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GROWTH RECORD ALBEIT THE "TIGHTENED" MONETARY POLICY

Turkey has demonstrated a noteworthy growth performance in a period when the ongoing debt crisis in Europe turned first into a banking crisis and then into a political crisis. Gross Domestic Product (GDP) grew year-on-year by 8.2 percent, the second highest growth following China.

Turkey's success becomes more evident when the growth performance during the first nine months of 2011 is addressed. Turkey is the growth champion of the world for the first nine months of the year. In the first three quarters of 2011, the Turkish economy grew by 9.6 percent compared to the same period in 2010. China and India, also known as the growth engines of the global economy, followed Turkey. The worst performing economies were troubled European countries, Greece and Portugal to begin with, and Japan, which is still struggling to dress the wounds of the latest earthquake.

[1] http://www.tepav.org.tr/en/ekibimiz/s/1034/Sarp+Kalkan

Table 1. Annual Growth Rates in the first three quarters of 2011

Fast Growth		Slow Growth/ Contraction	
Turkey	9.6%	Greece	-6.0%
China	9.4%	Portugal	-1.1%
India	7.4%	Japan	-0.6%
Chile	7.1%	Spain	0.8%
Peru	7.0%	United Kingdom	0.9%
Indonesia	6.5%	Norway	1.2%
Hong Kong	5.6%	Denmark	1.2%
Sweden	5.4%	Australia	1.5%
Singapore	5.4%	Holland	1.6%
Israel	5.1%	USA	1.7%

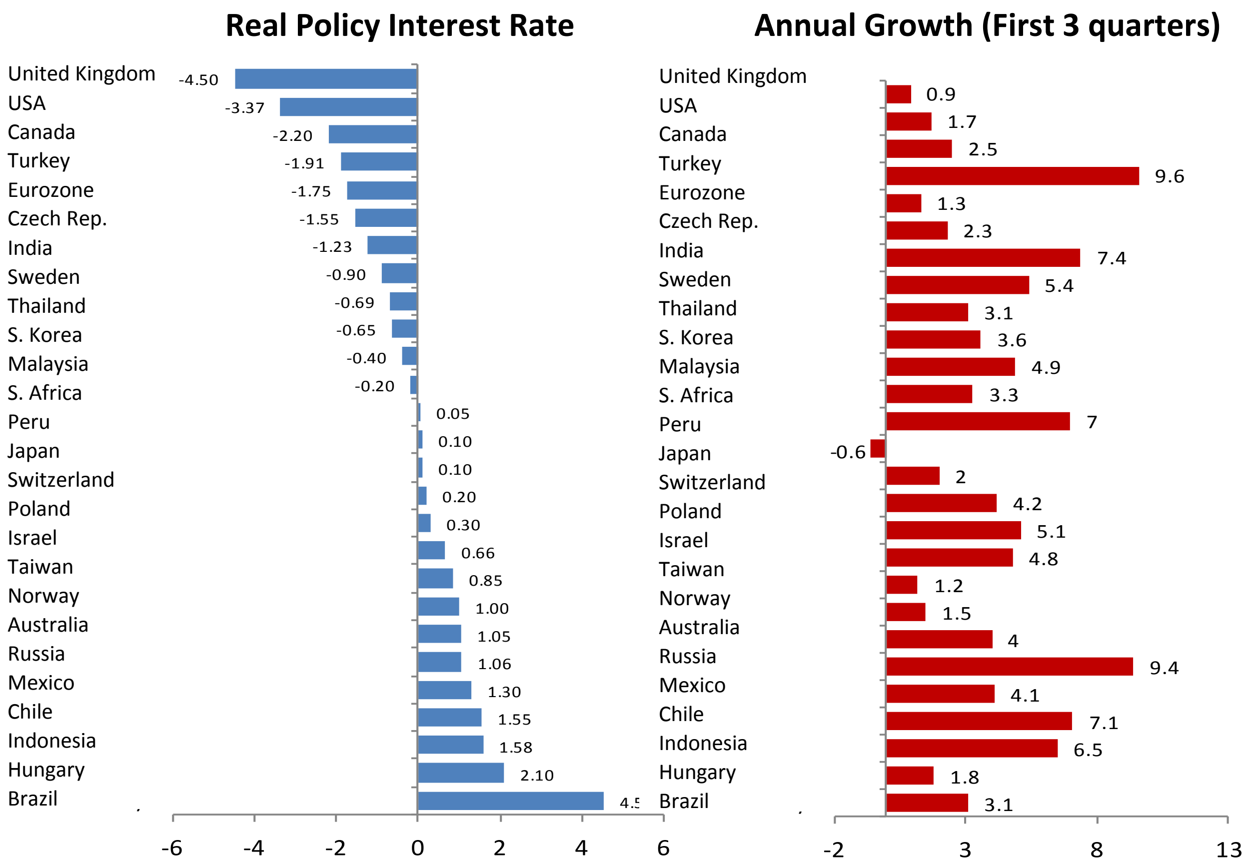
Source: EIU and TURKSTAT

In fact, this rapid growth performance was a big surprise for many who closely monitor markets. Remarks by the officials of the Central Bank of Turkey (CBT) that monetary policy was tightened amid the rising risks associated with current account deficit had an important role on this surprise effect. Then, how could Turkey achieve such an impressive growth performance albeit the monetary tightening?

The answer to this question is evident in the below figure. The left column shows the real policy interest rate set by selected central banks whereas the right column shows the annualized growth rate for the three quarters of 2011 in respective countries.

When observing the two figures together, one would naturally expect that countries, which had shown a laggard growth performance or suffered contraction in the first nine months of the year, loosened monetary policy in response in the fourth quarter by lowering real policy interest rate, even initiating negative real policy rates. On the other hand, one would expect rapid-growth countries to introduce monetary tightening with high policy rates.

Figure 1. Real Policy Interest Rate[2] and Growth Rates



Source: EIU, TURKSTAT, RGE Monitor

Reading the figure in line with these expectations, countries which funded markets at low cost via negative real policy rates appear on top of the figure. According to this, Turkey is the country implementing the lowest real policy rate, following United Kingdom, USA and Canada. In fact, the rate is higher even in Eurozone countries which struggle with the crisis. Among the top five of the list, all countries faced growth problems but Turkey. Given that there are around ten developed countries within the Eurozone, Turkey stands among an even larger group that failed to recover from the crisis.

Down the figure are countries that implement high real policy interest rates. Predominant among these are developing countries that attained relatively rapid

[2] Please see Roubini Global Economics, Central Bank Watch: Global Policy Loosening Begins, November 17, 2011" for real policy interest rates implemented by selected central banks during November 2011.

growth rates. Turkey's peer countries such as Russia, China, Mexico and Brazil also are in this group.

Table 2 takes a closer look at selected indicators for countries that attained high growth performance like Turkey. According to this, out of 8 countries that grew by more than 5 percent in the first nine months of 2011, only 3 implemented negative real policy interest rate: Turkey, India and Sweden. Moreover, among this three, Turkey is the one with the lowest real policy rate and the only country that has a current account deficit problem: Sweden enjoys a considerably high current account surplus and India has a reasonable current account deficit.

Table 2. Selected Indicators for High-growth Countries

(%)	Annual Growth, First 3 quarters	3rd Quarter Growth	Current Account Balance*	Real Policy Interest Rate
Turkey	9.6	8.2	-10.3	-1.9
China	9.4	9.1	5.2	1.1
India	7.4	6.9	-2.2	-1.2
Chile	7.1	4.8	0.1	1.6
Peru	7.0	6.5	-2.7	0.1
Indonesia	6.5	6.5	0.2	1.6
Sweden	5.4	4.6	5.8	-0.9
Israel	5.1	5.1	0.3	0.3

Source: EIU, TURKSTAT, IMF WEO, RGE Monitor *IMF estimate

Actually, this picture answers the above question. Turkey in fact could not achieve the desired monetary tightening, at least concerning the level of policy interest rate. This played a major role in achieving the record-high growth rate. The impact of other instruments like the interest rate corridor and reserve requirements is yet to be seen. Though this picture does not seem normal, all we can do is hoping that the CBT was right about its "new" monetary policy framework and the current policy rate.