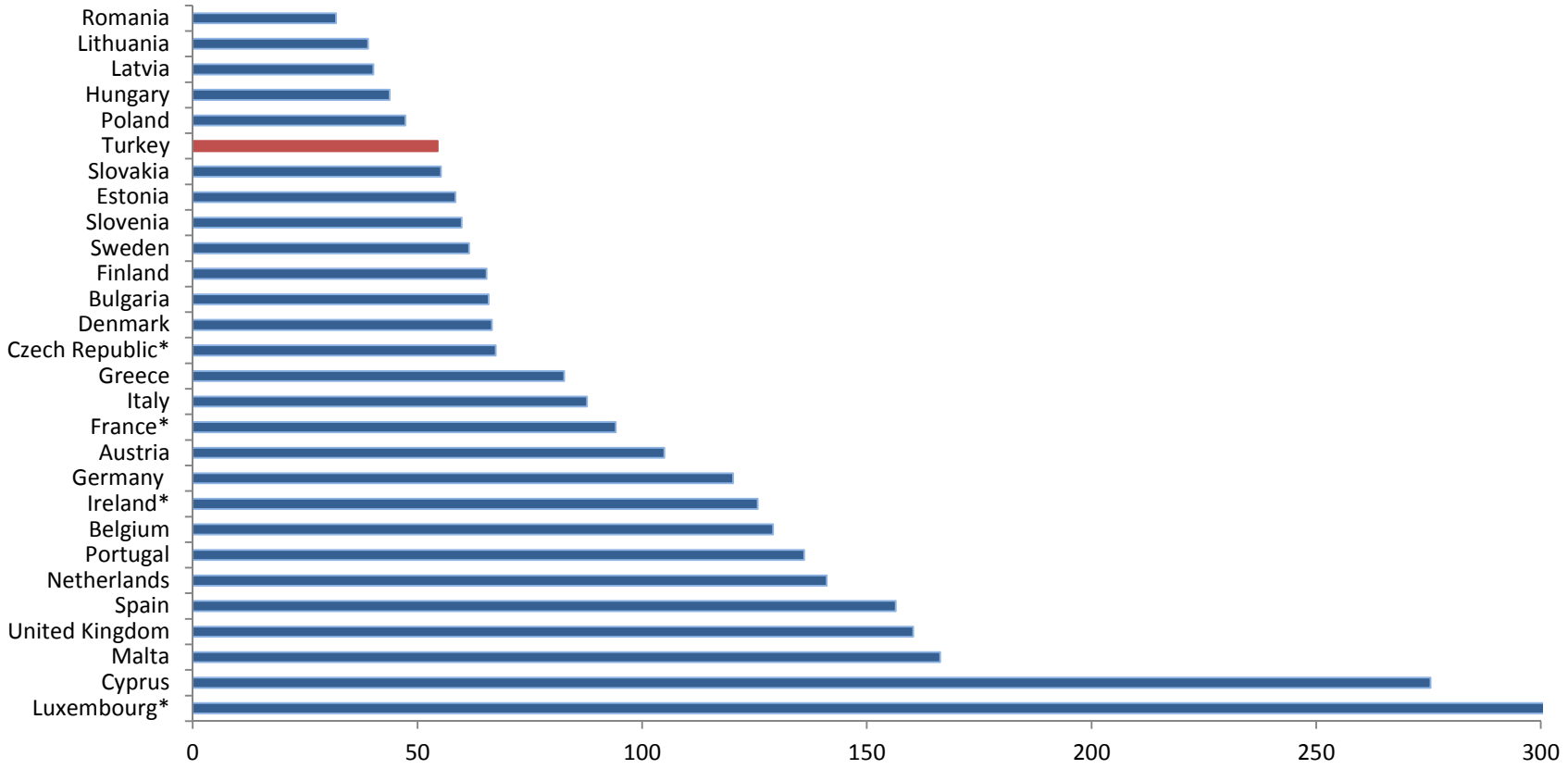
Total Loans to Non-Financial Companies
(% GDP, 2011q2)



Source: ECB, CBRT.

Strong stock balances

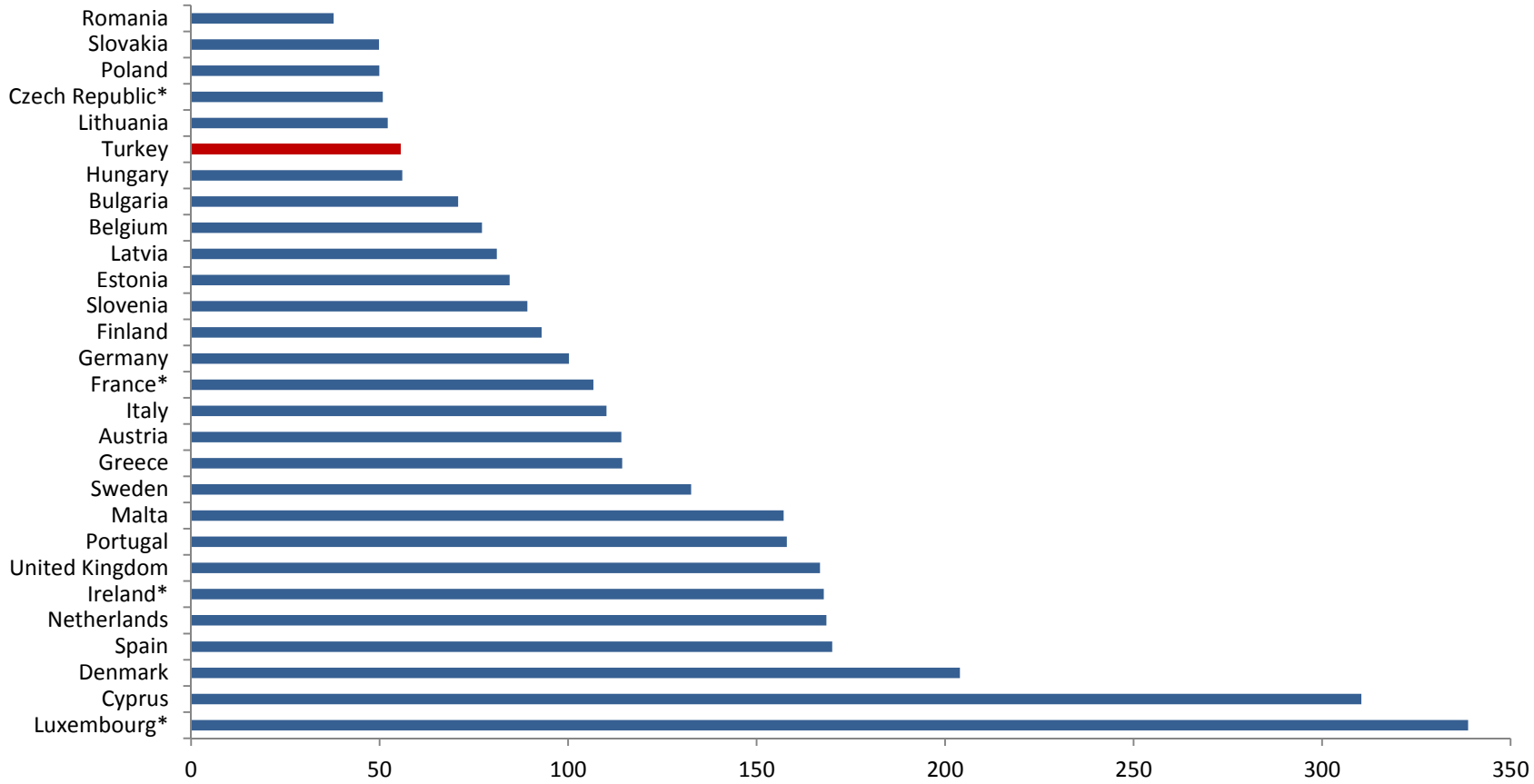
Deposits of Monetary Financial Institutions
(% GDP, 2011q4)



Source: Eurostat, ECB, CBRT.
* q4 2011 GDP volumes are forecasts.
Latest Observation: q3 2011 for Turkey, q4 2011 for other countries.

Strong stock balances

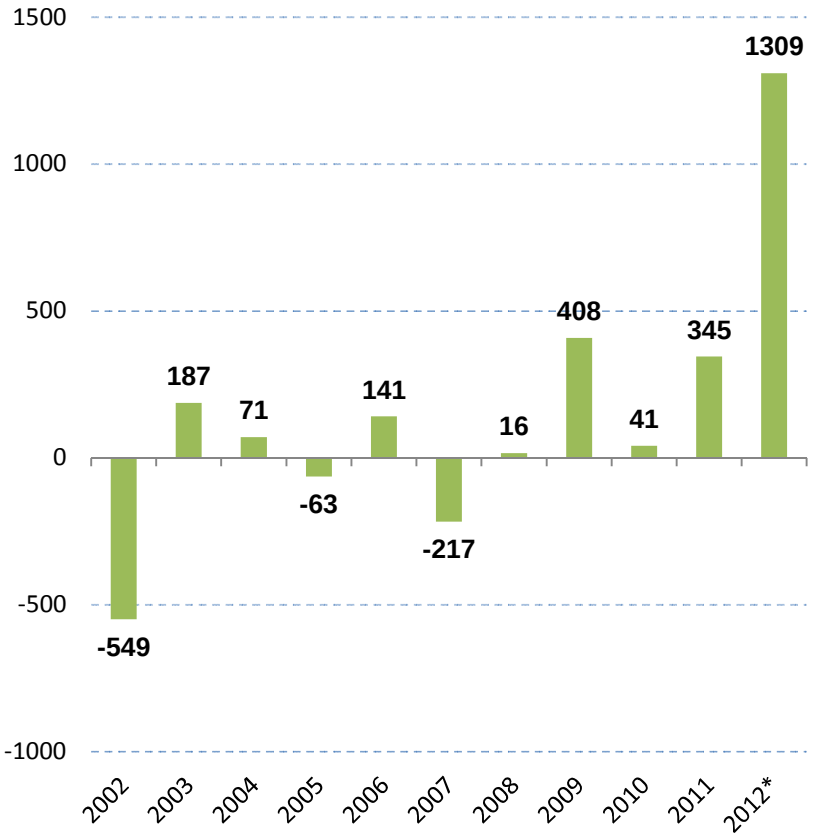
Loans of Monetary Financial Institutions
(% GDP, 2011q4)



Source: Eurostat, ECB, CBRT.
* q4 2011 GDP volumes are forecasts.
Latest Observation: q3 2011 for Turkey, q4 2011 for other countries.

Strong stock balances in banking sector

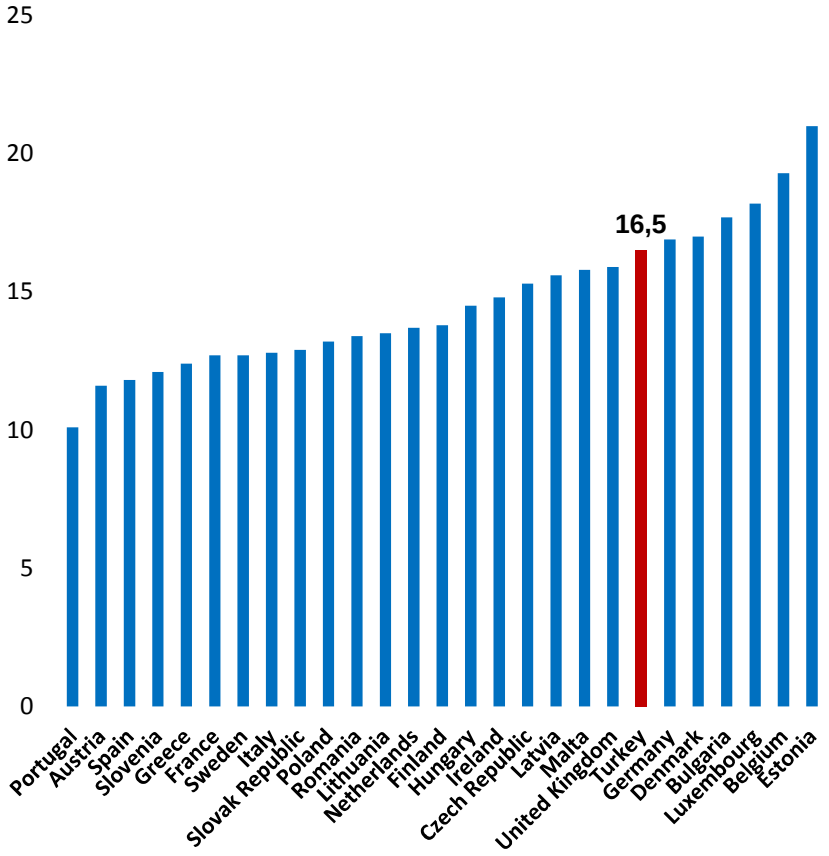
Net FX Position (Million USD)



Source: BRSA, CBRT.

* As of February 17, 2012

Capital Adequacy Ratio (%)

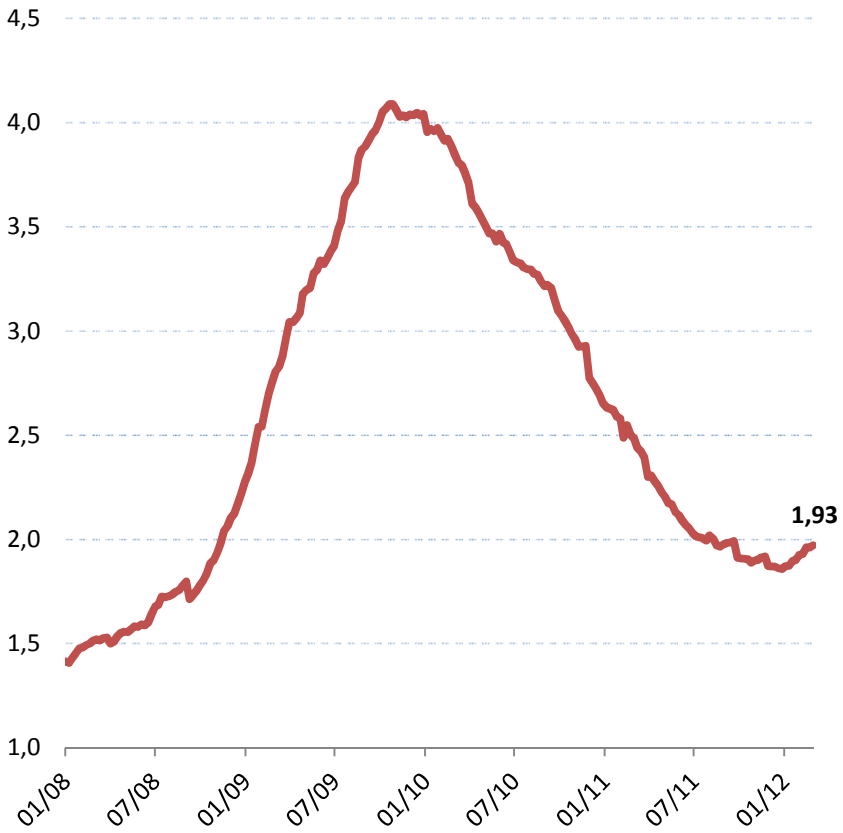


Source: FSI, IMF, CBRT.

Latest Observation: December 2011 for Turkey. Latest observation varies from December 2010 to September 2011 for other countries.

Strong stock balances in banking sector

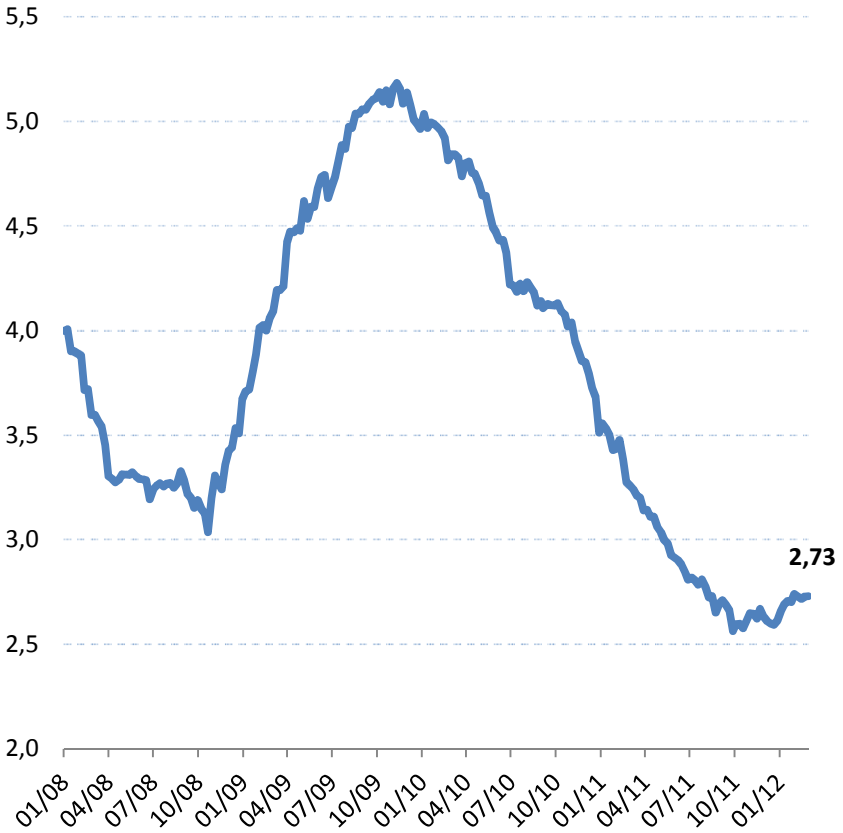
Non-Performing Consumer Loans (Percent)



Source: CBRT.

Latest Observation: March 2, 2011.

Non-Performing Corporate Loans (Percent)

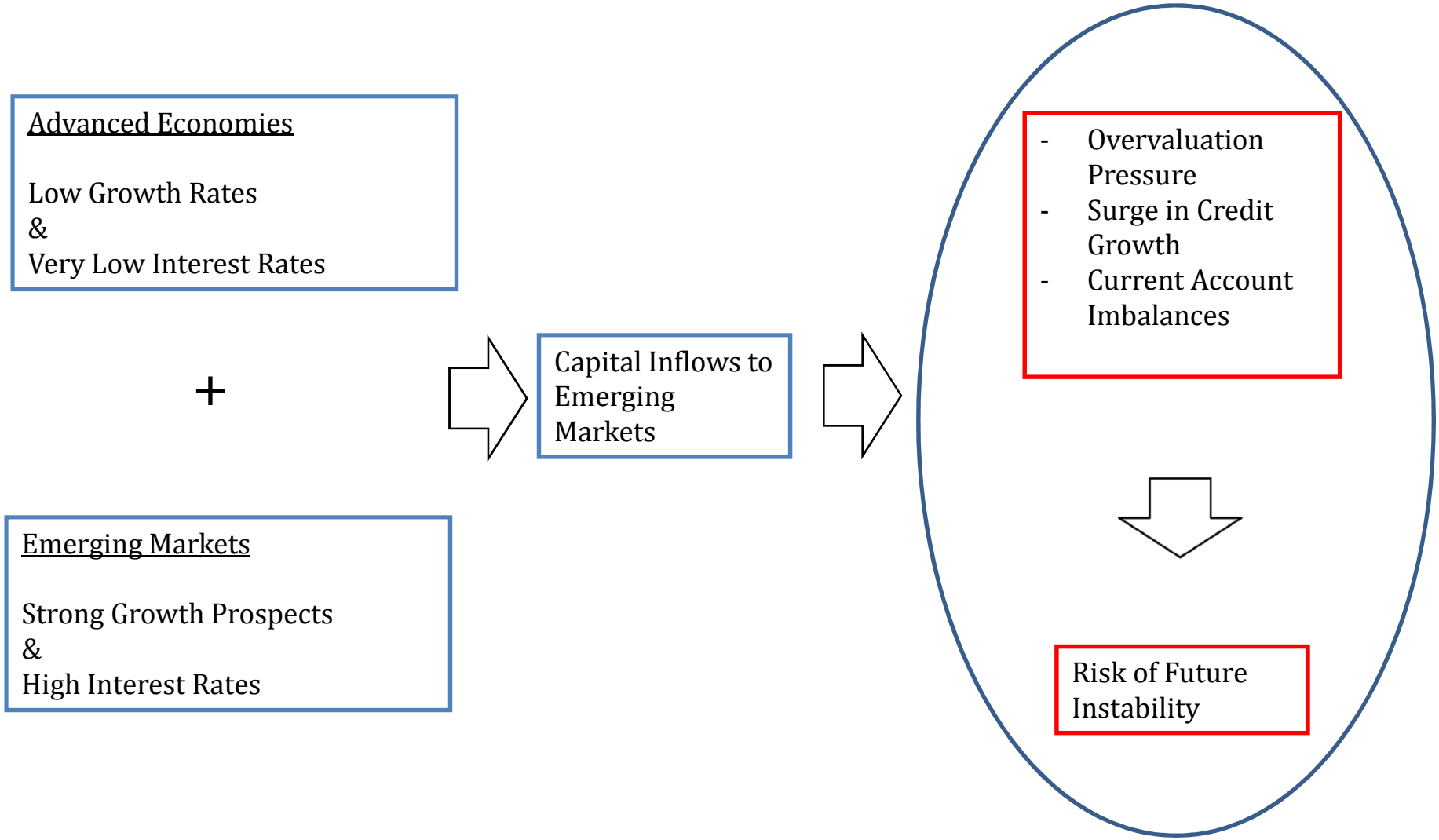


Source: CBRT.

Latest Observation: March 2, 2011.

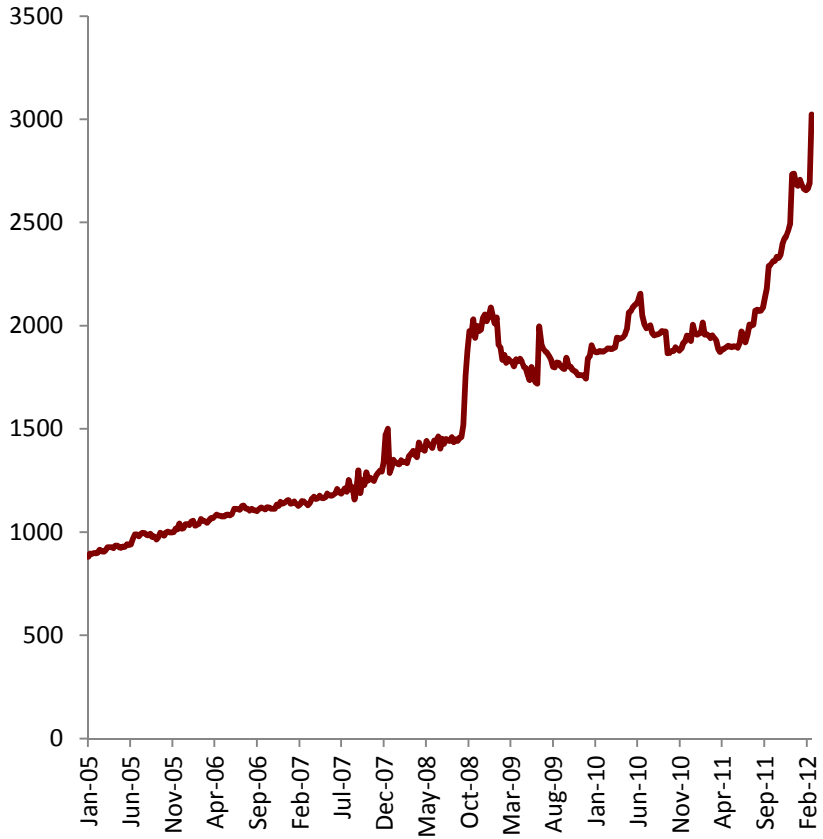
CURRENT CHALLENGES

Risk of Future Instability

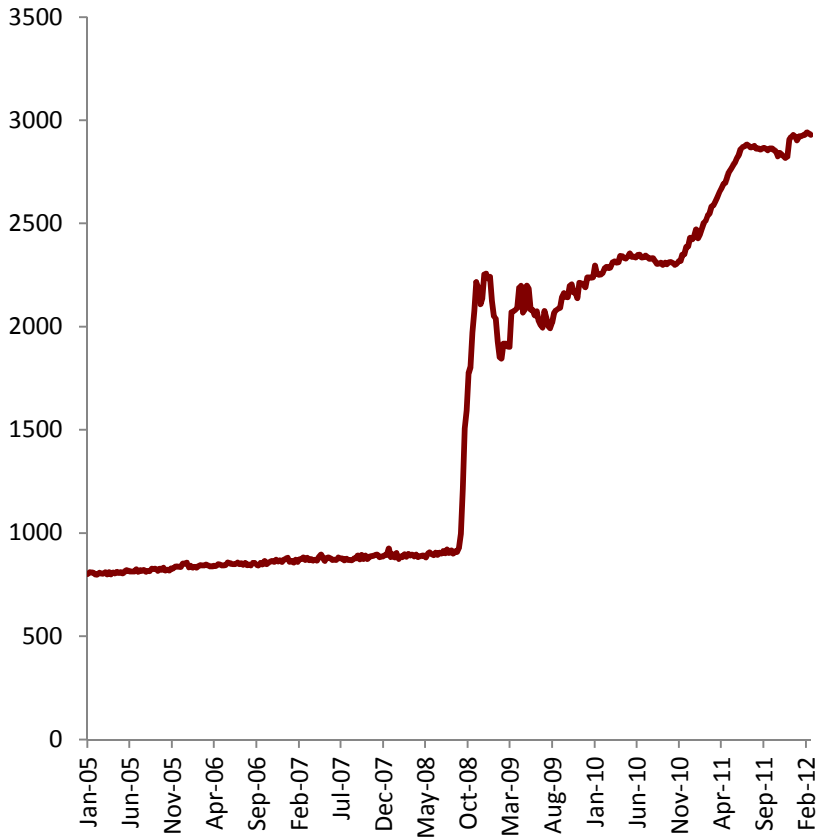


Monetary Expansion in the Eurozone and in the U.S.

ECB
(Total Assets – billion €)



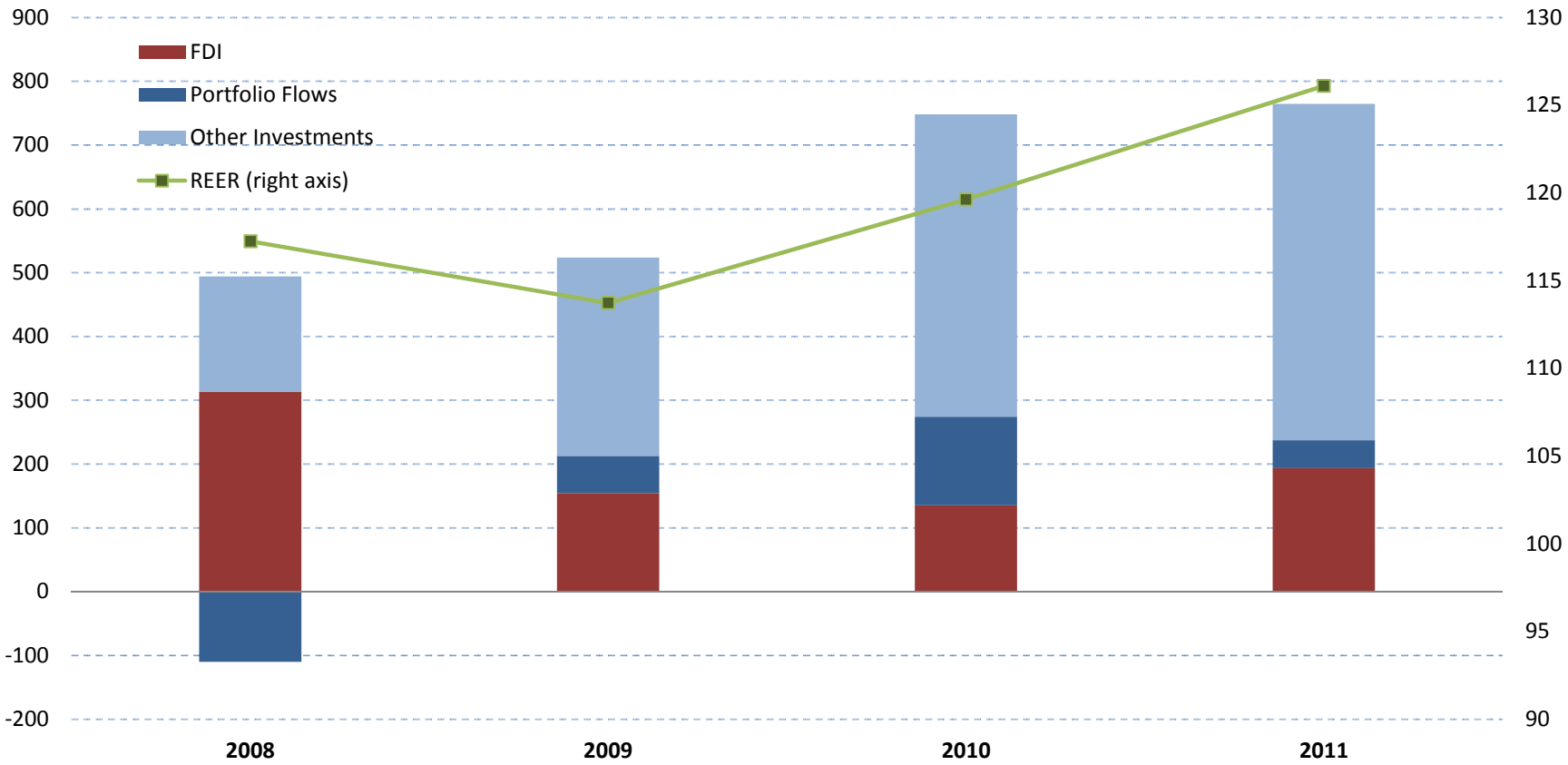
FED
(Total Assets - $ billion)



Source: Bloomberg

Capital flows to emerging markets have remained high.

Capital Flows to EMs* and Real Effective Exchange Rate (Billion USD, index 2005=100)

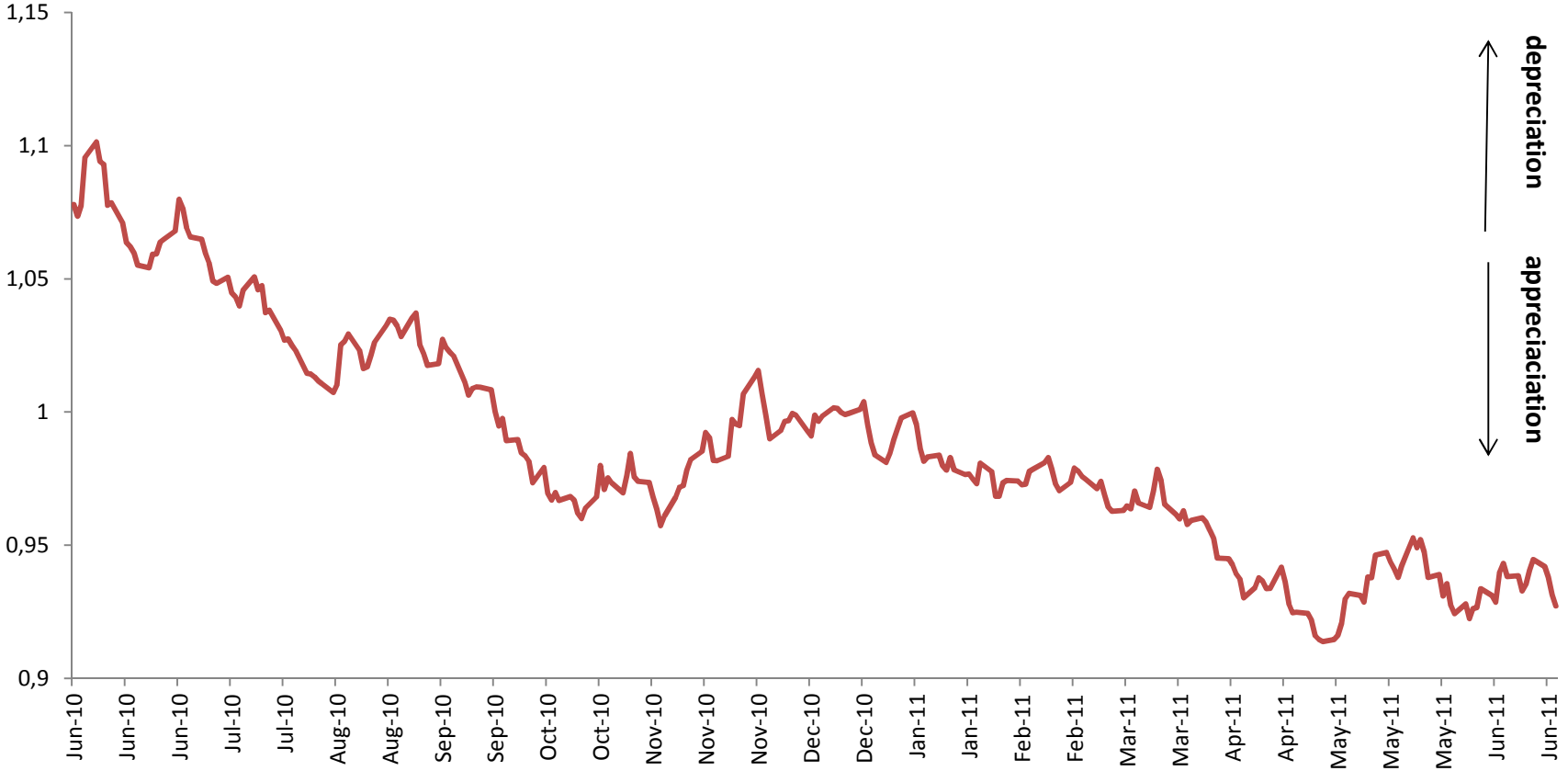


Source: IIF, CBRT.

* EMs cover 30 countries from Asia/Pacific, Europe, Latin America and MENA regions.

Appreciation of emerging market currencies due to high capital flows

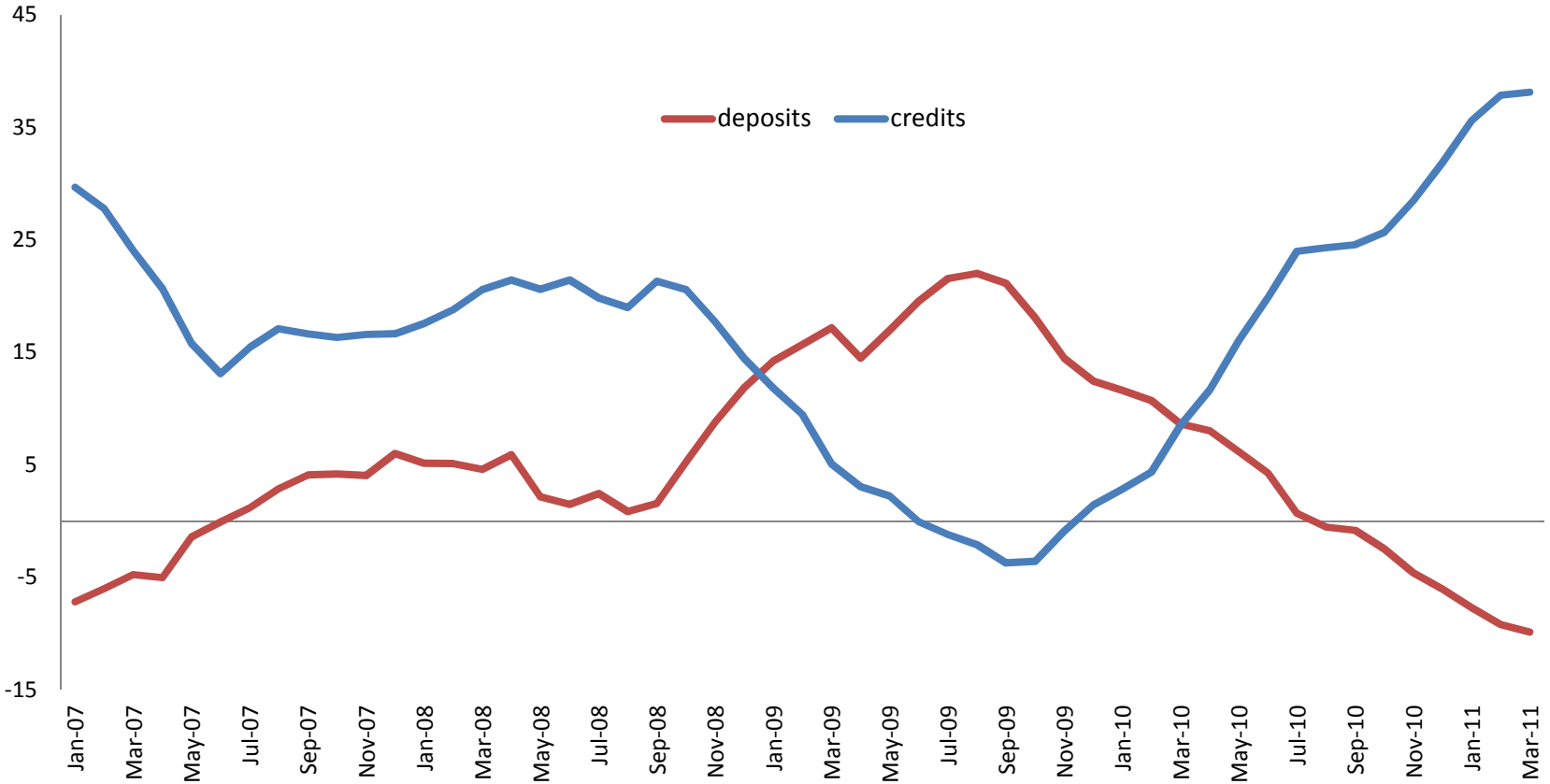
Average of EM Currencies Against USD



Source: Bloomberg

Cheap funding cost led to a rapid expansion in credits and historically low real interest rates discouraged savings in Turkey

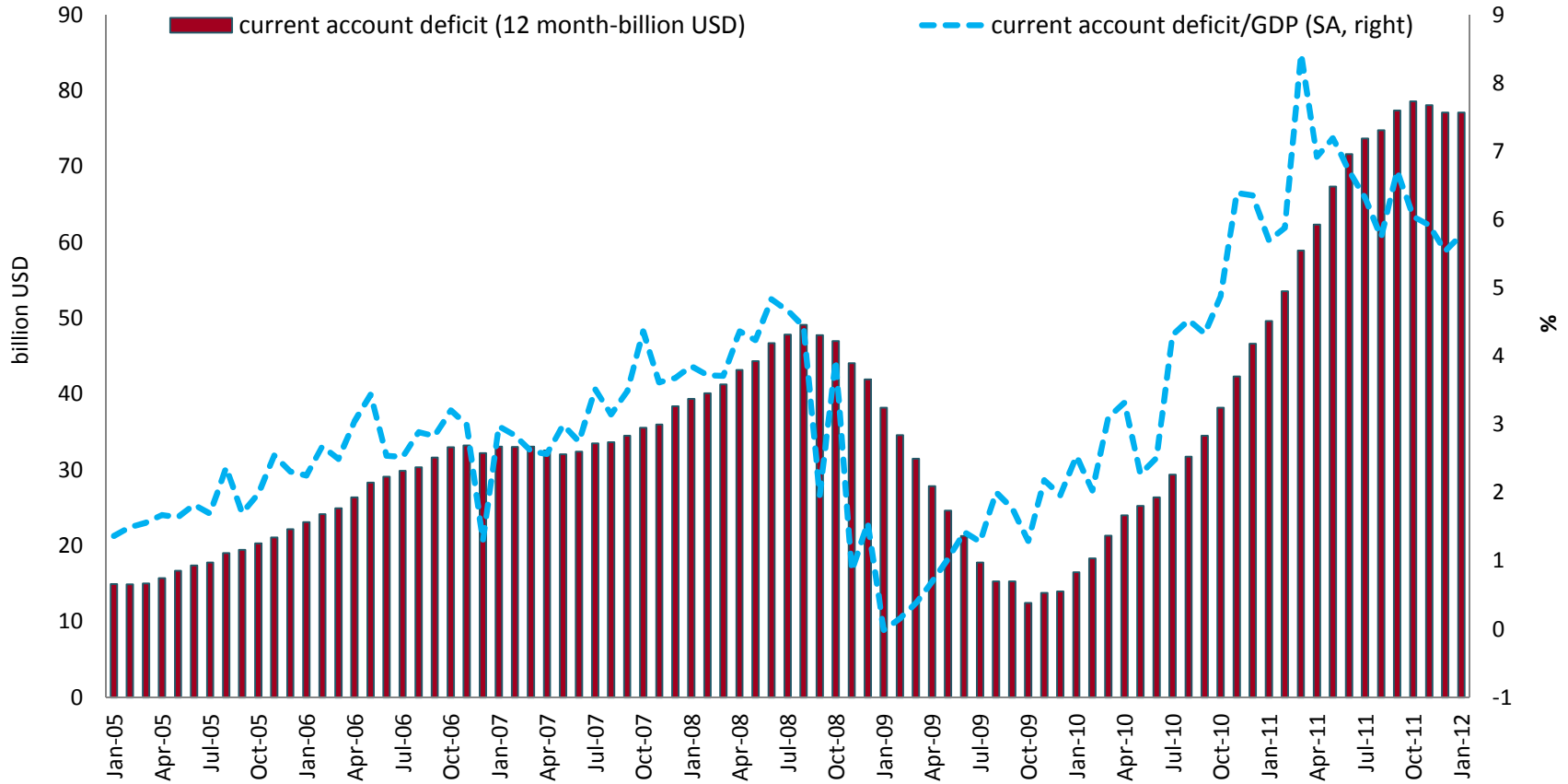
Deposits and Credits
(real- yoy % change)



Source: CBRT

Rapid credit expansion and lower savings led to a boom in current account deficit

Current Account Deficit



Source: CBRT

The challenge of the monetary policy

Rising current account deficit financed by portfolio and short term capital inflows have increased the risk of a suddent stop

Engineering a soft-landing without hampering the price stability objective

Changing view of central banking after the crisis...

- Before crisis:
  - single objective (price stability)
  - single instrument (short term policy rate)

- After Crisis:
  - multiple objectives (price stability, financial stability),
  - multiple instruments (macroprudential measures, liquidity and interest rate policy)

Monetary Policy in Turkey After the Financial Crisis

- Financial Crisis in 2008 has changed the policy environment of the monetary policy.
- A change in the conduct of monetary policy was inevitable.
- CBRT was one of the first central banks shifting to a new policy mix to contain the adverse effects of the financial crisis

Modifying the conventional IT framework

- Explain to public: Supplementary objective is financial stability

- Enrich the set of policy instruments

To reach the final objective: Rebalancing the economy through a slowdown in credit growth and a realignment of the exchange rate

CBRT policy toolkit

- One week repo rate
- TL required reserve ratios
- FX required reserve ratios
- Interest rate corridor
- FX liquidity facilities
  - FX purchasing and selling auctions
  - Adjustments in the FX liquidity provision facilities
  - Changes in the export rediscount facilities

Two pillars of the rebalancing strategy

- Keep short term interest rates as low as possible and use interest rate corridor to discourage short term capital flows

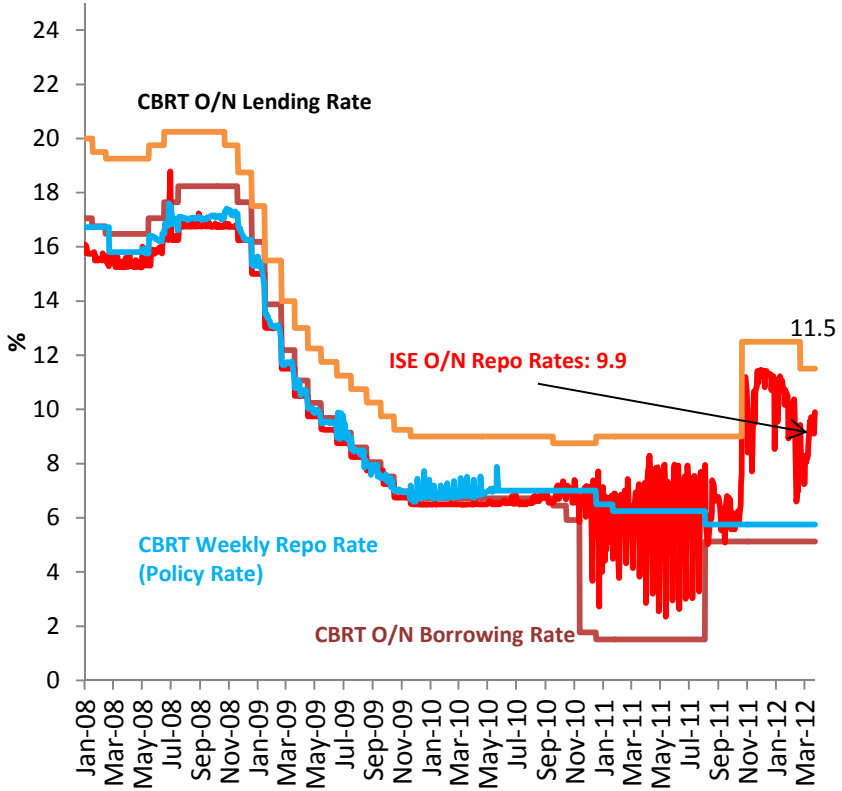
Orderly realignment of exchange rate

- Tighten through macroprudential instruments to curb credit growth and domestic demand (in accordance with other authorities)

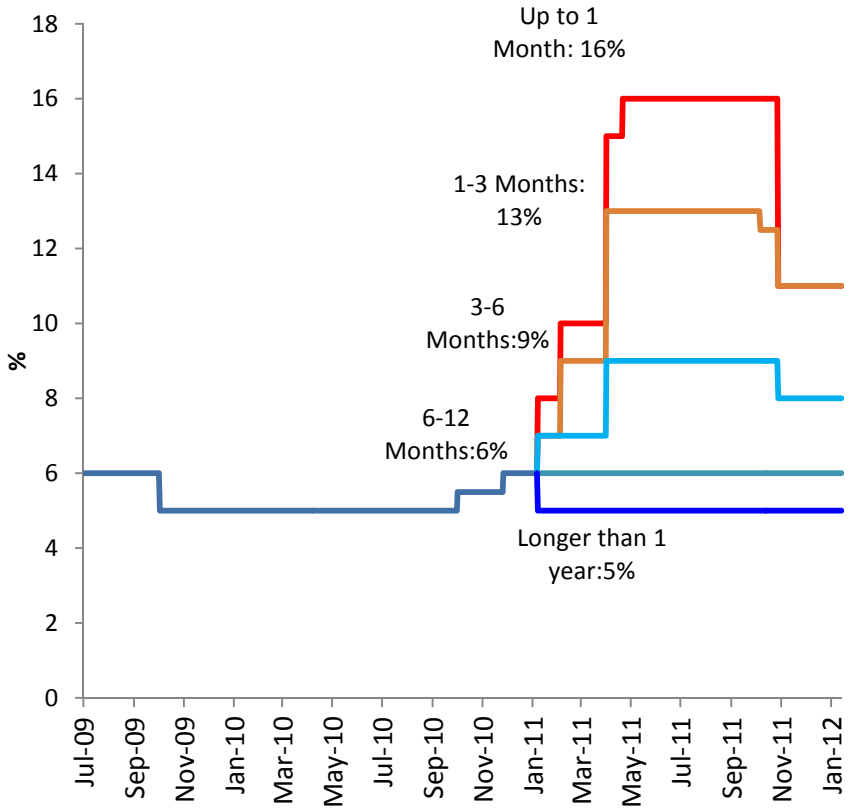
Reduce current account deficit to sustainable levels

Interest rate corridor and RRR were used effectively after November 2010

Interest Rate Corridor



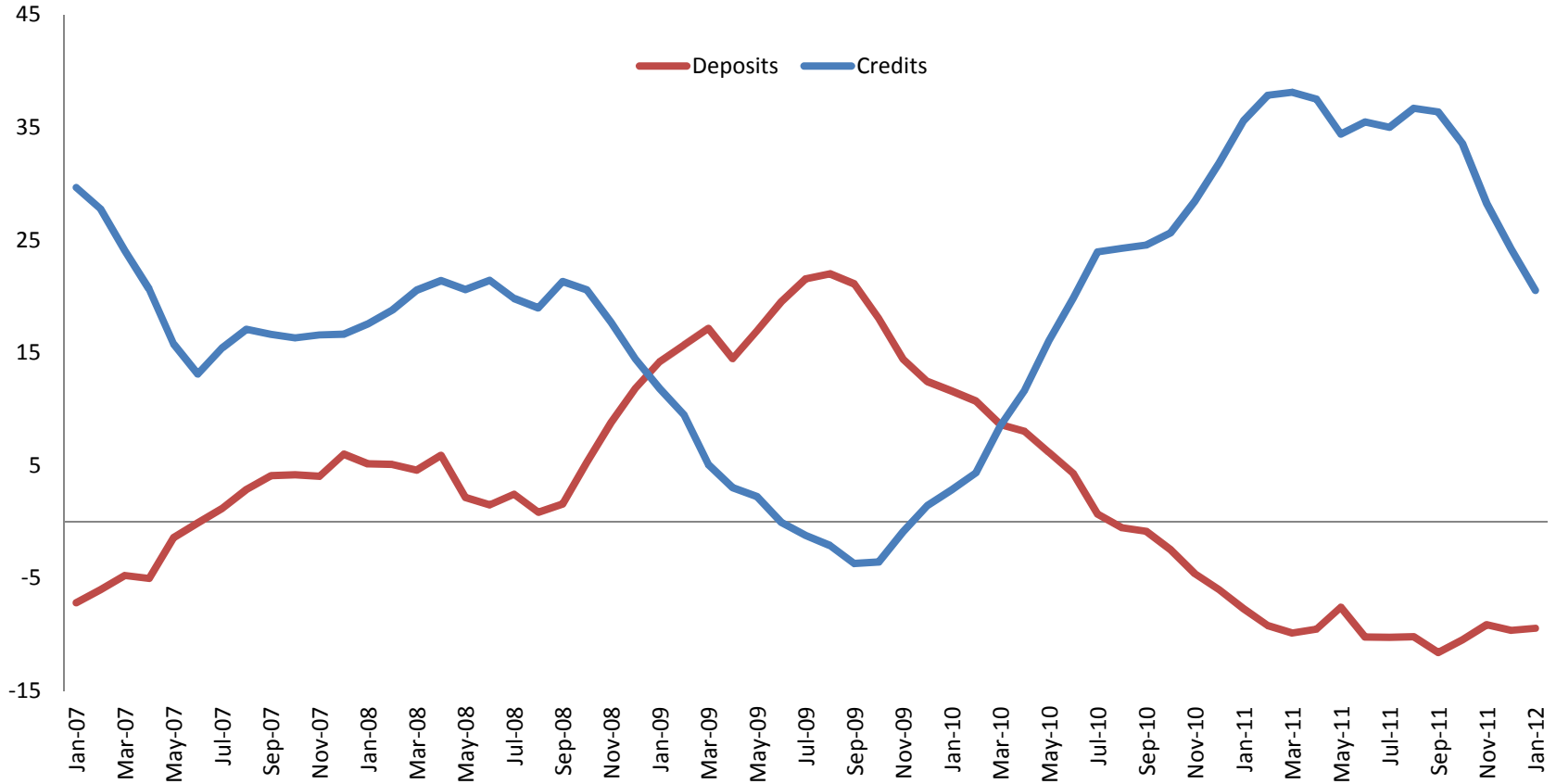
Required Reserve Ratios



Source: CBRT

Macroprudential tightening curbed the credit growth

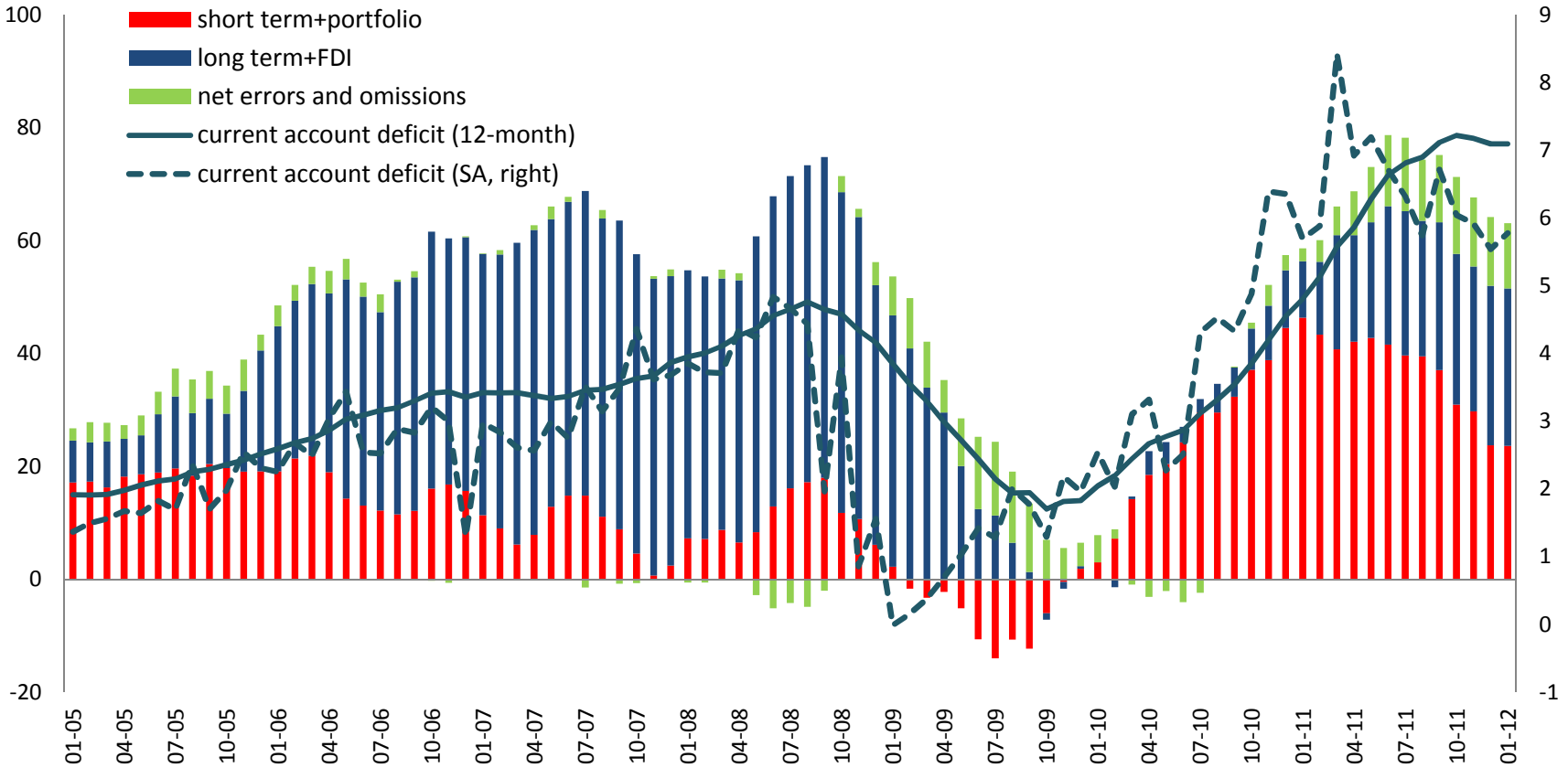
Deposits and Credits After the Macroprudential Tightening (real- yoy % change)



Source: CBRT

Macroprudential tightening has helped to improve the quality of financiang resources of CA deficit

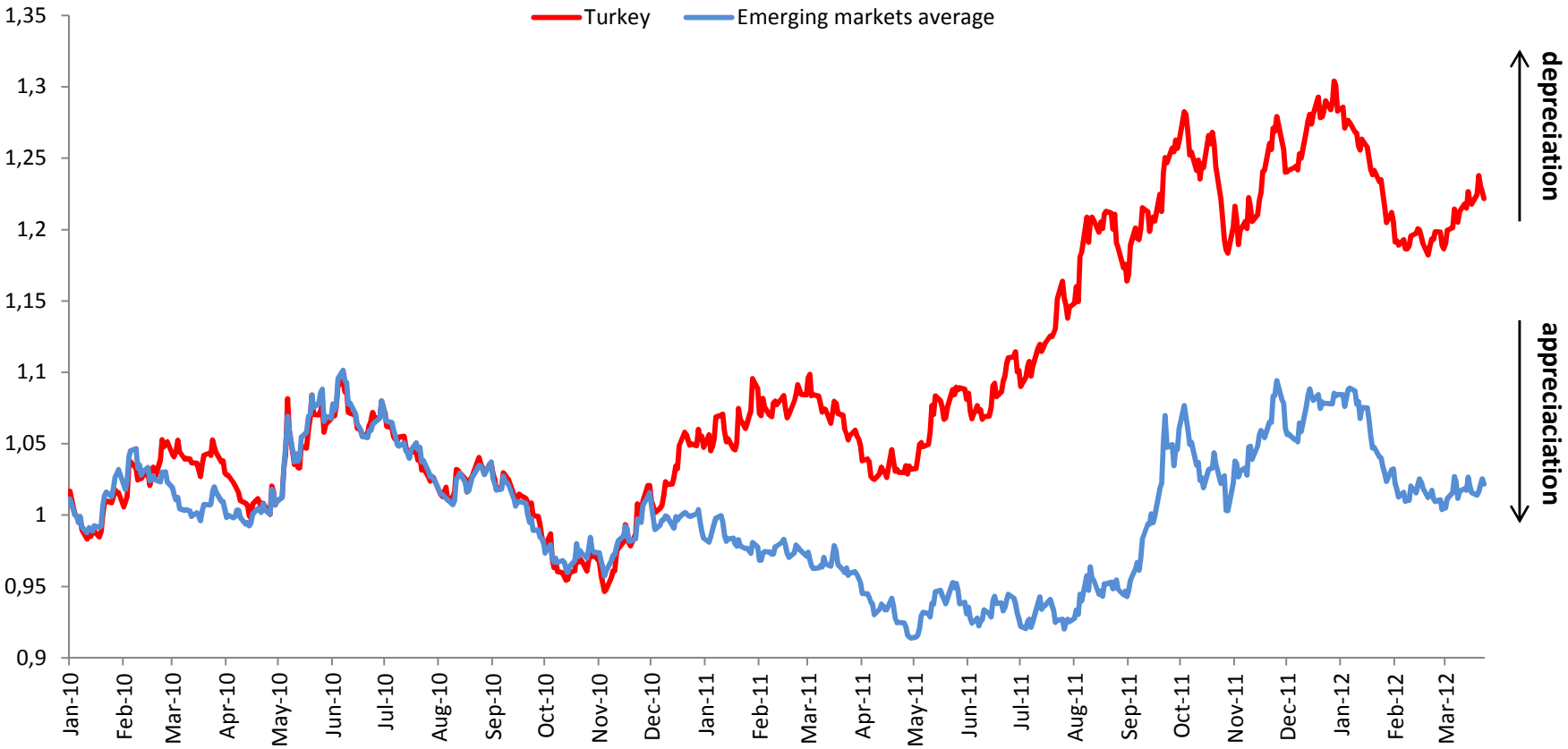
Current Account and Financing Resources



Source: CBRT

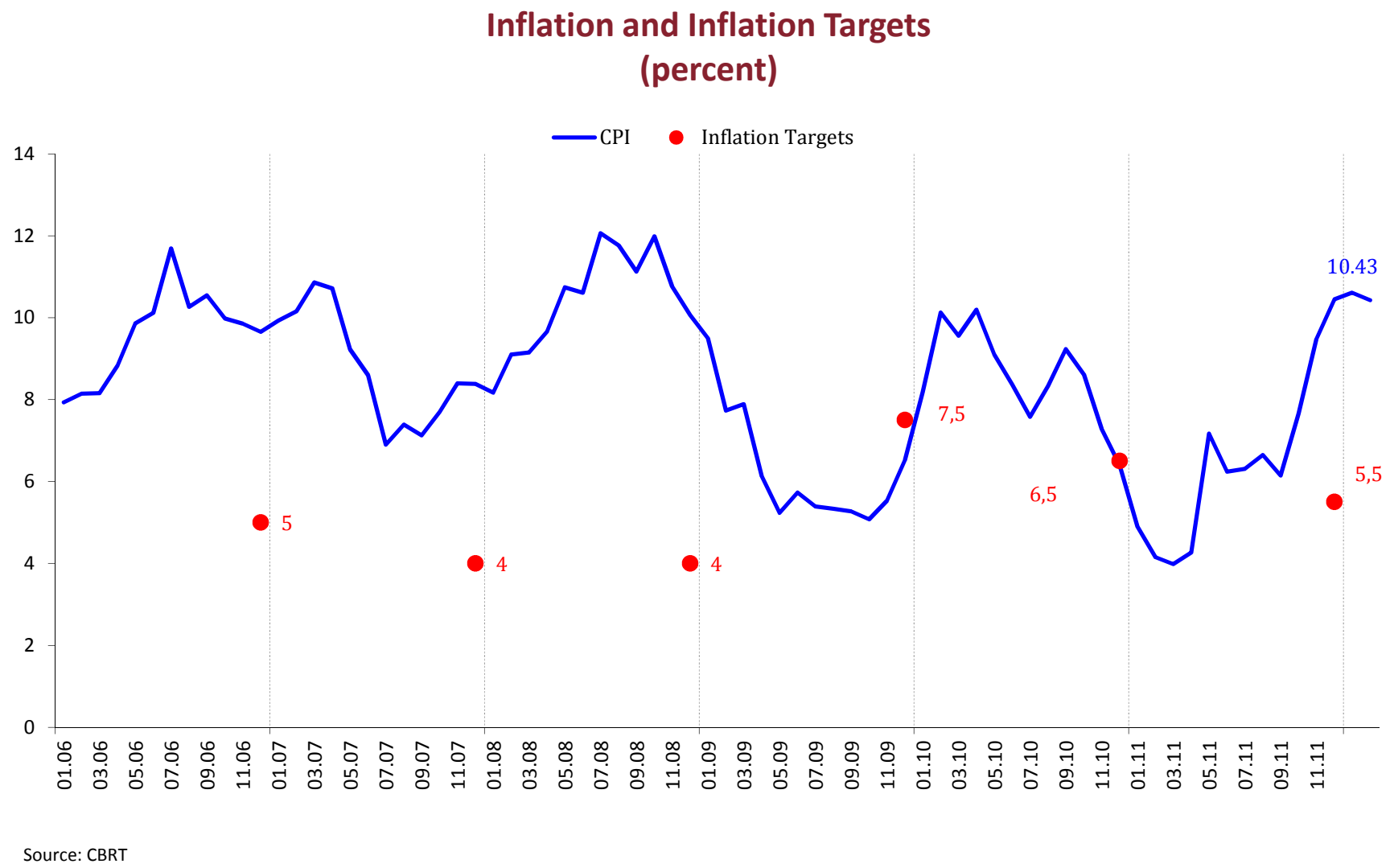
Turkish Lira depreciated more than expected…

Turkish Lira and EM Currencies Against the U.S. Dollar



Source: CBRT

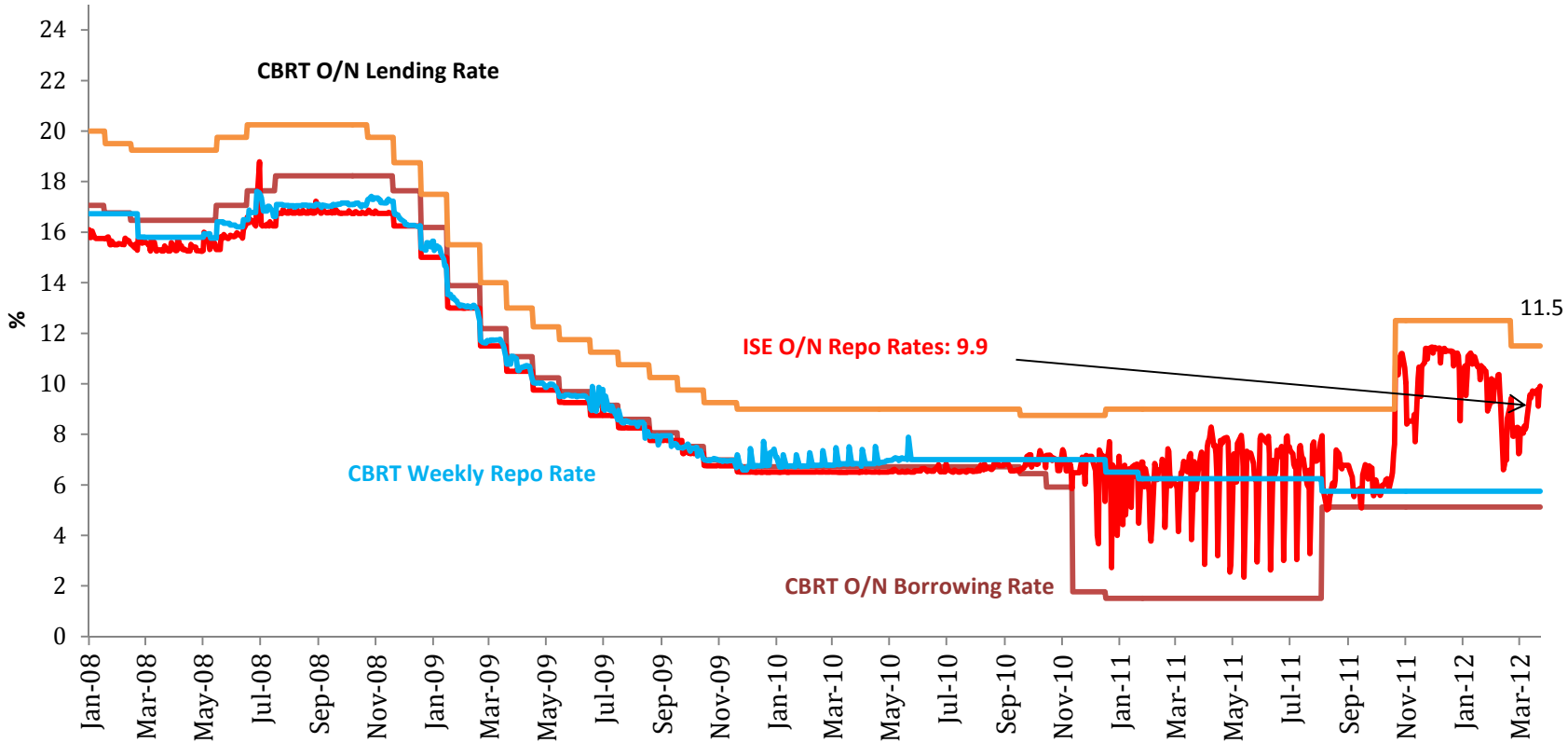
Exchange rate pasthrough, rising administired and energy prices led to an increase in inflation



Source: CBRT

In October 2011 monetary tightening needed, interest rate corridor was reversed…

Interest Rate Corridor



Source: CBRT

Enough FX liquidity was provided to the market: In 2011 and 2012 CBRT has sold 9.6 billion USD

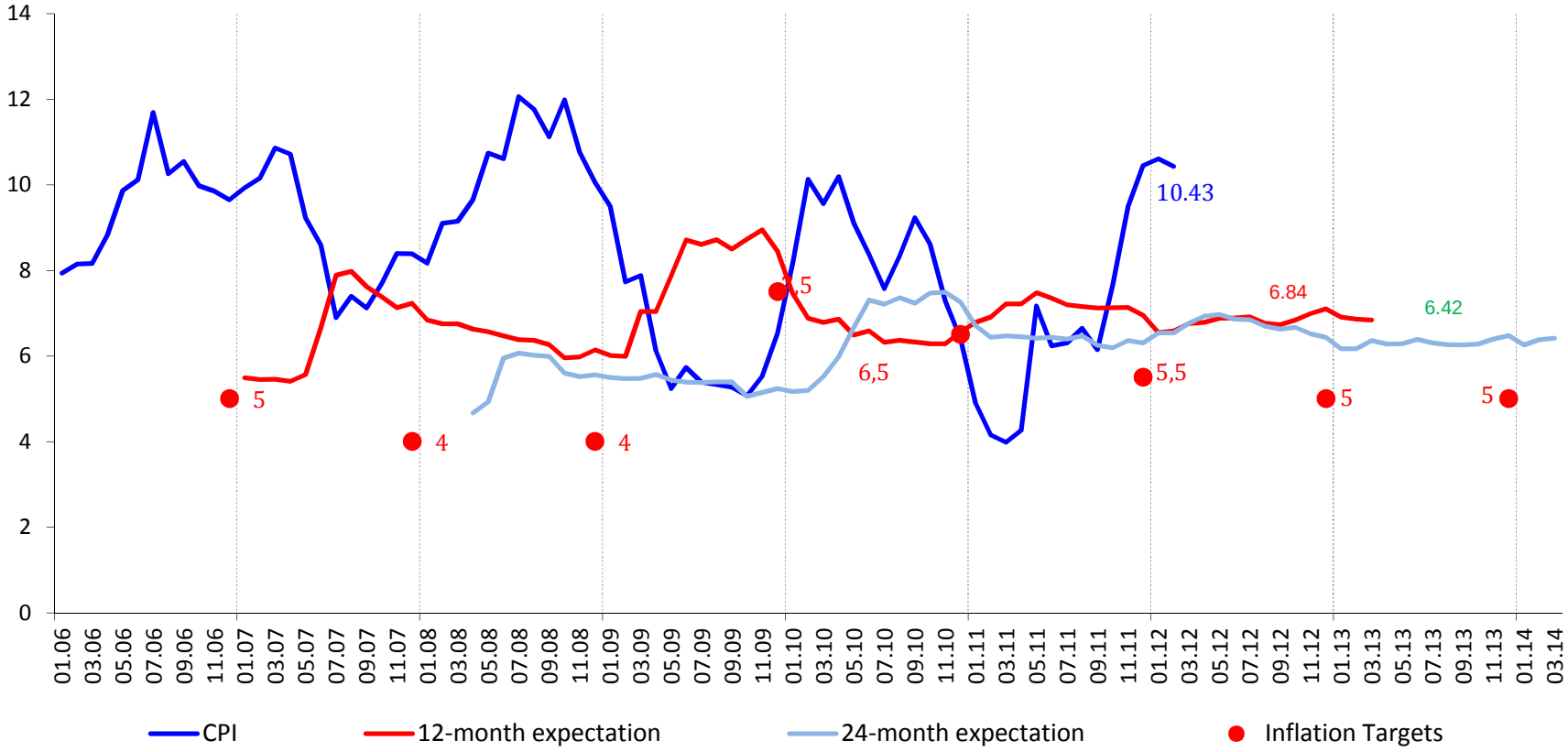
FX Reserves and FX Buying and Selling Auctions

CBT's Gross FX Reserves were USD 78.9 billion as of March 16, 2012					
The CBT's FX Purchases and Sales (as of March 09, 2012, there is no FX auction since January 24)					
Year	FX Buying Auctions	FX Selling Auctions	Buying Intervention	Selling Intervention	Total net FX Buying
2002	795		16	12	799
2003	5,652		4,229		9,881
2004	4,104		1,283	9	5,378
2005	7,442		14,565		22,007
2006	4,296	1,000	5,441	2,105	6,632
2007	9,494				9,494
2008	7,585	100			7,485
2009	4,314	900			3,414
2010	14,895				14,895
2011	6,450	11,210		525	-7,150
2012	0	1,450	0	1,006	-2,456
Total	**65,027**	**13,210**	**25,534**	**2,651**	**70,379**

Source: CBRT

Inflation expectations remain stable due to monetary tightening

Inflation and Inflation Expectations
(percent)



Source: CBRT

Policy Lessons:

- Post crisis dynamics show that financial stability is important as much as inflation

- The CBRT has formulated and implemented a new strategy to deal with macro financial risks posed by extraordinary global circumstances.

- The new policy mix has been effective in rebalancing the economy while controlling inflation expectations.

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MERKEZ BANKASI

THE RISING ROLE OF THE EMERGING MARKETS IN THE WORLD ECONOMY: THE CASE OF TURKEY

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CENTRAL BANK OF THE REPUBLIC OF TURKEY
March 2012