

# The Turkish Experience

Bank of Indonesia and IMF Joint Conference on  
Coping with Asia's Large Capital Inflows in a Multi-Speed  
Global Economy

Erdem Başçı

Deputy Governor, Central Bank of Turkey

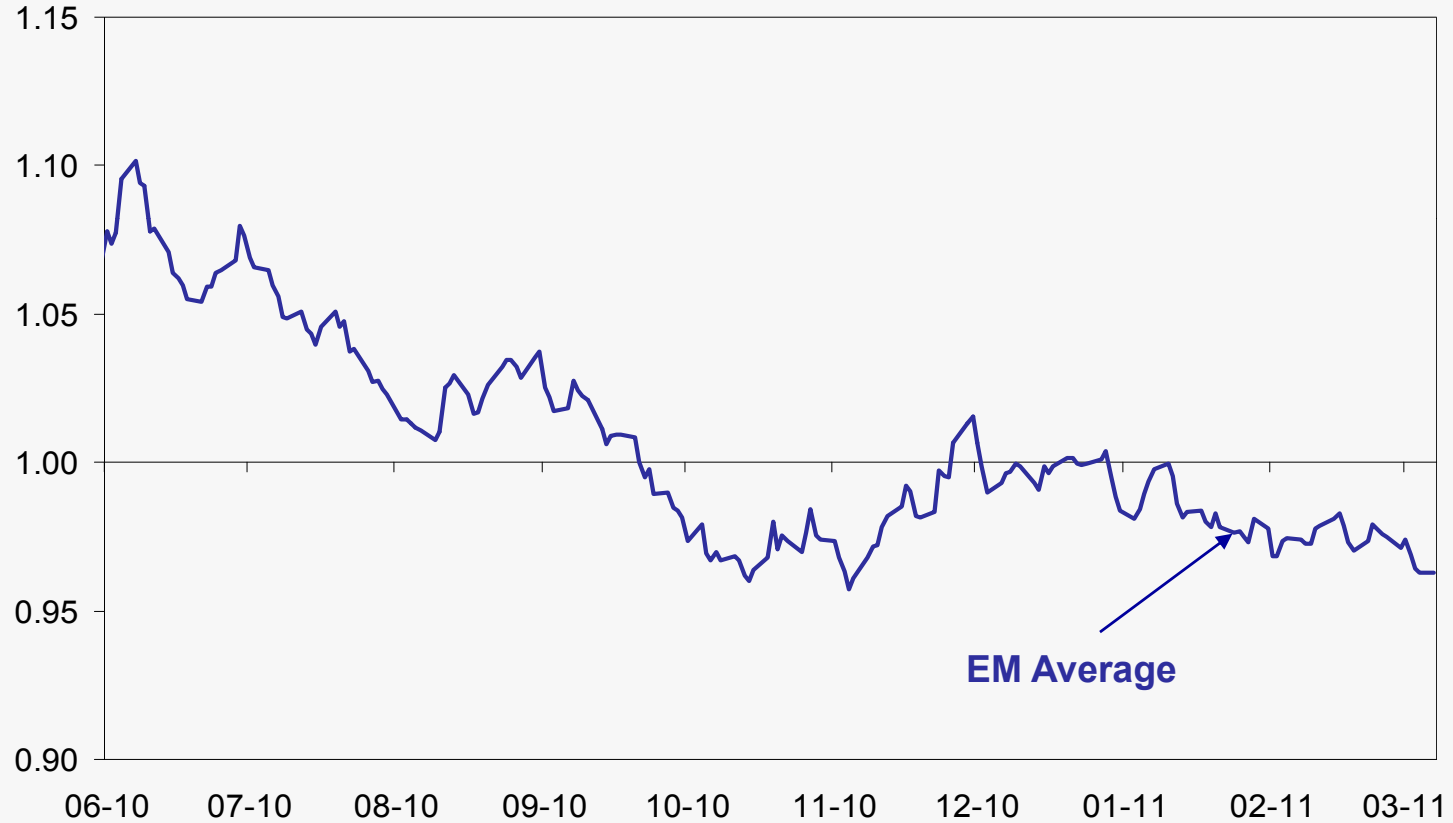
March 11, 2011  
Bali, Indonesia

# Quantitative Easing vs. Quantitative Tightening

- Quantitative easing in major economies has continued in response to weakness in economic activity and heightened sovereign risks, resulting in dramatic increases in central banks' balance sheets.
- Facing huge influx of capital, some developing countries have resorted to quantitative macroprudential tightening, even capital controls.
- Turkey has also initiated quantitative tightening, starting from April 2010.

# Appreciation Pressure

**EM currencies against USD\***  
(4 Jan 2010=1)



\*Average of emerging market currencies, including Brazil, Chile, Czech Republic, Hungary, Mexico, Poland, South Africa, Indonesia, South Korea and Colombia.

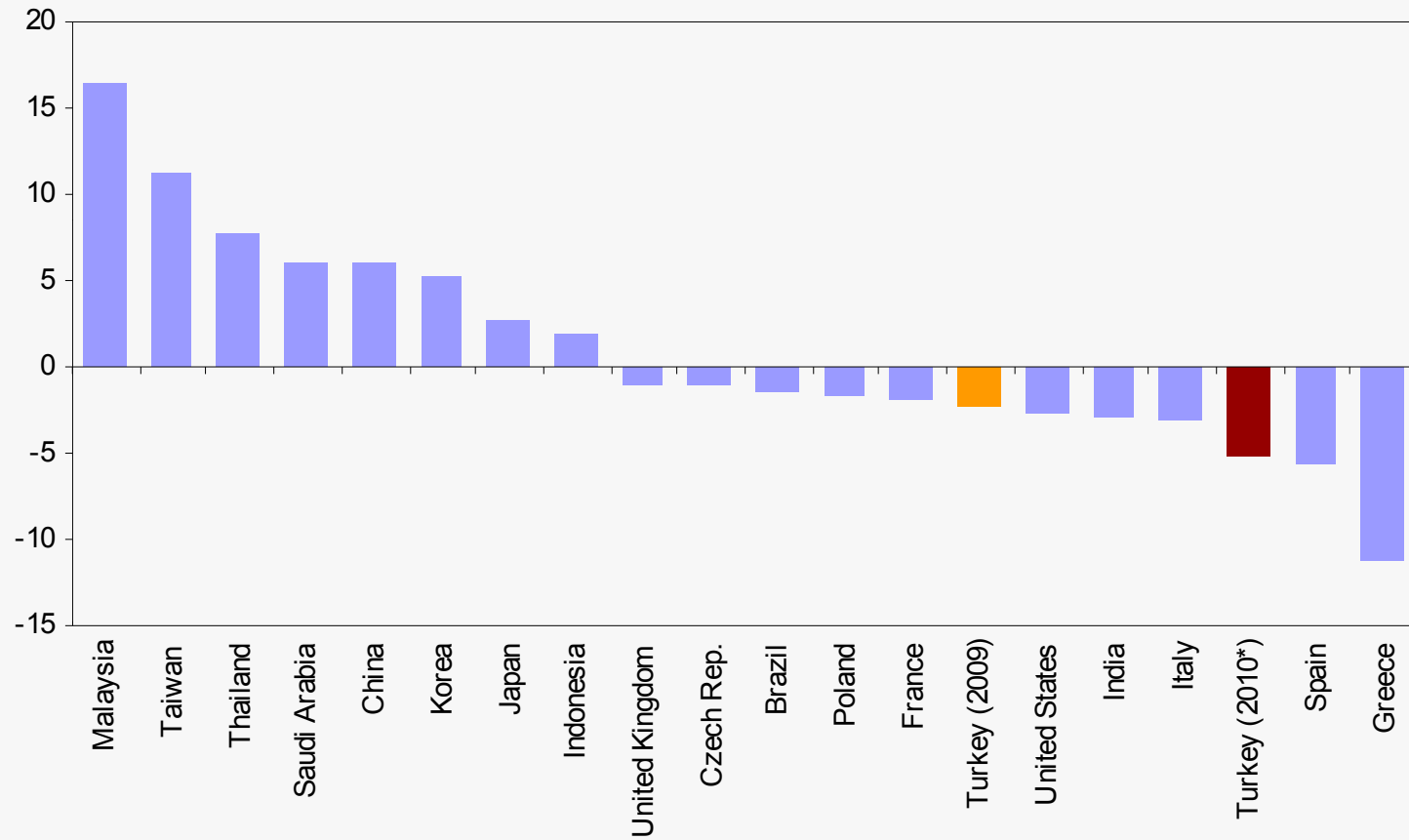
Source: Bloomberg, CBRT

## Two Approaches

- **Approach 1:** Use capital account measures to restrict inflows while tightening via interest rates (Brazil, South Korea)
- **Approach 2:** Use macroprudential measures to restrict domestic credit and domestic demand while keeping the short term interest rate differentials as low as possible (Turkey)

# Current Account Balance

**Current Account Balance**  
(2009, percent of GDP)



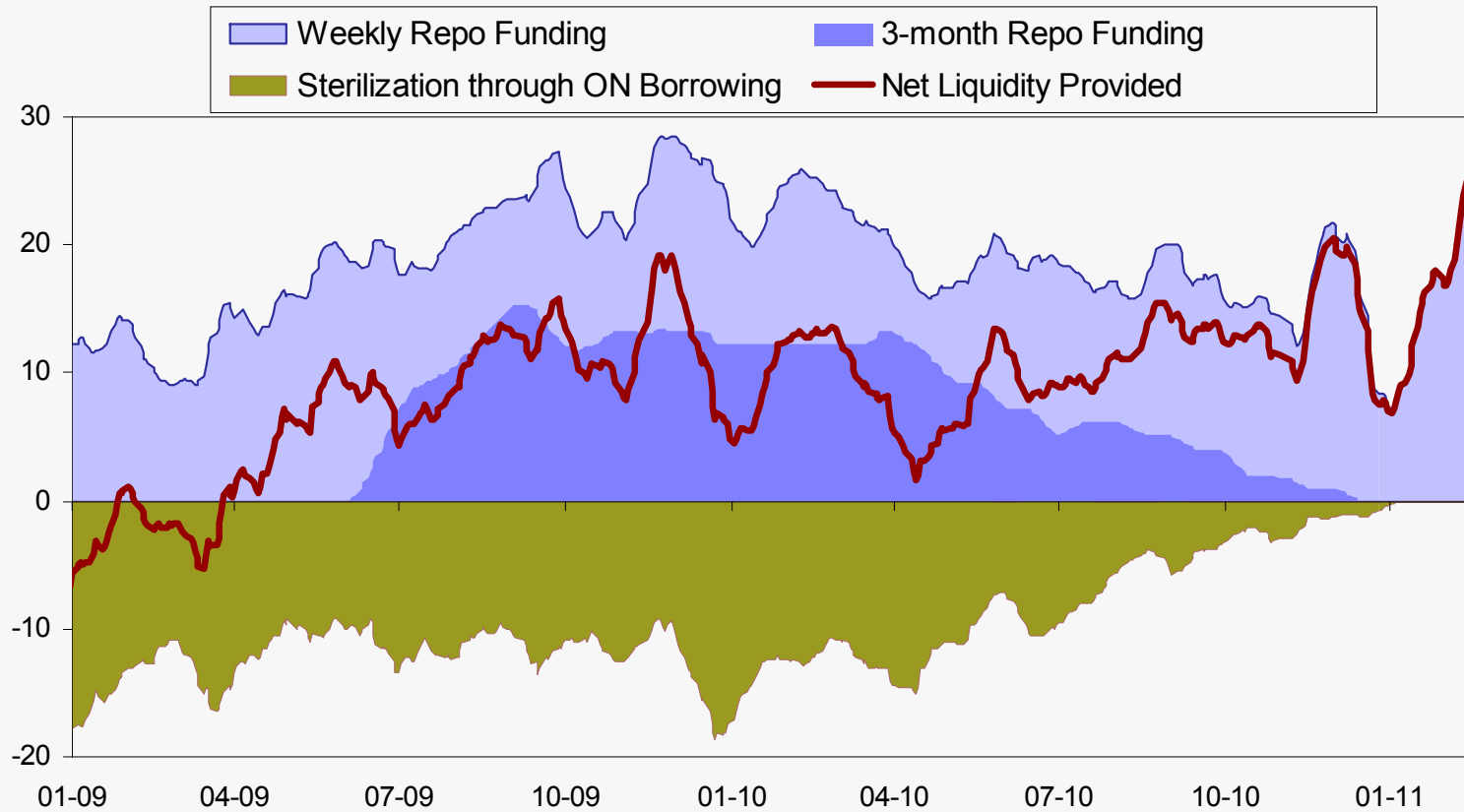
\* IMF WEO Estimate  
Source: IMF, CBRT

# Phases in Monetary Policy

- **Phase-1**: Full Liquidity Support (after the collapse of Lehman Brothers, September 2008)
- **Phase-2**: Monetary Exit Strategy (April 2010)
- **Phase-3**: New Policy Mix (starting from November 2010)

# Liquidity after Monetary Exit

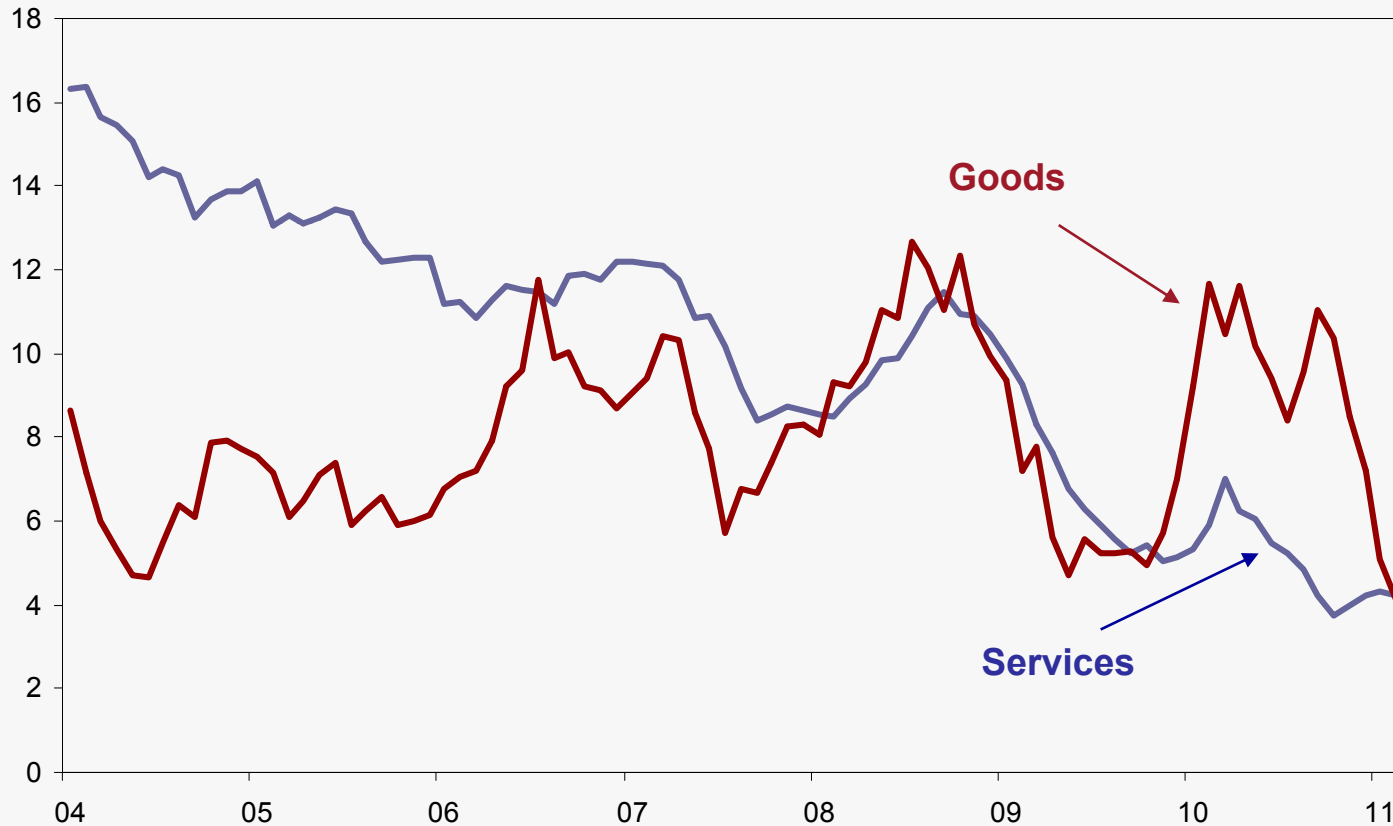
## Central Bank Liquidity (billion TRY)



Source: ISE, CBRT

# Price Stability after Monetary Exit

**Goods and Services Inflation**  
(year-on-year change, percent)



Source: TurkStat, CBRT



# Financial Stability: Objectives

1. **Debt Ratios**: Use of more equity, more prudent borrowing
2. **Debt Maturities**: Extending maturities of domestic and foreign borrowing and deposits
3. **FX Positions**: Strengthening FX positions of public and private sectors
4. **Risk management**: More effective management of exchange rate risk via instruments such as the Turkish Derivatives Exchange

# Macroprudential Tools

- Under the current economic conditions, it may not be possible to simultaneously ensure price stability and financial stability by means of policy rates alone.
- **Solution:** Using macroprudential tools in coordination with other public authorities.
- **Macroprudential tools:**
  1. *Reserve requirements*
  2. *Liquidity management*
  3. *Capital adequacy ratios*
  4. *Liquidity adequacy ratios*
  5. *Taxes*
  6. *Primary expenditures of government*

## Tools (in the order of priority):

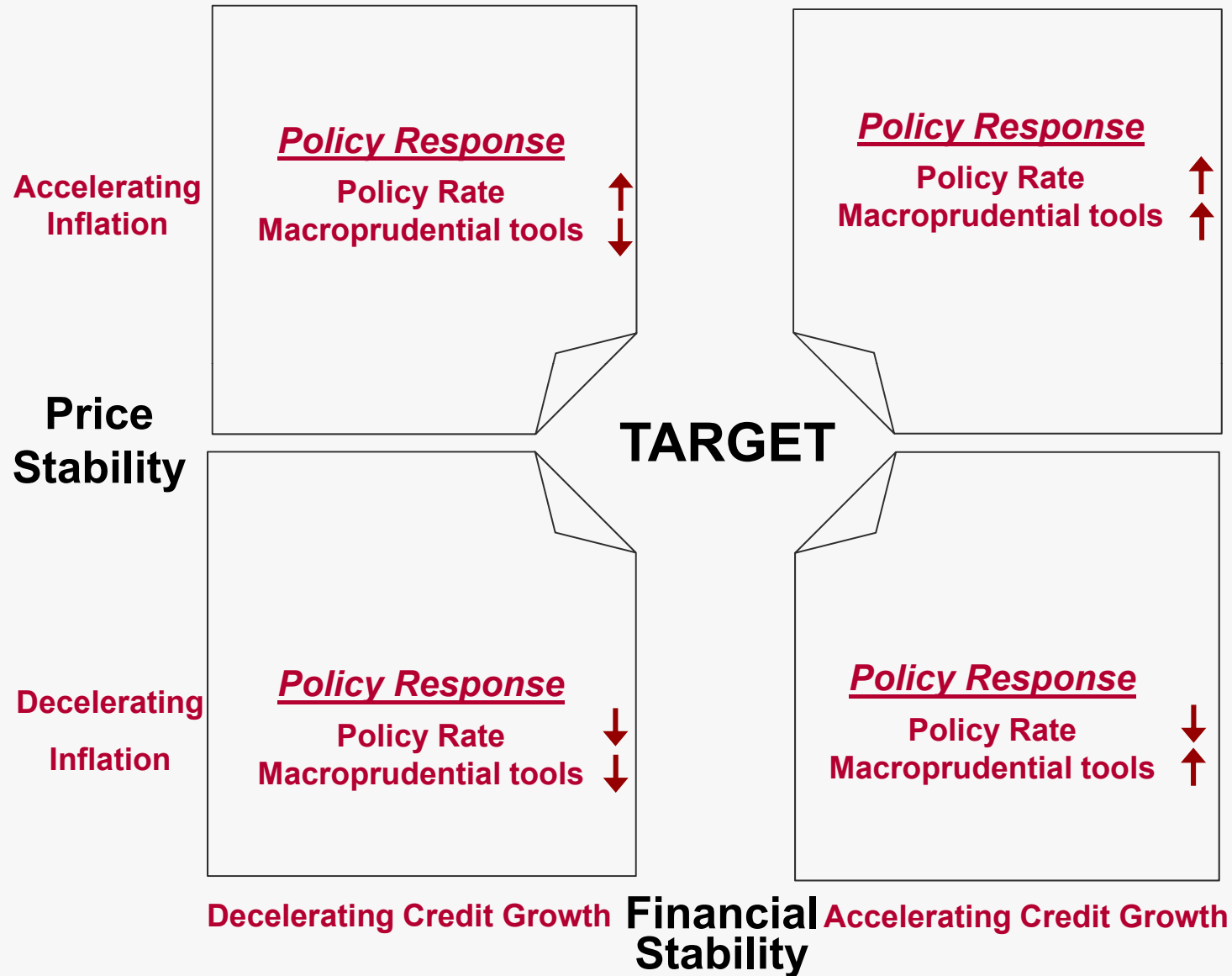
### **For Financial Stability:**

1. Required Reserve Ratios
2. TRY Liquidity Management
3. Short Term Interest Rates

### **For Price Stability:**

1. Short Term Interest Rates
2. TRY Liquidity Management
3. Required Reserve Ratios

# Two Targets, Two Instruments



# The New Policy Mix

## **A lower policy rate, a wider interest rate corridor and higher reserve requirements**

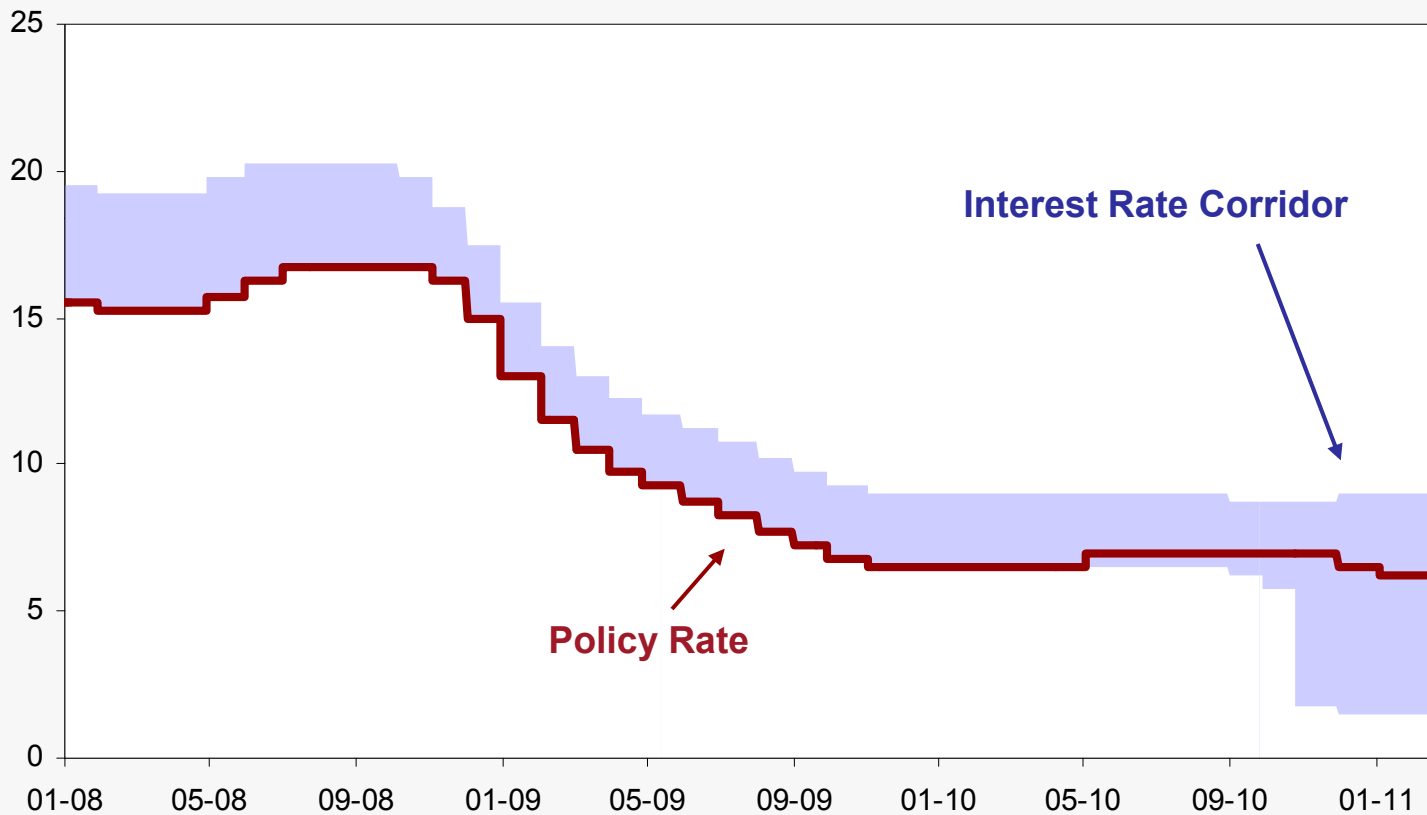
- The framework we adopt in spirit is not significantly different from the conventional inflation targeting framework.
- The only difference is that, previously our policy instrument was the one week repo rate, but now our instrument is a “policy mix”
- We seek to use these instruments in the right combination in order to cope with both inflation and macro-financial risks.
- The monetary policy stance in this framework is not only determined by the path of policy rates, but as a combination of all the policy instruments.

# Effectiveness of Required Reserves

- 1. Liquidity Channel (wider corridor)**
- 2. Cost Channel (no remuneration)**

# The Policy Rate and the Interest Rate Corridor

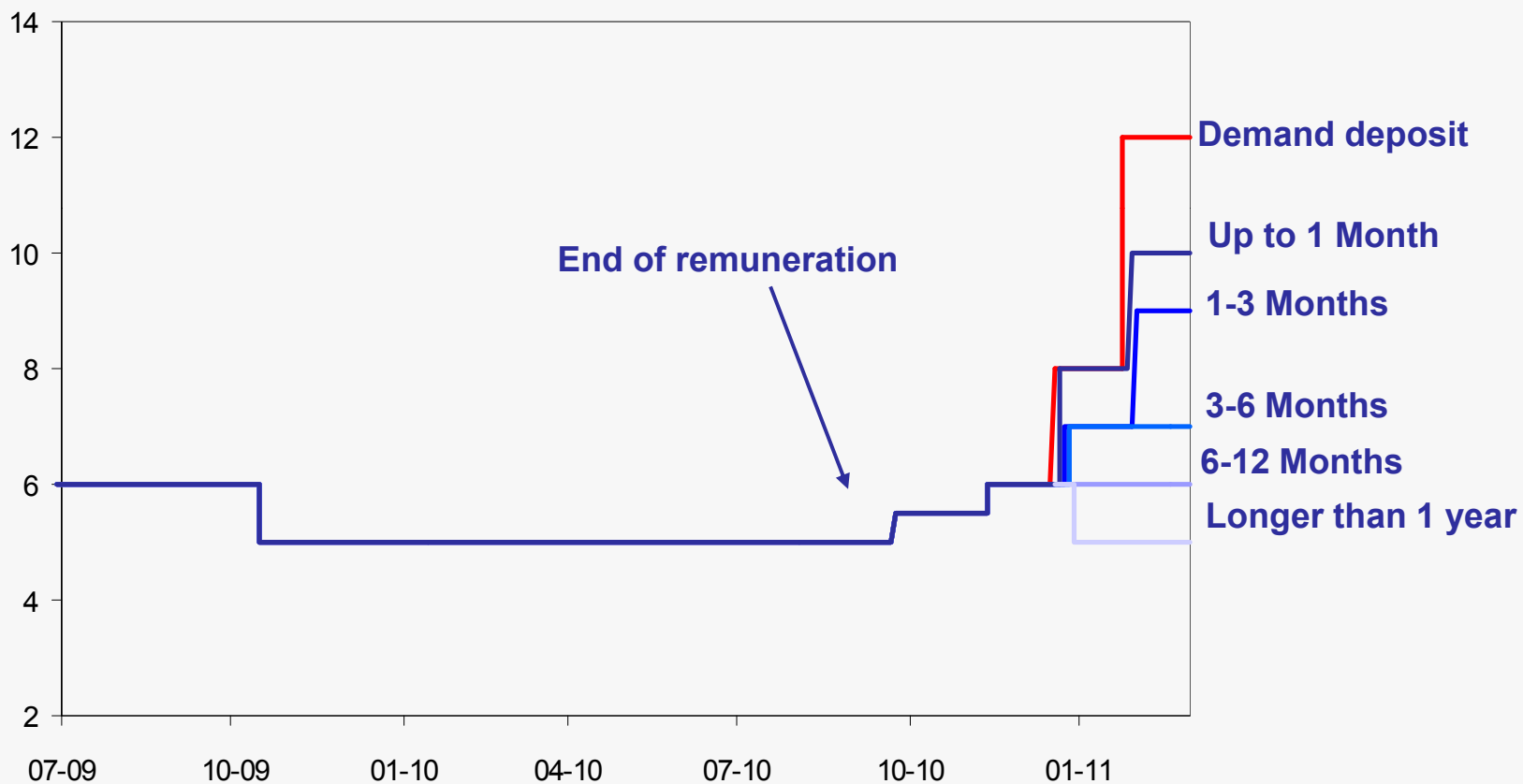
**Policy Rate and Interest Rate Corridor**  
(percent)



Source: CBRT

# Reserve Requirements as a Macroprudential Tool

**Reserve Requirement Ratios**  
(percent)

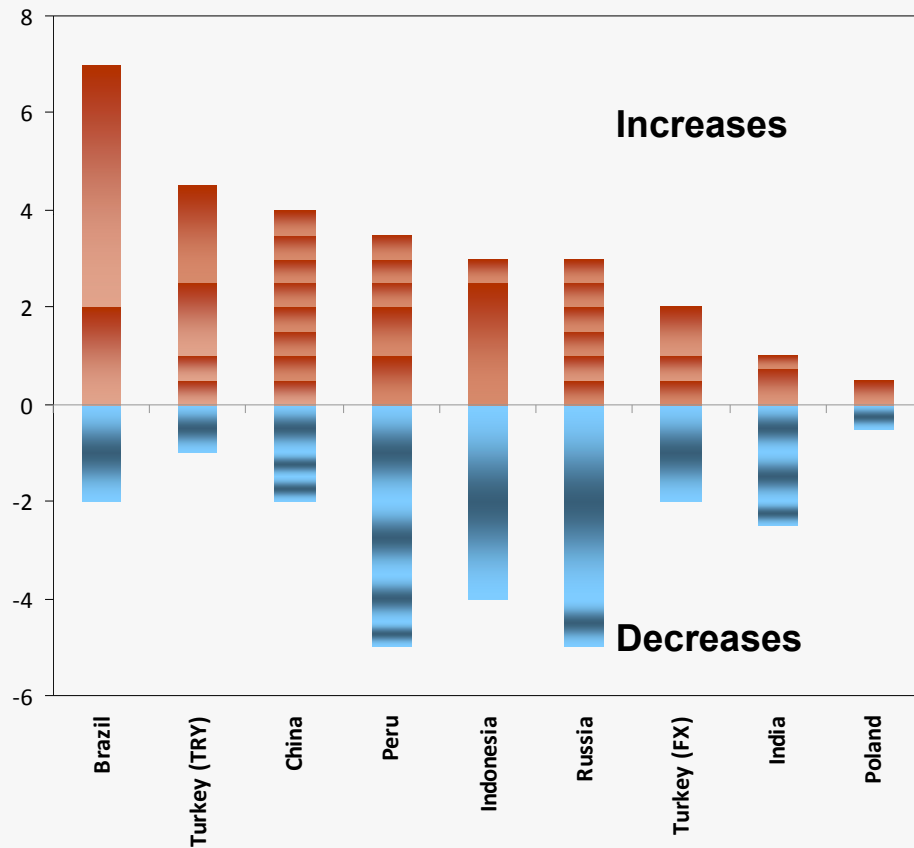


Source: CBRT



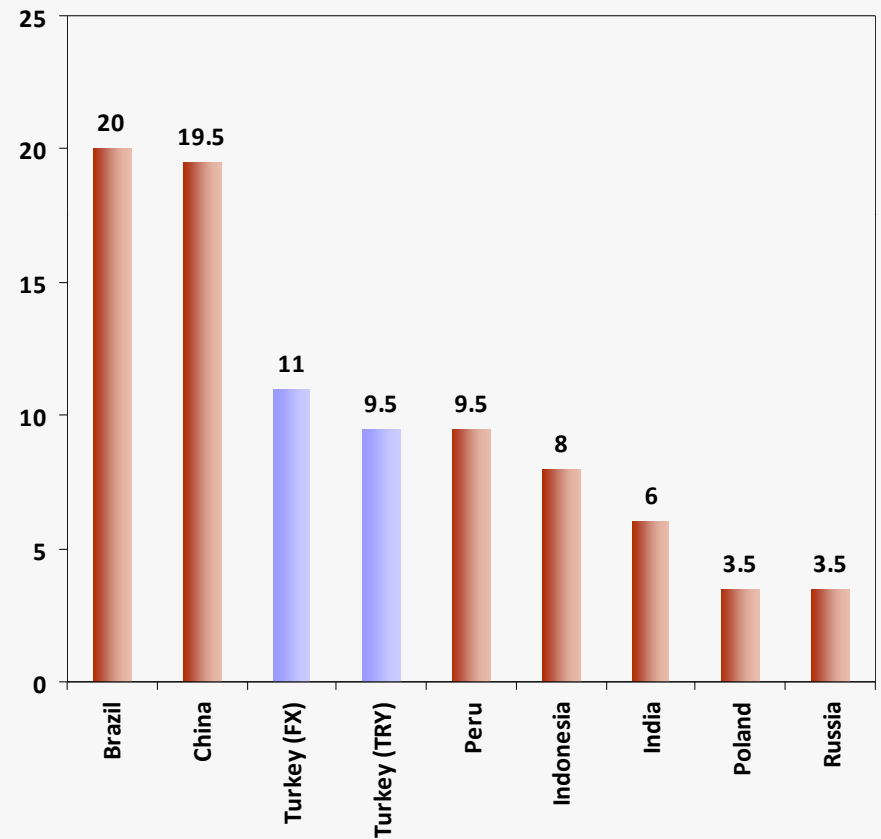
# Reserve Requirements as a Macroprudential Tool

**Change in RRR Since the Start of the Crisis**  
(percentage point)



Source: Central Banks, CBRT

**Current RRR**  
(percent)



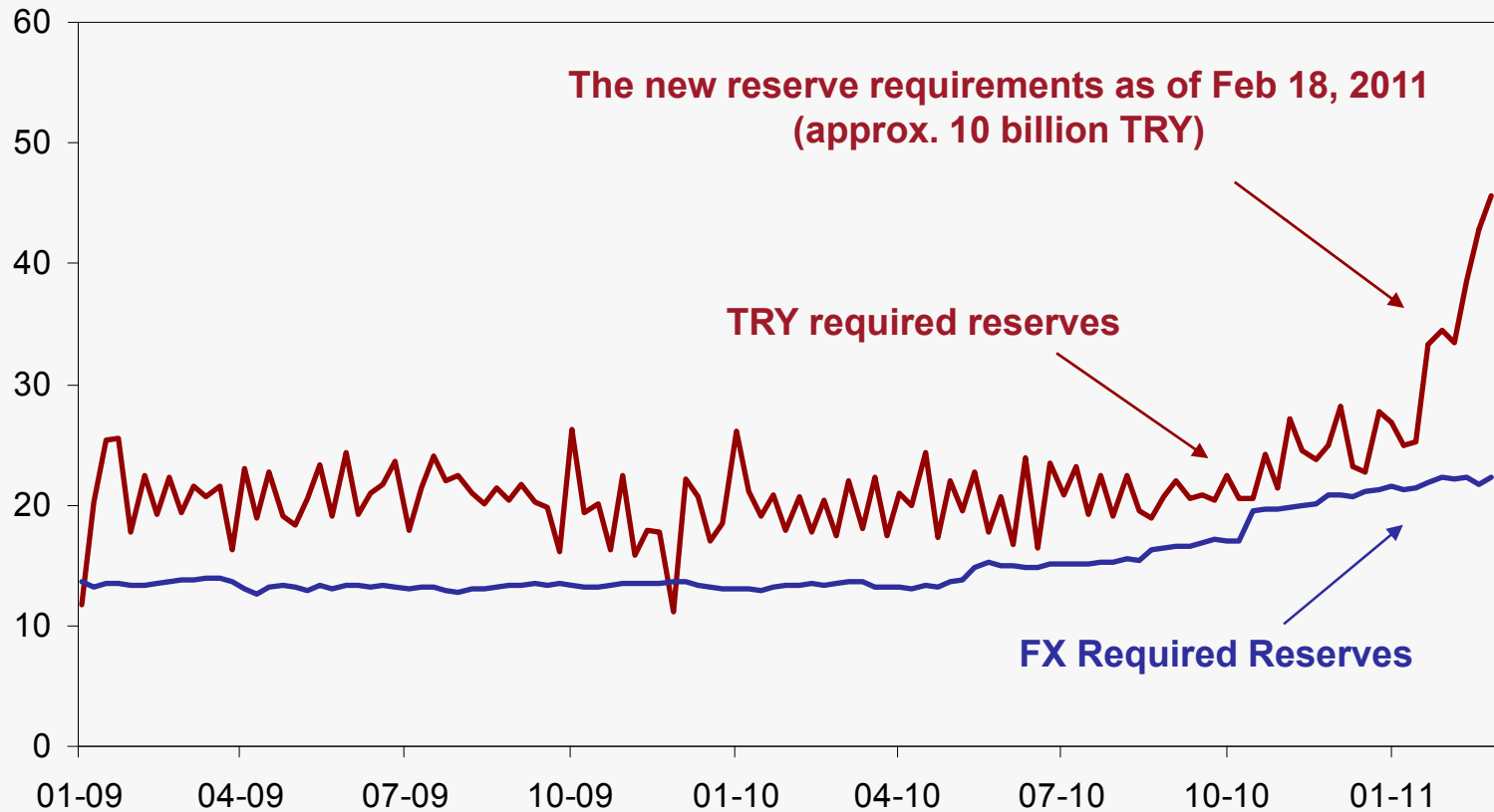
Source: Central Banks, CBRT

## Measures by Other Authorities

1. Fiscal discipline
2. No FX loans to households
3. Domestic currency bond market
4. Loan/value restrictions
5. Tax hikes on certain consumer loans
6. Restrictions on credit card borrowing

# Tightening the Liquidity

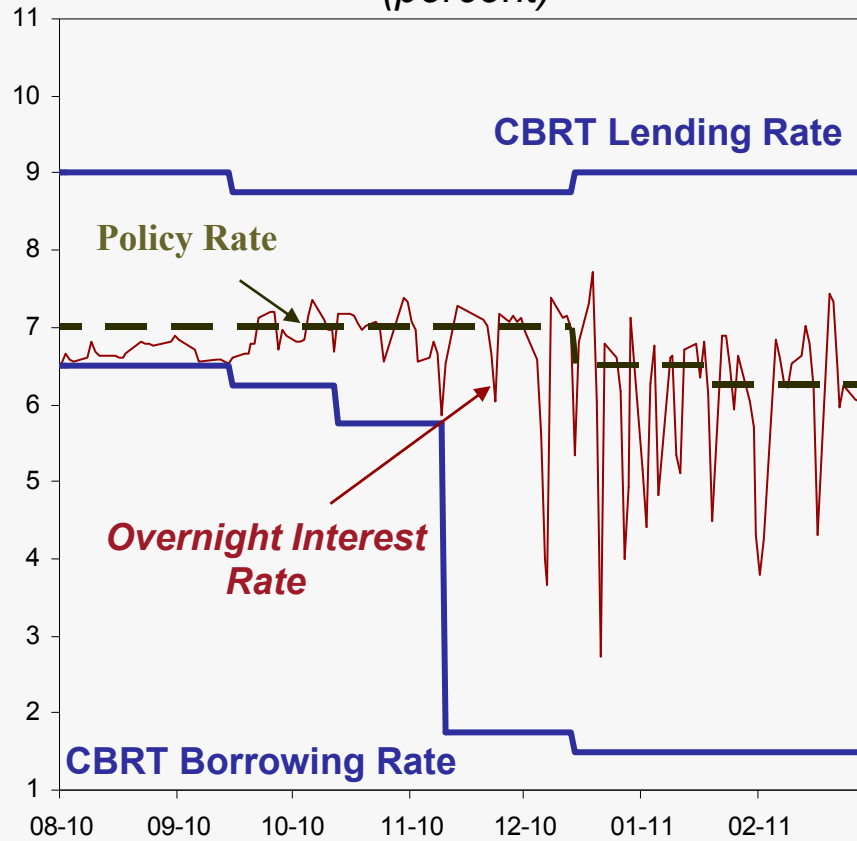
**Reserve Requirements Balances**  
(billion TRY)



Source: CBRT

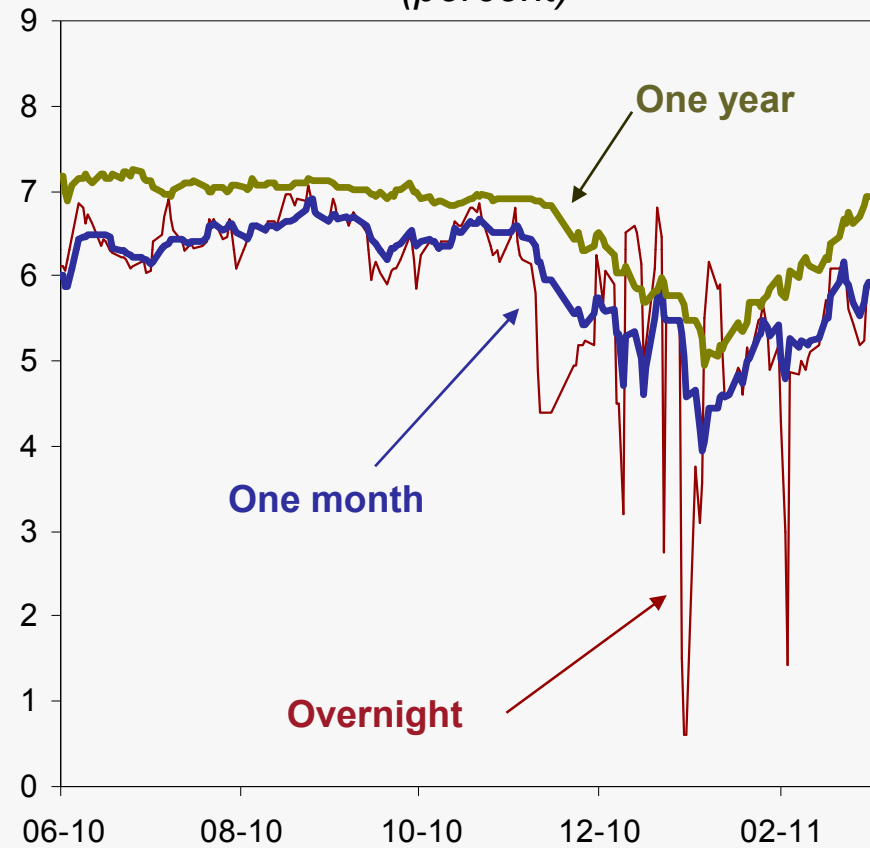
# Volatility in Money Markets

## Overnight Interest Rates (percent)



Source: ISE, CBRT

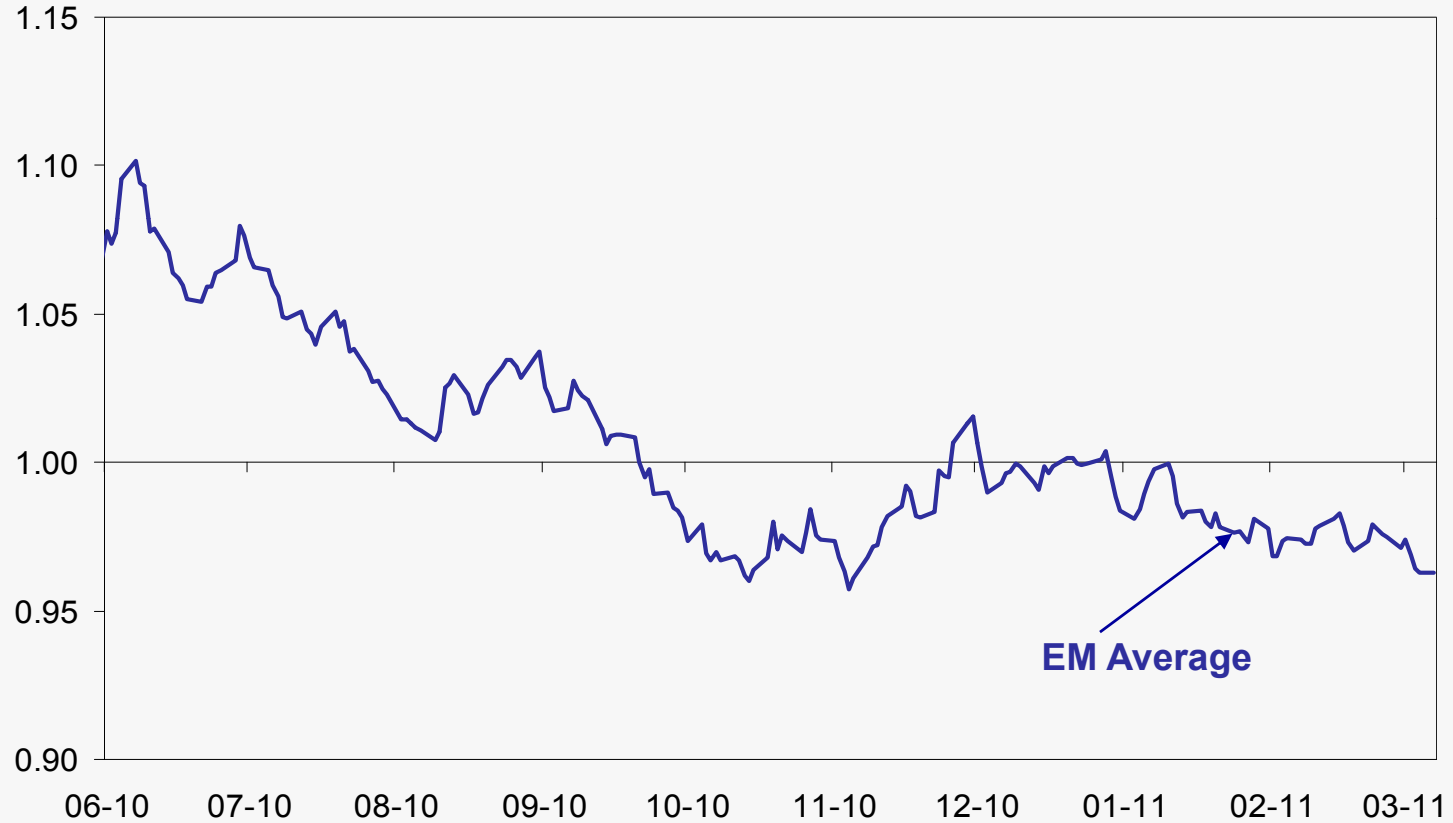
## Swap Rates (percent)



Source: Reuters, CBRT

# Appreciation Pressure

**EM currencies against USD\***  
(4 Jan 2010=1)

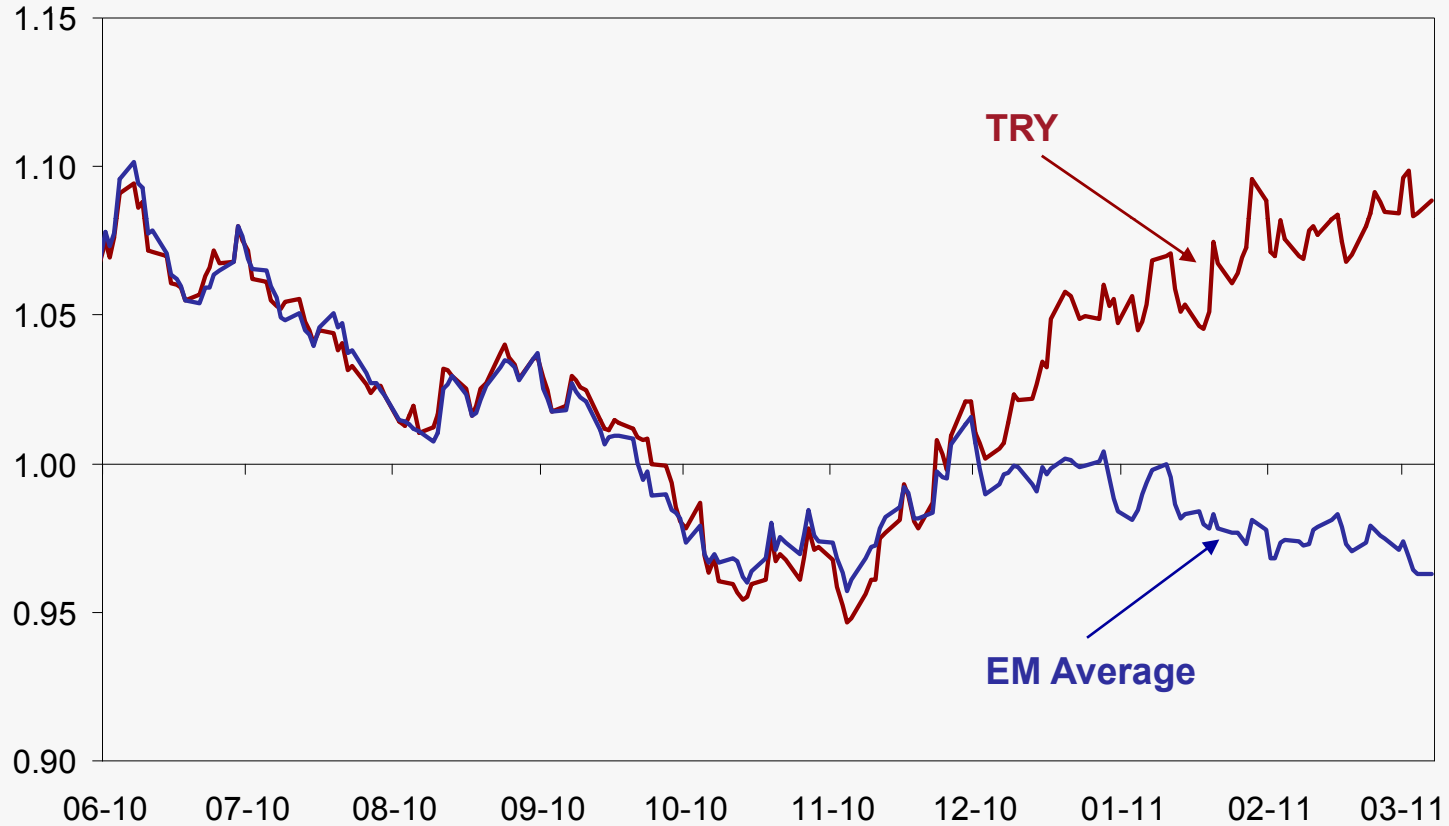


\*Average of emerging market currencies, including Brazil, Chile, Czech Republic, Hungary, Mexico, Poland, South Africa, Indonesia, South Korea and Colombia.

Source: Bloomberg, CBRT

# Initial Impact on Currency

**TRY and other EM currencies against USD\***  
(4 Jan 2010=1)

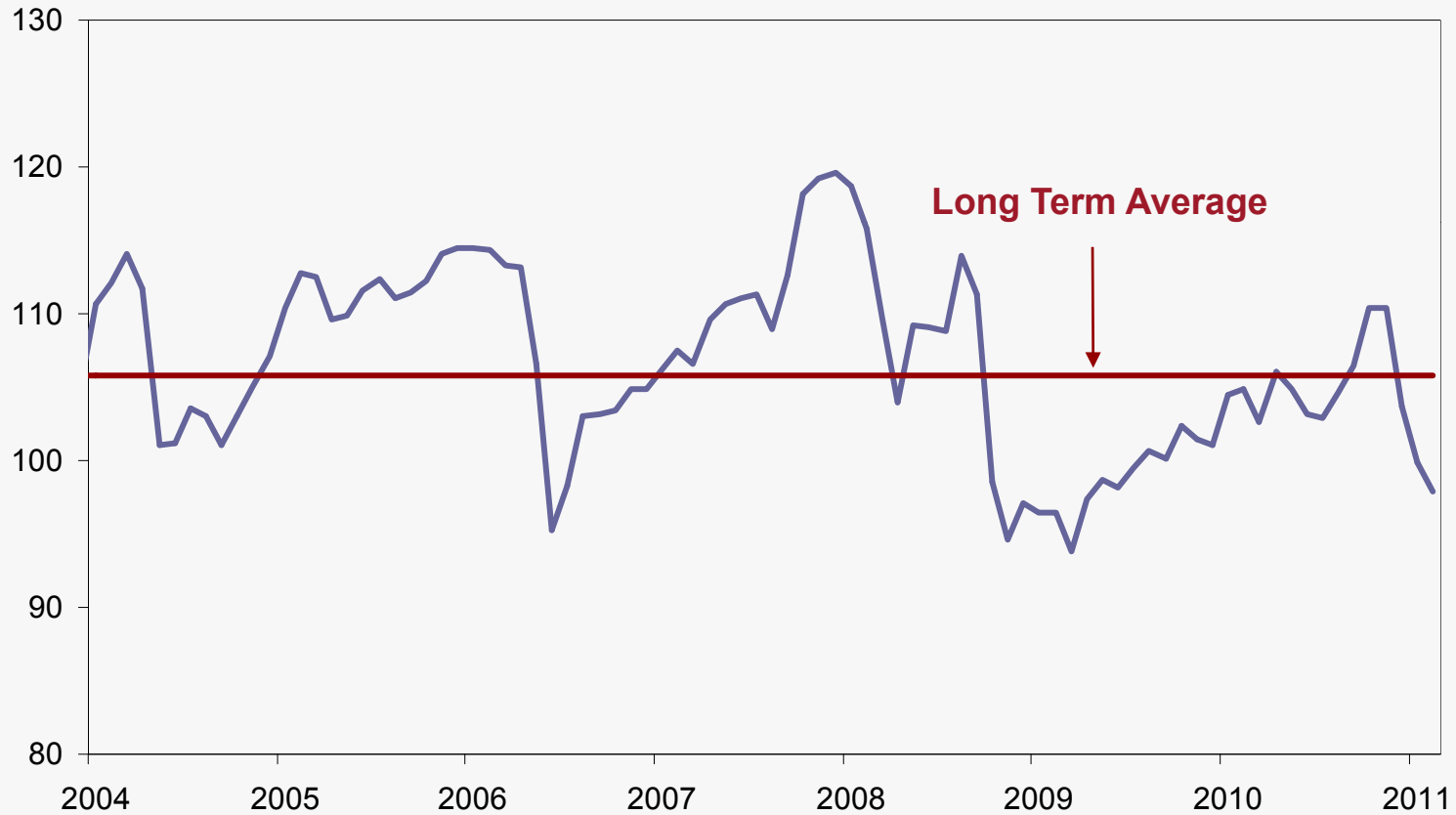


\*Average of emerging market currencies, including Brazil, Chile, Czech Republic, Hungary, Mexico, Poland, South Africa, Indonesia, South Korea and Colombia.

Source: Bloomberg, CBRT

# Initial Impact on Currency

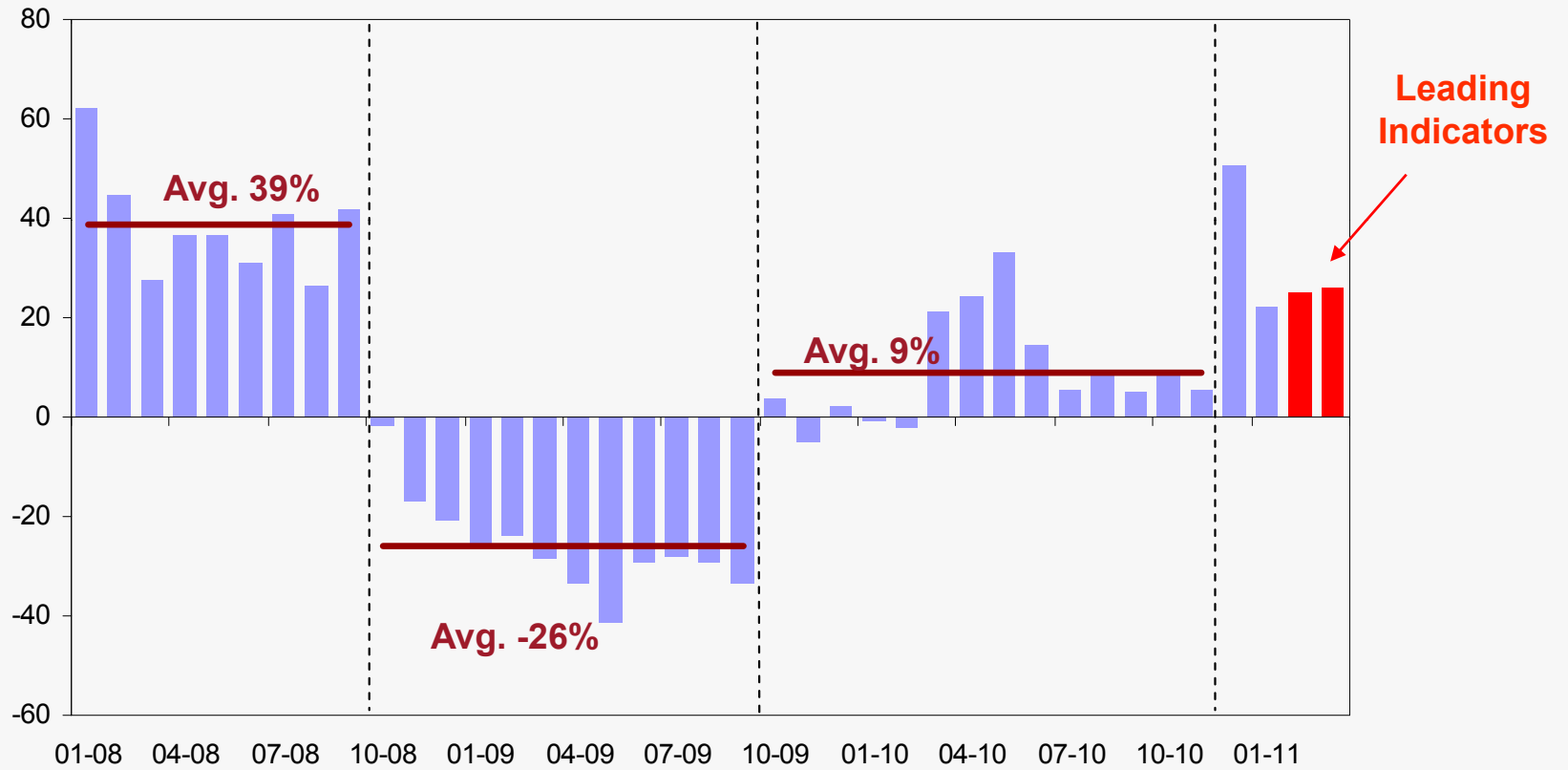
**Real Effective Exchange Rate**  
(CPI-based, against developing countries, 2003=100)



Source: CBRT

# Exports

**Goods Exports**  
(year-on-year percentage change)

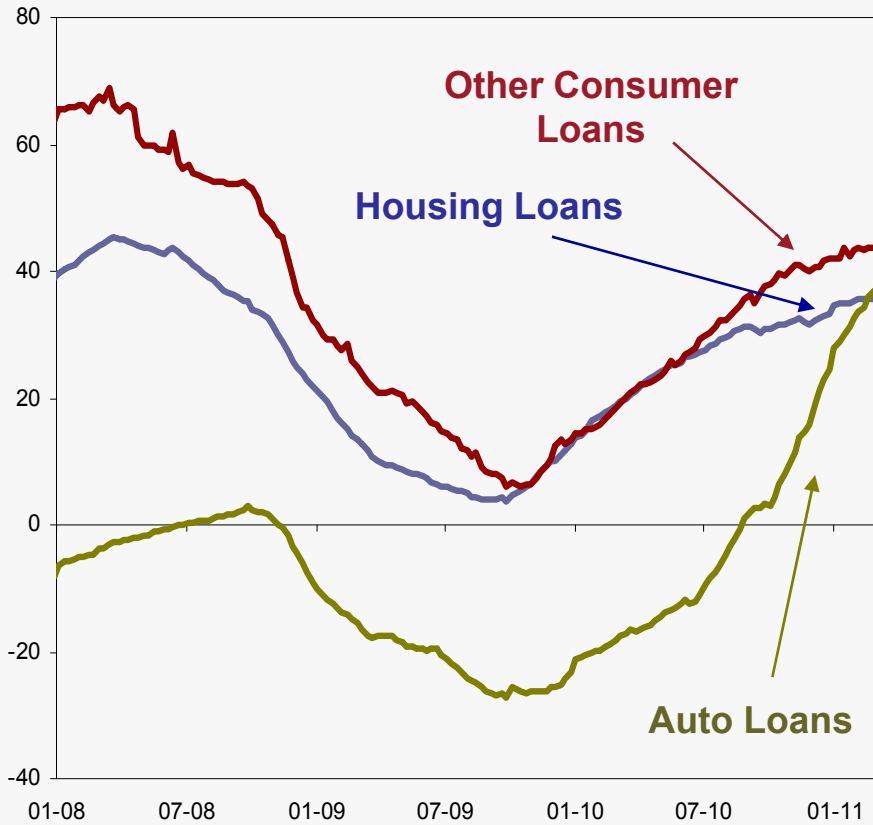


Source: TurkStat, Turkish Exporters Assembly, CBRT



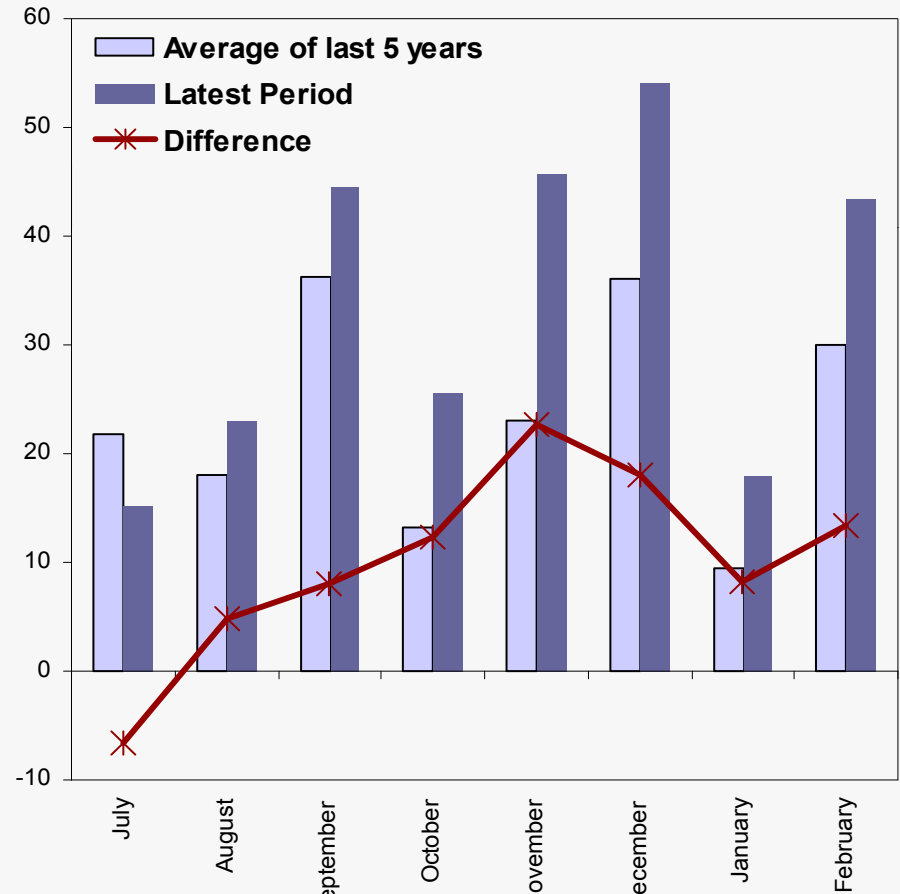
# Credit Growth

**Household Loans**  
(year-on-year change, percent)



Source: CBRT

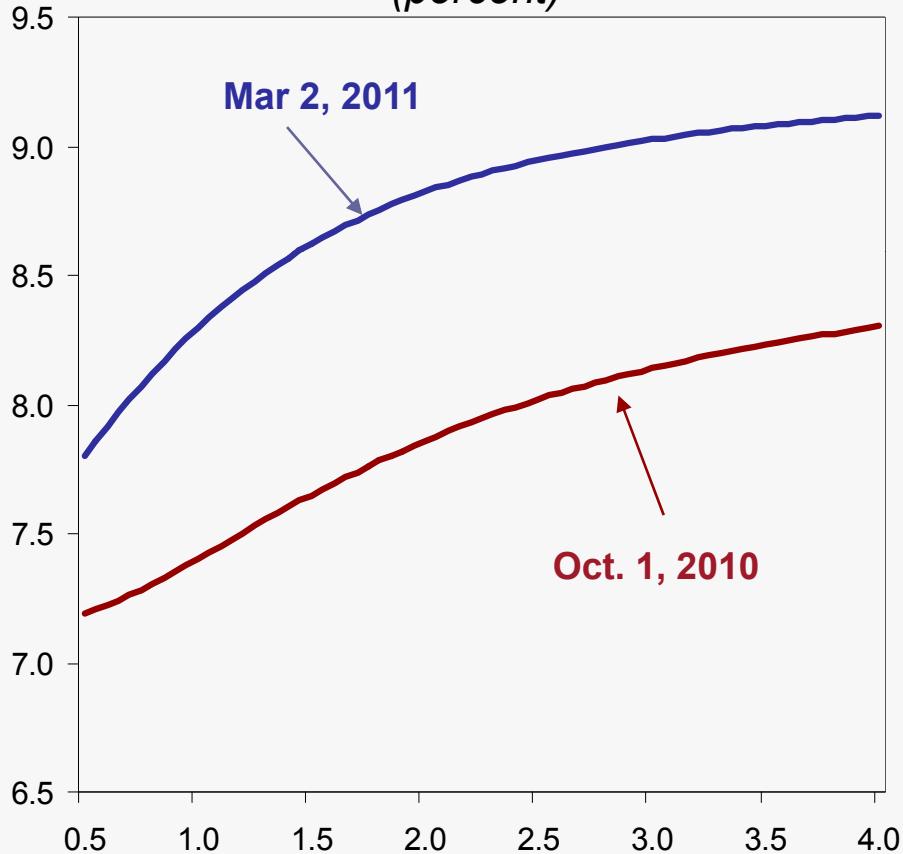
**Total Loans**  
(annualized monthly change, percent)



Source: CBRT

# QT and Inflation Expectations

**Yield Curve\***  
(percent)



\* Calculated from the compounded returns on bonds quoted in ISE Bills and Bonds Market by using ENS method.  
Source: ISE, CBRT

**Inflation Expectations\***  
(percent)



\* CBRT Expectations Survey results from the second survey period.  
Source: ISE, CBRT

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