

## Economic Growth Accelerates in the Last Quarter

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### Executive Summary

In order to monitor and analyze the changes in the Turkish economy on a regular basis, Betam tracks selected monthly indicators of economic activity in Turkey. Because most indicators are still not released as seasonally adjusted by the statistical agency, TurkStat, Betam seasonally adjusts these series as needed. Betam uses these monthly indicators in making real-time forecasts for quarterly GDP growth. Our forecasts and a summary of monthly economic activity in Turkey are updated and published every month starting January 2011 under the section “Monthly Economic Outlook and Forecasts” on our website. This report stands as the first of those in the series.

Using the latest monthly data released last week on November indicators, Betam expects the real GDP to grow by 2.2 percent in the last quarter. This amounts to a 8.7 percent annual growth for 2010 overall. Starting from the first quarter, the economy had grown by 0.5, 3.5 and 1.1 percent quarterly in 2010, respectively.

In the coming months we will be watching closely the effects of the Central Bank’s new policy mix on the economy. The big question is whether this policy, a decrease in the policy rate coupled with an increase in reserve requirements, will actually achieve the monetary contraction that the Central Bank is hoping for in order to contain inflation while making Turkey a less desired destination for short term

capital inflows that threaten financial stability and appreciate the Turkish Lira. To the degree that it achieves the purpose, the policy mix can have an adverse effect on GDP growth. However, a failure might drive the current account deficit up to unsustainable levels as well as increase inflation. Turkey’s current account deficit has reached 41,6 billion dollars in November and we expect the year-end figure to be 6.1 percent of the GDP.

### Selected Monthly Indicators

Table 1 lists the monthly indicators and show percentage changes in the fourth quarter.<sup>1</sup> A high increase in almost all indicators are observed in October followed by small declines in November. December figures of some indicators are still not released yet. We use our forecasts of these variables in calculating quarterly changes.<sup>2</sup> The fourth quarter changes show an increase from the third quarter suggesting acceleration in the real GDP growth in this quarter.

Looking closer to hard data, the Industrial Production Index (IPI), and exports decreased by 1.3 and 3.0 percent respectively in November compared to the previous month. The decrease came after substantial increases in October and both production and exports still remained above September levels. Capacity Utilization Rate (CUR) increased by 3.4 percentage points. Imports continued to increase but slowed pace. It only added 0.2 percent over the

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<sup>1</sup>All indicators are real (or inflation adjusted) and seasonally adjusted.

<sup>2</sup>The calculations are updated every month when the data is released.

6.6 percent increase in October. Most of the change came from imports of consumption and investment goods.

## Consumption Indicators

Durable and nondurable consumption goods production indices both decreased in November by 1.9 and 9.3 percent. Imports of consumption goods also declined, by about 2.9 percent. The Special Consumption Tax (SCT) increased in November by 1.5 percent (after adjusting for inflation) but slowed pace compared to October.

We expect all consumption indicators to increase in the fourth quarter. The last column of Table 1 shows the estimated quarterly changes. Only the capacity utilization rate in durables and non-durables is already released and it increased 1.6 and 2.7 percentage points, respectively.

## Investment Indicators

Intermediate goods, one of the leading indicators for industrial production, had increased by 1.8 percent in the third quarter. In October and November, imports of raw materials continued its rise, increasing by 3.7 percent and 0.7 percent, respectively from the previous month.

Production of intermediate goods had slightly decreased in the third quarter by 0.3 percent. But it increased both in October and November by 2.3 and 1.8 percent, respectively. The capacity utilization rate (CUR) for intermediate good production has also increased in both months. Overall, we expect an increase in intermediate good production in the fourth quarter.

Imports and production of capital goods also show an acceleration in the fourth quarter.

## Forecasts for 2010-Q4

Betam forecasts the seasonally adjusted real GDP growth from the third quarter to fourth quarter to be 2.2 percent. This amounts to a calendar adjusted 7.3 percent increase from the fourth quarter of 2009 to fourth quarter of 2010, and a 8.7 percent annual real GDP growth from 2009 to 2010. The year on year quarterly change in the third quarter was 6.3 percent (calendar adjusted).

Betam bases its forecasts on the monthly data summarized in Table 1. We update this table and our forecasts every month when the data is released and share it publicly.

## IPI fully recovered, CUR is not back to its pre-crisis level yet

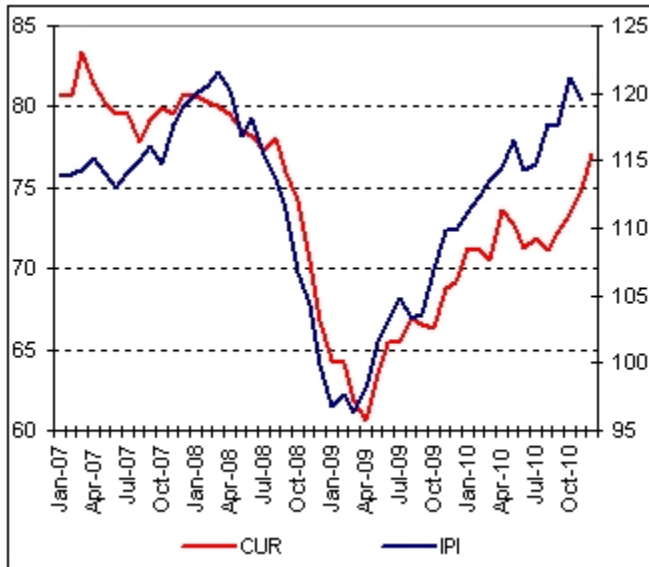
Figure 1 shows monthly changes of real and seasonally adjusted Capacity Utilization Rate (CUR) and Industrial Production Index (IPI) since January 2007. As shown in the figure, IPI nearly reached the highest point before the crisis which was in March 2008. On the other hand, CUR is way below the pre-crisis levels. CUR's 2007 average was 80.2 percent. In December 2010, CUR reached 77.1 percent according to Betam's seasonally adjusted numbers. Between December 2009 and December 2010, CUR increased 0.66 percentage point per month on average. According to these numbers, we expect that the industry will stay below pre-crisis capacity utilization level for a few quarters more.

Figure 4 shows the monthly changes of real and seasonally adjusted IPI's and CUR's components. Investment goods manufacturing is far from recovery. However, intermediate goods manufacturing is fully recovered from the crisis and other sectors are close to a full recovery. In December, all the components of IPI except intermediate goods experienced a decline. Durable, nondurable and investment goods manufacturing fell 9.3, 1.9 and 5.4 percent, respectively. When we analyze the components of CUR, we see that none of the sectors have recovered yet. Among all the sectors intermediate goods manufacturing seems to be in the best situation. In November and December intermediate and investment goods experienced the biggest increase. The sum of the two month increase in these sectors were 5.5 and 5.6 percentage points, respectively.

## After the unexpected increase in October, exports fell in November

Figure 2 shows monthly changes of real and seasonally adjusted import and export volume indices. Between November 2009 and November 2010, exports increased by 0.3 percent per month on average. On the other hand, the monthly average growth of imports was 2.4 percent. In October exports raised 3.9 percent which is above the regular growth trend of

Figure 1: CUR ve IPI (real, calendar day corrected and seasonally adjusted, left axis for CUR and right axis for IPI)



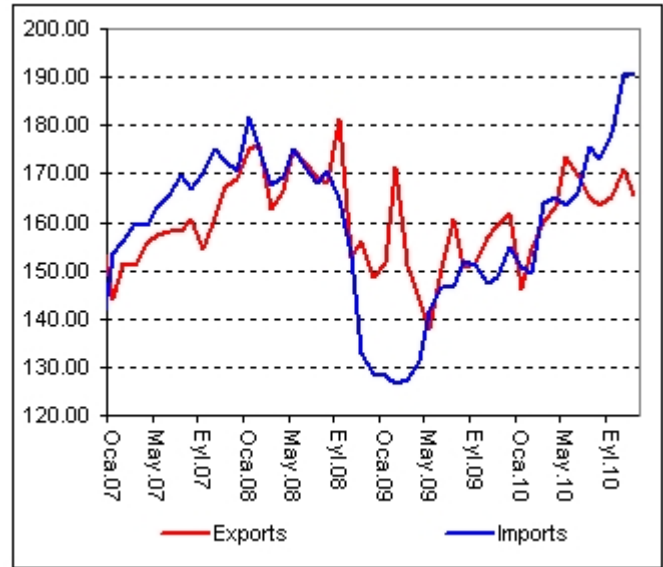
Source: TurkStat, Betam.

exports, however in November exports fell 3 percent and nearly returned to the October level. The surge in imports since the recovery began slowed down in November. Although, in September, imports increased 6.6 percent, in November they increased by 0.2 percent.

Figure 6 shows the monthly changes of real and seasonally adjusted imports of basic economic categories. About 70% of Turkey’s imports are intermediate goods which includes oil and natural gas, though lately the surge in imports is caused by imports of investments and consumer goods. Between November 2009 and November 2010 imports of investment goods, consumer goods and intermediate goods increased by 7, 2.2 and 1.4 percent per month on average respectively. After the high increase in October, imports almost stayed at the same level as in November. Imports of consumer goods decreased by 2.9 percent, while imports of intermediate goods and investment goods increased by 0.7 and 3 percent, respectively.

Figure 3 shows the monthly changes in exports for major manufacturing industries in Turkey. During the recession, the automobile industry had a large decrease in exports and is still way below the pre-crisis levels. Moreover, automobile industry experienced a decline both in October and November,

Figure 2: Volume indices of exports and imports (real, calendar day corrected and seasonally adjusted)



Source: TurkStat, Betam.

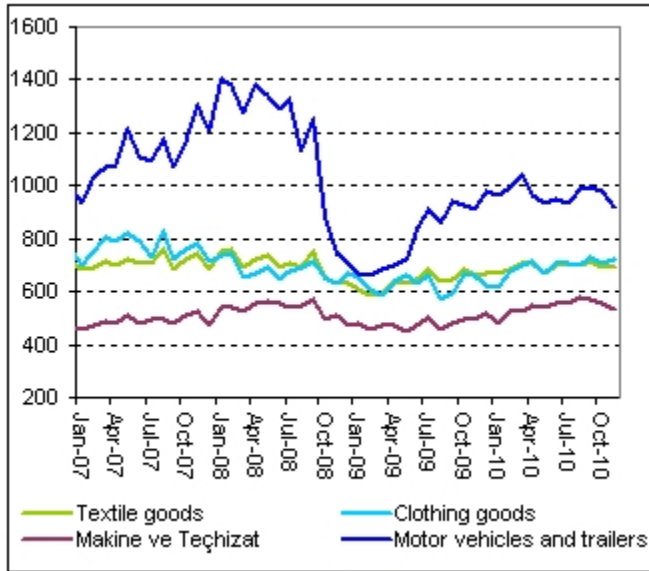
also machine and equipment sector experienced a similar decline in the last two months. In the last months, textile and clothing goods sectors had a volatile course and it’s likely to remain that way.

Figure 5 shows the export performance of all manufacturing sectors in October and November. Mainly exports of manufacturing sectors declined in November. The largest fall was observed in the metal industry, automobile industry and tobacco industry followed. Because the automobile industry and the metal industry are among the biggest exporters, the fall in these sectors pushed the monthly growth of aggregate exports to the negative values in November.

### Real GDP growth is expected to slow down in 2011

In 2010, economic growth in the Turkish Economy was driven by a surge in the internal demand while external demand remained weak due to the global crisis. As a result, the current account deficit increased substantially. Last month, the Central Bank of Turkey announced that the current account deficit was worrisome and posed a threat to financial stability in the country. As a result the Central Bank announced a new policy mix to curb the excessive

Figure 3: Monthly changes of important industries' exports (real, calendar day corrected and seasonally adjusted, million \$)



Source: TurkStat, Betam. Each component of exports are transformed into real series by using TUIK's price index of the corresponding component and then it is seasonally adjusted.

short term capital flows to Turkey, in order to decrease the current account deficit.

In the first quarter of 2011, we will be watching for the effects of the Central Bank's new policy on the economic activity. If the policy, an interest rate cut coupled with an increase in banks' reserve requirements, causes a monetary contraction, as the Central Bank hopes, consumption and investment demand will fall, depressing the internal demand. As long as Europe's demand for imports stays weak, Turkey's exports cannot increase substantially in the short-run. Therefore, the growth rate of real GDP might decrease substantially in 2011.

However, if the Central Bank's policy cannot be successful in reducing internal demand, then the current account deficit can reach unsustainable levels. Moreover, inflation, which is already off the 2011 target, might start to increase.<sup>3</sup> Of course, we have to note that the Central Bank cannot hope for much help from the government in terms of a tight fiscal policy since elections are going to be held mid-June in 2011. The critical point for the Turkish economy next year will be achieving a growth rate that will

<sup>3</sup>Inflation in 2010 was 6.48% which was in line with the target. The 2011 target is set to be 5.5%.

not cause inflationary pressures and keep the current account deficit at reasonable levels.

Table 1: Monthly and quarterly percentage changes of selected economic indicators, 2010

	October	November	December	Quarter III	Quarter IV
<b>Hard Data</b>					
Industrial production index (IPI)	3,1	-1,3		1,4	3,2*
Capacity utilization rate (CUR)	1,2	1,6	2,1	-0,8	3,4
Intermediate goods import	3,4	0,7		1,8	5,3*
Consumer goods import	13,6	-2,9		8,9	10,4*
Investment goods import	18,7	3,0		10,5	21,2*
SCT	5,2	1,5		3,9	5,7*
Automobiles	7,7	-6,8		1,7	9,2*
<b>IPI Detail</b>					
Nondurable consumer goods	2,2	-1,9		0,2	0,5*
Durable consumer goods	5,5	-9,3		4,8	0,7*
Intermediate goods	2,3	1,8		-0,3	4,2*
Investment goods	8,7	-5,4		2,1	8,3*
<b>CUR Detail</b>					
Nondurable consumer goods	0,6	0,5	0,5	1,5	1,6
Durable consumer goods	0,4	2,4	0,6	-1,9	2,7
Intermediate goods	3,3	0,8	4,6	-0,2	5,0
Investment goods	-3,3	5,2	0,4	1,3	3,5
<b>Soft Data</b>					
Consumer confidence index (TurkStat)	0,1	2,7		2,5	2,8
Real sector confidence index	5,3	2,7	1,5	-0,7	9,6
<b>Financial Data</b>					
İMKB	6,9	1,2	-3,8	4,8	9,8

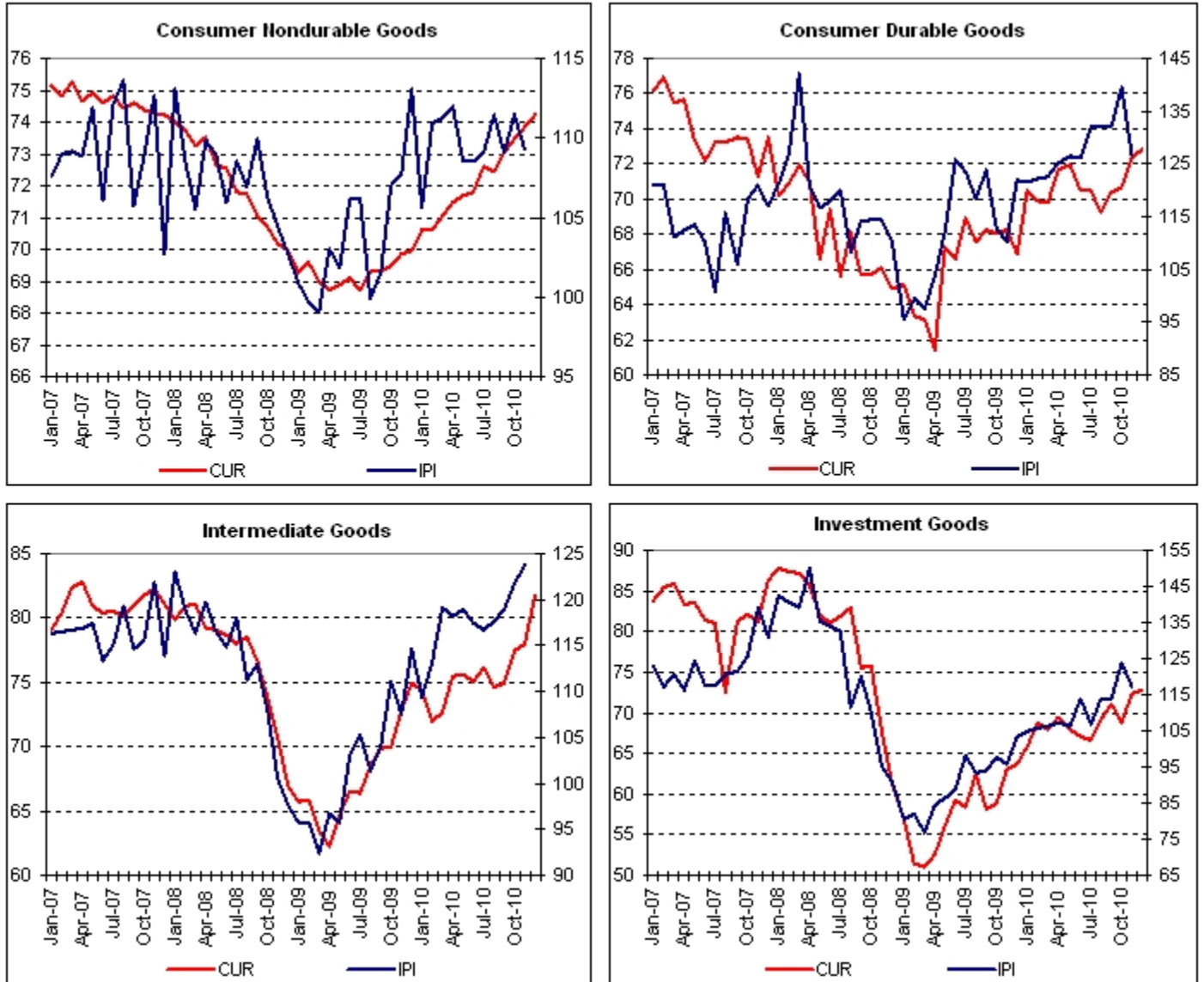
Source: TurkStat, TCMB, İMKB, Betam

Table 2: Betam's quarterly and annual growth rate forecasts (real, seasonally adjusted)

Betam's quarterly real GDP growth rate forecast (from 3rd quarter to 4th quarter)	2.2
Betam's annual real GDP growth rate forecast (2010)	8.7

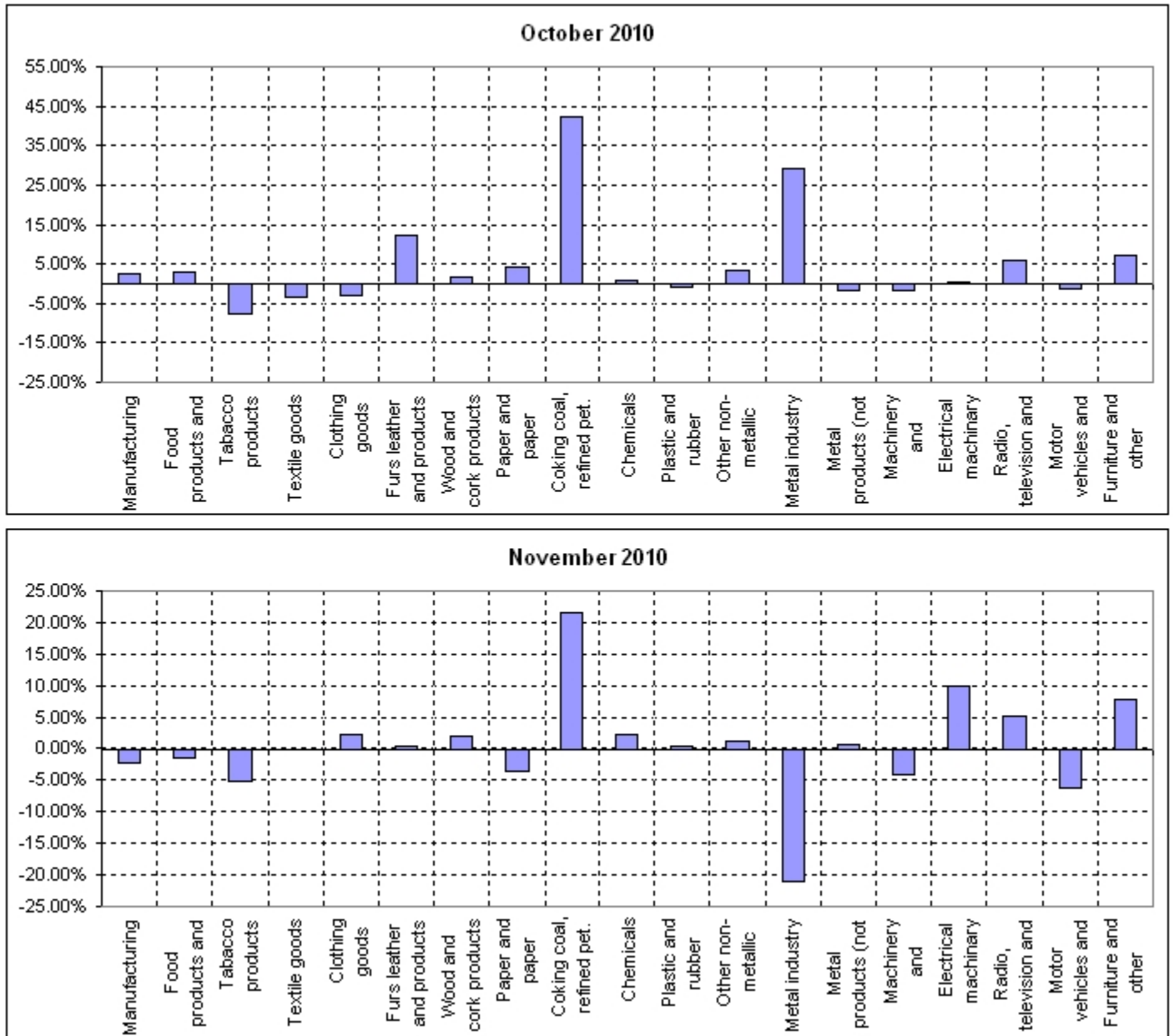
\* For some indicators December data are not yet released by TurkStat. Betam uses its monthly forecasts for these variables in its calculations for quarterly forecasts. Whenever the actual data is released, Betam updates its calculations and forecasts accordingly. The 4th quarter values thus reflect the changes from the third quarter based on these calculations.

Figure 4: Monthly changes of CUR's and IPI's components



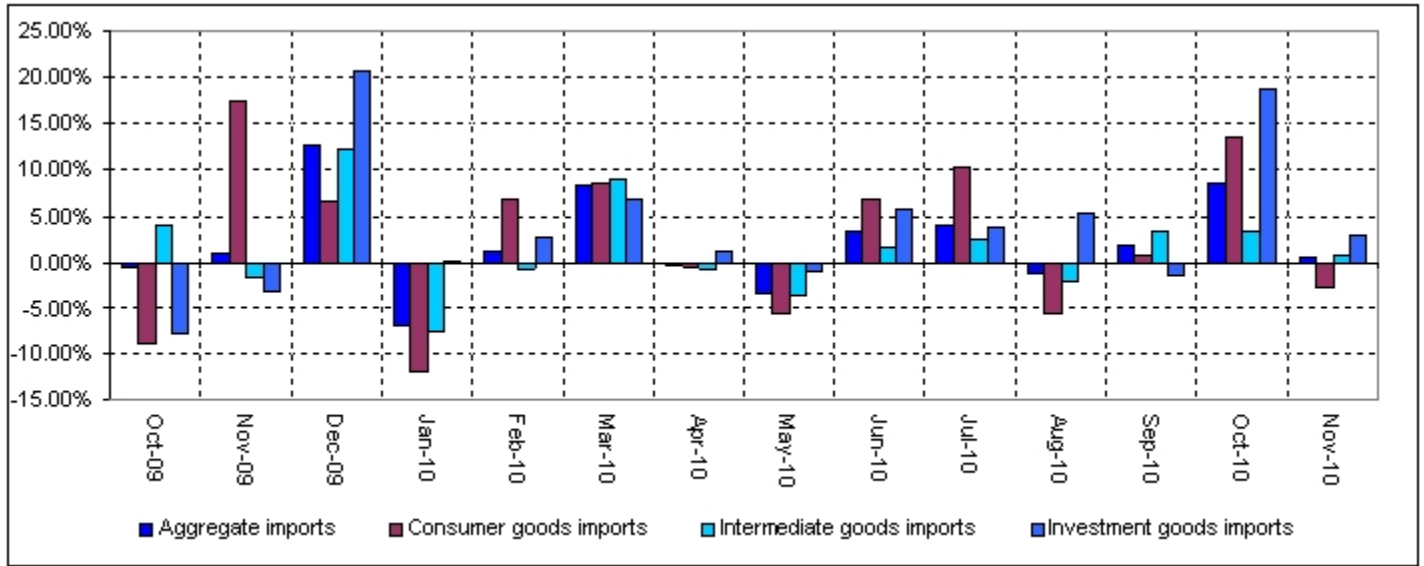
Source: TurkStat, Betam. Real and seasonally adjusted series

Figure 5: Monthly changes of manufacturing industry exports, October 2010 and November 2010



Source: TurkStat, Betam. Real and seasonally adjusted series

Figure 6: Monthly changes of imports' components



Source: TurkStat, Betam. Real and seasonally adjusted series