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INFLATION OUTLOOK IN TURKEY and
REVISION OF INFLATION TARGETS

Increase in food, energy and commodity prices have continued to influence the course of inflation in Turkey, as well as the rest of the world. In the second quarter of 2008, inflation breached the upper limit of the uncertainty band. As of August, annual inflation stood at 11.77 %.

Recent readings on economic activity suggest that the moderation in consumption and investment demand has continued in the second quarter. In addition, the cautious monetary policy stance and the tightening in global credit conditions are likely to restrain total demand in the period ahead. Under the assumption that government expenditures and incomes policy will evolve in line with the official projections, the underlying inflation is expected to lose pace in the medium term.

However, there is still uncertainty regarding the course of the disinflation process due to the backward looking pricing behavior of economic agents. Moreover, the continued fragility in global financial markets and the increase in commodity prices curb the risk appetite for investments in developing countries.

The Central Bank of the Republic of Turkey (CBT) wrote an open letter to the Government on July 28, 2008, which included the policy explanation of the underlying reasons for the breach of inflation of the upper limit of the uncertainty band and the policy response. The Bank also released its third Inflation Report in 2008 with renewed projections for inflation. Parallel to this, it has been anticipated that in order to prevent the materialization of the second round effects of supply-side shocks and to ensure a steady decline in inflation, cautious monetary policy will be maintained for a while.

Base Scenario

Assumptions	<ul style="list-style-type: none">• Food inflation: 14 % and 9 % in 2008 and 2009, respectively• Oil Prices: around 140 USD per barrel• Cumulative exchange rate pass-through of around 1.2 percentage points• Electricity tariffs adjusted as required by the automatic pricing mechanism
Interest Rate Response	<ul style="list-style-type: none">• Limited tightening towards the end of 2008
Inflation Forecasts*	<ul style="list-style-type: none">• End-2008: 10.6 %• End-2009: between 5.9 % and 9.3 % (mid point: 7.6 %)• End-2010: between: 4.0 % and 7.8 % (mid point: % 5.9)• Mid-2011: 5.4 %

*with 70 % probability

Revision of Inflation Targets

Due to ongoing supply shocks and problems related to global markets, it has been observed that even with the application of a cautious policy stance, it would take a relatively long time for inflation to reach the medium term target level of 4 % and that the said inflation targets can no longer serve as nominal anchors. In this framework year-end targets for 2009, 2010 and 2011 have been changed jointly by the CBT and the Government.

Medium Term Year-End Inflation Targets

2009	2010	2011
7.5 %	6.5 %	5.5 %

To find out more: www.tcmb.gov.tr

PRICE STABILITY and ECONOMIC GROWTH IN TURKEY

Turkey's Growth and Inflation

In the 30-year-long chronic inflation period, which took a start in the 1970s, the Turkish economy exhibited low and unstable economic growth performance compared to similar countries, due to lack of fiscal discipline, the failure to set the primary goal of achieving price stability as the monetary policy objective and the lack of confidence in policies.

In the aftermath of the 2001 crisis, the comprehensive restructuring process accompanied with the implementation of sound monetary and fiscal policies has not only led to fall in inflation, but also helped in achieving high growth rates. Throughout this process, amendments made in the CBT Law, adherence to the primary goal of achieving price stability and the grant of goal independence have served as primary factors that have brought inflation down.

	1970-1979	1980-1989	1990-2001	2002-2007
Growth rate*				
Average (%)	4.8	4.0	3.2	6.8
Standard Deviation	3.2	3.5	5.9	1.8
Inflation**				
Average (%)	24.1	49.6	74.8	13.9
Standard Deviation	15.7	26.7	21.9	8.7

* 1970 - 1998 (1987 prices) GNP, 1999 - 2007 (1998 prices) GDP

** 1970 - 1987 (1963=100) WPI,

1988 - 1994 (1987=100), 1995 - 2004 (1994=100), 2005 - 2007 (2003 = 100) CPI

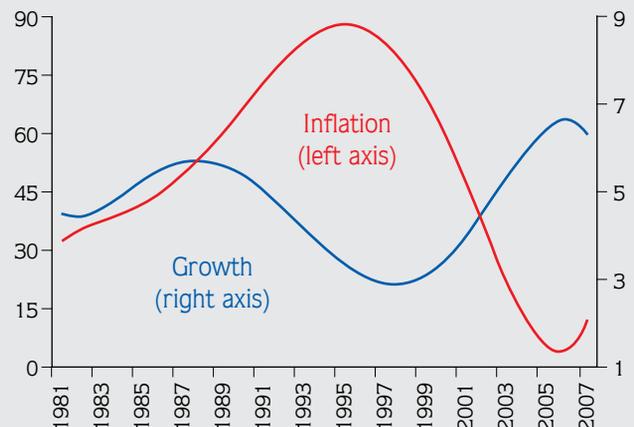
The CBT's most important contribution to macroeconomic stability and sustainable growth would be to achieve and maintain price stability.

As a result, average inflation decreased to 13.9 % in the 2002-2007 period, while average growth rate reached 6.8%. Furthermore standard deviation of both inflation and growth rates have declined significantly. In the period of falling inflation; investment accelerated, industrial production increased, capacity utilization improved, nonagricultural employment increased, total exports rose both in quantity and value (at fixed prices), Turkey's share in world exports increased and, all these developments contributed to economic growth.



Recently, the slowdown in the economic growth and the cutback in the disinflation process have shown that still more steps should be taken to achieve sustainable growth and price stability. At this point, the CBT's most important contribution to macroeconomic stability and sustainable growth would be to achieve and maintain price stability. However, as the goal of price stability has not been achieved yet, it is very important that the CBT continue its policies towards price stability regardless of the partial decline in inflation.

Inflation and Economic Growth Tendencies In Turkey (1981-2007, percentage)

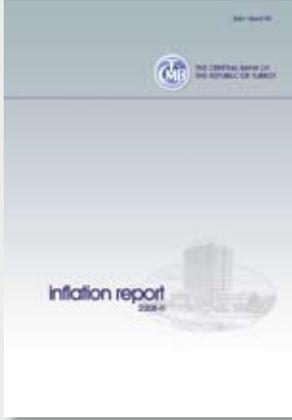


Source: TURKSTAT, CBT

PUBLICATIONS AND NEWS FROM THE CBT

PUBLICITY CAMPAIGN ON TRANSITION FROM “NEW TURKISH LIRA” TO “TURKISH LIRA”

As the first phase of currency reform, six zeroes have been dropped and the New Turkish Lira banknotes and coins were put into circulation on January 1, 2005. As the second and final phase of the operation, the prefix “New” will be removed, and the “Turkish Lira” will be reintroduced on January 1, 2009. Accordingly, the publicity campaign aiming at raising awareness about transition from the New Turkish Lira to the Turkish Lira was launched by a press conference on 27 August, 2008. The new banknotes and coins together with the improved security features will be introduced to the public by a press conference in October 2008.



INFLATION REPORT 2008-III

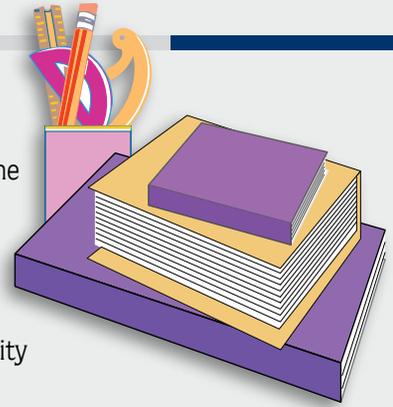
The Inflation Report 2008-III was released and announced at a press conference with the participation of Governor Yılmaz on July 28, 2008. The Report examines recent developments on the inflation front and monetary policy as well as developments in international markets and supply and demand conditions. The Report also includes boxes on several issues such as global inflation and monetary policy developments; medium term forecasts of food prices, the effect of seasonal elements and number of days worked on national income calculation, liquidity developments and monetary policy reference interest rate.

To find out more: www.tcmb.gov.tr (Periodic Publications)

FINANCIAL SUPPORT PROGRAM FOR ACADEMIC STUDIES

Within the framework of the “Financial Support Program for Academic Studies”; the CBT provided financial support for the following organizations:

- “15th World Economic Congress” of the International Economics Association (IEA) organized by the Turkish Economics Association (TEA) on June 25-29, 2008;
- “Summer Seminars on Economics 2008” organized by the Pamukkale University on July 1 - August 8, 2008,
- “12th World Congress of Accounting Historians” organized by the Marmara University Faculty of Economics and Administrative Sciences and the Association of Accounting and Finance Academicians on July 20-24, 2008.



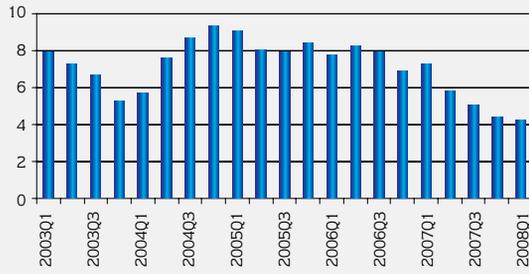
WORKING PAPERS

- “Oil Price Shocks, Macroeconomic Stability and Welfare in a Small Open Economy” (Deren Ünalmiş, İbrahim Ünalmiş, Derya Filiz Ünsal, Working Paper No. 08/02, May 2008)
- “On Roots of Housing Bubbles” (Erdem Başçı, İsmail Sağlam, Working Paper No. 08/03, July 2008)
- “How did the Turkish Industry Respond to Increased Competitive Pressures, 1998-2007?” (Gökhan Yılmaz, Rauf Gönenç, Working Paper No. 08/04, July 2008)
- “Entry to Export Markets and Productivity: Analysis of Matched Firms in Turkey” (Altan Aldan, Mahmut Günay, Working Paper No. 08/05, August 2008)
- “Can Central Bank Interventions Affect the Exchange Rate Volatility? Multivariate GARCH Approach Using Constrained Nonlinear Programming” (Tolga Çaşkurlu, Mustafa Ç. Pınar, Aslıhan Salih, Ferhan Salman, Working Paper No. 08/06, August 2008)
- “Tangos, Sambas or Belly Dancing? Or, do Spreads Dance to the Same Rhythm? Signaling Regime Sustainability in Argentina, Brazil and Turkey” (Santiago Herrera, Ferhan Salman, Working Paper No. 08/07, August 2008)
- “Monetary Pressures and Inflation Dynamics in Turkey: Evidence from P-Star Model” (K.Azım Özdemir, Mesut Saygılı, Working Paper No. 08/08, August 2008)

To find out more: www.tcmb.gov.tr (Publications)

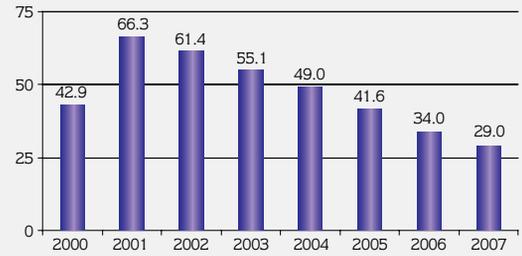
AT A GLANCE

GDP Growth Rate (Quarterly, percent)



Source: TURKSTAT

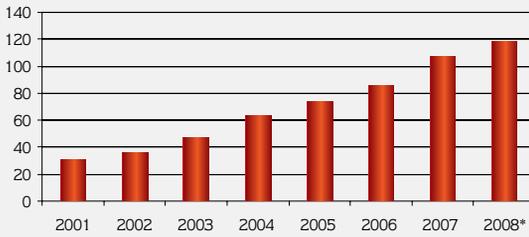
Total Public Net Debt Stock* / GDP (Percent)



Source: Treasury, TURKSTAT

* Total Public Net Debt Stock= Total Public Sector Gross Debt - Central Bank Net Assets - Public Sector Deposits - Unemployment Insurance Fund Net Assets

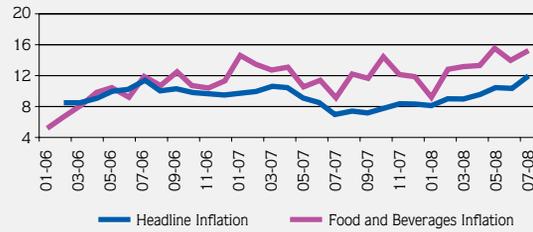
Exports (Billion USD)



Source: TURKSTAT

* As of June 2008, 12 month rolling sum

Headline Inflation and Food & Beverages Inflation (Annual percentage change)



Source: TURKSTAT

Payment Systems in Turkey

Developments in information technologies and the widespread use of electronic banking services starting from the 1990s brought about the establishment of the infrastructure of electronic banking, and the execution of interbank and fund transfers by modern communication techniques.

In this framework, the CBT built up the Electronic Funds Transfer (EFT) system in 1992, in order to allow swift

and regular fund transfers in Turkish Lira. With the introduction of new functions to the existing system and significant changes made in its software and hardware, the second-generation system began to operate in 2000.

In addition to the EFT system, another system called Electronic Securities Transfer System (EST) was established for the purchase, sale and other operations of securities. This system enables interbank operations related to government securities over the accounts held in the EST center.

The EFT and EST systems have provided the CBT with a leading role in the development of effective and safe payments and security balancing system services.



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CBT Interest Rates*

Overnight (%)

Borrowing

16.75

Lending

20.25

Central Bank Foreign Exchange Reserves (As of 22 August 2008, Billion USD)

75.46

CPI (Annual % Change, August 2008)

11.77

* As of 28 August 2008.