

**Remarks by**  
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**THE CENTRAL BANK OF THE REPUBLIC OF TURKEY**  
**at the**  
**SPRING MEETING OF IIF**  
**CONRAD INTERNATIONAL, İSTANBUL**  
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Ladies and Gentlemen,

It is indeed a great pleasure to speak before such a distinguished audience as this one, and I would like to thank the IIF for giving me this opportunity to address you.

Indeed, Charles and I began to prepare for this meeting back in October 1995 in Washington, D.C., during the Annual Meetings of the Boards of Governors of the World Bank and IMF. At that time I was head of a Turkish commercial bank which is a member of the IIF. I was ready and willing to arrange this meeting here in Istanbul. The member Turkish banks and Charles' office, and I myself, have all worked very hard since then. Then, almost three weeks ago, I was appointed as Governor of the Central Bank of Turkey. Owing to this stroke of fortune, I find myself a guest speaker at this meeting instead of being one of the banker guests, like yourselves.

Distinguished guest, I would like to make use of this opportunity to touch briefly on the current problems and challenges confronting Turkey's adjustment efforts, as a step toward our better understanding of how Turkey should proceed in order to attain sustainable growth over the medium term.

Turkey now stands at a decisive point for its economic future. Among the many challenges facing Turkey, two main issues will be crucial in determining Turkey's medium-term economic prospects. These are reducing inflation, and adapting the economy to accommodate the Customs Union with the European Union. The Customs Union has just entered into force. Joining it will enable Turkey to participate, in many sectors, in the largest single market in the world. In my view, the economic policies we choose to follow now will largely determine whether Turkey will be able to integrate itself further into the industrialized world, or will belong instead to the group of so-called problem countries.

It was recently pointed out at Davos, by Larry Summers, Assistant Undersecretary of the U.S. Treasury, that by the year 2000 some of the emerging economies will have joined the Club of industrialized countries while others, which will have missed their chance, will fall back into the second, third, or even fourth league. I strongly believe that Turkey will earn its rightful

place among the countries of the first league by virtue of the stage of development it will have attained and the dynamism of its economy.

Indeed, with its young population 60 million strong, its well established industrial and services sectors, its dynamic private sector which has shown repeatedly that it will respond positively to improvements in the macroeconomic environment, and its advanced stage of liberalization, Turkey is one of the leading candidates for the first league of countries. Most of Turkey's markets are well established and function efficiently. Its financial markets and institutions are well developed and conform to world standards.

I would like to remind you that liberalization and deregulation of the financial markets began in the early 1980s and accelerated rapidly during the 1990s. In the process, the Turkish lira has become fully convertible and restrictions on capital movements have been effectively removed. On the technical level, Turkey is already fully integrated into the world financial markets, being in this respect ahead of most members of the European Community.

However, the Turkish economy has suffered from chronic high inflation for the last two decades. Turkey's inflation is a unique and interesting phenomenon. Despite political willingness, Turkish inflation has resisted various attempts to reduce it to moderate levels. The main reason has been the persistent high inflationary expectations arising from the slowness to implement structural reforms and from a lack of confidence that the stabilization efforts will be sustained over the medium term.

There are so many urgent reasons for seeking an inflation breakthrough that I will not explain them in detail. A more determined and better designed attack on inflation is needed to change the widespread and well-entrenched inflationary expectations. This means even larger reductions in public deficits, which a broad consensus among observers considers the prime cause of inflation in Turkey. The existence of a primary surplus in the budget is not enough. A permanent improvement in the public sector deficits and more efficient functioning of the public sector- in combination with decisive progress with Privatization- will be the vital elements of the fight against inflation.

What is needed to achieve these two goals, of reducing inflation and preparing the economy for entry into the EU Customs Union, is a four-step special purpose macroeconomic program.

The first step will be to consider and undertake macroeconomic actions in a medium-term framework.

The second step will be to muster the political will to implement the medium-term program.

The third step will be to break the vicious circle of public indebtedness.

And the fourth step will be to reduce inflationary expectations.

Within this framework, it is especially the third and fourth steps that will be crucially important for the initial success of the medium-term program. During the last two-and-a-half years, the public sector has had limited access to foreign financing even despite its firm willingness to meet its external debt obligations. Neither the public sector nor the private sector has ever considered the possibility of not repaying their obligations. This is in the tradition of honor that characterizes Turkish economic history. Under these circumstances, the

Turkish Treasury was compelled to cover its financing needs and the bulk of its external obligations by means of domestic borrowing. During this period, Turkey's sizeable external debt service has been met primarily through private inflows which put enormous pressure on the domestic financial markets. The public sector's net external payments amounted to 9.5 billion dollars over the last two-and-a-half years.

This so-called "debt trap" has to be broken as part of the medium-term macroeconomic program in order to improve Turkey's access to long-term foreign financing.

The fourth step, of overcoming inflationary expectations, is the key element of achieving a better macroeconomic position. Simulations provided by the Turkish Central Bank's forecasting model already indicate that despite a high effect in the fiscal area (achieving an 8 percent primary surplus in the budget), enormous access to the international financial markets and sizeable revenues from Privatization of the SEEs, inflation will not come down from the level of 40 percent by the end of 1998. This is mainly due to the fact that the model and its simulations take no account of either "expectations" or "credibility", which suggests in turn that the solution to the problem of reducing Turkish inflation is closely linked to the "credibility" problem.

Distinguished Guests, at this stage let me summarize what a central bank should be like as an organization.

1. I believe it to be the most important responsibility of the central bank is to prevent inflation. To maintain price stability is the very essence of an independent central bank. Independence does not mean that the central bank should isolate itself from all other institutions and organizations, or from reality, or that it should act arbitrarily. What I mean by independence is that the central bank should contribute to the design of macroeconomic policies that the government draws up, and should implement its part of the economic program without concessions.
2. Central banks should be credible, reliable, and respectable institutions. Central banks are created not to be loved or criticized, but to be respected.

Central Banks are transparent.

1. Even though they enjoy the right of printing money, central banks must exercise this power being mindful of the responsibility that goes with it.
2. The central bank is the guardian of the economic stability which is much to be desired in a country.
3. The central bank is the institution responsible for maintaining modern and effective supervision over the structure and functioning of the banking system.
4. Central banks should be willing to collaborate in constructive and helpful ways. However, they should be extremely sensitive to the threat of being exploited or interfered with. In Turkey, the relationship between the State and the Central Bank has been established both by tradition and by negotiation. Our aim is to develop a fruitful collaboration.
5. Central banks seek for themselves to develop the most modern infrastructure and the most refined monetary instruments.

These are the qualities of a central bank in which I believe. I assume that I will have the power and responsibility to realize this vision of a central bank for the Republic of Turkey in the future.

At this moment, when national monetary policies are being internationalized, when borders are vanishing and economies are being globalized, we cannot keep our country and its central bank isolated from these trends. The conditions I have outlined are the minimum conditions for giving Turkey a modern central bank with an international identity.

Ladies and Gentlemen,

Let me emphasize that the challenges facing Turkey in the future are neither too easy nor too difficult. What is needed to achieve these aims is one simple thing: persistence-Persistence in the pursuit of the macroeconomic policies that are needed to reduce inflation.

Here let me quote Calvin Coolidge:

"Nothing in the world can take the place of persistence. Talent will not; nothing is more common than unsuccessful men with talent. Genius will not; unrewarded genius is almost a proverb. Education will not; the world is full of educated derelicts. Persistence and determination alone are omnipotent."

Ladies and Gentlemen,

Let me present to you my respects and thank you for your kind attention.

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