

II. Macroeconomic Outlook

Uncertainties have been decreasing since the second half of 2020 due to the gradual lifting of social isolation measures taken to tackle with the pandemic, the policy packages implemented during the pandemic, and vaccination programs. The expansionary changes to monetary policies, which started to be introduced on March 2020, are mostly in place. On the back of the global recovery and positive growth outlook, there have been net portfolio flows towards EME equity markets as of October 2020, while the rise in long-term bond yields in advanced economies has been effective in the fluctuations in portfolio flows towards EMEs.

The course of the pandemic, developments concerning Covid-19 vaccines and uncertainties regarding the duration of measures taken against the pandemic, significant discrepancies among countries with respect to growth, the reflections of increased credit risk, and elevated level of global indebtedness that significantly increased during the pandemic are the leading vulnerability factors with respect to financial stability. Thus, uncertainties about the economic outlook continue because of the lingering uncertainties regarding the course and effect of the pandemic as well as vaccination programs. In this framework, the duration of measures, timing of exit from measures, management of trade-offs stemming from this process and discrepancies among countries about vaccination will be determining factors on the growth outlook. The discrepancies among countries with respect to economic growth as well as uncertainties about monetary policies of advanced economies may lead to volatilities in capital flows towards EMEs.

The strong course in domestic economic activity continues, underpinned by domestic and external demand. This improvement was mainly driven by the acceleration in industrial production and global trade, while the recovery in the services sector is limited by developments linked to the pandemic and global travel restrictions that are still partly in place. The current account deficit is adversely affected not only by strong domestic demand conditions but also the rise in imports prices. Meanwhile, the strong uptrend in exports, the significant decline in gold imports, and the slowdown observed in loans on the back of tightening in financial conditions support the projected recovery in the current account. Measures taken to preserve employment have curbed adverse impacts of the pandemic on the labor market, while the uptrend in labor force participation rate has been pushing the unemployment rate up over the past few months. The rise in international commodity prices, demand and cost factors, supply constraints in certain sectors and the elevated levels of inflation expectations have been affecting pricing behavior and the inflation outlook.

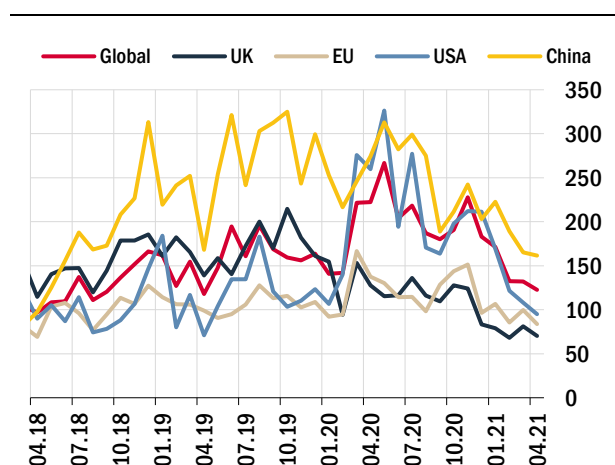
II.1 International Developments

Since June 2020, uncertainties pertaining to global growth have been decreasing owing to gradual easing of lockdown measures, economic and financial support measures introduced during the pandemic and vaccination programs in many countries (Chart II.1.1). Even if the general trend is downwards, policy uncertainties differ across countries due to the speed of vaccination and the course of the pandemic. Moreover, uncertainty about the global economic policy temporarily increased in October and November 2020 due to the volatilities the US Presidential elections caused in financial markets and the impact of the second wave of the pandemic in some countries.

Expansionary changes introduced in monetary policies starting from March 2020 are still mostly in place globally. In the FOMC meetings held since December 2020, it was emphasized by the US Federal Reserve (Fed) that the monthly asset purchases of USD 120 billion will continue until significant improvement is recorded in achieving the price stability and maximum employment targets. FOMC members expect the policy rate to be close to 0 percent until the end of 2023 (Chart II.1.2). However, in line with the increasing inflation expectations, the market expects that there will be two rate hikes, one in 2022 and another one in 2023.

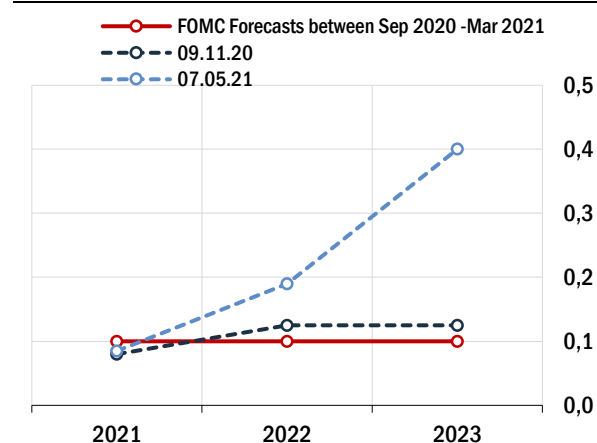
The size of the Pandemic Emergency Purchase Program, which was announced by the European Central Bank (ECB) as EUR 750 billion in March 2020, was updated to EUR 1.85 trillion, with additions of EUR 600 and EUR 500 billion within the scope of the monetary policy decisions of June and December 2020, respectively. It was announced that the program would be terminated in March 2022 at the earliest; however, it may be extended until it is clear that the pandemic is over. Moreover, the monthly asset purchase program of EUR 20 billion continues.

Chart II.1.1: Economic Policy Uncertainty Indices (Index, 2012=100)



Source: Bloomberg Last Observation: 04.21
Note: Indices are not comparable in terms of their levels.

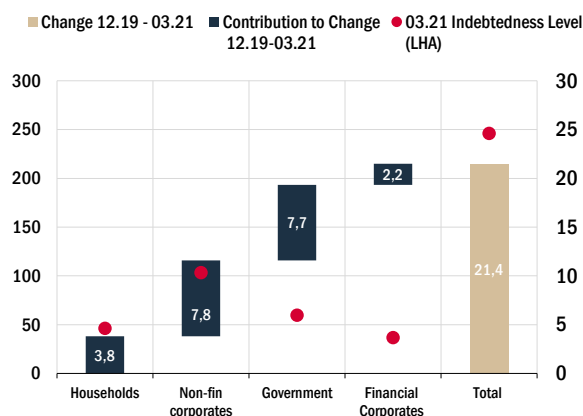
Chart II.1.2: Median Policy Rate Forecasts of FOMC Members (Solid Lines) and Market Expectations (Dashed Lines) (%)



Source: Bloomberg Last Observation: 07.05.21
Note: Dashed lines indicate 30-day Fed fund futures implied rates. Policy rate forecasts of FOMC members remained the same for both September 2020, December 2020 and March 2021 meetings.

Global indebtedness, which has been on an uptrend since the 2008 Global Financial Crisis, has increased significantly due to the abundant liquidity support provided during the pandemic. While a significant part of this increase came from the public sector with the measures taken to support the economy, the corporate sector debt also showed a sharp increase in both advanced and emerging economies. High indebtedness of both the corporate sector and public sector stood out as a vulnerability factor. Facing liquidity squeeze due to the pandemic, lending to corporate sector has increased in EMEs and debt to GDP ratio has increased in all sectors from the end of 2019 until the first quarter of 2021 (Chart II.1.3). The FX indebtedness of EMEs, which decreased due to the regulations introduced after the Global Financial Crisis, continues to remain low, particularly for the households (Chart II.1.4). In 2020 and in the first quarter of 2021, FX indebtedness continued to decrease across all sectors.

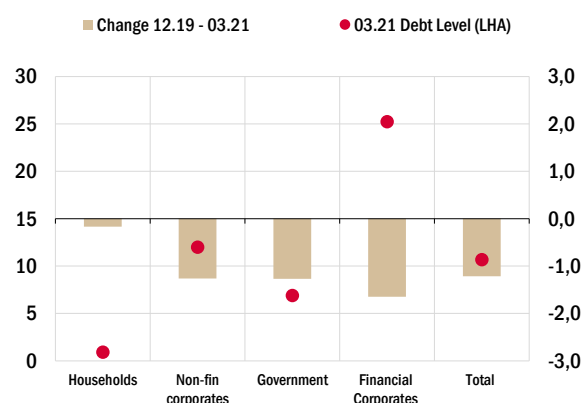
Globally, SMEs and large firms differ in terms of indebtedness and their access to finance. Moreover, the impact of the pandemic differs across sectors. The rise in indebtedness coupled with weak profitability of sectors that are more seriously affected by the pandemic due to restrictions and travel bans, has started to affect the balance sheets and therefore the credit ratings of companies. The ongoing support policies reduce the likely default and insolvency of companies with cash flow problems.

Chart II.1.3: Indebtedness in EMEs (% GDP)


Source: IIF Last Observation: 03.21

Note: The average is calculated based on GDP weights of countries. EMEs: Argentina, Brazil, Chile, China, Colombia, Czechia, Egypt, Ghana, Hong Kong, Hungary, India, Indonesia, Israel, Kenya, Lebanon, Malaysia, Mexico, Nigeria, Pakistan, Philippines, Poland, Russia, Saudi Arabia, Singapore, South Africa, South Korea, Thailand, Turkey, Ukraine and United Arab Emirates.

Data for 2020-Q4 and 2021-Q1 are estimations.

Chart II.1.4: Share of FX in Total Indebtedness of EMEs (% Total Indebtedness)


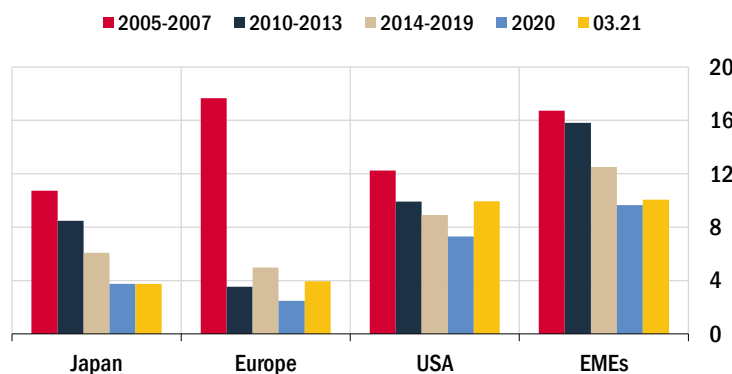
Source: IIF Last Observation: 03.21

Note: EMEs: Argentina, Brazil, Chile, China, Colombia, Czechia, Hong Kong, Hungary, India, Indonesia, Israel, South Korea, Malaysia, Mexico, Poland, Russian Federation, Saudi Arabia, Singapore, South Africa, Thailand, Turkey and Ukraine.

Data for 2020-Q4 and 2021-Q1 are estimations.

As a result of global financial reforms, banks entered the Covid-19 pandemic with strong capital structures and liquidity positions. In the following period, owing to the measures promptly taken by regulatory authorities and central banks, there was no liquidity problem in the sector and a significant erosion in the capital levels of the banks was prevented by the limitations imposed on dividend distributions. Notwithstanding, with the end of extraordinary measures introduced to tackle the pandemic, particularly the regulatory flexibility measures such as loan guarantees and deferral of repayments, the course of global economic activity will be closely monitored in terms of the soundness of the global banking system, and lending appetite regarding the profitability of banks, the financial situation of debtor companies.

The return on equities of the banking sector took up a downward trend since the Global Financial Crisis. The current downward pressure on return on equities was mainly driven by the significant decline in global economic activity, the possible effects of the increased credit risk on asset quality and expectations that the interest rates, already low for a long time, would remain so (Chart II.1.5). Low profitability may adversely affect the cash flow of banks, causing their market values to remain low, and making it difficult to raise capital.

Chart II.1.5: Banks' Return on Equities (%)


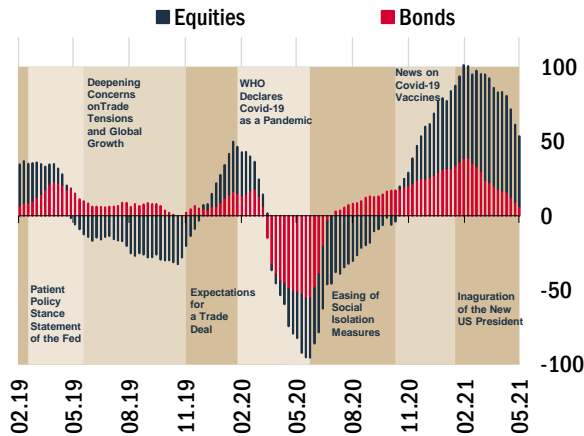
Source: Bloomberg

Last Observation: 03.21

Note: Tokyo Stock Exchange TOPIX Banks Index, Bloomberg European 500 Banks and Financial Services Index, S&P 500 Banks Industry Group Index, MSCI EM Banks Index have been used.

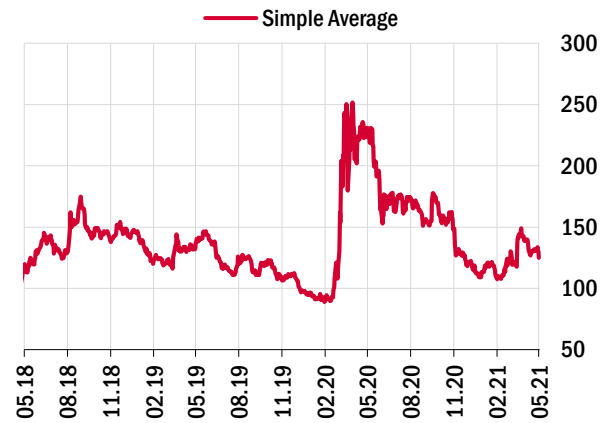
As of October 2020, there have been net portfolio flows towards equity markets on the back of the global recovery and favorable growth outlook (Chart II.1.6). Nevertheless, portfolio movements towards EME bond markets have been fluctuating. These developments were mainly driven by the accelerated increase in long-term bond rates in some advanced economies led by the USA in February 2021. This increase largely reflects the market's expectation for a recovery in the economic outlook and an increase in inflation. In addition to the positive developments regarding vaccination, the comprehensive stimulus package of USD 1.9 trillion commissioned in March by the new US administration that took office on 20 January 2021, also contributed to the shaping of these expectations. In this context, the effect of volatility in bond prices as of mid-February was reflected on EM risk premiums that had shown a downtrend in the previous reporting period (Chart II.1.7).

Chart II.1.6: Weekly Capital Flows to EMEs
(13- Week Cumulative, USD Billion)



Source: EPFR Last Observation: 05.05.21

Chart II.1.7: CDS Premiums in EMEs
(Basis Points)

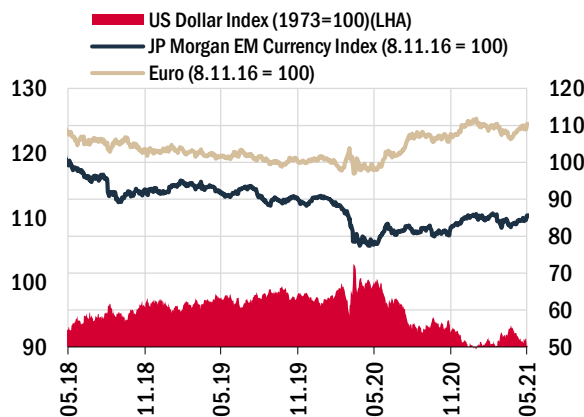


Source: Bloomberg Last Observation: 07.05.21

Note: Emerging economies include Brazil, Czechia, Indonesia, S. Africa, Colombia, Hungary, Poland, Romania, Turkey and Chile.

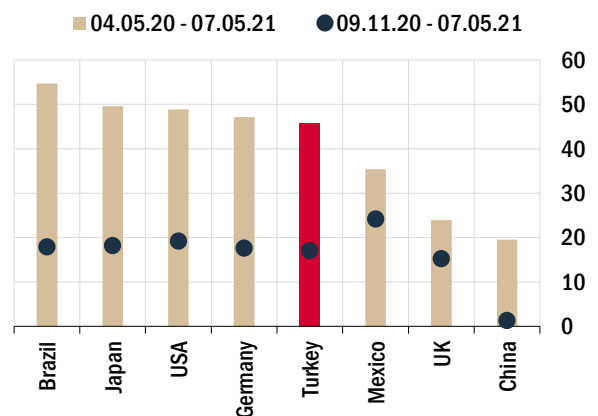
From May 2020 until the end of February 2021, the US dollar depreciated against currencies of major advanced economies (Chart II.1.8). The US dollar index has followed a fluctuating course since March, and this has been reflected on the EM Currency Index in the current reporting period. Stock markets in both advanced and emerging market economies, especially Turkey and peer countries have exhibited a positive performance since May 2020, when quarantine measures started to be phased out (Chart II.1.9). In the last reporting period, stock markets maintained their strong performances.

Chart II.1.8: Exchange Rate Indices (Index)



Source: Bloomberg Last Observation: 07.05.21

Chart II.1.9: Stock Indices (% Change)

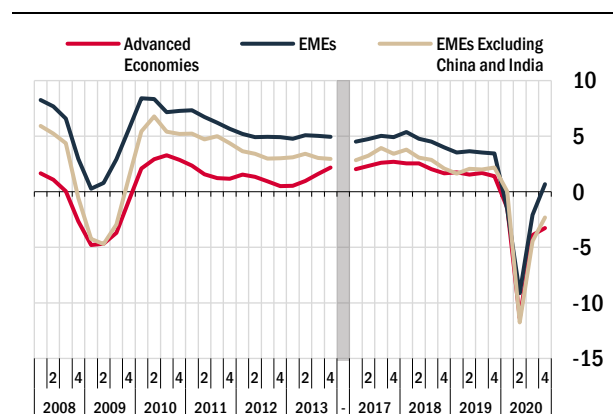


Source: Bloomberg Last Observation: 07.05.21

Note: Turkey - BIST 100, Germany DAX, UK - FTSE 100, Mexico - IPC, Japan - Nikkei 225, China - Shanghai Composite, USA - S&P 500, Brazil - IBOV indices have been used.

In the first half of 2020, global economic activity contracted significantly due to the restrictions taken against the pandemic. With the easing of quarantine measures in May and June 2020 and the introduction of vaccines in the following period, the global economic activity started to recover (Chart II.1.10). The level and speed of recovery varies across countries, while China diverges from other countries in a positive way. Leading indicators of growth also indicate that the recovery will continue in the first quarter of 2021 in both advanced and emerging economies (Chart II.1.11).

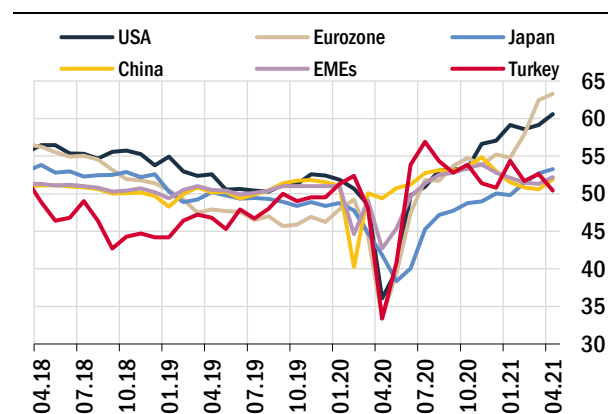
Chart II.1.10: Y-o-Y Growth Rates in Advanced Economies and EMEs (%)



Source: Bloomberg, CBRT Last Observation: 12.20

Note: Advanced Economies: USA, Euro Area, Japan, UK, Canada, S. Korea, Switzerland, Sweden, Norway, Denmark, and Israel. EMEs: China, Brazil, India, Mexico, Russia, Turkey, Poland, Indonesia, S. Africa, Argentina, Thailand, Malaysia, Czechia, Colombia, Hungary, Romania, Philippines, Ukraine, Chile, Peru, and Morocco.

Chart II.1.11: Manufacturing Industry PMI (Index)



Source: Bloomberg, CBRT

Last Observation: 04.21

Lingering ambiguity over the course and impact of the pandemic as well as the vaccination programs cause the uncertainty on the economic outlook to continue. Most of the measures taken since the beginning of the epidemic are still in effect. The liquidity pressures that emerged at the early stages of the pandemic were addressed with comprehensive measures taken on a global and local scale, while large-scale contractions were experienced in economic activity. At this stage, uncertainties regarding the pandemic continue, and the discrepancies between countries in terms of the duration of the measures, the timing of the exit from the measures, the management of trade-offs that this process will create, and vaccination rate will determine the economic outlook. The divergence between countries with respect to economic growth and uncertainties about monetary policies of advanced economies may cause volatility in capital flows towards EMEs. In this whole process, it is important to monitor carefully inter-sectoral and cross-border connections.

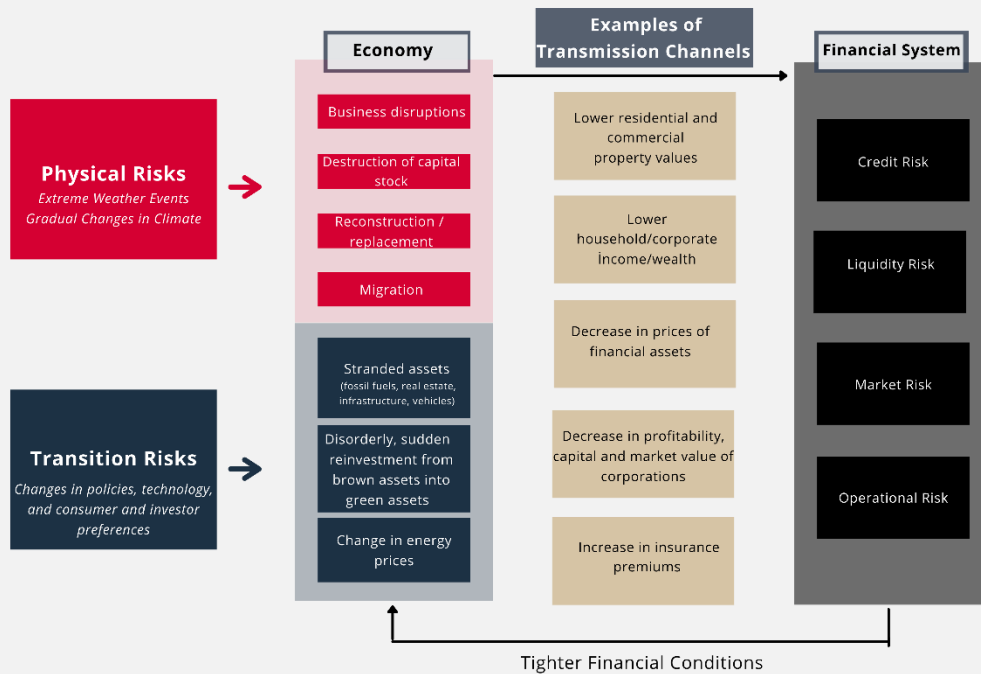
In the medium and long term, the increasing role of non-bank financial intermediation, likely risks of climate change on financial stability (Box II.1.I), operational vulnerabilities and cyber risks during the adaptation period to digitalization have been ranking higher in the financial markets agenda.

Box II.1.1

Climate-Related Financial Risks and Green Finance

International financial institutions consider climate change as a structural problem that entails various risks to the financial system. The risks to financial stability from climate change are typically divided into two main areas as physical risks and transition risks (Graph II.1.1.1). These risks can affect the values of financial assets and liabilities and they may affect financial systems in various ways primarily by credit risk and market risk. Physical risks denote risks to financial stability due to sudden weather events like floods and hurricanes stemming from or likely to stem from climate changes and gradual changes in climate such as droughts or rising sea levels. For example, increase in the frequency and severity of natural disasters may cause a decrease in the values of residential and commercial real estates, and thus a decrease in incomes of households and firms. This in turn may affect the financial sector by means of increased default risk in loan portfolios and a decrease in collateral values. The intensity of physical risks can also affect the pricing capacity of insurance companies, and insurance premiums can increase to cover more frequent and higher claims. Meanwhile, assets that cannot be insured due to high premiums may increase the credit risk of banks if they are shown as collateral. A decrease in financial asset prices may cause losses on the balance sheets of banks, other financial institutions and asset owners.

Graph II.1.1.1: Financial Risks Stemming from Climate Change



Source: NGFS, IMF, BCBS, CBRT

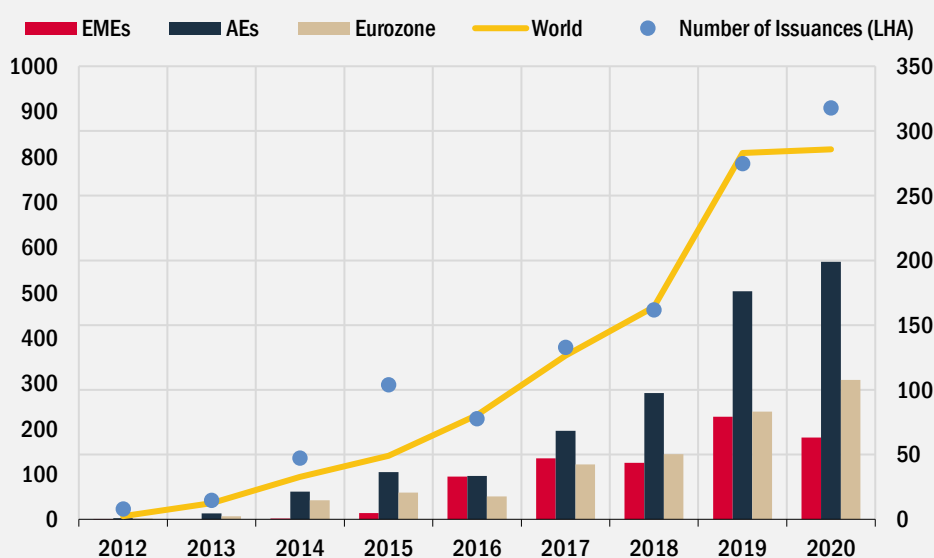
Transition risks, on the other hand, include risks that a disorderly transition to low-carbon economy will cause to financial stability. These risks stem from reallocation of resources in the economy and thus may lead to structural changes. Today, an important example of transition plans to a low-carbon economy is the European Union's growth strategy called the European Green Deal, which aims to make Europe the first carbon -neutral continent by eliminating or offsetting greenhouse gas emissions (i.e. achieve net zero emissions) by 2050. Changes in the scope of European Green Deal may affect our country mainly in the fields of industry, commerce and finance. Thus, under the coordination of the Ministry of Trade, Turkey's public institutions have been working to manage transition risks. Meanwhile, many other countries have also been working to ensure an orderly transition to a low-carbon economy, to reduce and manage risks of the transition. While it is likely that companies with low carbon-intensive technology will be positively affected by this process, other companies may experience great losses. In the process of technological change and adaptation process of policies to fight against climate change, these companies may face a decrease in profitability and market values, disruptions in business processes, difficulties in generating income and loan repayments, and increased financing costs due to the change in consumer and investor demands. If this process occurs in a disorderly manner, vulnerabilities of companies may increase.

Risks pertaining to climate change can also spill over from the financial system to the general economy. In this context, tightening in financial conditions and credit restrictions may be observed in sectors and regions that are exposed to physical and transitional risks, and the market values of companies in these sectors may suffer.

While climate change poses risks to the economy and the financial system on the one hand, climate-related financing instruments has the potential for meeting the financing needed for the mitigation of physical risks and transition risks on the other. With increasing awareness of climate-related risks, the transaction volumes of green and sustainable financing instruments have started to increase as well. Green financial instruments, particularly in the bonds and loans have been making rapid progress, as well as Islamic finance instruments, insurance and equities. In addition to these, investment options based on Environmental, Social and Corporate Governance (ESG) principles are increasing.

The volume of green bonds is increasing globally, with Europe leading the way (Chart II.1.1.1). Green bonds are issued to finance investments that benefit and protect the environment in areas such as infrastructure, energy and transportation. The Green Bond Principles published by the International Capital Market Association (ICMA) determine the criterias that a bond must meet in order to be called a green bond.

Chart II.1.1.1: Total Volume and Number of Issuances of Green Bonds
(USD Billion, Units)



Source: IMF

Last Observation: 12.20

Note: Country groups have been determined in line with IMF categories.

AE: Australia, Austria, Belgium, Canada, Denmark, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Japan, Korea, Latvia, Lithuania, Luxembourg, Netherlands, New Zealand, Norway, Portugal, Singapore, Slovenia, Spain, Sweden, Switzerland, Taiwan, United Kingdom

EME: Argentina, Brazil, Chile, China, Colombia, Costa Rica, Egypt, Fiji, Georgia, Hungary, India, Indonesia, Malaysia, Mauritius, Mexico, Morocco, Namibia, Panama, Peru, the Philippines, Poland, Russia, Seychelles, South Africa, Thailand, Turkey, United Arab Emirates

Euro area: Austria, Belgium, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Netherlands, Portugal, Slovenia, Spain

Green loans are also used to finance environmental projects partially or completely. The criterias that must be fulfilled by a loan to be classified as a green loan have been determined by the Loan Market Association (LMA) as the Green Loan Principles.

Sustainable financing, which has a wider scope, is based on the principle that the funding provided to companies on the basis of their compliance with various social criteria as well as the environment.

Sustainable banking is growing in Turkey as well; many banks increase environmentally friendly practices such as electronic invoices, online banking, and mobile payments related to their own activities, obtain funds from abroad via sustainable finance, and allocate these resources to domestic projects serving to mitigate climate change. While obtaining resources, banks fulfilling various performance criteria pertaining to sustainable banking on a predetermined timetable can have cost advantages in sustainability-oriented syndicated loans. As for the use of funds, green and sustainability-related loans

are provided for environmentally friendly housing projects as well as to projects about energy efficiency and renewable energy, sustainable water management, environmentally friendly transportation, and support for entrepreneurial women. In addition, the amount of green/sustainable bonds issued by the banking sector has gradually increased and reached a total of USD 2.7 billion since 2016 (Table II.1.1.I.1). International organizations and multilateral development banks can also provide financing for sustainability-oriented projects. The environmental projects in our country are financed by institutions such as the European Bank for Reconstruction and Development (EBRD), the World Bank, the Council of Europe Development Bank, the French Development Agency and the German Industrialization Fund.

Table II.1.I.1: Sustainable and Green Bond issued by the Turkish Banking Sector
(USD Million)

Date of Issuance	Amount	Term	Type	Currency
18.05.2016	300	5 years	Green Bond	USD
28.03.2017	300	10 years	Tier-2 Green Bond	USD
30.06.2017	150	5 years	Green Bond	TL
11.06.2018	75	6 years	Gender Equality Bond	USD
21.08.2019	50	10 years	Green Bond	USD
20.12.2019	50	5 years	Green Bond	USD
21.01.2020	50	5 years	Green Bond	USD
5.08.2020	50	5 years	Green Bond	USD
8.12.2020	750	5 years	Sustainable Bond	USD
14.01.2021	350	5 years	Sustainable Bond	USD
28.01.2021	600	5 years	Sustainable Bond	USD

Source: Information compiled from Public Disclosure Platform's announcement and data from commercial banks.

In Turkey, the Banking Regulation and Supervision Agency (BRSA), the Capital Markets Board (CMB) and Borsa Istanbul (BIST) have regulations on energy efficiency and sustainability. With the Regulation on Banks' Loan Transactions, the BRSA encourages energy efficiency in houses by determining the ratio of the loan amount to the value of the house taken as collateral higher for houses with high-energy performance. With the amendment made in the Corporate Governance Communiqué on 2 October 2020, the CMB regulated the implementation of the basic principles expected to be disclosed by publicly-held corporations while carrying out ESG activities in the "Sustainability Principles Compliance Framework", on a voluntary basis, and made it mandatory to report whether they were implemented or not, with the principle of "Comply or Explain". BIST offers sustainable investment options to responsible investors in the BIST Sustainability Index including companies with high corporate sustainability performance, and published a sustainability guide for companies in 2014.

The main challenge in tackling climate change is that, on the one hand, the risks have already begun to materialize and the situation requires urgent action, on the other hand, disorderly and sudden transition to a low-carbon economy creates new risks. Therefore, a strategic and long-term approach is needed to manage climate-related risks. The first phase of this approach requires a stocktake of the situation and measurement of risks. Data collection, ensuring the consistency of the existing data and bridging data gaps for this purpose emerge as important challenges. These needs and challenges have led to an acceleration in the work of many international organizations on climate change, particularly in recent years, and this work has been monitored and supported by G20.

The Financial Stability Board (FSB) has been working on the effects of climate change on financial stability, and preparing guidelines for financial institutions to help them report about climate via the Task Force on Climate-Related Financial Disclosures (TCFD).¹ In 2021, the FSB will present to the G20 reports on data gaps and reporting standards, as well as financial authorities' regulatory and supervisory approaches. The International Financial Reporting Standards (IFRS) Foundation, on the other hand, will prepare its climate-related reporting standards in line with TCFD recommendations. The International Organization of Securities Commissions (IOSCO) is collaborating with the IFRS on the preparation of companies' climate reporting standards. IOSCO is also working on including climate risks of asset management companies to risk frameworks and arranging ESG ratings.

¹ <https://www.fsb.org/work-of-the-fsb/financial-innovation-and-structural-change/climate-related-risks/>

Basel Committee on Banking Supervision (BCBS) has been carrying out analytical studies on the transmission channels of climate-related financial risks to the banking sector and the measurement methods of these risks, and published reports on the subject in April.² The BCBS examines climate-related financial risks within the traditional risk categories faced by the banking sector and addresses these risks within the scope of future inclusion in the Basel Framework.

The IMF has focused on climate-related issues in the global reports it has published in recent years. The World Bank considers climate change as a risk factor for development, collects data in this area, provides financing for projects and prepares low-carbon economy adaptation guidelines. The OECD addresses climate change from many perspectives. These are evaluating the effects of climate change on economic development, adapting to a low-carbon economy, green finance, contributing to international climate change studies, fossil fuels and taxation, their impact on agriculture and ecosystems, and environmentally-friendly growth in cities.

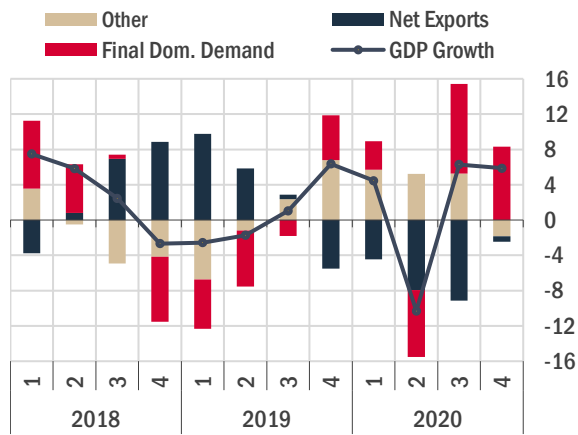
Climate-related financial stability risks, which have rapidly become a priority on the global financial agenda recently, are important issues that need to be carefully addressed in the medium and long term. The COVID-19 pandemic and climate risks can be considered as large global negative externalities, the social and economic effects of which may be greater than anticipated. In this respect, the issue requires cooperation, coordination and a long-term strategic approach at both regional and global levels.

² <https://www.bis.org/bcbs/publ/d517.htm>
<https://www.bis.org/bcbs/publ/d518.htm>

II.2 Main Domestic Macroeconomic Developments

Starting from the third quarter of 2020, economic activity registered a strong recovery that was more pronounced in domestic demand. In this period, imports increased due to the continuation of the brisk course in domestic demand supported by the measures taken to limit the negative effects of the pandemic on the economy as well as by the growth in loans while strengthening gold demand, which was also affected by the increase in global gold prices, made a significant contribution to imports. On the other hand, the curbing effect of net exports on growth decreased as of the final quarter of 2020 (Chart II.2.1), and net exports made a positive contribution to quarterly growth. The most recent indicators reveal that the strong course of economic activity continued in the controlled normalization period of January-April 2021 (Chart II.2.2). Despite the strong course of industrial production, the persistent spread of the pandemic weighs on the recovery in the services sector, particularly in tourism. In addition to recent pandemic restrictions, the decelerating impact of the tight monetary and financial conditions on credits and domestic demand is expected to become more pronounced in the upcoming period. On the other hand, the global pandemic and the vaccination rollout continue to create uncertainty about economic activity in either direction.

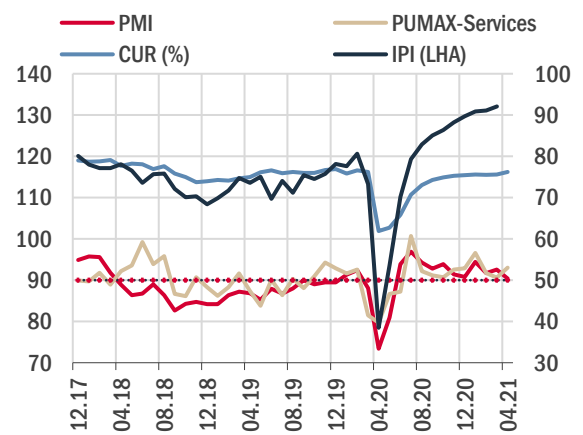
Chart II.2.1: Annual GDP Growth and Contribution to Growth from the Expenditure Side (% Points)



Source: TURKSTAT

Last Observation: 2020Q4

Chart II.2.2: Selected Leading Indicators of Economic Activity (Index, %)



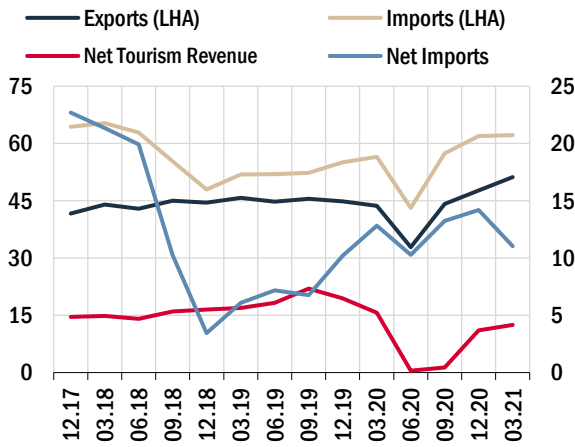
Sources: CBRT, ISO, MUSIAD

Last Observation: 04.2021

Note: The Manufacturing Industry Capacity Utilization Rate (CUR) is seasonally adjusted while the Industrial Production Index (IPI) and the Services Sector Purchasing Managers' Index (PUMAX-Services) are seasonally and calendar adjusted. The dotted line shows the stable state in the Manufacturing Industry Purchasing Managers' Index (PMI) and PUMAX indices compared to the previous month.

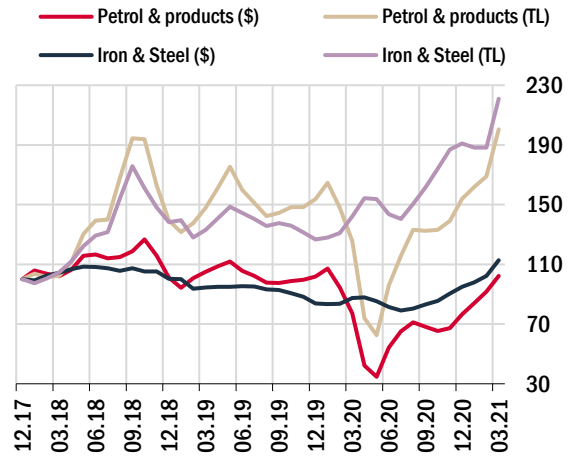
The deterioration in the foreign trade balance, which had observed since the first quarter of 2019, reversed in the first quarter of 2021 mainly due to the recovery in exports of goods. With the partial easing of the pandemic measures that restricted global mobility, tourism revenues have recovered to some extent since the last quarter of 2020 (Chart II.2.3). The upward trend in exports observed in the second half of 2020 continued into the January-April 2021 period as the global growth outlook improved gradually and the pandemic restrictions in European countries including our major trade partners remained mainly limited to the services sector. On the other hand, rising commodity prices in the international markets affect both the current account and domestic prices negatively through the imports channel. While import prices in foreign currency have increased since mid-2020 in iron and steel products and since the last quarter of 2020 in crude oil and byproducts, the rise in import prices in TL has been more evident over the last one-year period due to exchange rate developments (Chart II.2.4).

Chart II.2.3: Foreign Trade and Tourism Revenues (3-Month Total of Seasonally Adjusted Monthly Data, Billion USD)



Sources: CBRT, TURKSTAT Last Observation: 03.21
 Note: For foreign trade, exports (fob) and imports (cif) data according to the general trade system have been used.

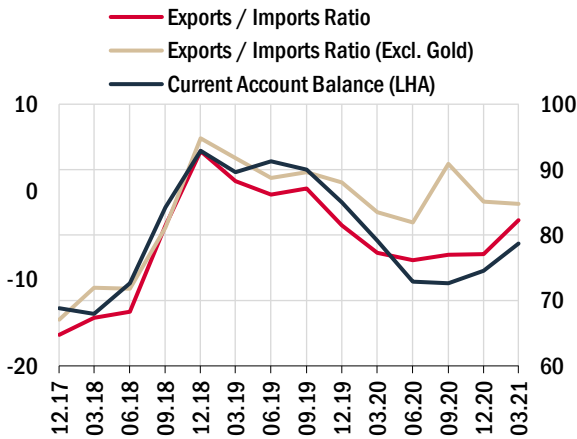
Chart II.2.4: Commodity Import Prices (Unit value indices, December 2017=100)



Source: TURKSTAT Last Observation: 03.21

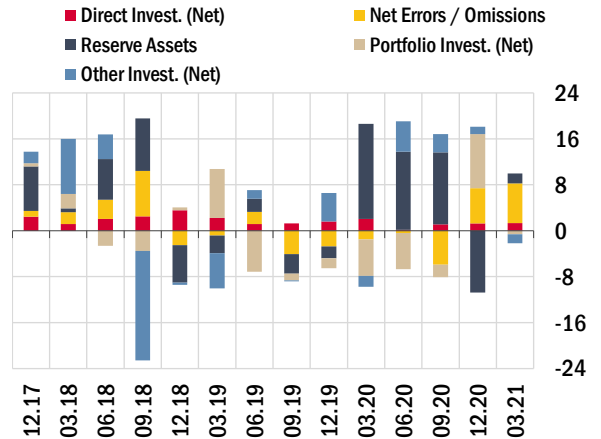
With exports following a relatively stronger course, the export/import coverage ratio has increased since the third quarter of 2020. Despite the rise in commodity prices, the strong upward trend in exports, the significant fall in gold imports, and the slowdown in loans due to the tightening in financial conditions support the expected improvement in the current account (Chart II.2.5). With the improvement in capital flows since the last reporting period, the increase in the financing need stemming from the current account has slowed, and the role of reserves in financing the current account deficit has decreased (Chart II.2.6).

Chart II.2.5: Export/Import Coverage Ratio and Current Account Balance (3-Month Total of Seasonally Adjusted Monthly Data, % and Billion USD)



Sources: TURKSTAT , CBRT Last Observation: 03.21

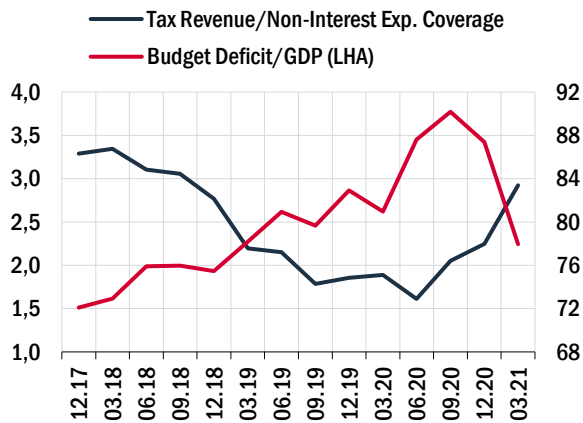
Chart II.2.6: Financing Sources of Current Account Balance (3-Month Total, Billion USD)



Source: CBRT Last Observation: 03.21

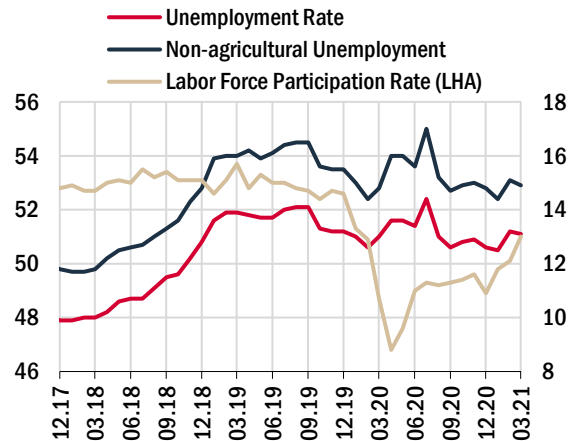
Although there was a rise in public expenditures due to the pandemic, tax revenues increased and primary expenditures decreased since the third quarter of the year on the back of the strong course of domestic demand, which had a positive impact on the budget balance (Chart II.2.7). While measures to maintain employment have curbed the negative effects of the pandemic on the labor market, the rise in the labor force participation rate has had an upward impact on the unemployment rate in recent months (Chart II.2.8).

Chart II.2.7: Central Government Budget Indicators (12-Month Cumulative, %)



Source: MTF Last Observation: 03.21
 Note: GDP data for 2021Q1 has been calculated using the annual growth rate of IPI.

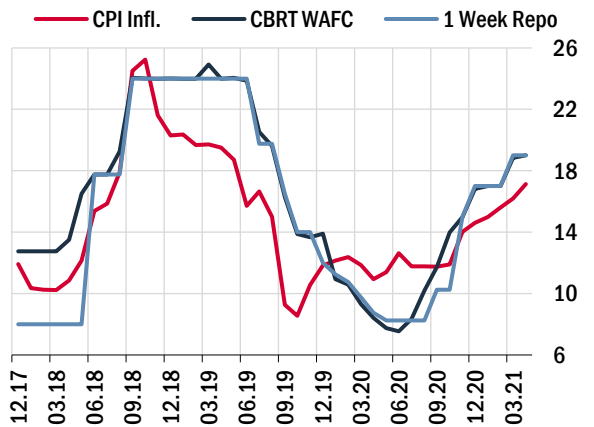
Chart II.2.8: Labor Market Indicators (Seasonally Adjusted, %)



Source: TURKSTAT Last Observation: 03.21

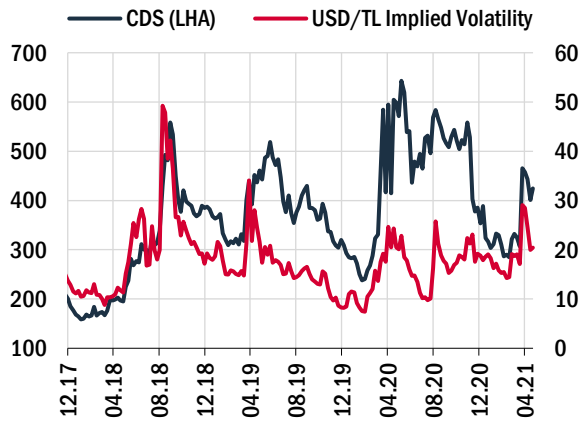
In addition to the increases in international commodity prices, demand and cost factors, high levels of inflation expectations, and supply constraints in some sectors cause inflation indicators to remain high (Chart II.2.9). Due to the upside risks to the inflation outlook, the CBRT delivered a monetary tightening in the current reporting period through its policy rate. It is assessed that setting the policy rate at a level above actual and expected inflation to maintain a strong disinflationary effect will help achieve a permanent fall in inflation and ultimately achieve the medium-term target, and that the stability to be restored in the general price level will significantly contribute to a decline in country risk premiums and exchange rate volatility that have increased partially in the recent period (Chart II.2.10).

Chart II.2.9: Inflation and Policy Rates (Annual % Change, Monthly Average %)



Sources: CBRT, TURKSTAT Last Observation: 04.21
 Note: WAFC (weighted average funding cost) has been weighted by daily net amounts of funding, showing the average of the last 5 business days of each month in the 2017-2019 period, and the average of the days between two MPC meetings in 2020 and later.

Chart II.2.10: CDS Premium and Exchange Rate Volatility (Basis Points)



Source: Bloomberg Last Observation: 23.04.21
 Note: CDS premium with 5-year maturity, exchange rate volatility with 1-month maturity.