

INFLATION OUTLOOK

The sudden contraction in aggregate demand and the fall in commodity prices since the last quarter of 2008 has led to a sharp decline in inflation rates all over the world. In Turkey, a similar trend has also been observed in this period, and CPI inflation has edged down over the last three quarters. As of June, inflation remained well below 6.8 percent, which is the lower limit of the uncertainty band set around the target path.

In August, measures of underlying core inflation remained subdued and inflation went down to 5.33 percent year-on-year. At a closer look, the annual rate of increase in prices of services continued to fall steadily, and annual inflation in the unprocessed food category decreased mainly on account of slowing fruit and vegetable prices. In goods excluding energy and food, annual inflation edged up modestly owing to the more modest August discounts on clothing compared to a year earlier, the rise in the prices of tobacco products, and price hikes in some durable goods. It is observed that cumulative drops in commodity prices over the last year have exerted downward pressure on domestic inflation starting from the last quarter of 2008, particularly through processed food and energy prices.

Anticipating that inflation would decrease sharply following the last quarter of 2008, the Central Bank of Turkey (CBT) focused on alleviating the adverse impact of the global crisis on the domestic economy. The CBT has lowered policy rates totaling 900 basis points since November 2008, more than any other emerging markets central bank operating within an inflation targeting framework. Data released on inflation and economic activity since the inception of the rate cutting cycle and the favourable course of risk indicators have vindicated the preemptive monetary policy of the CBT, and strengthened the impact of policy decisions on expectations, bringing government bond yields to historically low levels.

In the coming period, demand uncertainty and the low level of capacity utilization are expected to continue to weight down on investment and employment, while high unemployment rates would suppress domestic demand going forward. The continuity of the global problems and the absence of positive signals for recovery in developed economies have suggested that external demand conditions will remain weak for the foreseeable future. Therefore, it is expected that, the support of the aggregate demand conditions on the downward trend of inflation will continue in the medium term.

To find out more: <http://www.tcmb.gov.tr> (Governor's Remarks)

Inflation Forecasts

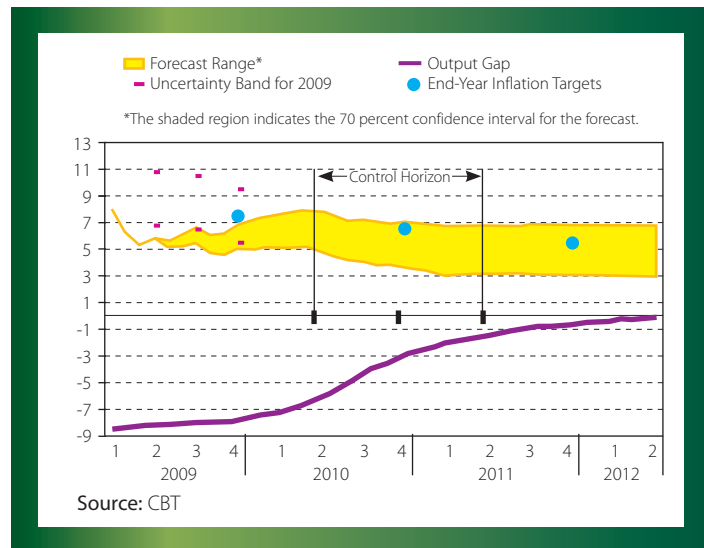


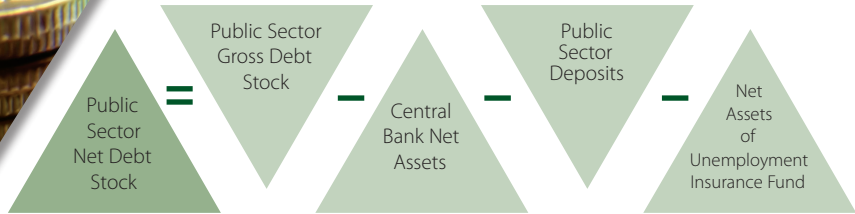
Table 1: Base Scenario

Assumptions	Interest Rate Response	Inflation Forecasts*
<ul style="list-style-type: none"> Oil Prices: Average 60 USD per barrel for 2009, and 70 USD in 2010 and thereafter. Food inflation: 7.5 % at end-2009 and 6 % for the following years Gradual increase in imported input costs World interest rates remain low for an extended period of time. Adopting a medium-term fiscal program to establish fiscal discipline 	Some further easing in the near term, and then constant policy rates until the end of 2010.	<ul style="list-style-type: none"> End-2009: between 4.9 % and 6.9 %, (mid point: 5.9 %) End-2010: between 3.7 % and 6.9 %, (mid point: 5.3 %) End-2011: 4.9 % Mid-2012: 4.8 %

*With 70 % probability

PUBLIC NET DEBT STOCK

Public net debt stock indicates the total debt of the public sector at given time. In order to perceive risk factors precisely, in the analysis of public net debt stock, the financial liabilities of the public sector should be taken into account as well as its assets. The methodology used to calculate public net debt stock can be summarized as follows:



In economics literature, the sustainability of public debt stock is defined as maintaining the ratio of public debt stock to gross domestic product (GDP) at an accepted level in the long term. As one of the indicators of strength of an economy, keeping public debt stock at a sustainable level is also a significant determinant of inflation and growth dynamics.

In Turkey, as a result of the fiscal discipline maintained by the economic programme implemented after the crisis in 2001, the public sector borrowing requirement and the debt rollover ratio decreased owing to the increase in borrowing maturity. Hence the public debt burden was eased and interest rates dropped significantly. There has been a considerable recovery in the public debt stock.

As presented in Table 1, after the rapid increase in the ratio of total net debt stock to GDP to 66 percent in 2001, a gradual decrease was observed and it came down to 28 percent in 2008. Also there was a rapid increase in the ratio of net external debt to GDP in 2001, but the ratio decreased remarkably by the end of 2008. On the other hand, the ratio of net domestic debt stock to GDP remained almost constant at around 30 percent.

Table 1: Public Net Debt Stock / GDP

	2000	2001	2002	2003	2004	2005	2006	2007	2008
Net external debt / GDP	14%	28%	25%	17%	13%	6%	4%	1%	2%
Net domestic debt / GDP	29%	39%	36%	38%	36%	35%	30%	28%	26%
Total net debt stock / GDP	43%	66%	61%	55%	49%	42%	34%	29%	28%

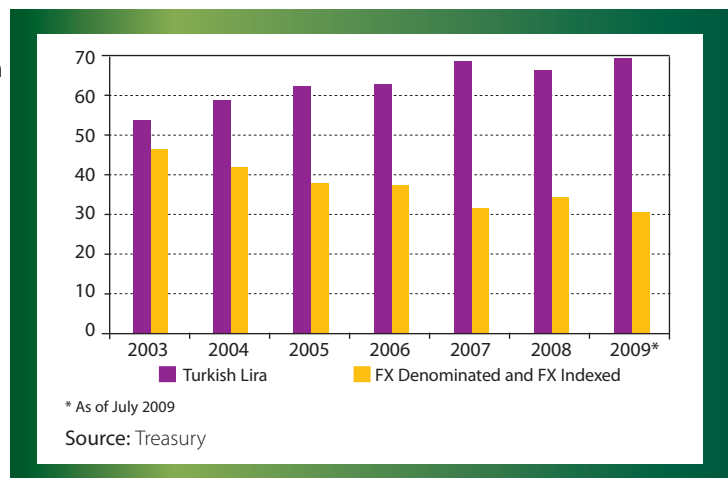
Source: Treasury

One of the main reasons of downward change in the debt stock ratio has been the decline in the share of FX denominated and FX indexed debt in the outstanding total debt of central government in recent years. The increase in the outstanding debt figures was mainly due to the increase in the net domestic debt.

On the other hand, developments in the exchange rate and the increase in the external debt had limited effects.

The sustainability of public finance and lowering public debt stock play important role in the decline of real and nominal interest rates to historically low levels.

Composition of Central Government Debt Stock (%)



INTERNATIONAL SEMINAR ON THE FINANCIAL CRISIS AND ITS IMPACT ON RESERVE MANAGEMENT AT CENTRAL BANKS

The CBT organized an international seminar on "The Financial Crisis and Its Impact on Reserve Management at Central Banks" on May 19-22 at Naim Talu Training, Seminar and Recreation Facility in İzmir. At the seminar in which authorities from the World Bank and 47 officials from Afghanistan, Albania, Azerbaijan, Bosnia-Herzegovina, Bulgaria, Algeria, Morocco, Iran, Montenegro, Libya, Mongolia, Poland, Serbia, Syria, Moldova, Slovakia, Ukraine and Tunisia participated, the officials from the World Bank made presentations and participants shared their country experiences regarding reserve management practices.



OPEN LETTER

The inflation stood at 5.73 percent as of June 2009 breaching the lower limit of the uncertainty band, which was set at 6.8 percent for the end of the second quarter. The CBT wrote an "open letter" accompanied with the Inflation Report, that explains the reasons why inflation exceeded the lower limit of the uncertainty band, assesses the measures taken to bring inflation back in line with the medium-term targets, and presents the medium-term inflation outlook. The CBT sent the letter to the Government and announced the letter to the public on July 29, 2009.

INFLATION REPORT 2009-III

The Inflation Report 2009-III was released via a press conference with the presentation made by Governor Yılmaz on July 29, 2009. The Report summarizes the economic framework of monetary policy decisions, examines recent macroeconomic developments on a local and global scale, and presents updated medium-term inflation forecasts in the framework of economic developments in the last three months. The Report also includes five information boxes which focus on global economic recession and economy policies, monitoring main trends in exports, the effect of the country risk profile on policy rates during the crisis, effects of the global crisis on fiscal balances of developing and developed countries and impacts of temporary tax adjustments on consumer prices.

To find out more: <http://www.tcmb.gov.tr> (Periodic Publications)



IMF – WORLD BANK ANNUAL MEETINGS

The Annual Meetings organized by the IMF and the World Bank Group bring central bankers, ministers of finance, private sector executives, and academics together to discuss issues of global concern such as world economic outlook, economic development, aid effectiveness and poverty reduction.

The Annual Meetings are usually held for two consecutive years at the IMF and World Bank headquarters in Washington DC, and every third year in another member country. The 2009 Annual Meetings of the Boards of Governors of the World Bank Group and the IMF will be held in Istanbul, Turkey on October 6-7, 2009. This will make Turkey the only country to host the Annual Meetings twice. The first time was in 1955, also in Istanbul. The Annual Meetings will be preceded by meetings of the International Monetary and Financial Committee (IMFC), and the Development Committee, on October 4-5. About 13,000 people are expected to attend the Annual Meetings this year.



To find out more: <http://www.imf.org/external/am/2009/index.htm>

<http://www.istanbul2009turkey.org/istanbul2009/index.php?module=IWB>

WORKING PAPERS

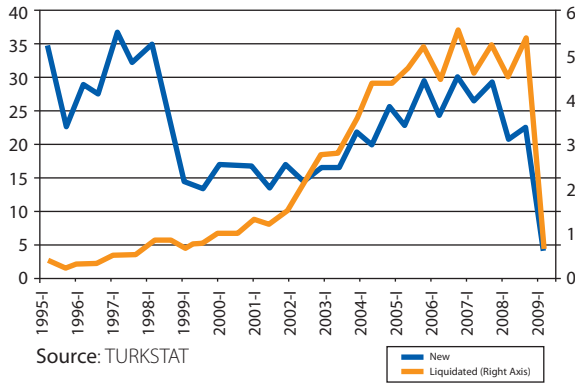
- Monetary Shocks and Central Bank Liquidity with Credit Market Imperfections (Pierre-Richard Agénor, Koray Alper, Working Paper No. 09/06, July 2009)

To find out more: <http://www.tcmb.gov.tr> (Publications / Research Papers)

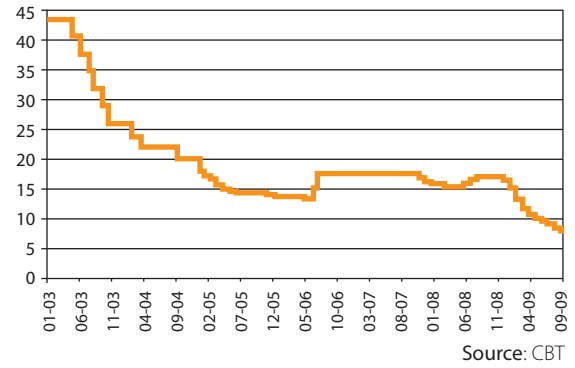


AT A GLANCE

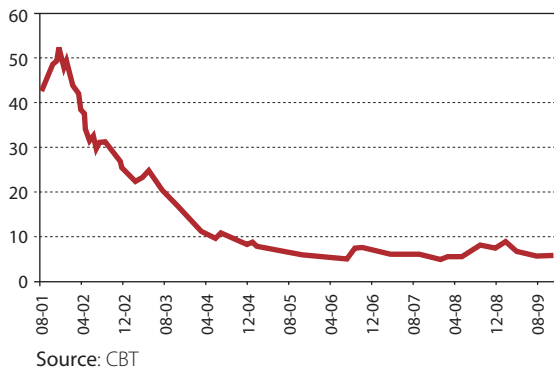
Newly Established and Liquidated Firms (6-month cumulative, thousands)



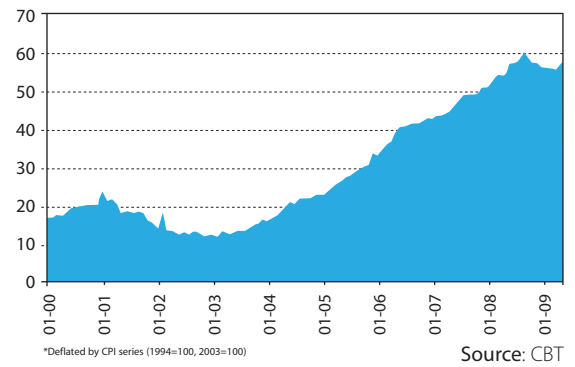
CBT Overnight Interest Rates (Bid) (Simple, %)



CPI Expectations Over The Next Twelve Months (%)



Banking Sector Domestic Loans* (January 2000=100)



DATA RELEASE CALENDAR

The Official Statistics Programme, based on the Statistics Law of Turkey, has been prepared for a 5-year-period in order to determine the basic principles and standards dealing with the production and dissemination of official statistics, and to produce reliable, timely, transparent and impartial data required at national and international level. Within the framework of studies on the Official Statistics Programme 2007-2011 prepared by the Turkish Statistical Institute (TURKSTAT), the "Data Release Calendar" with publication dates of the data produced by the CBT has been available on the website of the CBT since 2007. The Data Release Calendar of other data groups under the Official Statistics Programme can be accessed through the website of TURKSTAT under the heading "National Data Release Calendar".

To find out more: <http://www.tcmb.gov.tr> (Data/Data Release Calendar)
<http://www.turkstat.gov.tr/ingtakvim/tkvim.zul>

CBT Interest Rates*	Borrowing	Lending	Central Bank Foreign Exchange Reserves (As of 28 August 2009, Billion USD)	69.82
Overnight (%)	7.75	10.25	CPI (Annual % Change, August 2009)	5.33

* As of 19 August 2009.

Published quarterly by the Central Bank of the Republic of Turkey Issue: 15 September 2009

Owner on behalf of the Central Bank of the Republic of Turkey and Managing Editor
Hüseyin Zafer

Printed in
Central Bank of the Republic of Turkey Banknote Printing Plant Department

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Distributed free of charge

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