

October 26, 2010

Ali BABACAN
Minister of State and Deputy Prime Minister
ANKARA

The Central Bank of Turkey (CBT) has been implementing an inflation targeting regime since the beginning of 2006. Under this regime, the CBT is accountable for achieving its main goal of price stability, and for the policies implemented to pursue this goal. Within this framework, as stipulated by Article 42 of the Law, the accountability process is triggered when there is a significant deviation or potential deviation from the established inflation targets.

The inflation target for end-2010 was jointly set with the Government at 6.5 percent. The CBT policy document "Monetary and Exchange Rate Policy in 2010", issued on December 10, 2009 stated that if the absolute value of the difference between the actual inflation rate and the target rate exceeds 2 percentage points at the end of any quarter, the accountability mechanism would be enforced. In this context, it was stated that the CBT, in the case inflation falls outside the band within that year, would explain through the quarterly Inflation Report the reasons for the breach, and the measures that would be taken to ensure that inflation would revert to the pre-established targets. Should inflation fall outside the uncertainty band at the end of the year, the CBT would write an open letter to the Government.

The inflation outturn as of September 2010 was 9.24 percent, breaching the upper limit of the uncertainty band, which was set at 8.5 percent. Accordingly, attached, for your consideration, is the latest Inflation Report issued on October 26, 2010, which explains the reasons for the breach of the target, and the strategy adopted by the CBT to bring inflation back in line with the medium-term targets.

Yours Sincerely,

CENTRAL BANK OF TURKEY
Head Office

Durmuş Yılmaz
Governor

Erdem Başçı
Deputy Governor