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2021 Macroeconomic Imbalance Indicators: European Union and Turkey

The Macroeconomic Imbalance Procedure Scoreboard, which includes the Macroeconomic Imbalance Indicators of the EU countries for 2021, was published on November 21, 2022 as a statistical supplement to the Alert Mechanism Report prepared by the European Commission and published annually.[1] The highlights of the report within the scope of indicators can be summarized as follows:

In the post-pandemic period, EU economies have largely compensated for the contraction in GDP and entered a strong growth period, but the outlook for the EU economy has changed significantly with the Russian invasion of Ukraine in February 2022. During the pandemic, the high savings of households and the postponement of their consumption caused a rapid increase in domestic demand with the removal of restrictions; financial incentives also continued to support domestic demand beyond the acute pandemic period. On the other hand, the supply bottlenecks accompanying the increasing domestic demand put upward pressure on the prices of manufactured products. In addition, the rapid recovery of the global economy increased the demand for energy and other commodities and led to an increase in energy inflation. In 2022, after Russia's invasion of Ukraine, the interruption of Russian gas supply to Europe caused energy prices to rise rapidly, making energy prices the main determinant of Harmonized Index of Consumer Prices (HICP) inflation.

In 2021, the current account balance of most member countries returned to their pre-COVID-19 crisis position, but in 2022, high energy prices adversely affected the external balances. It is observed that the travel restrictions brought with the COVID-19 crisis have had permanent effects in some countries where the tourism sector is dominant, and these countries continue to have high current account deficits in 2021. Current accounts in many countries have reached pre-pandemic levels, and recovery has accelerated in countries with current account surpluses. Although external stock positions, followed by the Net International Investment Positions (NIIP) indicator, have narrowed with higher GDP growth, they still maintain their importance. Export market share developments also show that the effects of the COVID-19 crisis are partially reversed. In 2022, the increase in energy prices to much higher levels affected the current accounts negatively in all countries, a contraction in non-energy trade balances in which exchange rate effects played a role in some countries, and in parallel, their export shares decreased.

Due to the effects of the pandemic conditions on the labor market, it has become difficult to interpret data and measure productivity, but it is possible to indicate a general increase in unit labor costs. The developments in real effective exchange rates differ between countries depending on the inflation dynamics. In 2021, before the pandemic, wages increased rapidly especially in countries with a tight labor market. This trend continues to strengthen in 2022 and poses an important risk factor for cost competitiveness in the Eurozone. On the other hand, although the real effective exchange rates based on inflation did not show a great change throughout the region due to the depreciation of the Euro, there are significant differences between countries. In this differentiation, the changing inflation levels depending on the structure of the energy markets of the countries and the effect of the energy price shock on the price dynamics play a role.

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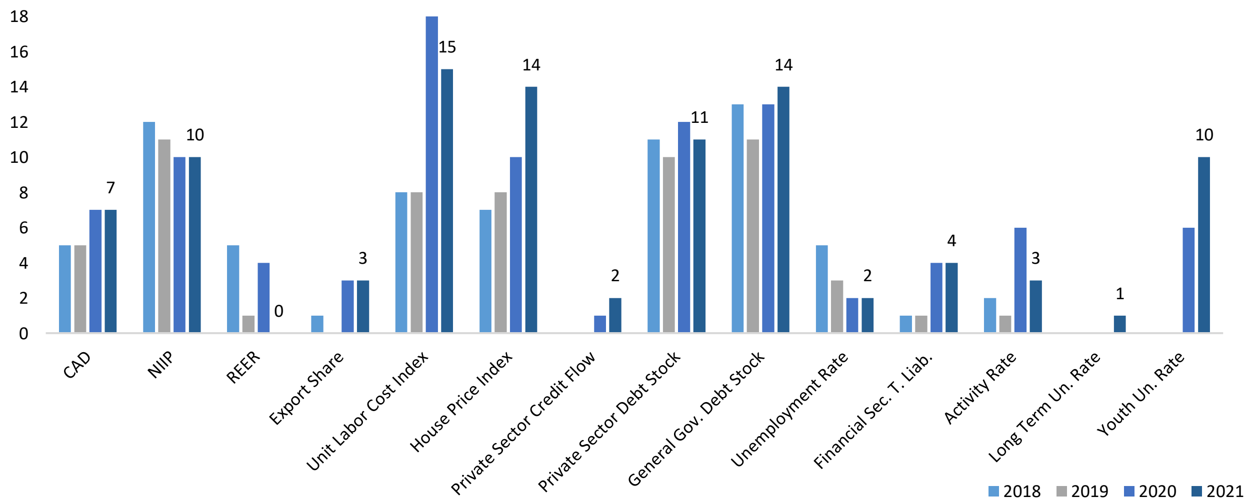
[1] European Commission (2022). Alert Mechanism Report 2023. Brussels, 21.11.2022. https://ec.europa.eu/eurostat/documents/16624/9862137/AMR-report-2023.pdf/490c55c2-76e8-e16b-702d-86d378d96dae?t=1669131990686

With the revival of economic growth in 2021, public and private sector indebtedness ratios decreased and this trend continues in 2022. Net credit utilization of companies has been positive across the EU, and indebtedness indicators have improved in most EU countries with the recovery of investments. Although the ratio of non-financial corporate debt stock to GDP continues to decline, it was above the threshold or above 2019 levels in about half of the EU countries. The related indicator continued to decline across the EU in the first half of 2022, despite the increase in loans reflecting increased liquidity needs. In other words, the effect of new credit use on the corporate debt to GDP ratio was offset by real GDP growth and the sharp rise in inflation. The ratio of public sector debt to GDP also declined in 2021, but remained well above the 2019 level in almost all member states. Although the heavy support provided to households and companies for high energy prices in 2022 increases the indebtedness of the public sector, the continuation of economic growth ensures the continuation of the improvement in indicators.

The capital adequacy of the banking sector is high, while the profitability is structurally low. Credit supply to companies continued despite the gradual expiration of government guarantees during the COVID-19 pandemic and macroprudential tightening in some countries. In an environment where housing prices are rising rapidly throughout the EU, household credit utilization is also increasing steadily. Non-performing loans decreased, and the bank's profitability remained structurally weak in spite of its sluggish recovery. The worsening economic outlook in 2022 is expected to adversely affect assets and credit risks.

While government subsidies stabilized employment, household incomes were preserved, and household disposable income increased in real terms in most EU countries, although there were significant differences between countries. While household consumption decreased during the pandemic period, their savings increased and there were high increases in disposable income after COVID-19. On the other hand, unemployment remained stable in 2020 with policy measures, and in 2021 and beyond, unemployment started to decline with the recovery in demand and the sharp increase in job openings.

Figure 1. Number of EU countries exceeding MIP thresholds * (2018-2021)

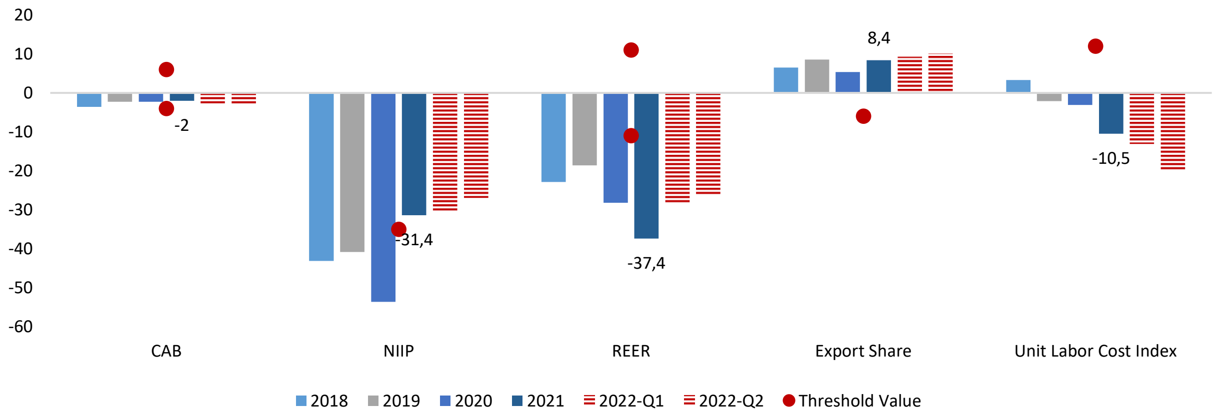


Source: Eurostat

* CAB, Current Account Balance; NIIP, Net International Investment Position; REER stands for Real Effective Exchange Rate.

In Turkey, unlike EU countries, real effective exchange rate and unit labor costs are at historically low levels and current account balance is deteriorating despite Turkey's strong competitive position. The Turkish lira has depreciated significantly in the last two years, and despite the rapidly increasing inflation rate in 2022, the real effective exchange rate indicator has maintained its high negative value. Similarly, unit labor cost indicator differs from EU countries with its high negative value. The sharp decline in the said indicator reflects the erosion in the purchasing power of labor force and the contraction in the share of labor in national income with the rapidly increasing inflation. Despite the strong competitive position implied by low price and cost indicators, the improvement observed in the current account balance in 2021 could not be sustained and as of September 2022, the highest current account deficit value of the last 4 years was reached. The deceleration of exports and historically low terms of trade indicate that the current account deficit will increase further. The GDP share of the net international investment position increased in 2021 due to the strong growth of 11.4 percent and remained above the threshold of -35 percent. This trend continues in 2022 (Figure 2, Table 1).

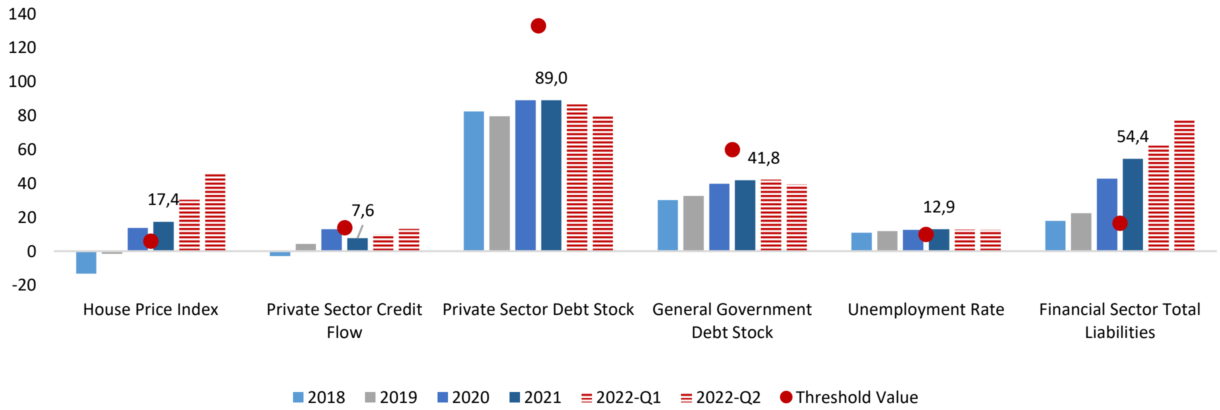
Figure 2. MIP Turkey: External Imbalances and Competitiveness Indicators * (2018-2021)



Source: TURKSTAT, CBRT, Ministry of Treasury and Finance, WTO and TEPAV calculations.
* CAB, Current Account Balance; NIIP, Net International Investment Position; REER stands for Real Effective Exchange Rate.

Indicators of financial liabilities and asset prices were well above the threshold values, indicating significant vulnerabilities towards financial stability Despite the strong growth in GDP, general government indebtedness increased in 2021, however, there was no change in indebtedness due to the slowdown in loan utilization by the private sector. While accelerating inflation and negative real interest rates in 2022 increased the private sector's use of new loans, the continuation of growth ensured the continuation of the improvement in sectoral indebtedness indicators. Although these indicators are below the thresholds defined for the EU, Turkey differs significantly from EU countries with its rapid and high increases in real house prices and financial sector liabilities Total liabilities of the financial sector increased by 54.4 percent in 2021 and by 77.6 percent as of the second quarter of 2022. In addition to high inflation, the increase in Turkish lira savings due to currency-protected deposits is also effective in the acceleration observed in 2022. On the other hand, the house price index indicator, which measures the annual real price change in the housing market, is calculated as 17.4 percent in 2021 and 45.9 percent in the second quarter of 2022. This shows that housing market developments also constitute a financial risk factor (Figure 3, Table 1).

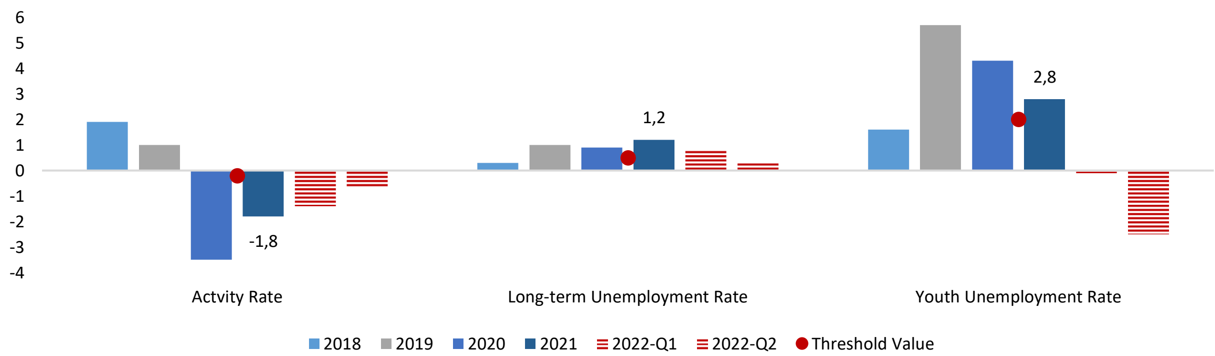
Figure 3. MDG Turkey: Internal Imbalance Indicators (2018-2021)



Source: TURKSTAT, CBRT, Ministry of Treasury and Finance and TEPAV calculations.

Turkey also differs negatively from EU countries with its shrinking labor force participation and high unemployment rates. The activity rate indicator, which is defined as the labor force participation of the economically active population and followed as a 3-year change, had an increasing trend before 2020, but reversed with the COVID-19 pandemic and declined by more than 3 points. The downward trend still continues, albeit at a slower pac. On the other hand, indicators of long-term unemployment rate and youth unemployment rate continued to increase above the threshold value in 2021, and partial improvements were observed in 2022 (Figure 4, Table 1).

Figure 4. MIP Turkey: Labor Market Indicators (2018-2021)



Source: Source: TURKSTAT and TEPAV calculations.

Table 1. MIP Scoreboard: EU and Turkey (2021)

	External Imbalances and Competitiveness					Internal Imbalances						Labor Market Indicators		
	Current Account Balance	Net International Investment Position	Real Effective Exchange Rate	Export Share	Nominal Unit Labor Cost Index	House Price Index	Private Sector Credit Flow	Private Sector Debt Stock	General Government Debt Stock	Unemploy. Rate	Financial Sector Total Liabilities	Activity Rate	Long-term Unemploy. Rate	Youth Unemploy. Rate
	Ratio to GDP 3-year average	Ratio to GDP	CPI-based 3-year change	Ratio to world exports 5-year change	3-year change	Real annual change	Ratio to GDP	Ratio to GDP	Ratio to GDP	3-year change	Annual change	Ratio of population aged 15+ 3-year change	Ratio of 15+ to active population 3-year change	Ratio to active population aged 15-24 years 3-year change
Turkey	-2.0	-31.4	-37.4	8.4	-10.5	17.4	7.6	89.0	41.8	12.9	54.4	-1.8	1.2	2.8
Belgium	0.5	59.9	0.6	2.4	5.4*	4.5	3.8*	169.0*	109.2	5.9	7.5	1.1	0.0	2.2
Bulgaria	0.5	-18.4	3.8	12.2	16.4	2.5*	4.4	84.4	23.9	5.5	9.5	0.6	-1.0	-0.1
Czech Republic	0.5	-15.6	5.0	-1.1	13.9	16.4	2.9	78.8	42.0	2.5	7.9	0.0	0.1	1.5
Denmark	8.5	77.0	-1.1	6.5	6.1	9.5	12.3	214.7	36.6	5.2	11.7	1.4	0.0	0.3
Germany	7.3	70.7	0.5	-5.9	7.4*	8.2*	5.7*	120.4*	68.6	3.4**	7.2	1.2	-0.2	0.3
Estonia	-0.1	-13.0	1.9	17.8	10.7	10.4	6.5	95.3	17.6	5.9	17.5	-0.2	0.3	4.7
Ireland	-4.2	-145.5	-2.6	39.9	-7.9	4.2	2.6*	168.1*	55.4	5.7	18.8*	1.8	-0.3	0.7
Greece	-5.0	-171.9	-3.1	9.6	4.0*	6.4***	-0.1*	120.7*	194.5	16.7	14.3	-0.8	-3.3	-5.7
Spain	1.2	-71.5	-0.5	-10.5	12.3*	1.5	2.5*	139.1*	118.3	14.8****	6.6	0.0****	-0.2****	0.5****
France	-0.3	-32.1	-0.4	-11.4	4.6*	4.7	6.5*	167.8*	112.8	8.1****	7.3*	0.2****	-0.2****	-3.1****
Croatia	1.8	-35.1	-1.5	7.9	6.4*	4.5	3.0*	88.5*	78.4	7.2	11.7	2.4	-0.6	-1.8
Italy	3.4	8.1	-1.8	-6.2	4.6	0.9	3.3	113.5	150.3	9.6	6.2	-1.1	-1.1	-2.5
Cyprus	-7.5	-117.8	-2.4	24.9	4.1*	-4.3	4.3*	248.4*	101.0	7.4	-0.8	1.7	-0.1	-3.1
Latvia	-0.7	-27.4	2.3	13.4	14.5	7.3	0.9	58.0	43.6	7.3	13.2	-1.8	-1.1	2.6
Lithuania	4.0	-7.4	4.4	37.9	19.2	11	5.9	53.9	43.7	7.3	25.2	0.9	0.6	3.2
Luxembourg	4.2	30.6	0.6	13.1	11.2*	12.4	53.9*	340.6*	24.5	5.9	11.4	2.1	0.4	2.7
Hungary	-1.9	-53.1	-4.1	0.0	12.4*	10.0*	12.7*	80.5*	76.8	3.8	16.4	2.1	-0.1	3.6
Malta	-0.8	52.8	-1.2	-0.9	12.9	3.8*	9.4	131.8	56.3	3.8	7.7	3.5	-0.9	0.3
Holland	6.4	93.0	2.2	1.1	11.2*	11.2*	11.7*	229.3*	52.4	4.5	-0.3*	1.0	-0.4	0.4
Austria	1.9	14.7	1.2	-2.7	9.9	9.9	7.4	129.7	82.3	5.7	8.0	0.1	0.3	1.0
Poland	0.3	-39.5	-0.4	24.9	9.9**	3.7	4.0	71.6	53.8	3.3	13.6	3.4	-0.1	0.1
Portugal	-0.6	-94.7	-2.8	-5.3	12.5*	7.9	4.0*	156.9*	125.5	6.8	7.1	0.7	-0.3	3.1
Romania	-5.7	-47.2	1.0	10.6	14.4*	-1.1	3.8*	48.1*	48.9	5.5	14.3	3.2	-0.2	0.5
Slovenia	5.8	-6.8	-0.4	11.6	12.8	7.8	3.5	66.4	74.5	4.7	14.1	0.6	-0.3	3.9
Slovakia	-1.8	-61	3.1	-2.9	14.1	3.0	5.5	95.0	62.2	6.4	24.0	0.2	-0.8	4.8
Finland	0.3	-1.4	-0.7	4.9	6.0	2.8	6.1	150.1	72.4	7.4	9.4	1.8	-0.2	-0.2
Sweden	5.6	21.2	2.1	-1.0	5.5	8.1	16.6	215.2	36.3	8.1	10.9	0.6**	0.2	7.9
Threshold values for EU countries	%-4/6	%-35	%+/-5 (Eurozone) %+/-11 (Non-Eurozone)	%-6	%9 (Eurozone) %12 (Non-Eurozone)	%6	%14	%133	%60	%10	%16.5	-0.2 points	0.5 points	2 points

Source: For EU data: Eurostat, MIP Scoreboard, Main Tables (https://ec.europa.eu/eurostat/web/macroeconomic-imbalances-procedure/data/main-tables); for Turkey data: TURKSTAT, CBRT, Ministry of Treasury and Finance, WTO and TEPAV calculations. * Provisional. **Series interruption. ***Forecast. **** Includes those who are expected to return to the same job when COVID-19 health measures terminate in Spain and France.