

# MACROECONOMIC OUTLOOK AND MONETARY POLICY IN TURKEY

April 1, 2021

Ankara

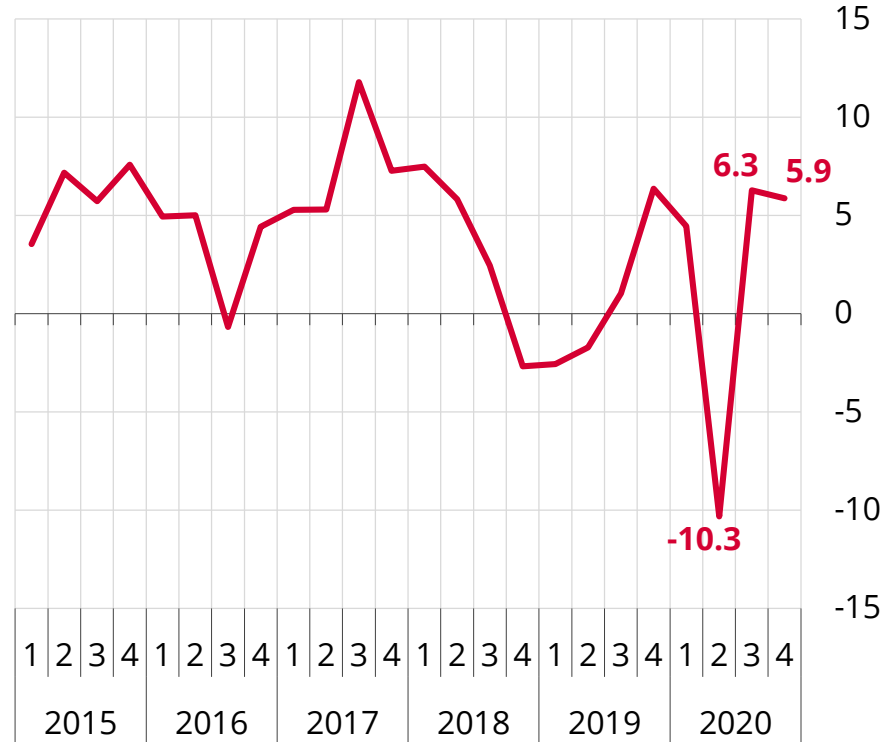


# Economic Activity

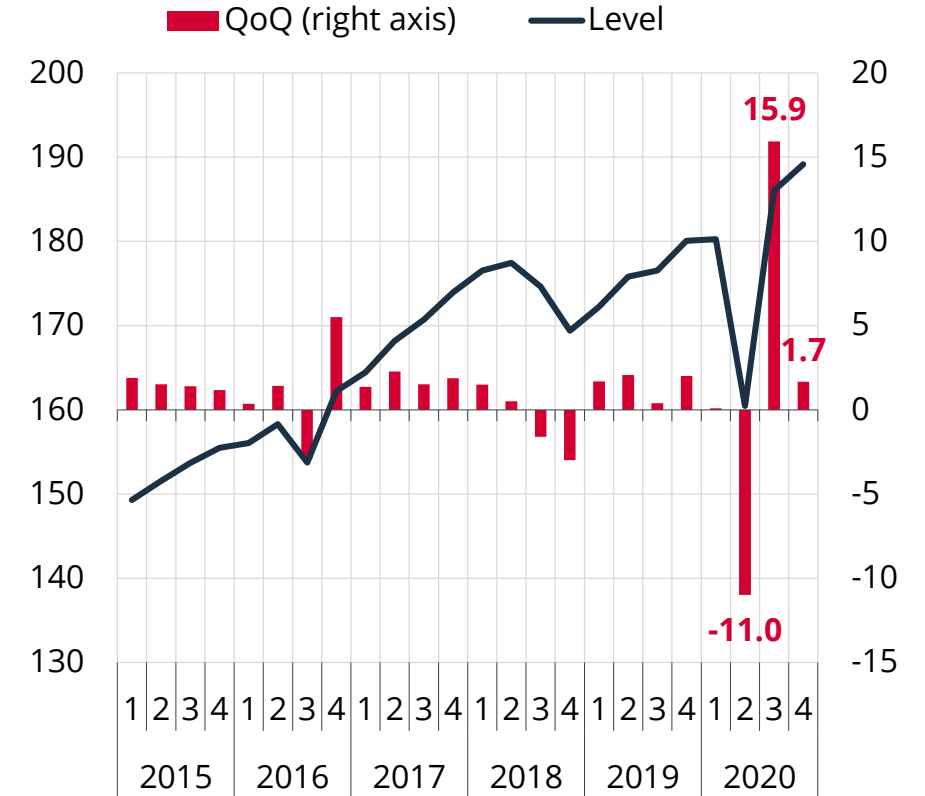
Economic activity remained strong in the last quarter of 2020.

The vigorous rebound in the second half of the year paved the way for a positive annual growth rate of 1.8%.

### Gross Domestic Product (Y-o-Y Growth Rate, %)



### Gross Domestic Product (Seasonally and Calendar Adjusted, Chain-Linked Volume Index, 2009=100)



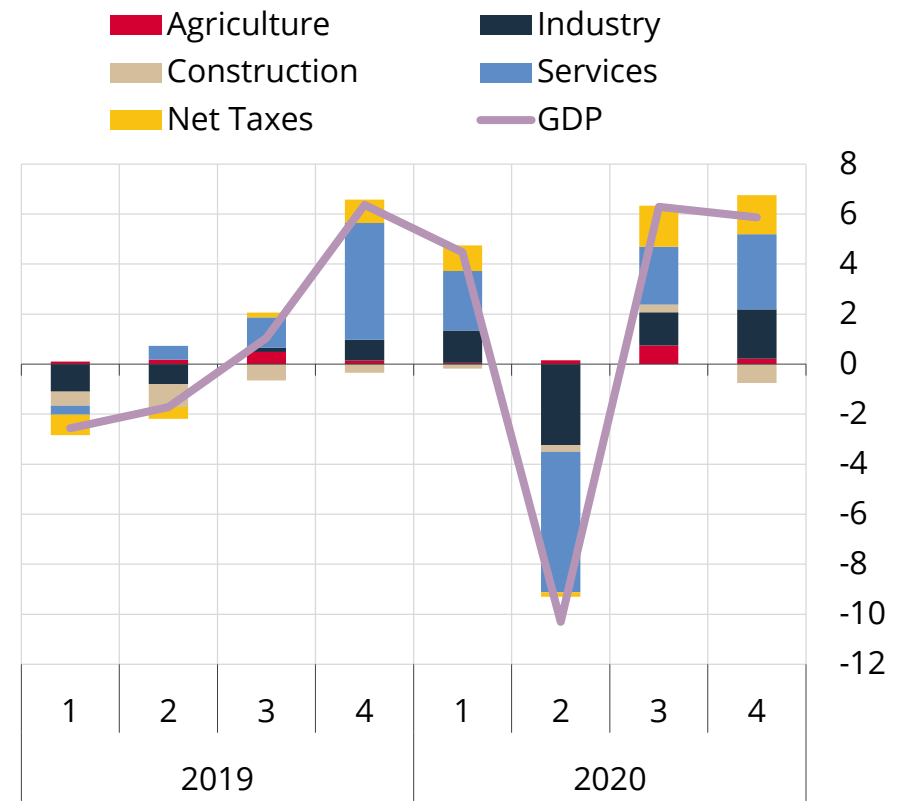
Source: TURKSTAT

Last Observation: 2020Q4

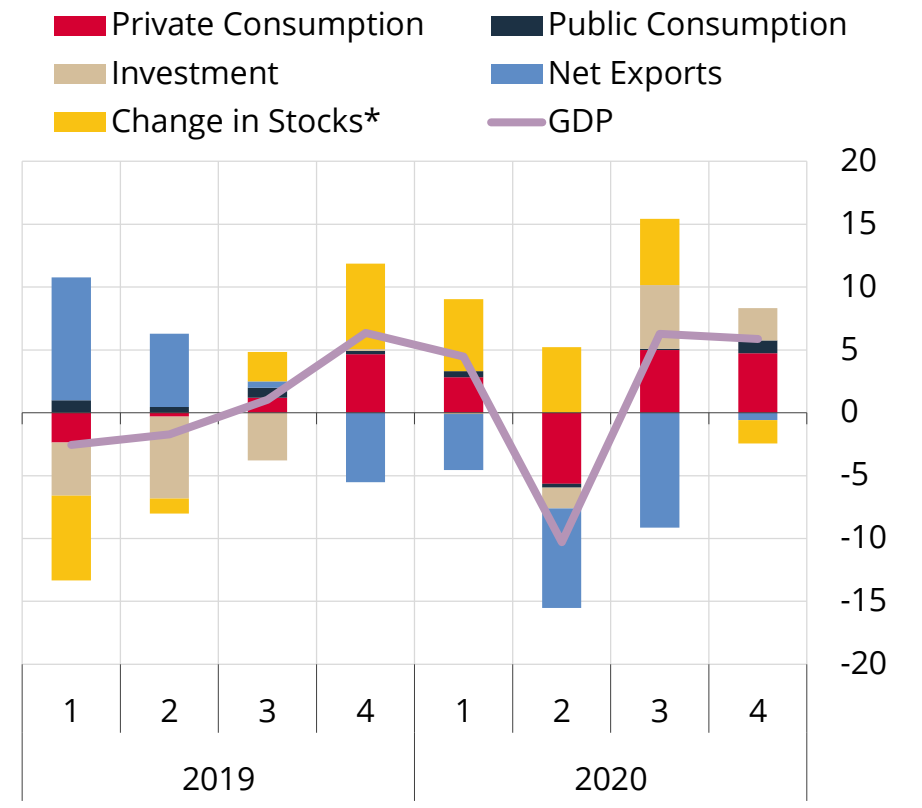
# Economic Activity

Domestic demand was brisk, as envisaged. The overall growth picture (pace and composition) was broadly consistent with the MPC's earlier assessment that demand conditions were at inflationary levels in the last quarter of 2020.

### Contribution to Annual GDP Growth from Production Side (% Point)



### Contribution to Annual GDP Growth from Expenditure Side (% Point)



Source: CBRT, TURKSTAT

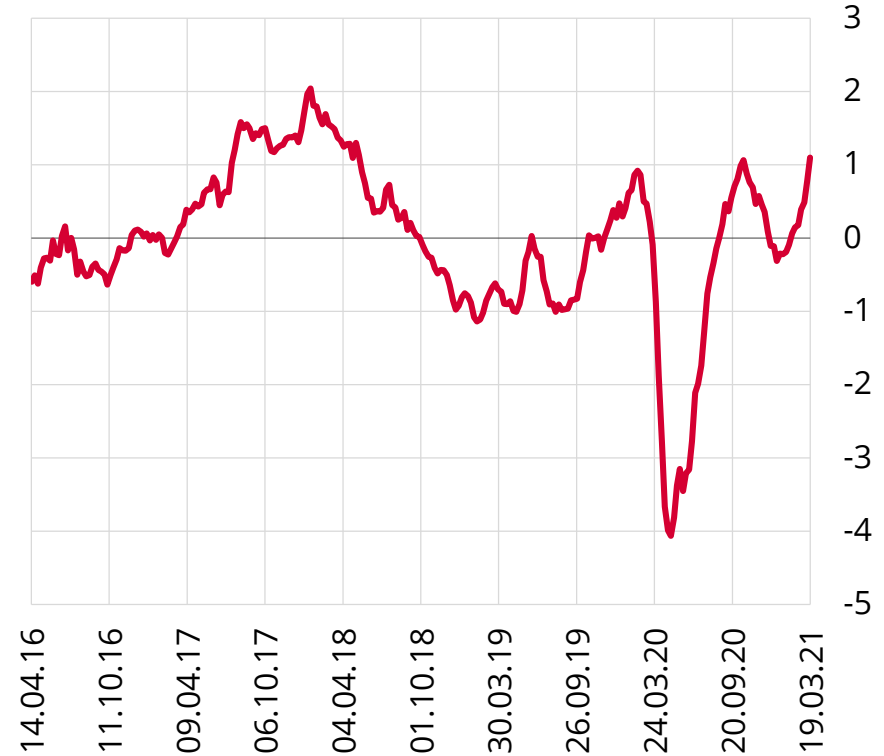
Last Observation: 2020Q4

\* Includes statistical discrepancy due to chain linking.

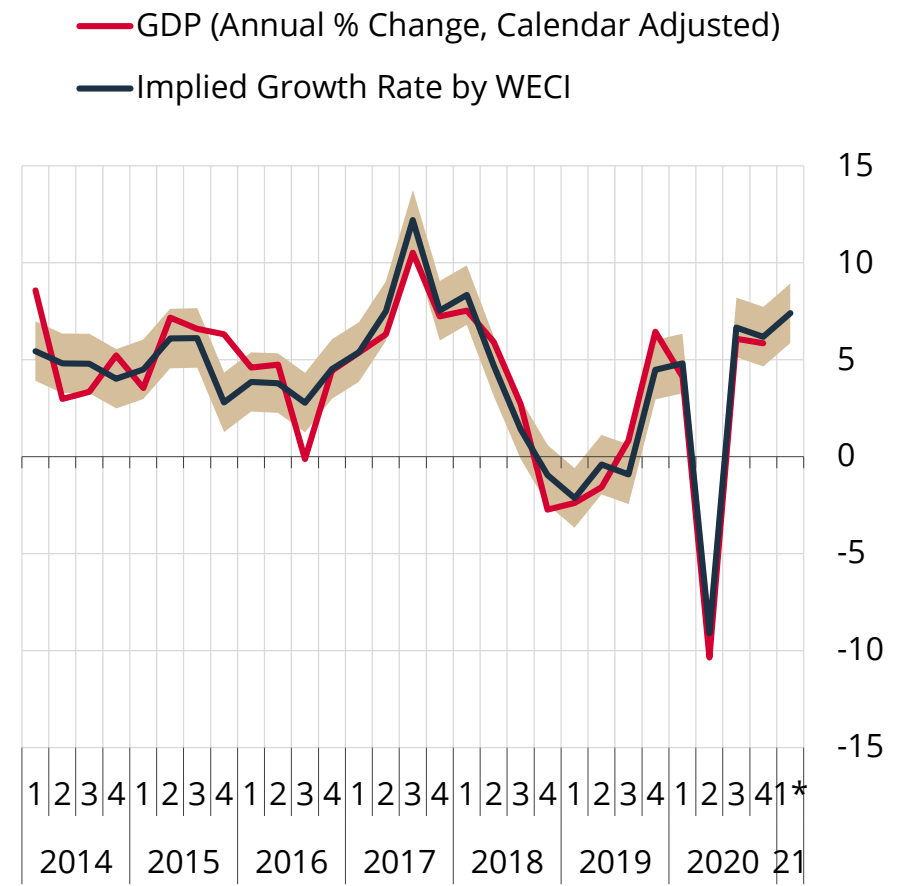
# Economic Activity

High-frequency data indicate that economic activity has gained strength amid credit developments and partial normalization. Being higher-than-projected, it remains above-trend with a strong momentum. Nevertheless, risks for economic activity remain significant depending on possible developments regarding the course of the pandemic.

**Weekly Economic Conditions Index\*\* (WECI, 4-Week Moving Average)**



**GDP and WECI\*\*\* (%)**



Source: CBRT

\* Last Observation: March 19, 2021

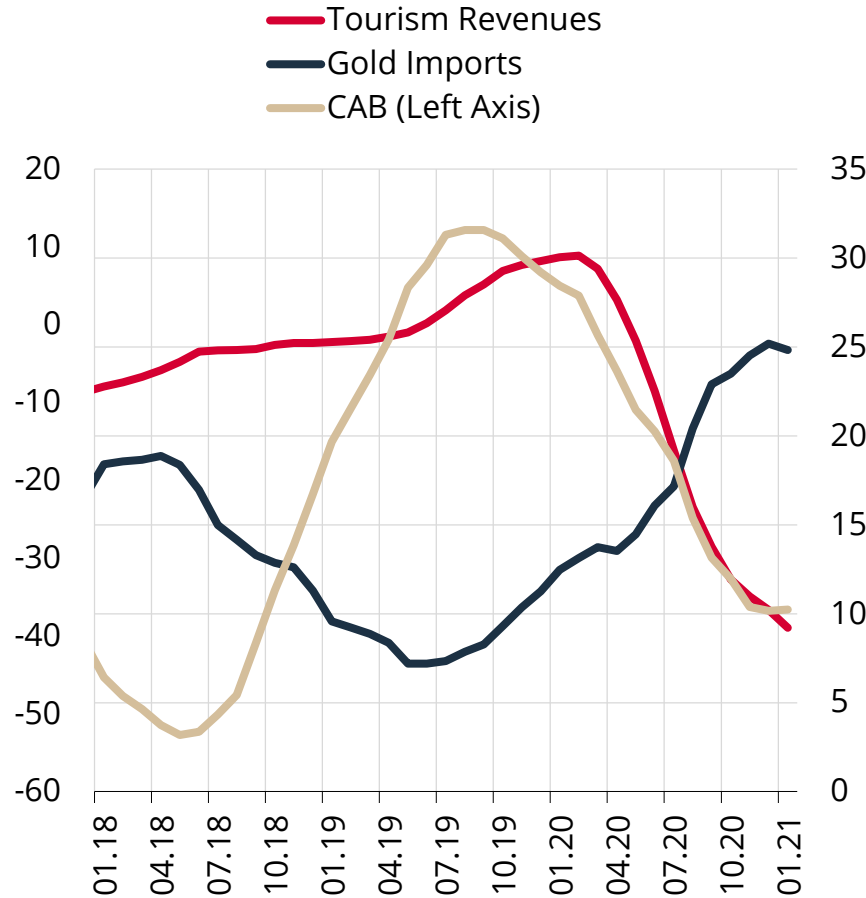
\*\* The index is constructed in a way that the mean and standard deviation of the index are 0 and 1, respectively. Index value shows the distance (high/low) from the mean in terms of the standard deviation.

\*\*\* Forecast band shows one standard deviation of the forecast error.

# External Balance

Strong domestic demand due to the cumulative effects of high credit growth during the pandemic and the rise in import prices continue to adversely affect the current account balance.

**Current Account Balance, Gold Imports, Tourism Revenues**  
(Billion USD, 12 Month Cumulative)

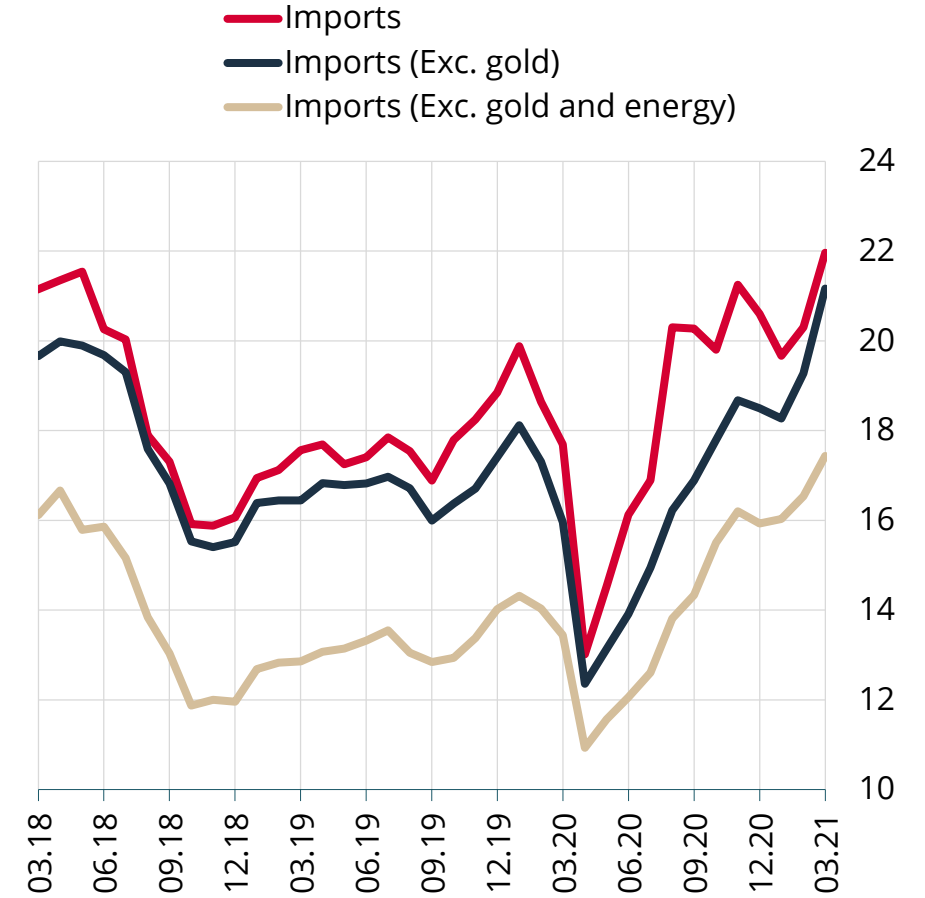


Source: CBRT, TURKSTAT

Last Observation: January 2021

\*March data are provisional.

**Imports\***  
(Billion USD, Seasonal and Calendar Adjusted)



Source: TURKSTAT, Ministry of Trade

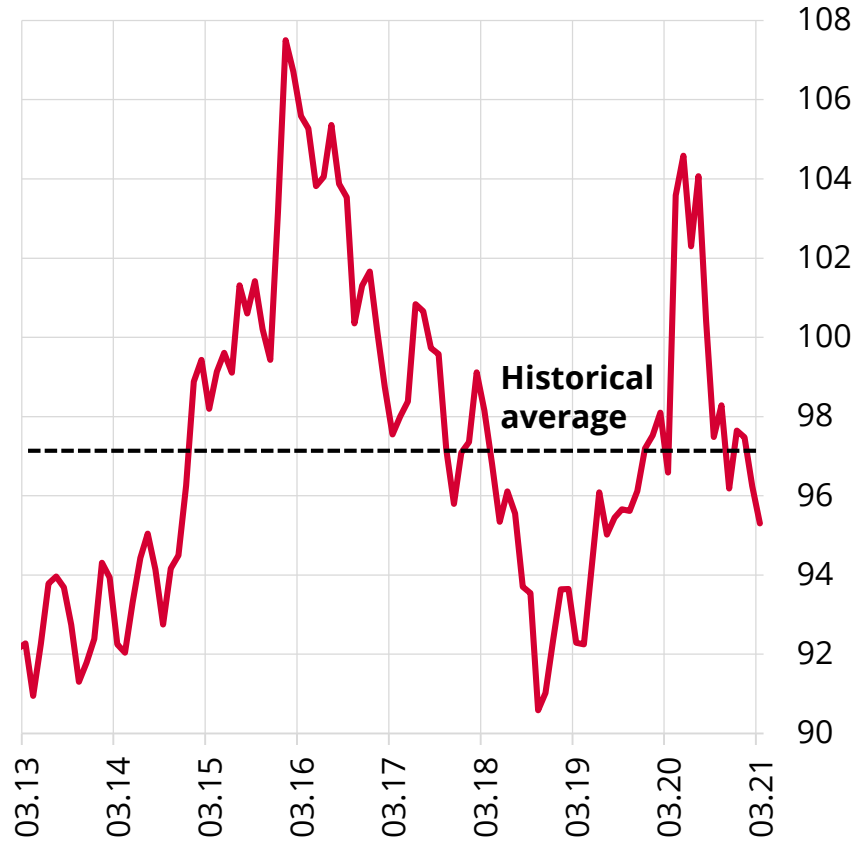
Last Observation: February 2021

# External Balance

Import prices have risen faster than export prices since the second half of 2020 and the developments in terms of trade have had a more pronounced impact on the foreign trade deficit.

Gold imports have decelerated markedly and started to hover around the historical average since the second half of January.

### Terms of Trade\* (Px/Pm, 2015=100)

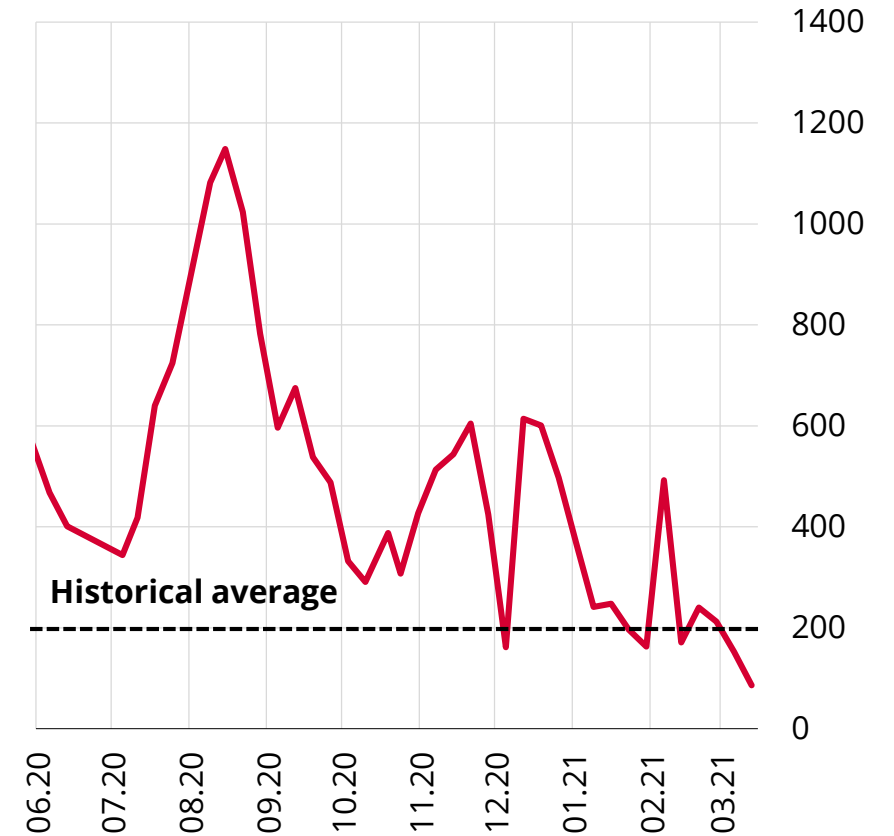


Source: CBRT, TURKSTAT

Last Observation: January 2021

\* February and March 2021 unit prices are CBRT's forecasts.

### Gold Imports (Weekly, Million USD)



Source: Ministry of Trade

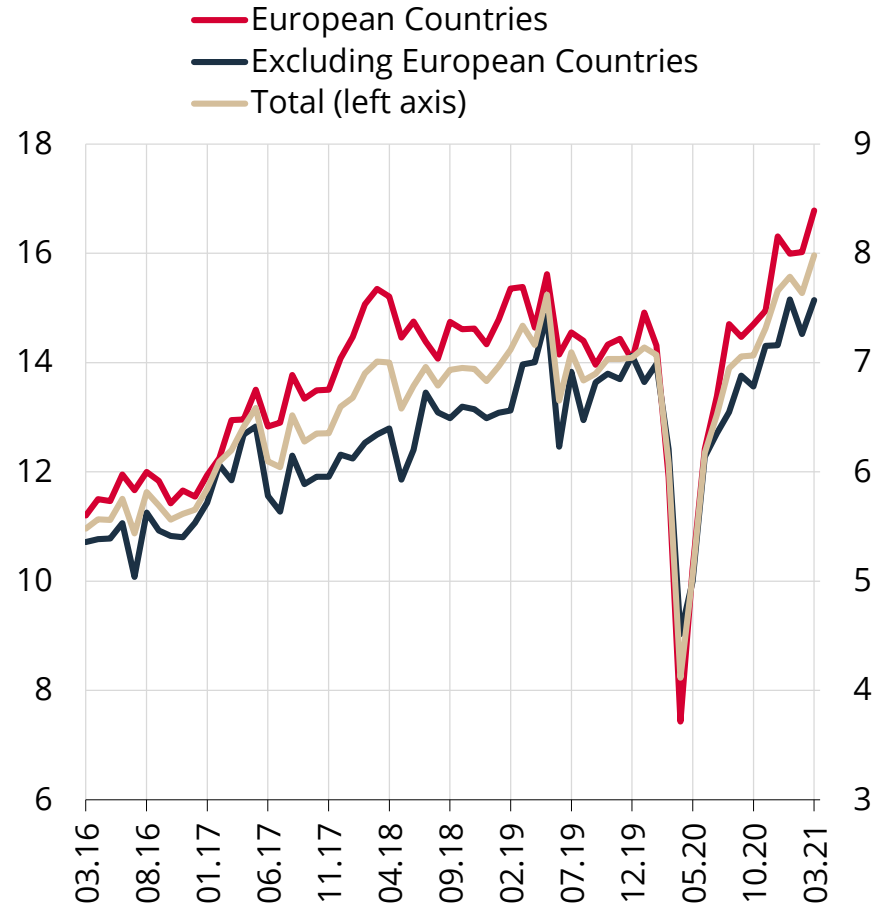
Last Observation: 27 March 2021

# External Balance

Exports to both European and non-European countries display a strong upward trend.

Despite the restraining effects of pandemic measures, strong outlook for the manufacturing industry in Eurozone support export growth.

**Exports\* (Billion USD, Seasonal and Calendar Adjusted)**

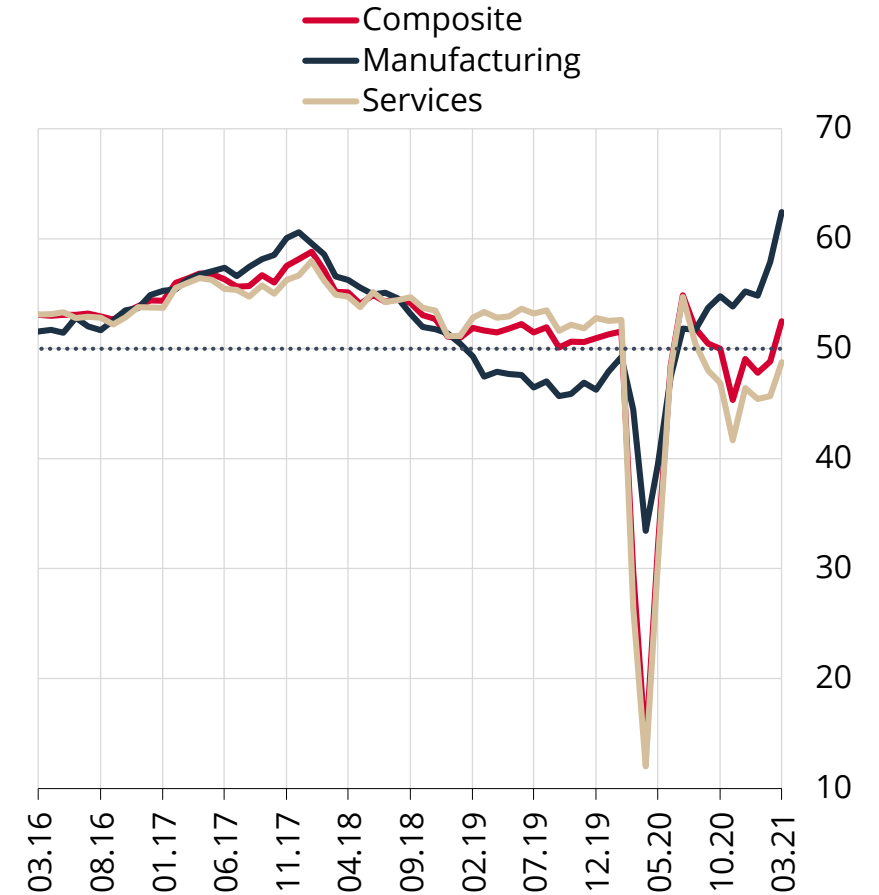


Source: CBRT, TEA, TURKSTAT

Last Observation: February 2021

\* March data are provisional.

**Eurozone PMI (Seasonally Adjusted, Level)**



Source: IHS Markit

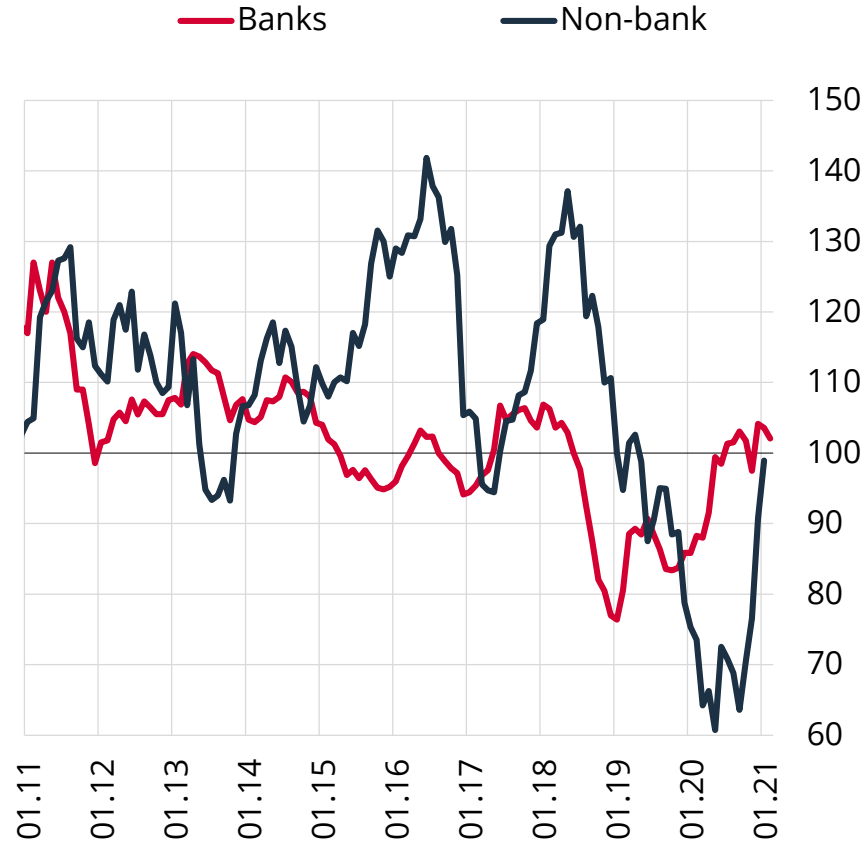
Last Observation: March 2021

# External Finance

Corporate and banking sector have no difficulty in renewing their FX debt.

Portfolio flows to EMs have been affected by rising global inflation expectations and long-term bond rates leading to uncertainties about advanced economy monetary policies, and volatility in global financial markets.

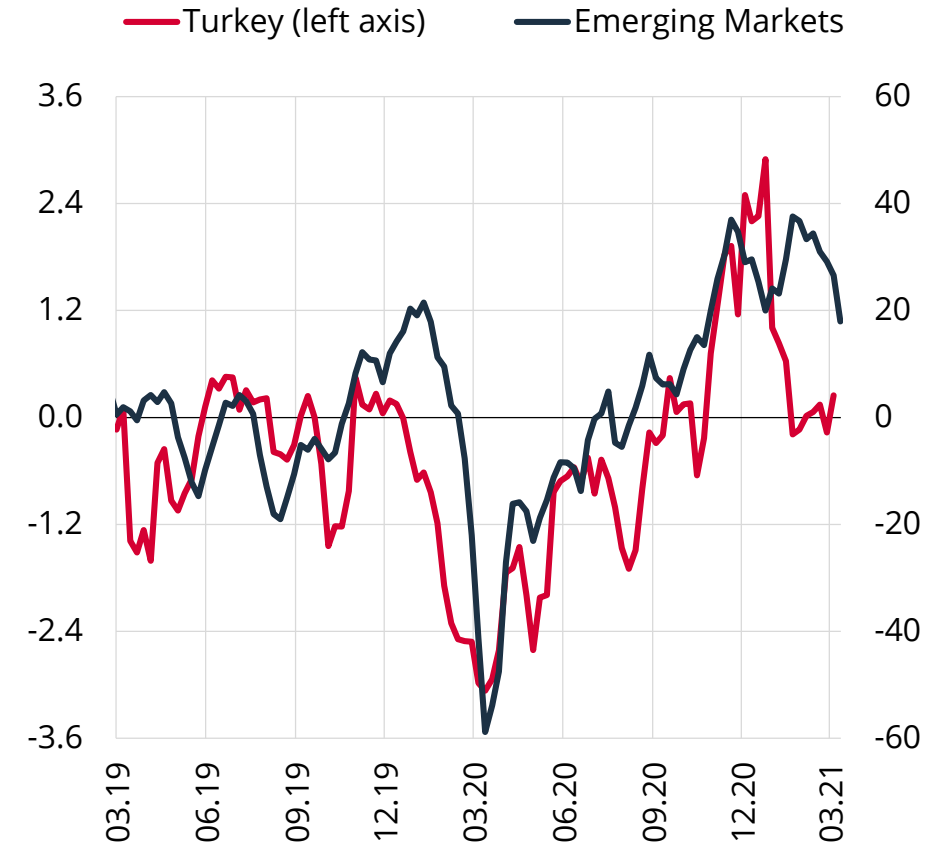
External Debt Rollover Ratio (6 Months, %)



Source: CBRT

Last Observation: Banks: February 2021  
Non-bank: January 2021

Portfolio Flows to Turkey and Emerging Markets\* (4-Week Cumulative, Billion USD)



Source: CBRT, EPFR

Last Observation: March 19, 2021 for Turkey;  
March 26, 2021 for Emerging Markets

\* Turkey data include portfolio inflows to stocks and GDDS market. Repo is included in the GDDS data. Emerging Markets data are from the EPFR database and include all the database-covered funds' weekly net investments in equity and GDDS markets in emerging economies.

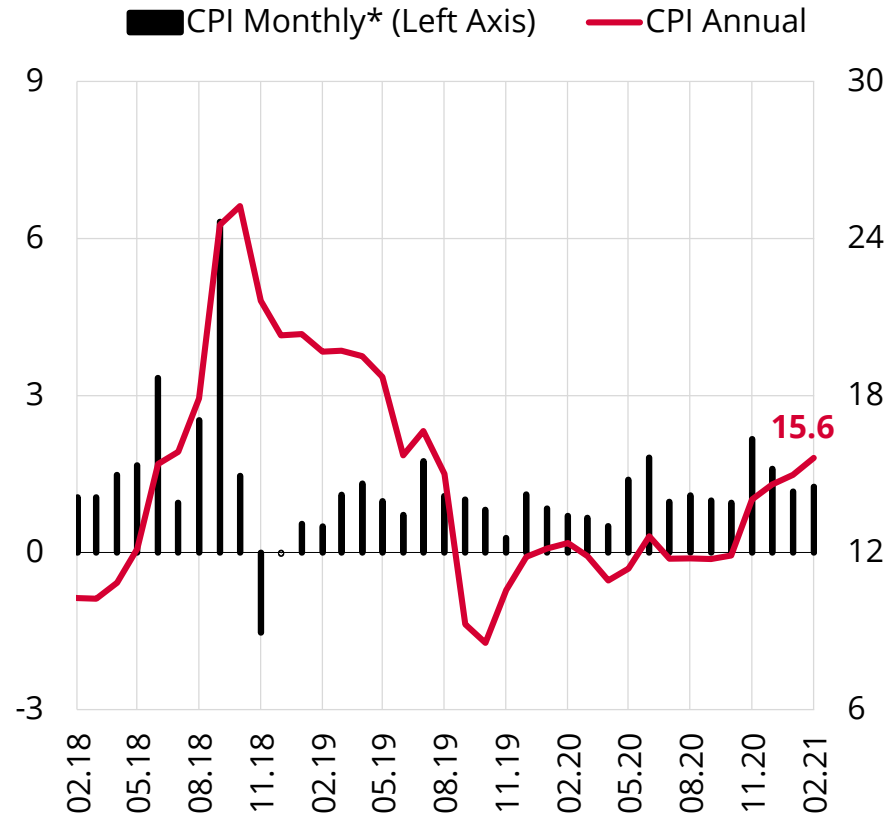


# Inflation

Domestic demand conditions, accumulated costs, rise in international food and other commodity prices, and high levels of inflation expectations continue to affect inflation outlook adversely.

Producer inflation has been on an uptrend on the back of soaring commodity prices, disruptions in the supply chain and brisk demand conditions.

### Consumer Prices (Monthly, Annual % Change)

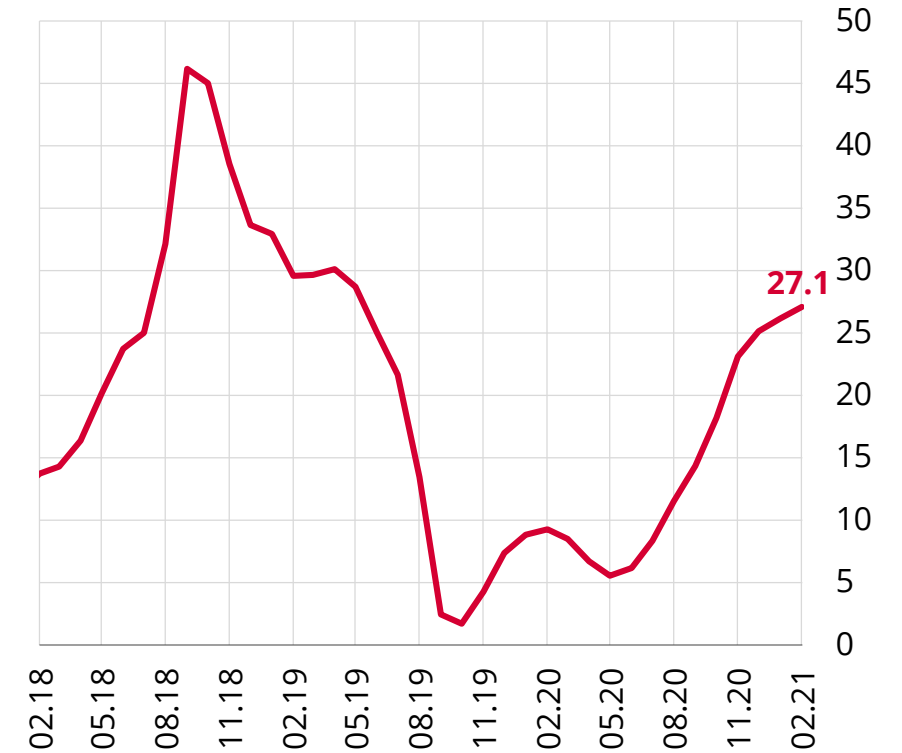


Source: CBRT, TURKSTAT

Last Observation: February 2021

\* Seasonally Adjusted.

### Domestic Producer Prices (Annual % Change)



Source: TURKSTAT

Last Observation: February 2021

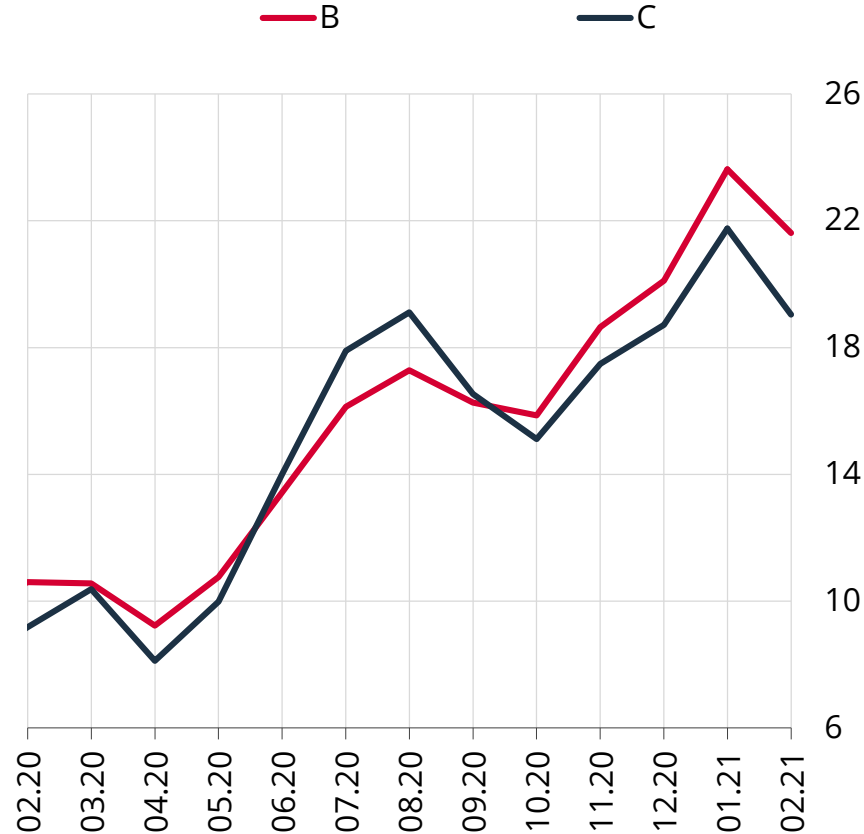
# Underlying Inflation

Underlying inflation eased in February, but remained elevated.

Core goods trend partly improved, while processed food was flat at a high level.

Services inflation has been sticky in double digits, reflecting the backward indexation behavior in wage and price setting.

**Core Inflation\* Trend**  
(Seasonally Adjusted, Annualized, 3-Month Moving Average % Change)

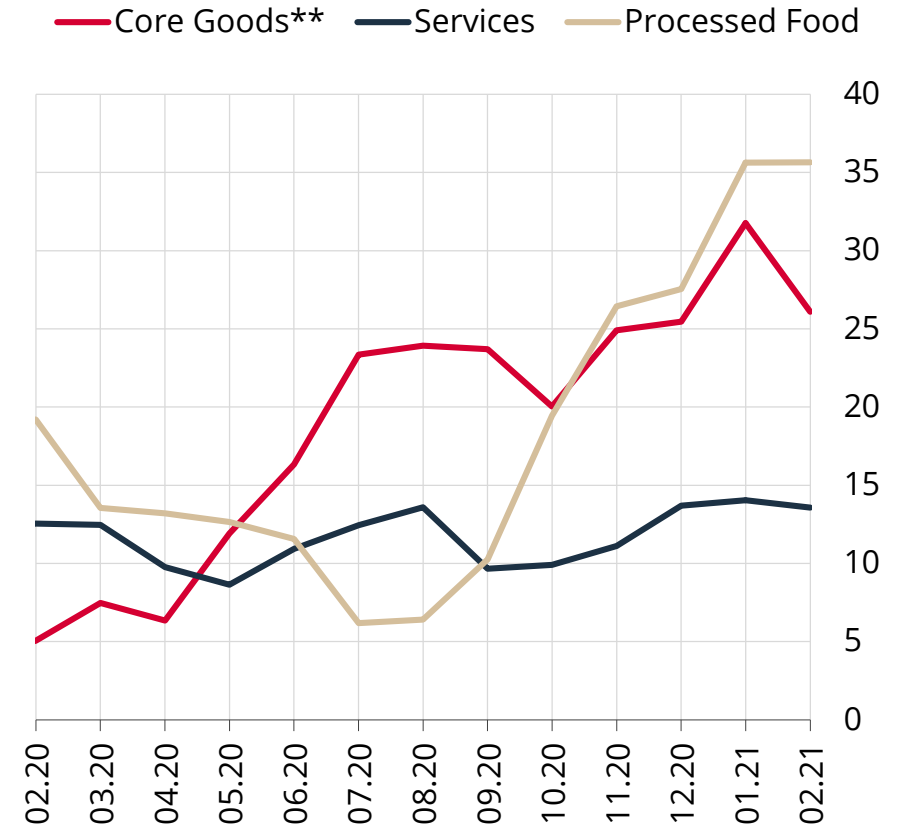


Source: CBRT

\* B and C indices adjusted for tax effect.

\*\* Core goods trend adjusted for tax effect.

**Subgroups of B Index**  
(Seasonally Adjusted, Annualized, 3-Month Moving Average % Change)



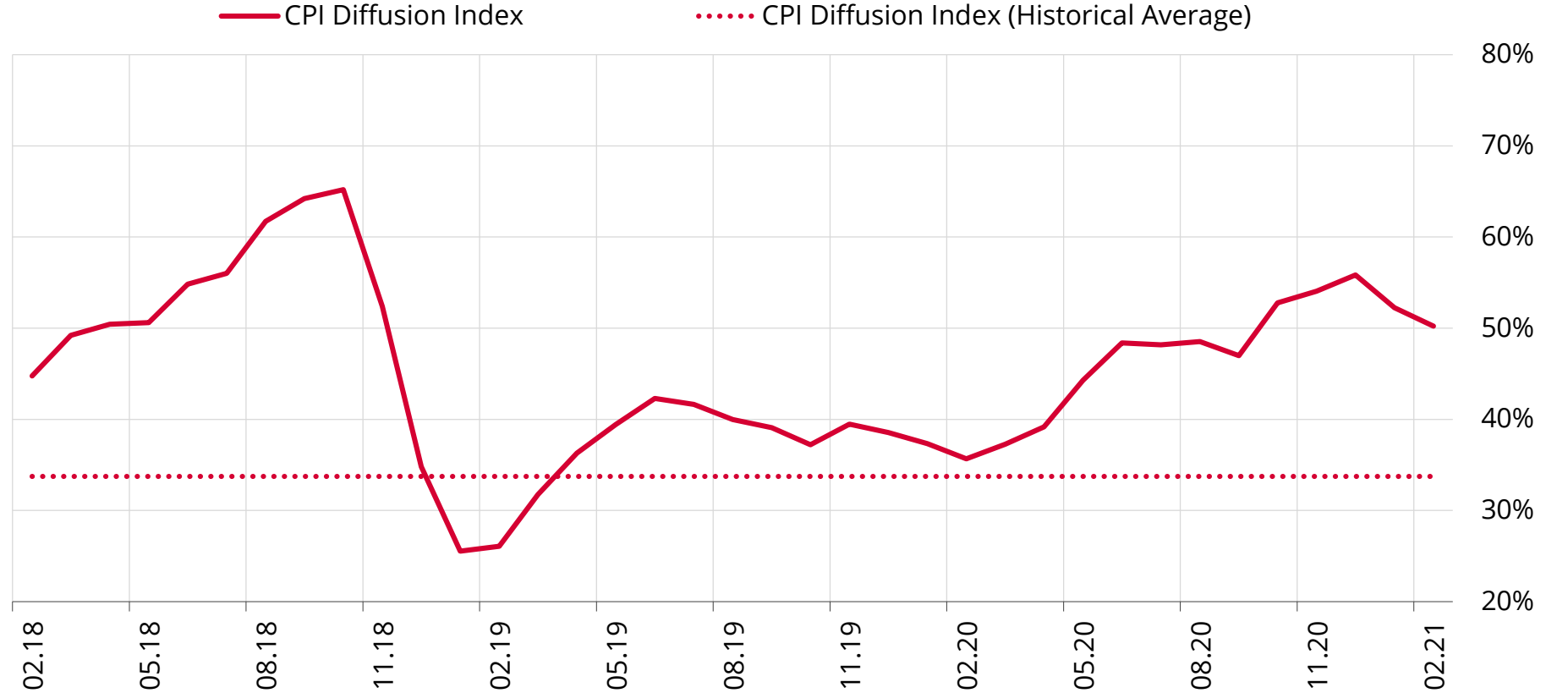
Last Observation: February 2021

# Underlying Inflation

Diffusion index has been hovering above its historical average for the last two years.

Upward price revisions are still widespread across goods and services.

## CPI Diffusion Index (Seasonally Adjusted, 3-Month Average)



Source: CBRT, TURKSTAT

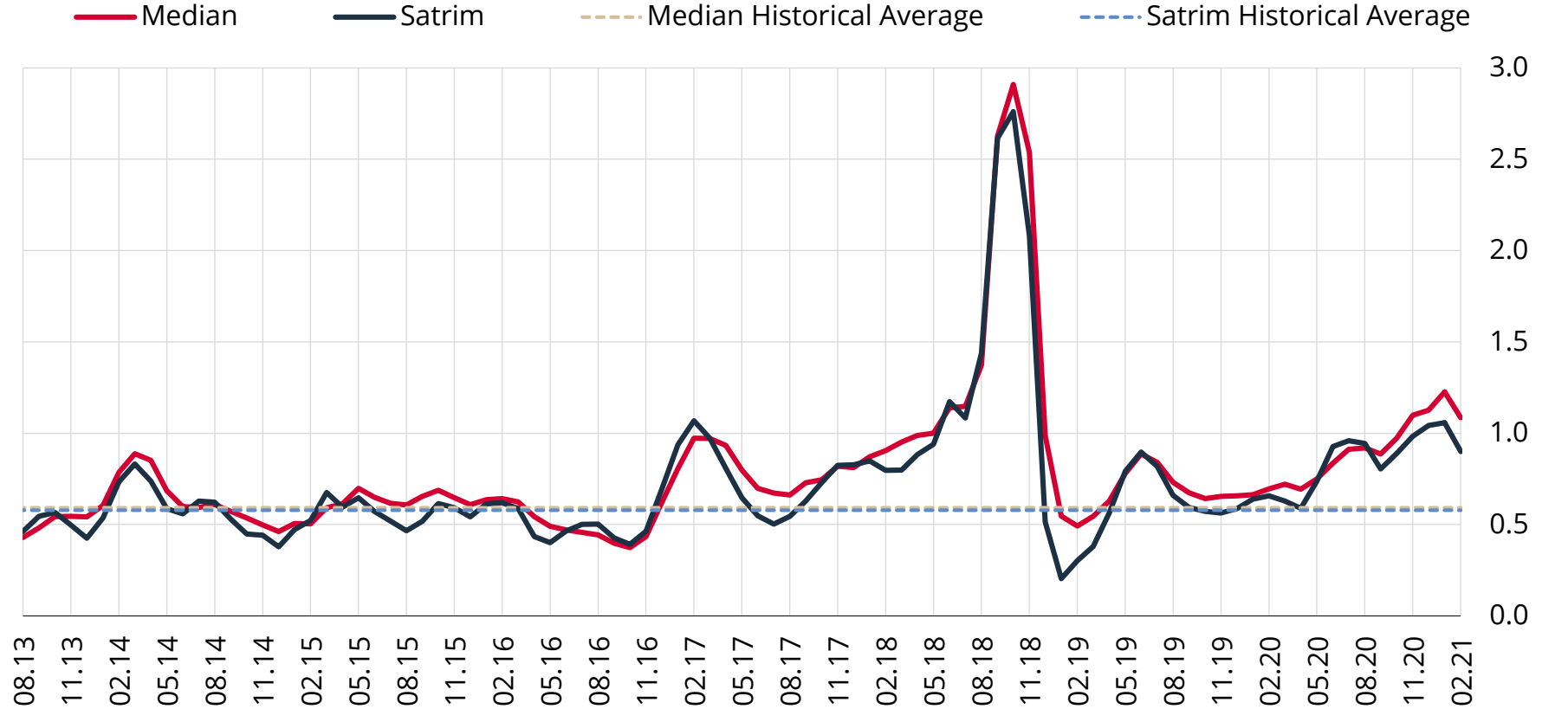
Last Observation: February 2021

\* Diffusion index is the ratio of the spread between the number of items displaying price increases and those displaying price decreases within a month to the total number of items.

# Underlying Inflation

Alternative indicators of underlying inflation still remain high with respect to their historical averages and year-end interim target.

Median and SATRIM\*  
(Seasonally Adjusted, 3-Month Moving Average % Change)



Source: CBRT

Last Observation: February 2021

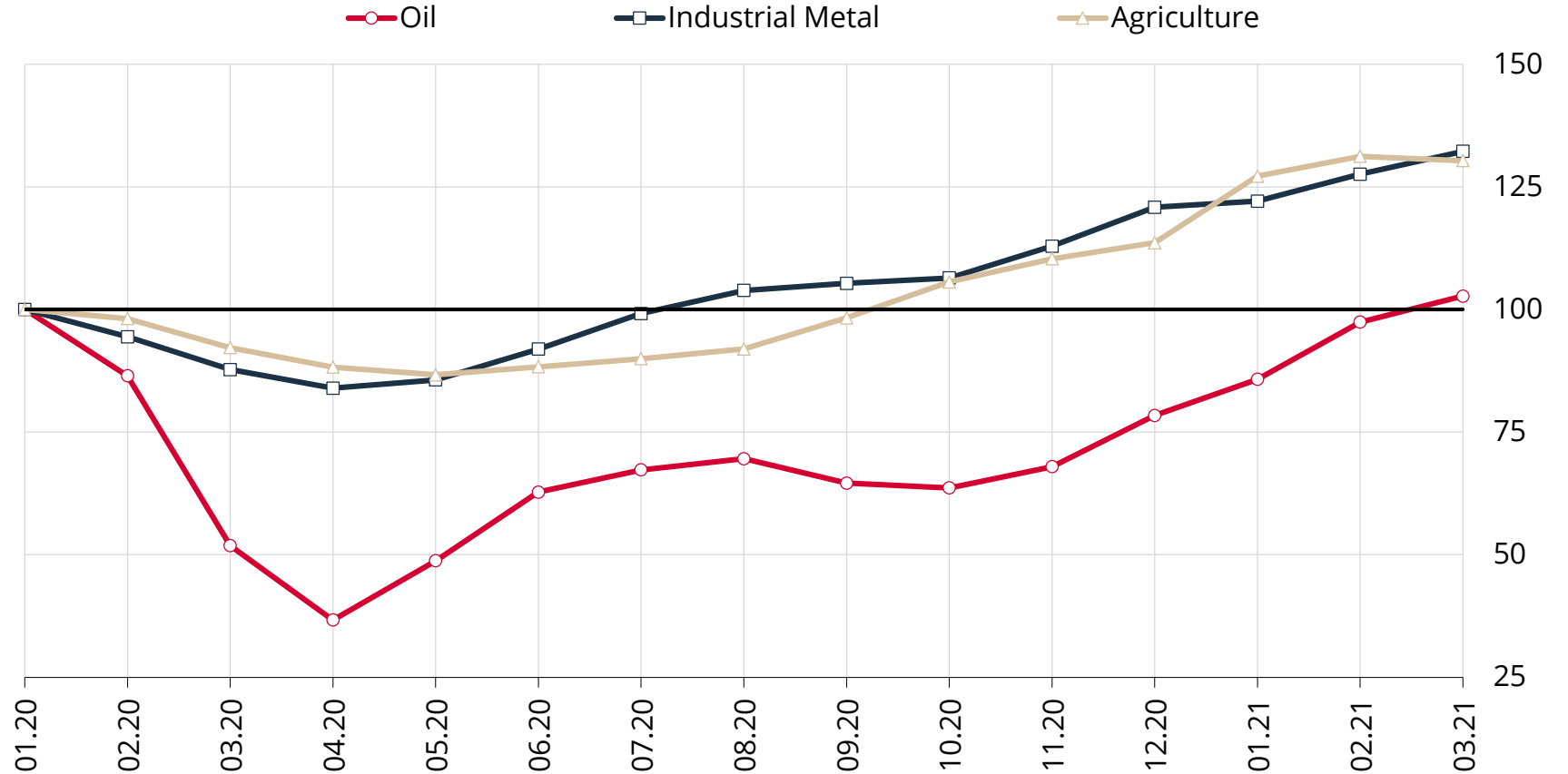
\* SATRIM is calculated by trimming off 19.5 percent (39 percent in total) from the lower and upper parts of the seasonally adjusted monthly variation rates distribution of inflation subgroups.

# Determinants of Inflation: Import Prices

International commodity prices continue to exert upward pressure on producer and consumer prices.

While the sliding scale tax scheme eases the pressures on energy prices, food and core goods are affected by the rise in agriculture and metal prices.

### International Commodity Prices (January 2020 = 100)



Source: Bloomberg

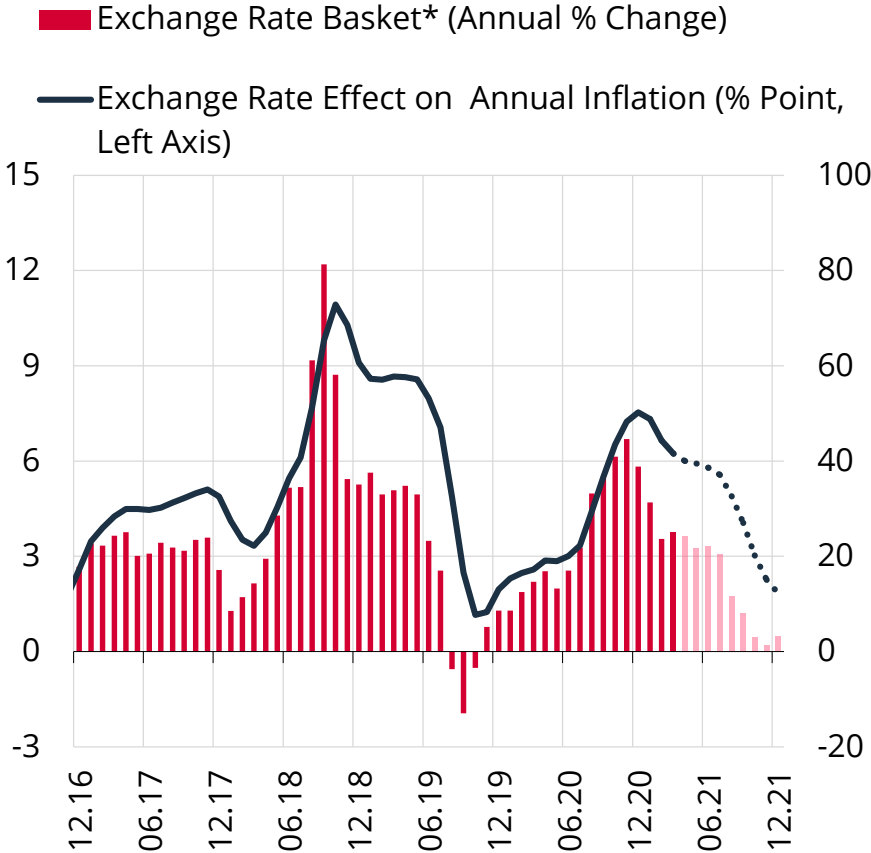
Last Observation: March 29, 2021

# Determinants of Inflation: Exchange Rate Pass-Through

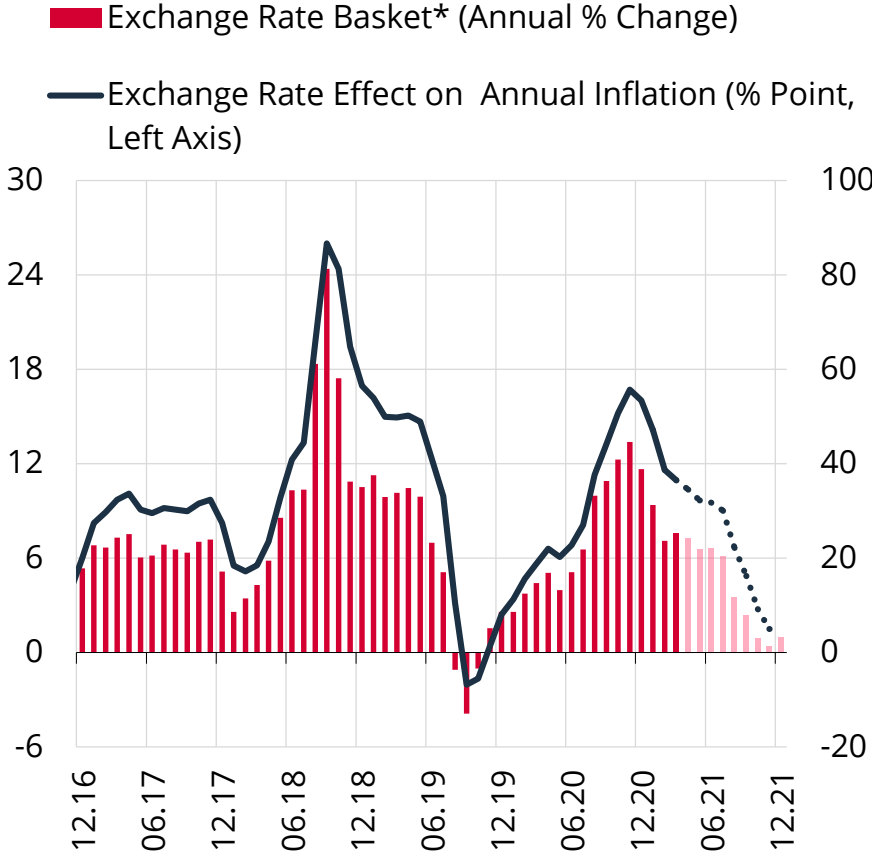
Depreciation of TL led by strong credit impulse and resulting macroeconomic imbalances have been the main driving force behind inflation in 2020.

Cumulative effects of exchange rate on inflation are expected to dissipate in the second half of the year, while recent volatility pose upside risks to inflation outlook.

**Contribution of Exchange Rate to CPI (% Point)**



**Contribution of Exchange Rate to PPI (% Point)**



Source: CBRT

Last Observation: March 2021

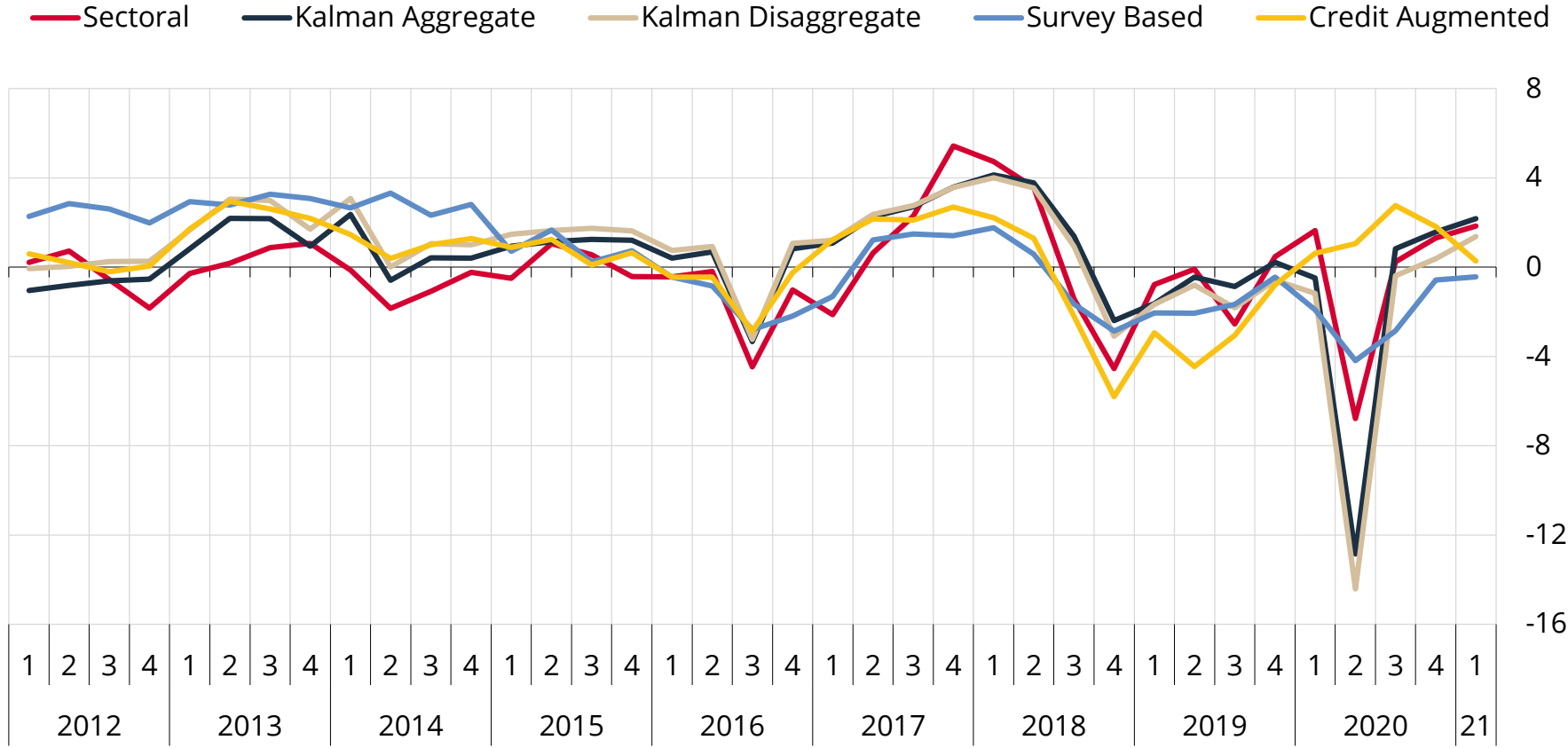
\* Exchange rate basket (0.5 USD + 0.5 Euro) is assumed to remain constant at 8.84 after March 2021.

# Determinants of Inflation: Output Gap

Cyclical assessments based on various measures of output gap indicate that the economy has been operating above its non-inflationary level since 2020-Q3.

The data for the first quarter point to a stronger course compared to the outlook presented in the January Inflation Report regarding the cyclical state of the economy.

Output Gap Indicators (%)



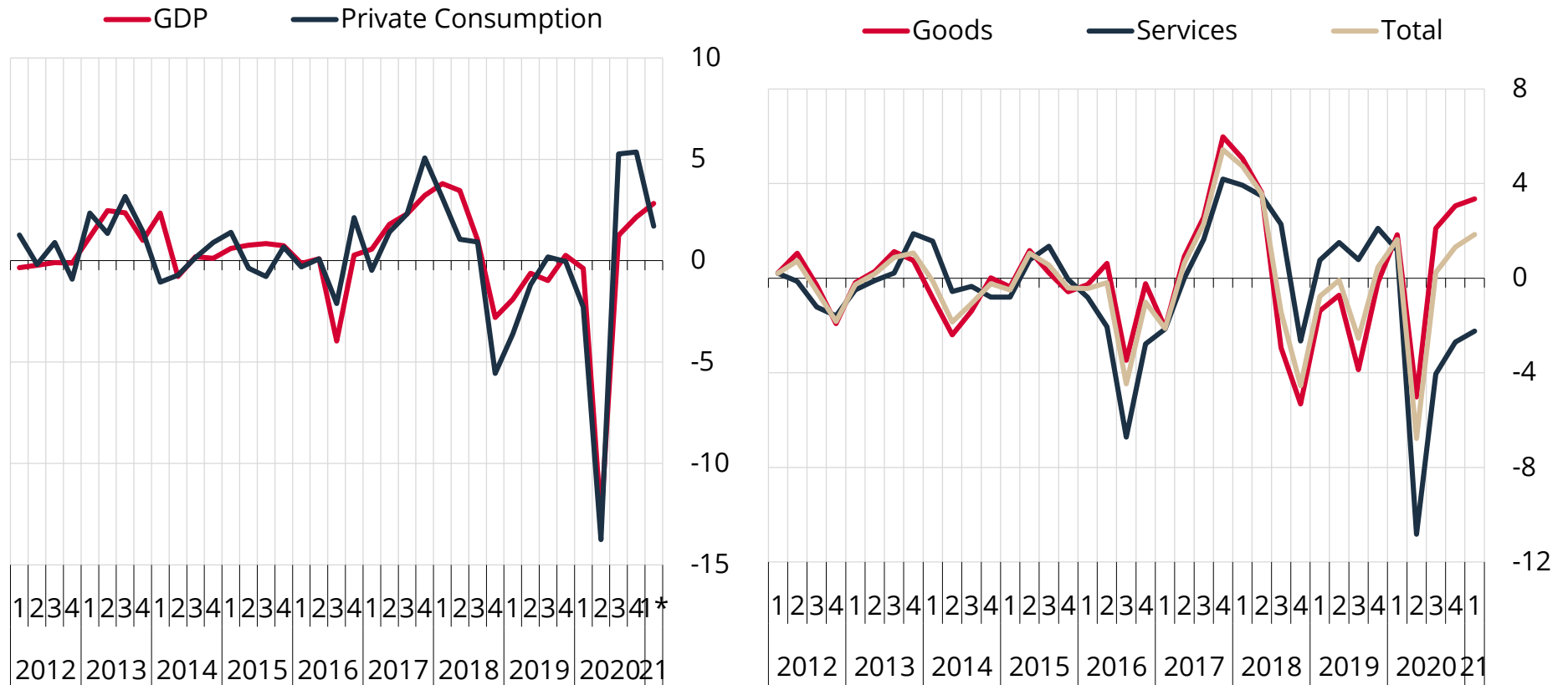
Source: CBRT

# Determinants of Inflation: Output Gap

The heterogeneity in sectoral demand conditions makes it difficult to gauge the aggregate output gap.

Consumption demand for goods, particularly for durables, clearly signals the presence of demand pressures on inflation.

## Output Gap Indicators\*\* (%)



Source: TURKSTAT, CBRT

Last Observation: January 2021

\*Forecast

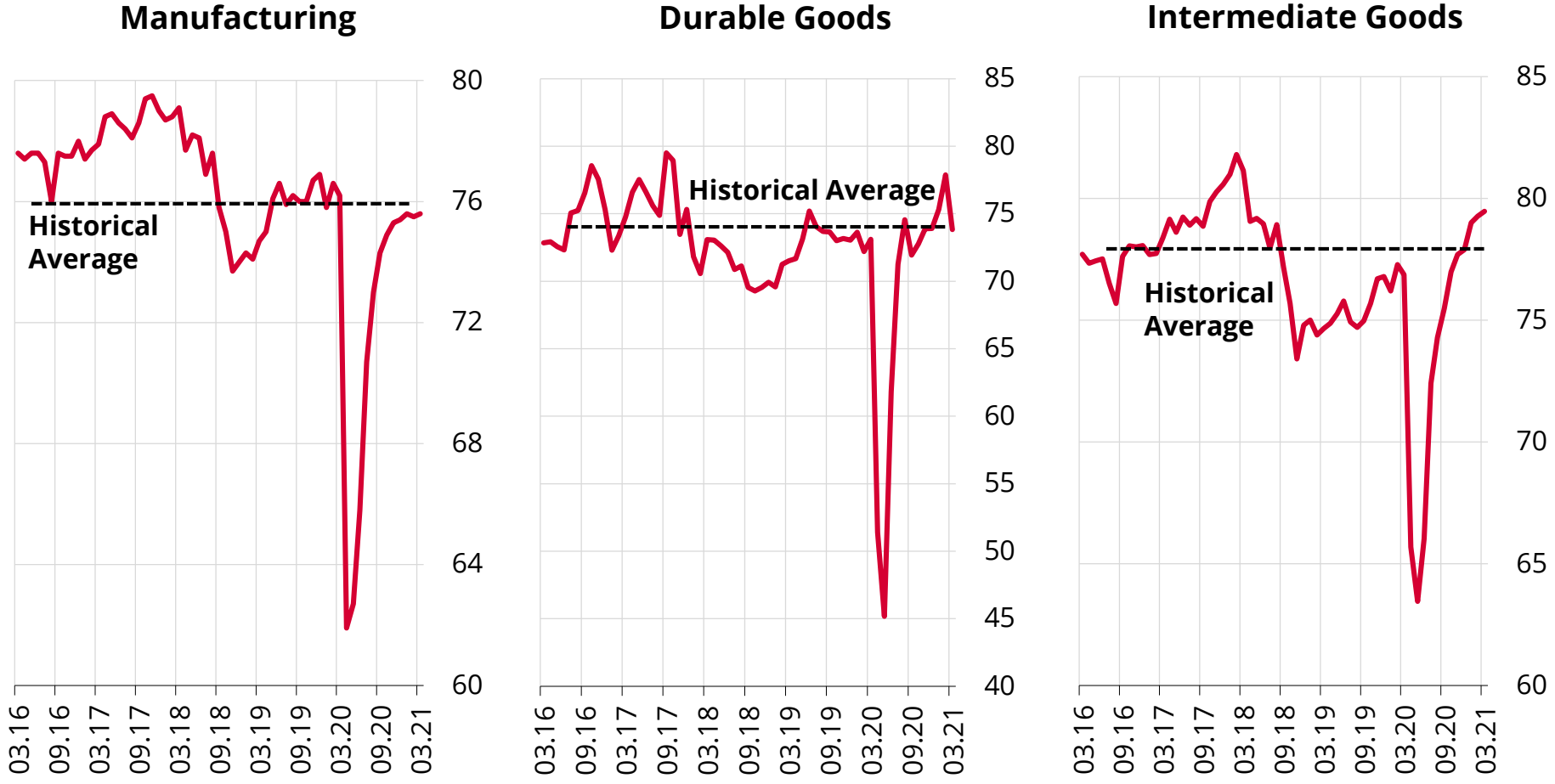
\*\*Percentage deviation from trend estimated with HP-Filter.



# Determinants of Inflation: Output Gap

Capacity pressures in durable and intermediate goods are more pronounced.

## Capacity Utilization Rate (Seasonally Adjusted, %)



Source: CBRT

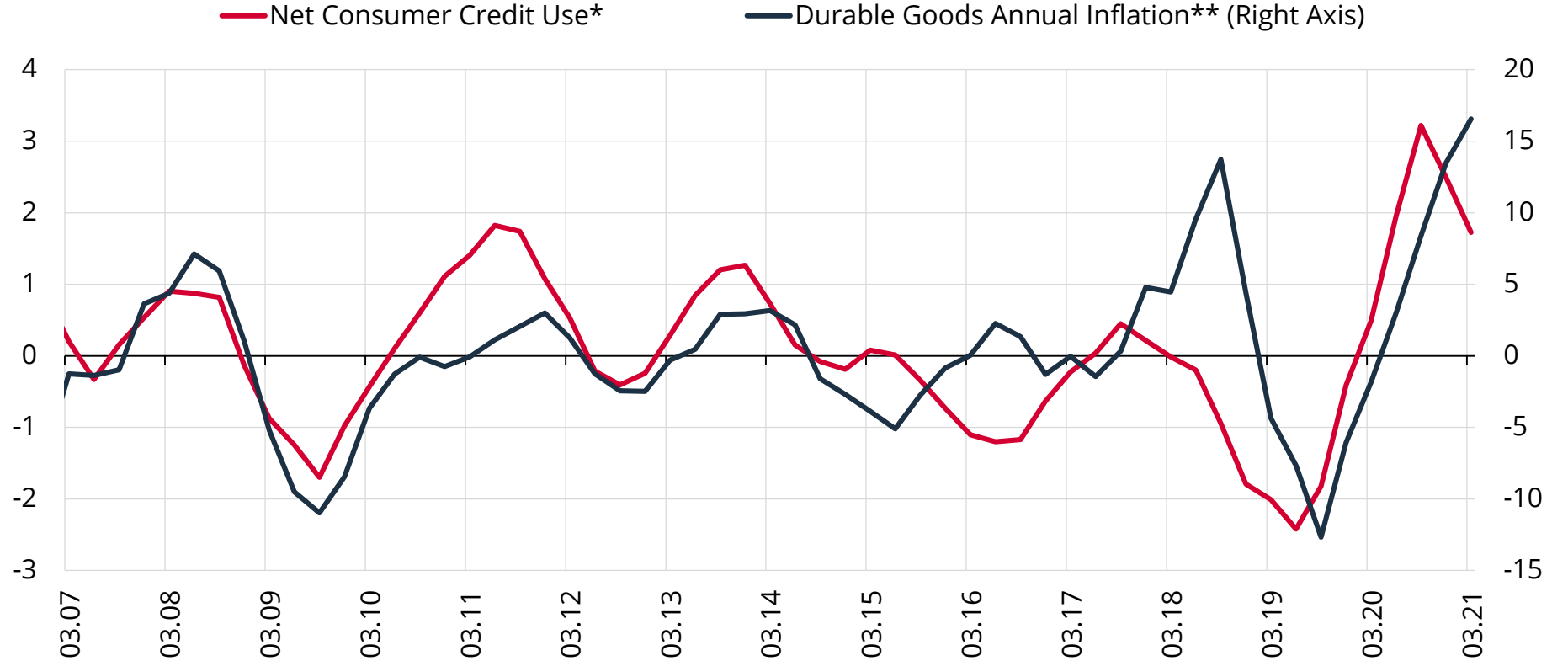
Last Observation: March 2021

# Determinants of Inflation: Credit

Strong credit impulse was the major source of demand-pull inflation in certain groups, particularly durable goods.

Personal loan demand remains brisk, and business and household surveys indicate that the demand for durable goods is still higher than long-term averages.

## Net Consumer Credit Use and Durable Goods Inflation (%)



Source: CBRT

Last Observation: 2021 Q1

\* Ratio of quarter-on-quarter change of exchange rate-adjusted credit use to the trend of seasonally adjusted nominal GDP of the previous quarter. Percentage difference from the historical average with 4 month moving average is used. The first quarter of 2021 displays realized data for the credit use and forecast for GDP.

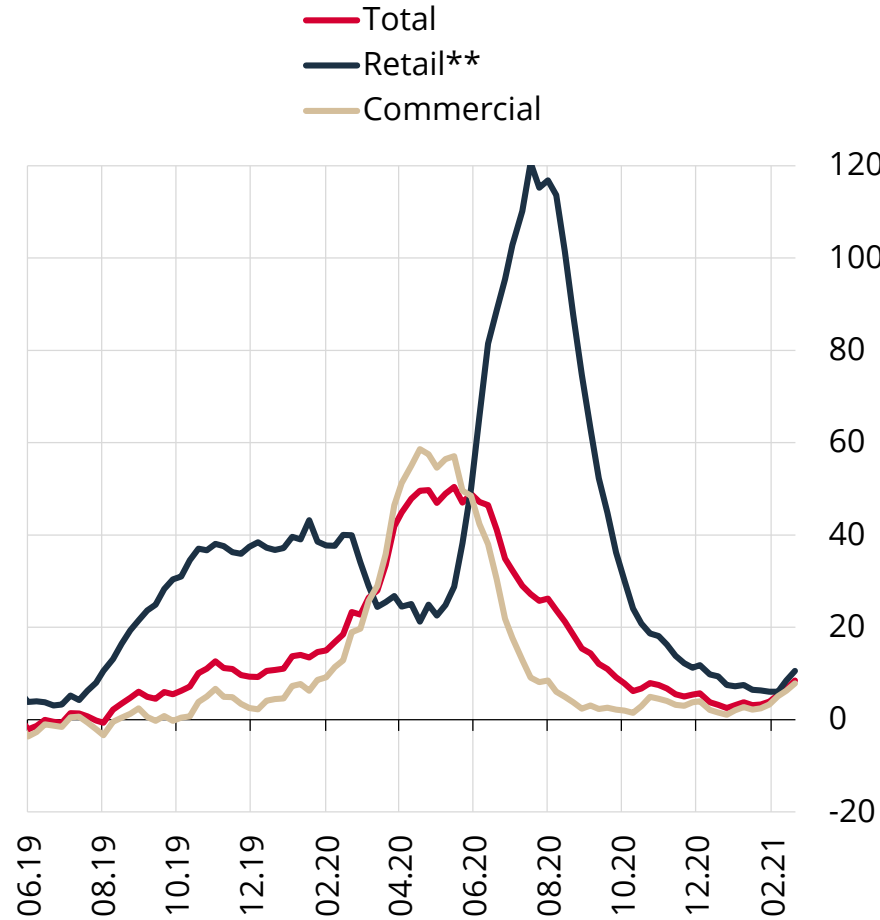
\*\* Durable goods inflation adjusted for tax, exchange rate and international commodity price effect. Last observation is February 2021.

# Determinants of Inflation: Credit

Credit growth, which has slowed down amid tighter financial conditions, has recently trended upwards.

Despite this uptick in personal and commercial loans, the limiting effect of the slowdown in loans on domestic demand and imports is expected to be more pronounced in the upcoming period with the additional monetary tightening.

**Loan Growth (Annualized 13-Week Average Growth, Adjusted for Exchange Rate, %)**

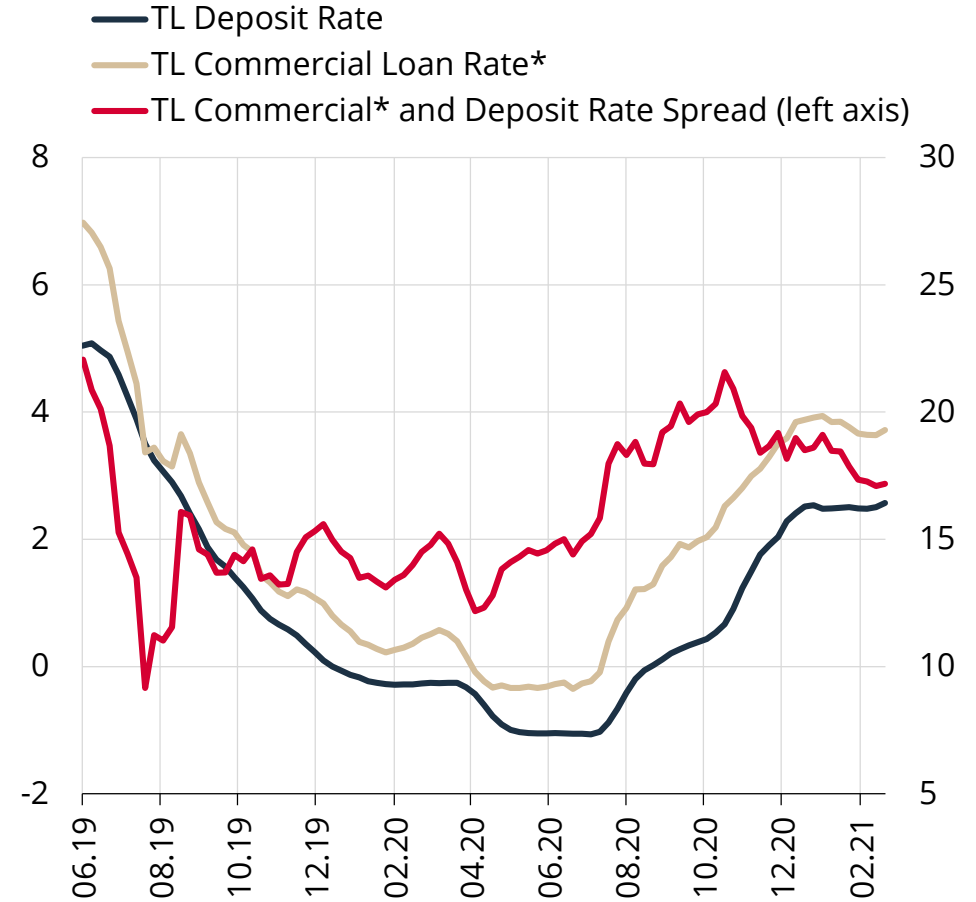


Source: CBRT

\* Zero interest loans are included in the commercial loan interest rate.

\*\* Includes individual credit cards.

**Loan and Deposit Rates (Flow, Annual, 4-Week Moving Average, %)**



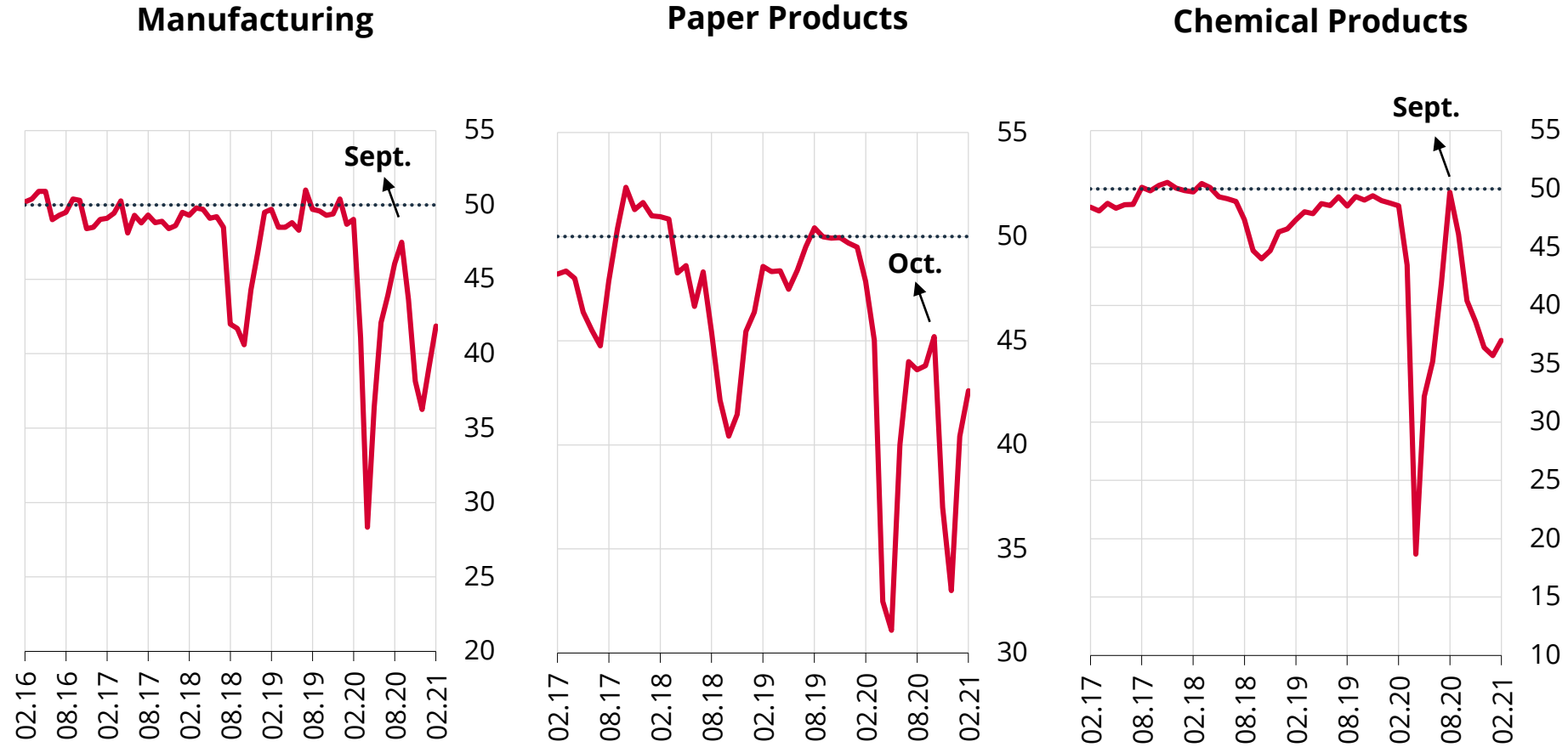
Last Observation: March 19, 2021

# Determinants of Inflation: Supply Constraints

The lags in delivery times and disruptions in global and domestic supply chains put producer prices under pressure.

Historical dynamics, characterized by the exchange rate and international commodity prices, fall short of explaining the recent rise in producer inflation, pointing to the role of supply-side inflationary factors.

PMI - Delivery Times\* (Seasonally Adjusted)



Source: IHS Markit

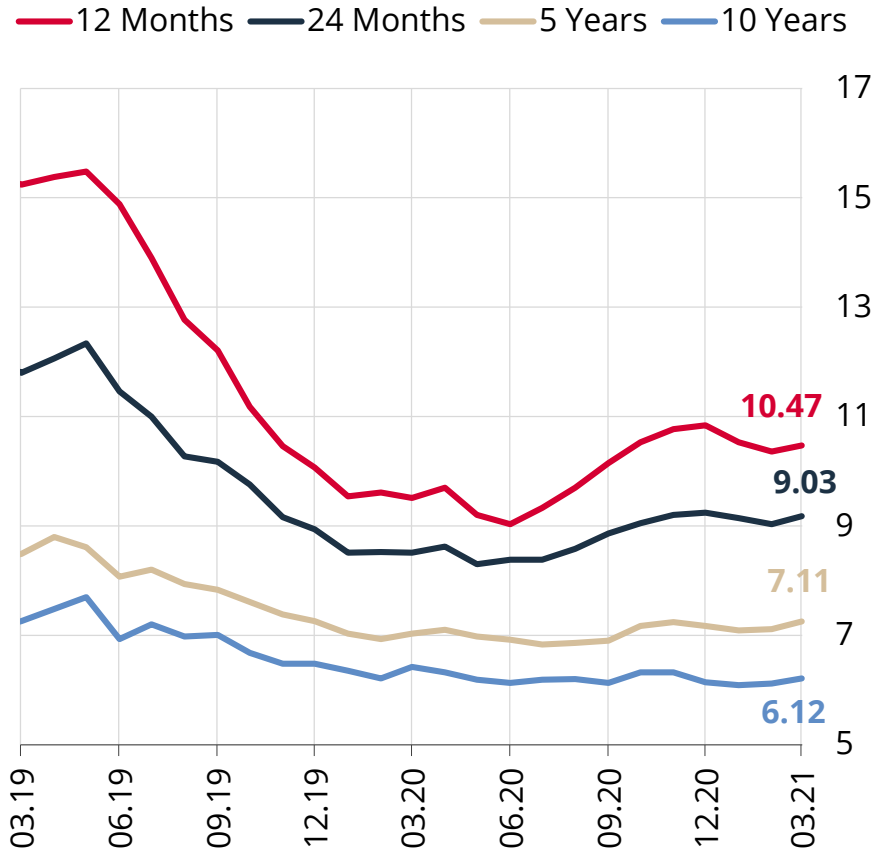
Last Observation: February 2021

\* Lower values of the series indicate a longer delivery time.

# Determinants of Inflation: Expectations

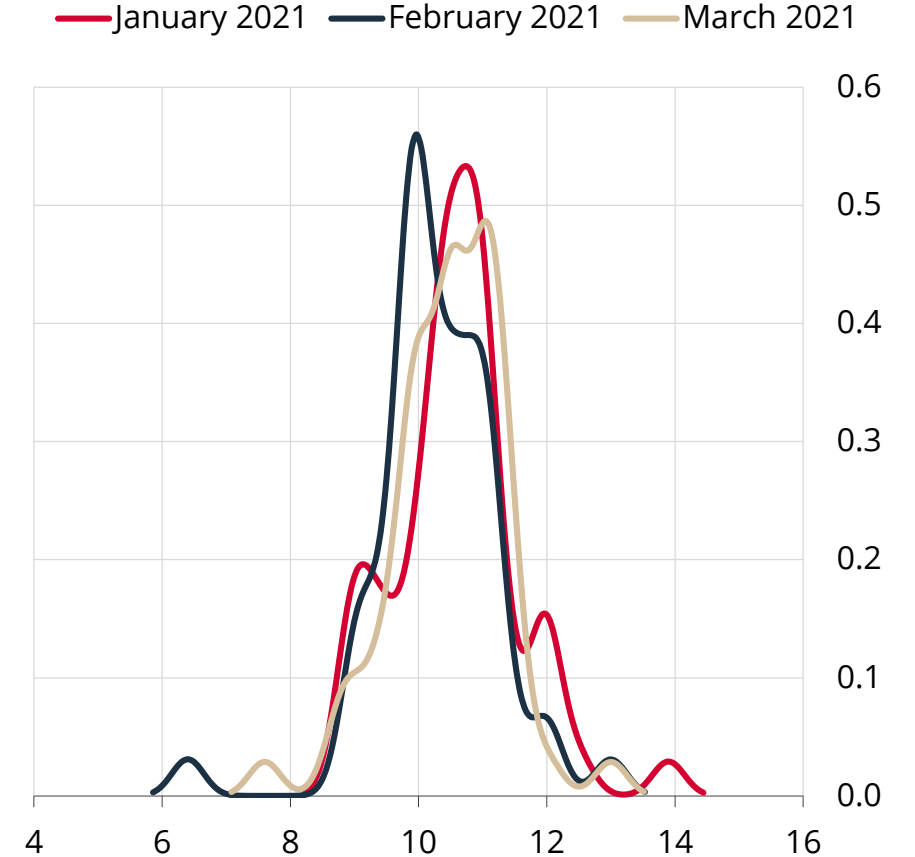
The credibility gap, with medium-term inflation expectations running above the interim targets, calls for a tight monetary policy stance for an extended period.

### Inflation Expectations (%)



Source: CBRT

### Distribution of Inflation Expectations (12-Month Ahead)

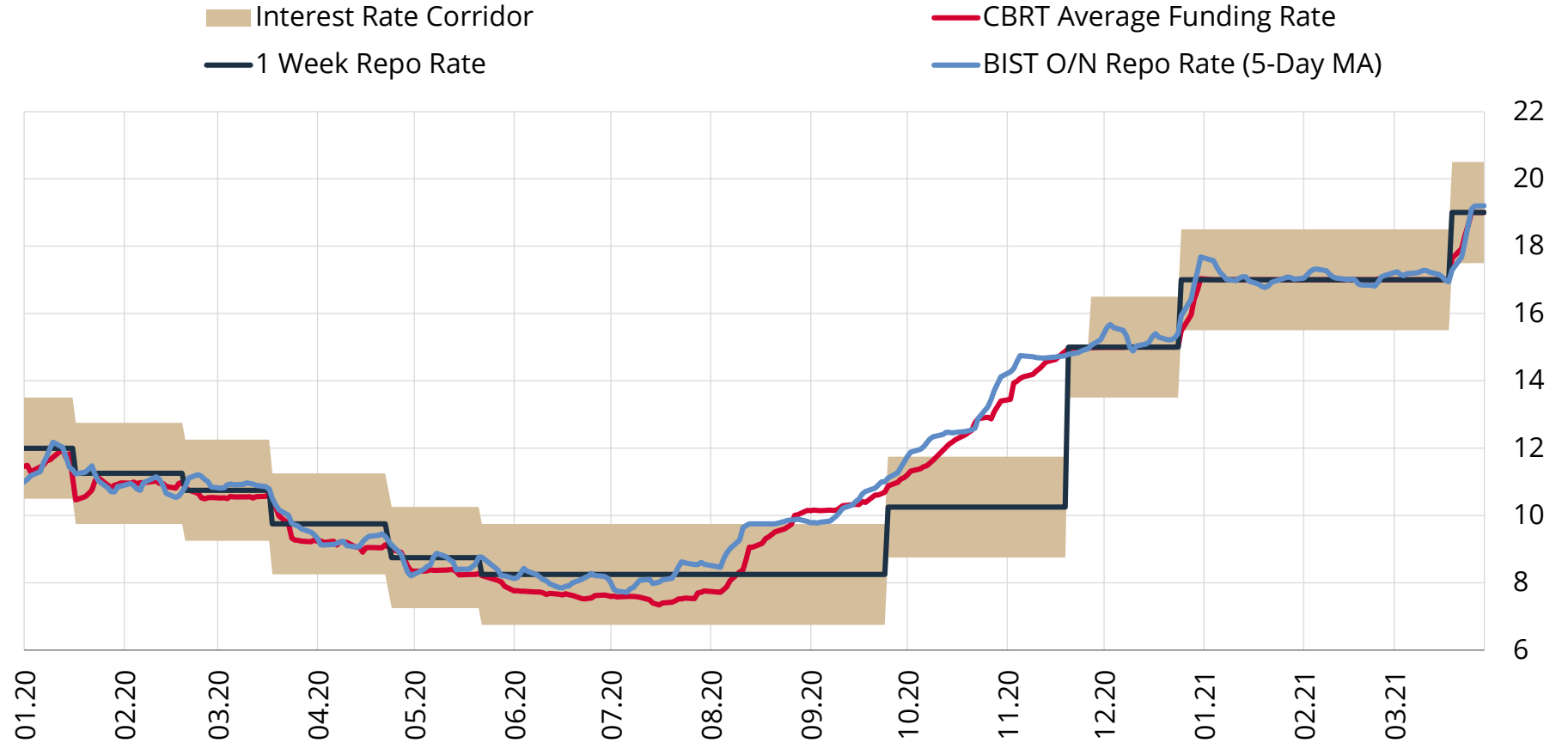


Last Observation: March 2021

# Monetary Policy

The balance between the monetary policy rate and actual/expected inflation will be sustained decisively to maintain a strong disinflationary effect until permanent price stability and the 5 percent target are reached.

## Short-Term Interest Rates (%)

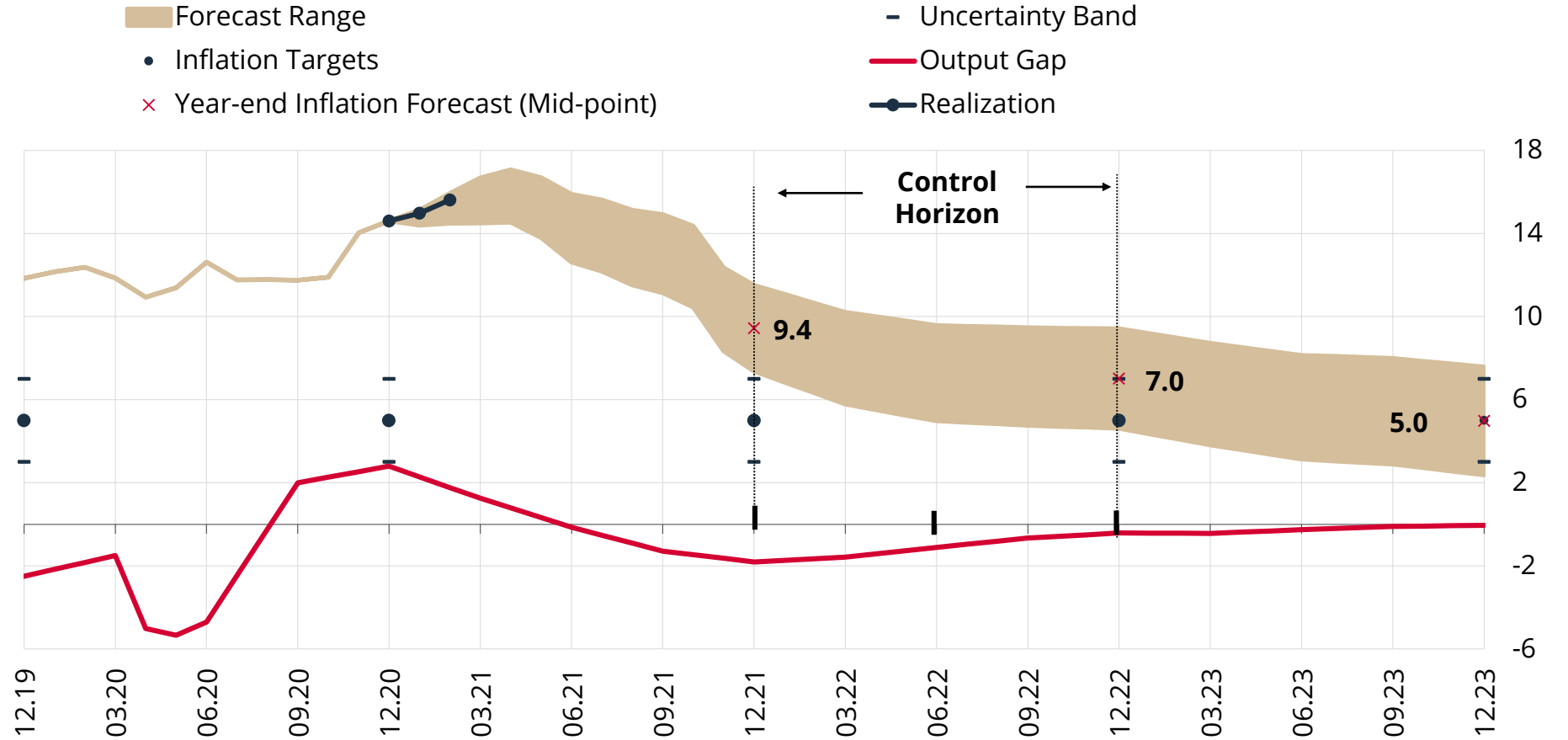


Source: BIST, CBRT

Last Observation: March 29, 2021

# January IR Forecasts

## January 2021 Inflation Report Forecasts for Inflation and Output Gap\* (%)



Source: CBRT, January 2021 Inflation Report

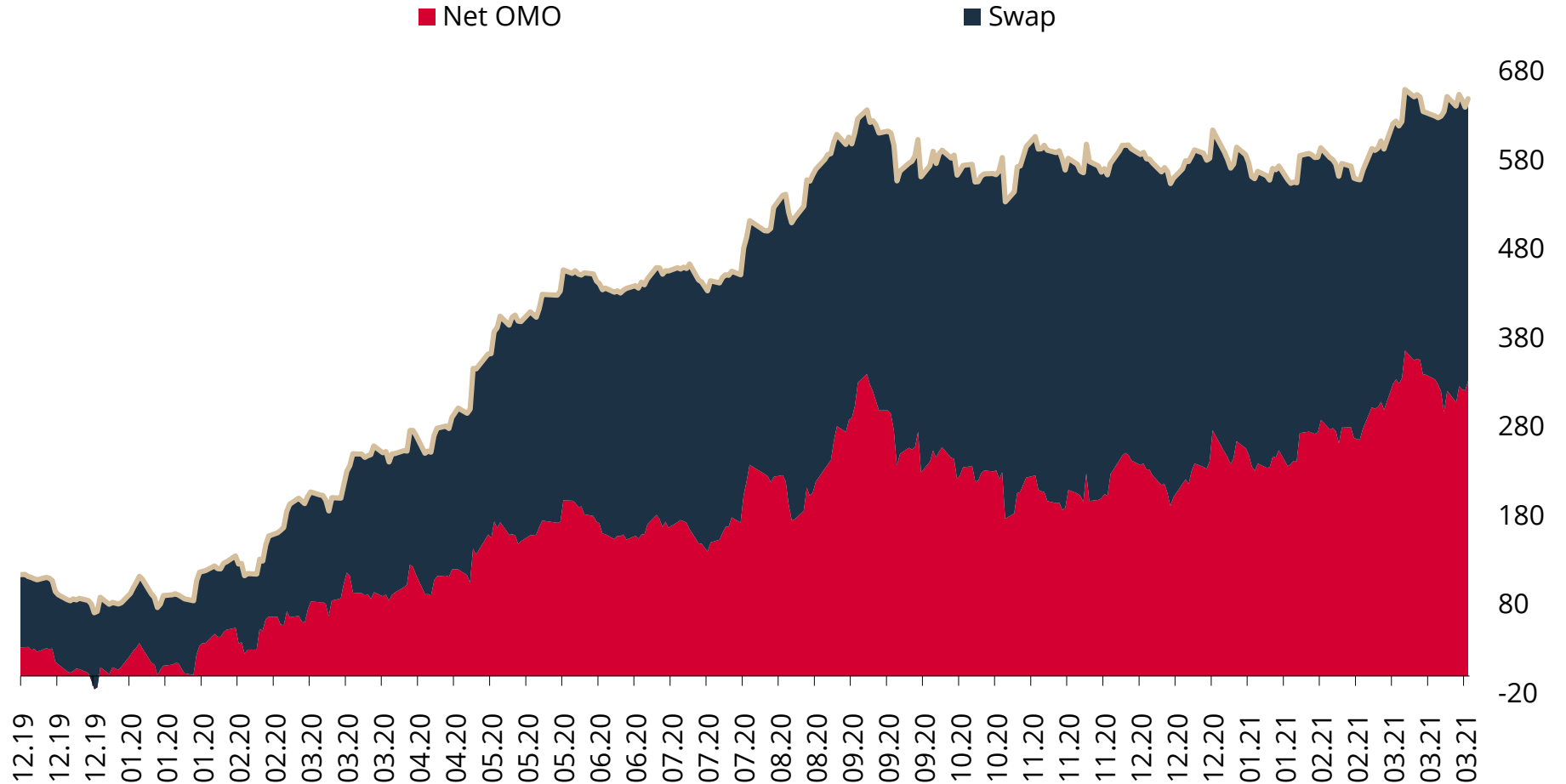
\* Shaded area denotes the 70 percent confidence interval for the forecast.

# Liquidity Management

Considering the structural demand for FX swaps by the banks, the CBRT will continue swap transactions in order to contribute to the TL and FX liquidity management of banks.

However, the use of the swap facility provided to banks is projected to decline gradually during the year depending on market conditions.

## Funding Need of the Banking System



Source: CBRT

Last Observation : March 26, 2021

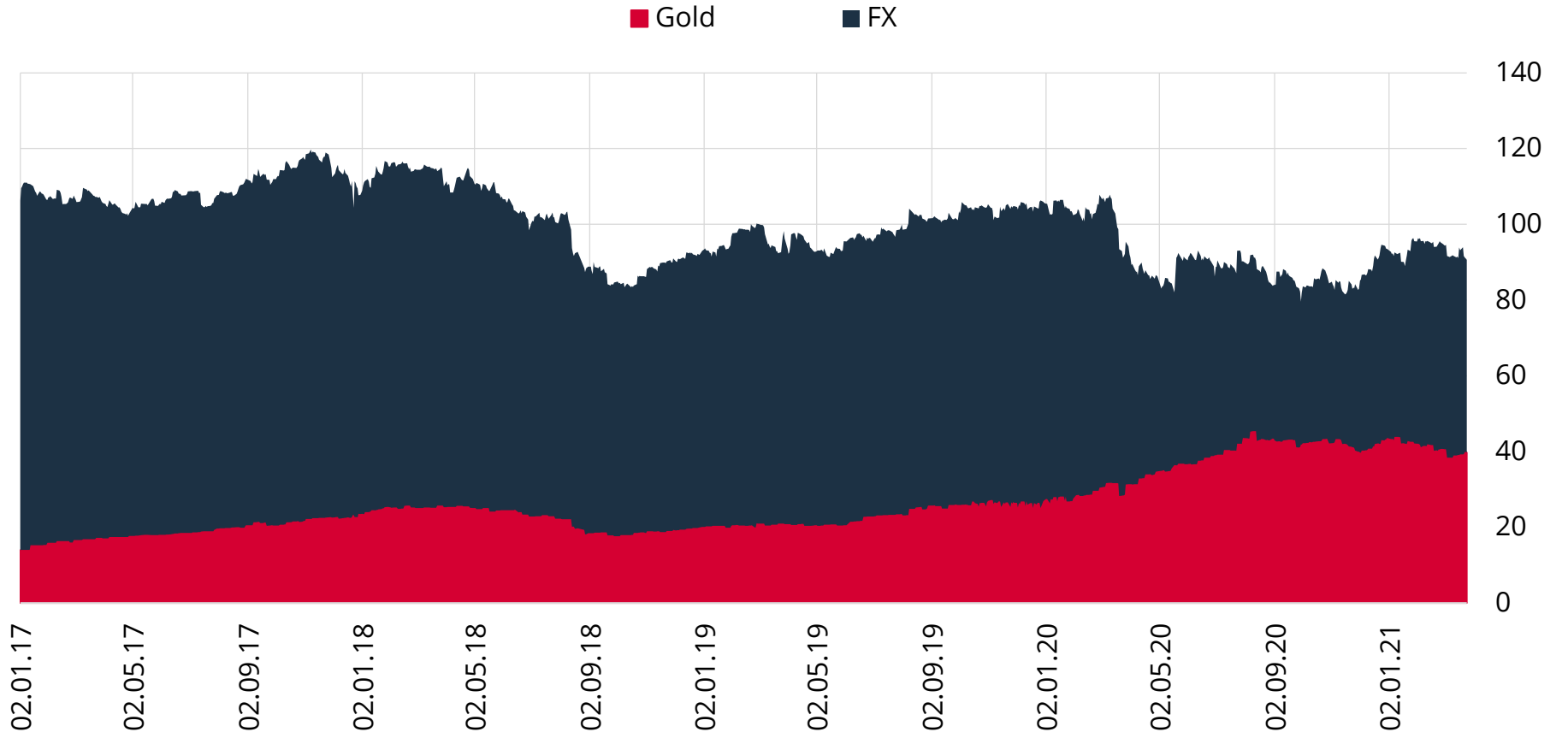


# Reserves

The CBRT reserves have stabilized and started a mild recovery. Maintaining the tight policy stance and building policy credibility will support a gradual accumulation of reserves.

For effective monetary policy and financial stability, FX reserves will be strengthened and relevant tools will be used to this end under appropriate conditions in a transparent way.

### CBRT Reserves (Billion USD)



Source: CBRT

Last Observation: March 26, 2021

# Overview

- Economic activity is on a strong course.
- As the pandemic-related restrictions are being eased, economic activity is expected to pick up in services and related sectors.
- Strong domestic demand due to the cumulative effects of high credit growth during the pandemic and the rise in import prices continue to adversely affect the current account balance.
- Domestic demand conditions, cumulative cost effects, in particular the exchange rate effects, increasing international food and other commodity prices and high levels of inflation expectations continue to affect the pricing behavior and inflation outlook adversely.
- While the expectation that the decelerating impact of the monetary tightening on credit and domestic demand to become more significant is maintained, the projected gradual waning in demand and cost factors is being delayed by the recent upward trend in credit growth and increase in import costs.
- Considering the upside risks to inflation expectations, pricing behavior and the medium-term inflation outlook associated with these developments, the CBRT has decided to implement a front-loaded and strong additional monetary tightening.
- The tight monetary policy stance will be maintained decisively, taking into account the end-2021 forecast target, for an extended period until strong indicators point to a permanent fall in inflation and price stability.
- Additional monetary tightening will be delivered if needed.

# MACROECONOMIC OUTLOOK AND MONETARY POLICY IN TURKEY

April 1, 2021

Ankara





**TÜRKİYE CUMHURİYET  
MERKEZ BANKASI**

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