

VAKIFBANK TURKISH ECONOMY WEEKLY

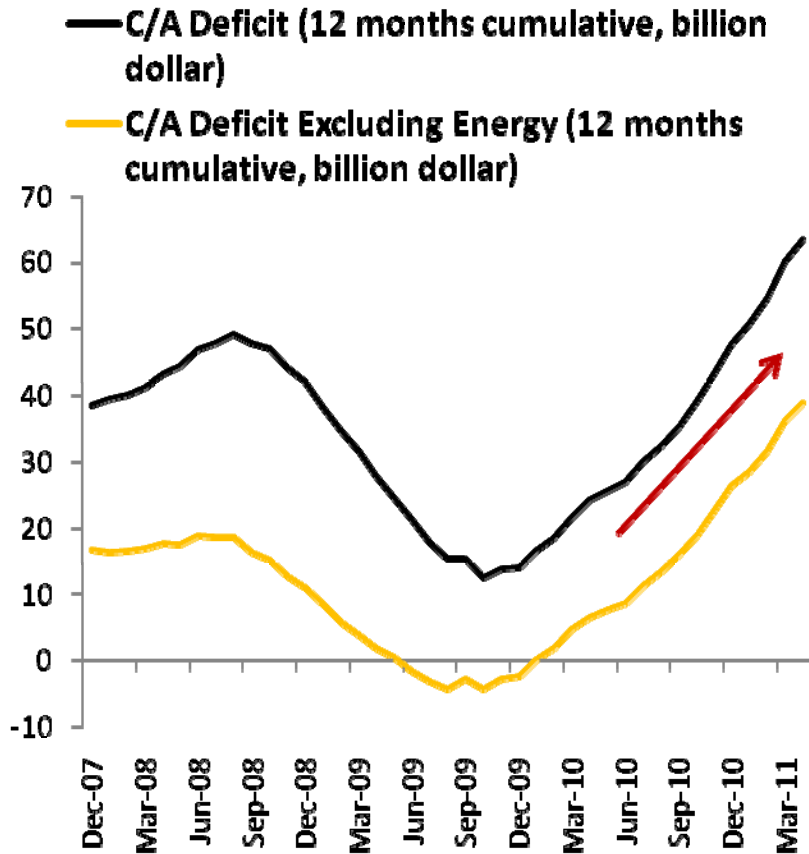
*Current account deficit, exchange rate
and credit growth: Recent developments
in Turkey...*



T. Vakıflar Bankası T.A.O



Current Account (C/A) deficit increased by 77% to \$7.68 billion in April 2011 compared to the same month of 2010...



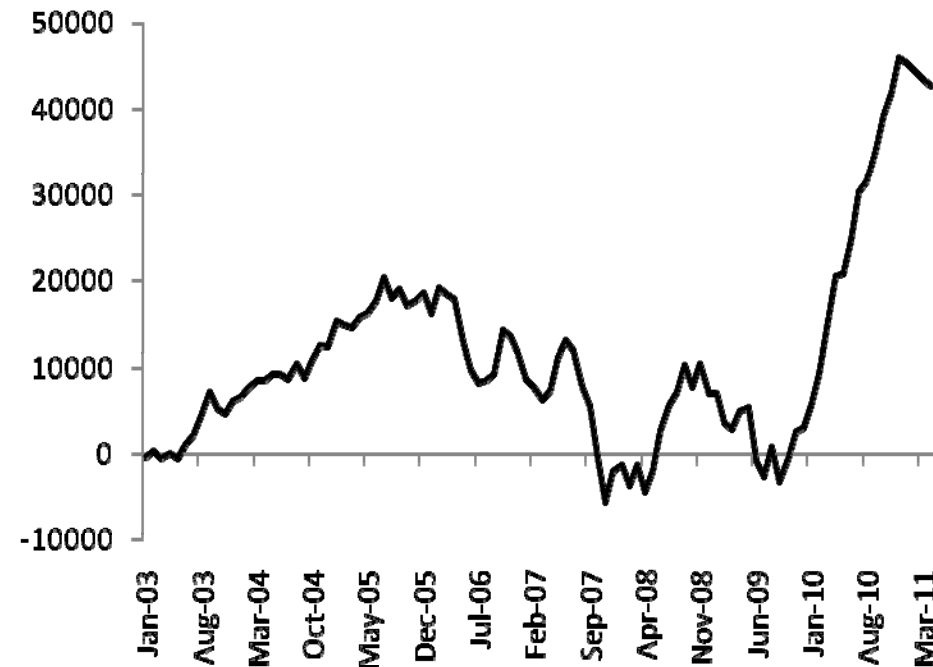
Source: CBRT, Turkstat

- ✔ In January-April 2011 period, C/A deficit increased by 113.8% to \$29.6 billion.
- ✔ Moreover, last 12 months cumulative C/A deficit increased by 160.6% to \$63.418 billion.
- ✔ Although 12 months cumulative C/A deficit is increasing, the growth rate of C/A is decreasing.
- ✔ C/A excluding energy moving in similar trend to C/A deficit indicates that the main reason behind the expansion C/A deficit is not only the high oil prices but also the strong domestic demand conditions.
- ✔ Last 12 months cumulative C/A deficit excluding energy increased to \$39 billion but its yearly increasing rate decreased to 108% from 169%.
- ✔ Hence, it can be said that rising oil prices negatively affected the C/A deficit of Turkey as Turkey is an oil importer country.

Short term capital inflows to Turkey are decreasing...

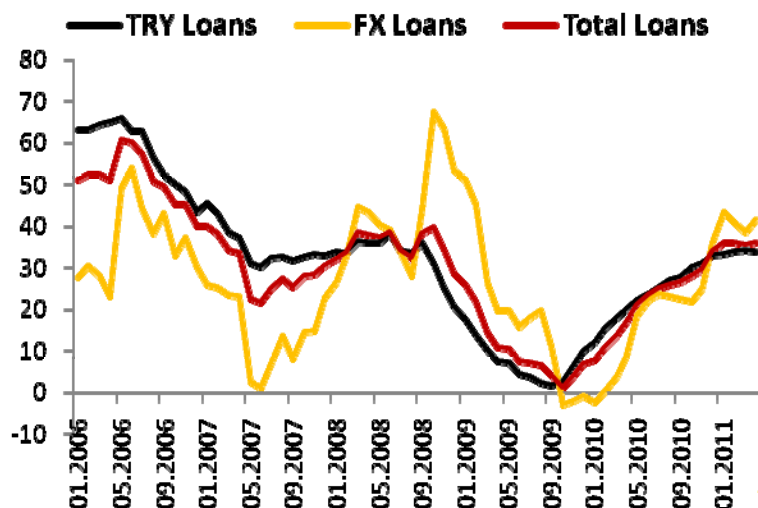
- While the short term capital inflows have increased since 2009 September, they have decreased since the beginning of 2011. This situation arised from the low level of real interest rates.
- Real interest rate level is relatively low in Turkey compared to other emerging countries. This makes Turkey less attractive for the foreign investors.

**Short Term Capital Inflows
(12 months cumulative, billion dollar)**

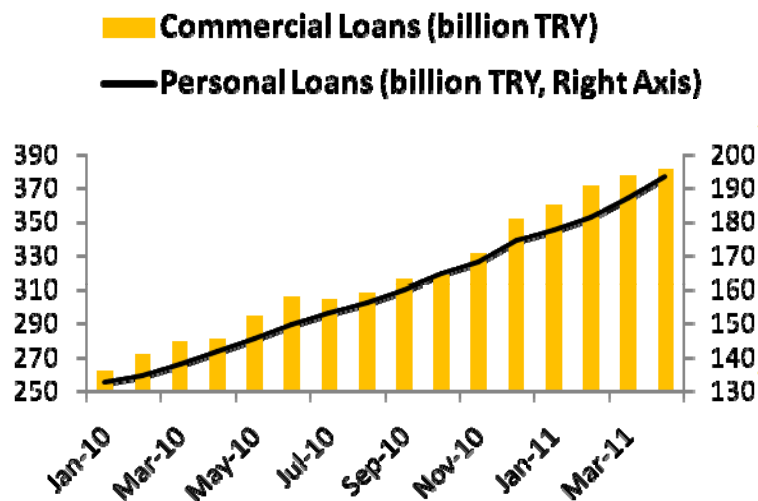


Source: CBRT

Loan growth negatively affected current account deficit...



Source: BRSA



Source: BRSA

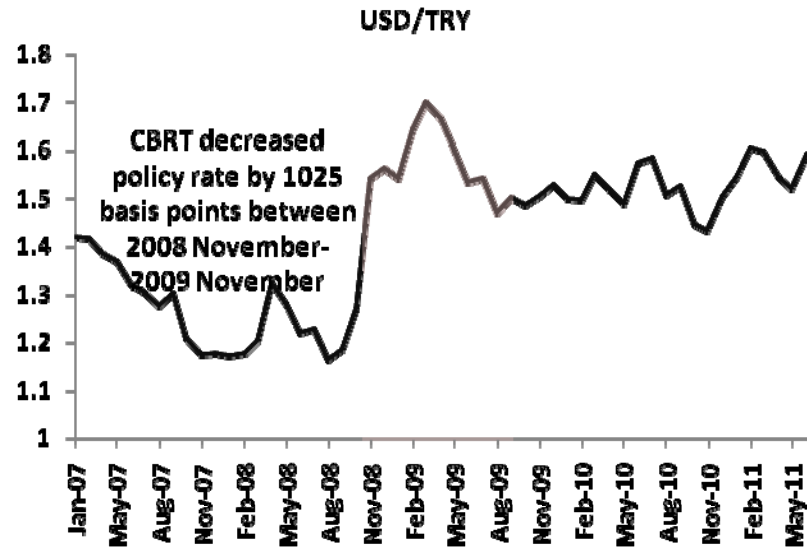
Loans have increased since the second half of 2009 because of economic recovery and had a rapid growth trend in 2010. Total loans increased by 36% to 573 billion TRY in April 2011. While TRY loans and total loans have preserved high levels, FX loans have increased more than TRY loans and total loans. Especially, due to the increase in TRY required reserve ratios (RRR), the rate of rise in TRY loans was limited. However FX loans have increased more than TRY loans as FX RRRs were not changed since April 2011.

On the other hand, both personal and commercial loans have continued to rise. Consumer loans, personal loans and commercial loans increased respectively by 41.6%, 36.4% and 35.7% in April 2011.

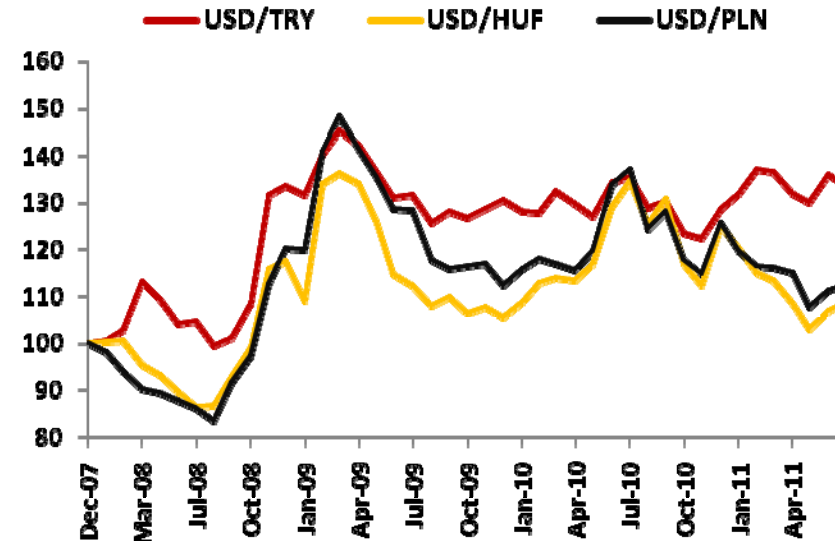
Recently rising capital inflows have relieved decoupling between the growth rates of domestic and external demand. This situation negatively affected current account deficit by rapid credit expansion and stimulated import demand.

Rapid increase in loans and current account deficit triggered concerns about the financial stability. Under these circumstances, CBRT increased TRY RRRs. However the effects of RRR hikes on loan growth were relatively limited.

Foreign exchange rate is also an important factor in conducting monetary policies...



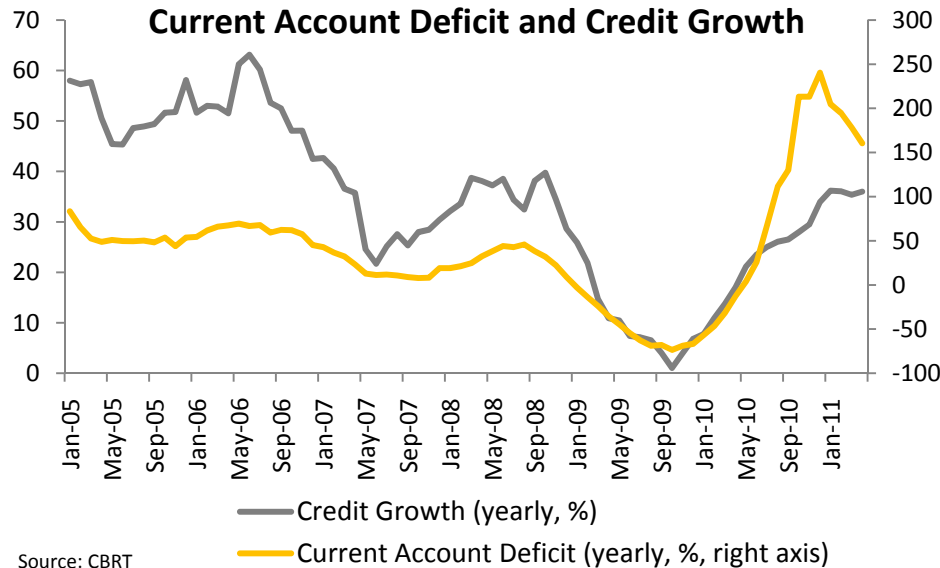
Source: Reuters



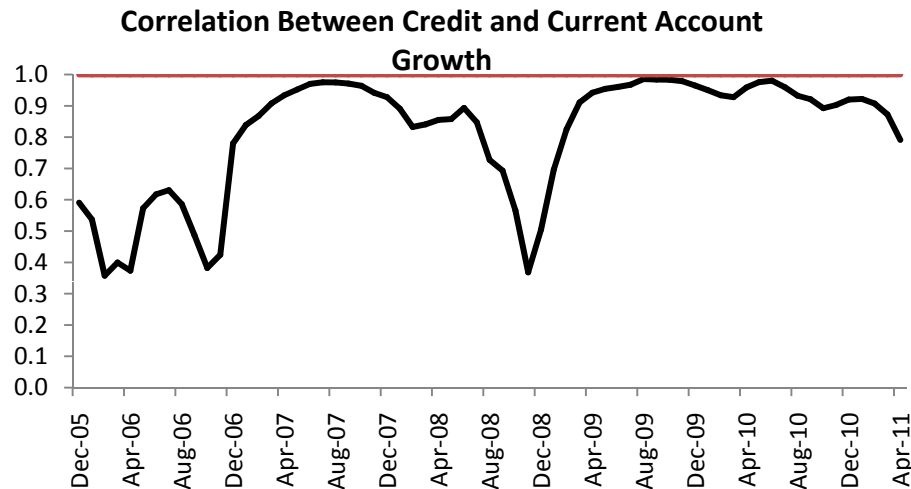
Source: Reuters

- ✓ CBRT decreased the policy rates by 10.25 points from November 2008 to November 2009 against the global financial crisis. Despite many EM countries have started rate hikes since 2010 to control inflation, Turkey has continued loose monetary policy so as to weaken the lira and narrow Turkey's current account deficit. So TRY is the currency that has lost the highest value against dollar compared to other emerging countries' currencies like Poland Zloty and Hungary Forint.
- ✓ Even so weak TRY has not sufficient enough to narrow C/A deficit yet. This indicates the measures taken so far were not as effective as accepted to slow down the growth rate of C/A deficit. Moreover, it points out that ensuring productivity growth and implementing some structural measures are essential to narrow C/A deficit.





High linear relationship between current account and the credit growth...



Source: CBRT



Source: Vakifbank

-  The unorthodox policy mix of the CBRT aims limiting credit growth to prevent high increase in current account deficit.
-  The recent realizations of credit growth and current account deficit have not indicated a totally stabilisation yet as both of them are still at high levels.
-  The correlation between current account and credit growth shows that there is a high linear relationship between them.
-  Under these assumptions, it would be useful to continue to observe the lagged impacts of the measures taken to narrow import and also current account deficit in the forthcoming months.

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