Overview

Global economic developments remain important in terms of financial stability. The divergence across countries with respect to economic recovery has continued since the release of the November 2014 volume of the Financial Stability Report. The US has shown a stronger growth performance compared to other advanced economies, whereas economic growth is still weak in the euro area. There has been a deceleration in the growth rates of emerging economies which constitute a significant portion of global growth. Inflation is below the targets in advanced economies, while it is moving upwards in emerging economies. Signals for a rate hike and uncertainties regarding the normalization process in the monetary policy in the US keep the sensitivity of global markets to data flow at high levels. In such a conjuncture, the US dollar has appreciated against other currencies and capital movements in emerging economies have fluctuated.

Indicators for the first quarter of 2015 suggest that domestic economic activity has lost some momentum due to the deceleration in external demand. The economic activity is estimated to resume the moderate upward trend as of the second quarter of the year, on the back of the partial recovery in European Union growth. On the inflation outlook front, cautious monetary and fiscal policies as well as macroprudential measures have favorably affected core inflation indicators. In addition, low levels of commodity prices have backed the downward trend in inflation. However, the high increases in food prices and exchange rate developments in the first quarter of the year have contained the improvement in inflation more than envisaged. In this framework, the CBRT has maintained its cautious monetary policy stance.

The current account balance has improved, while the persisting fiscal discipline has underpinned the downtrend both in risk premiums and inflation. The CBRT has maintained its cautious monetary policy stance on the one hand and on the other, aimed at reducing macrofinancial risks with measures that will support the FX liquidity, core liabilities and long-term borrowing.

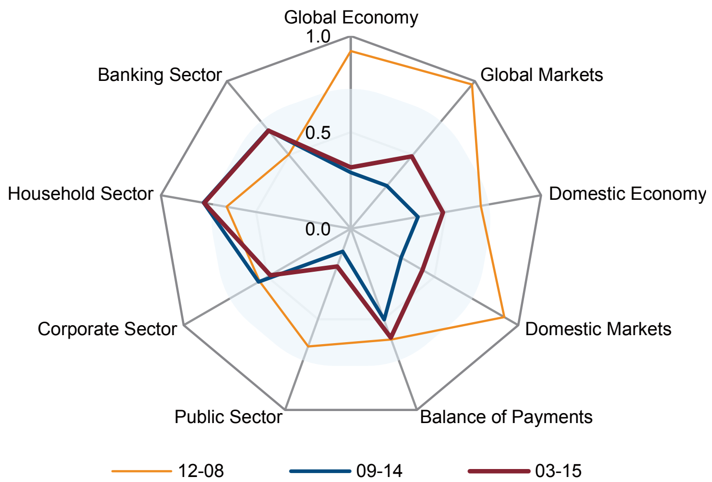
The improvement in the ratio of household financial liabilities to their financial assets continues due to the impact of macroprudential measures taken. Households borrow only in Turkish lira and with a fixed rate, which contributes to the solvency of households in a period of increased volatility in financial markets. The credit demand of the corporate sector is mainly shaped by the financing of the Turkish lira working capital and the need to roll over the current debt. FX loans extended to the corporate sector are predominantly long-term loans; the short-term short position is low and FX loans are used rather by large companies that can manage the exchange rate risk well. All these facts are believed to restrain the exchange rate risk. Moreover, with a new legal arrangement introduced to lower the high leverage caused by the tax advantage of financing through borrowing, a new tax incentive was offered for the growth in money capital. This incentive is expected to encourage equity financing.

Loan growth rates in the banking sector are at reasonable levels and commercial loan growth has outpaced consumer loan growth thanks to the macroprudential measures, which altogether support balanced growth. Although the non-performing loan ratio remains flat, factors such as the weak economic activity and the exchange rate volatility require the credit risk to be monitored. Current capital buffers are adequate enough to cover potential credit risk losses. The robust liquidity outlook continues in the banking sector.

With the contribution of the change that the CBRT introduced in its reserve requirement implementation to extend the maturity of non-deposit FX sources, the average maturity of banks' external funding has extended. The CBRT also started remunerating TL required reserves to encourage core liabilities, while banks have increased their use of core funding sources, which is a positive development in terms of financial stability. Steps taken towards supporting FX liquidity, core liabilities and long-term borrowing are aimed at increasing the resilience of the Turkish economy to global shocks. If needed, additional measures may be taken in the same manner.

The macro display chart below presents the schematic reflection of the developments in financial stability in Turkey within the framework of the evaluations made. Accordingly, global markets, domestic economy and domestic financial market developments have been weaker in the last six-month period compared to the previous six-month period.

Financial Stability Map[1,2]



(1) Getting closer to the center means that the contribution of the related sector to financial stability has increased on the positive side. The analysis allows a historical comparison within each sub-sector. A cross-sector comparison is available only in terms of the direction of the change in the positioning as to the centre.
(2) For the methodology used in the financial stability map, see Financial Stability Report v.13, November 2011-Special Topic IV.10.