TÜSİAD

TURKISH INDUSTRIALISTS' AND BUSINESSMEN'S ASSOCIATION

TÜSİAD
Quarterly Economic Survey

NO: 9

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TÜSİAD TURKISH INDUSTRIALISTS' AND BUSINESSMEN'S ASSOCIATION

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Foreword

TÜSİAD, stands for "Türk Sanayicileri ve İşadamları Derneği" ("The Turkish Industrialists' and Businessmen's Association") which was founded in 1971 by a group of leading names in Turkish industry and business. TÜSİAD is an independent, non-profit institution whose primary purpose is to promote public welfare. TÜSİAD is scientific and objective in its researches. It is emphasised that this study does not necessarily reflect the views of the TÜSİAD members nor, of course, is it to be considered in any way whatever to be an official publication.

The ninth issue of TÜSİAD Quarterly Economic Survey is prepared by utilising the most recent data and estimations available in April, May and June 1996 by Economic Research Department.

LIST OF TABLES AND GRAPHS

RISING INFLATION, INCREASING BUDGET DEFICIT AND THE WORSENING OF THE PUBLIC SECTOR'S FINANCING PROBLEM INDICATE THAT ECONOMIC INSTABILITY HAS CONTINUED TO BECOME SEVERER.

The economy has been growing very fast since the second quarter of 1995, and it has continued to grow in the first quarter of 1996 at a rate far beyond expectations. Though foreign trade and expenditure-based GNP figures are not yet available, it is estimated that growth has been fuelled by a rise in domestic demand. The fast growth has been accompanied by an increase in the rate of inflation and by a budget deficit which is expected to go up to record highs in the days lying ahead. It is estimated that, due to the expansionist economic policies, high wage increases, and the enlargement of credit facilities, the fast growth will go on in the coming period. In addition, as the volume of voluntary domestic savings will remain much below the required levels, inflation is expected to accelerate and push the volume of forced savings to even higher levels.

As a result of the deleterious developments in public finance, the share of interest payments in total expenditures has continually increased. To be able to make interest payments, governments have resorted to borrowing at real interest rates which have remained far above the rates of increase of real income and as a result the public budget has become an interest-payment budget. While interest payments exert great pressure on the budget, increasing financing needs due to higher current expenditure will worsen the problems being faced. In a situation of the lack of more appropriate resources for the financing of the public deficit, the financing of the expenditures by short-term domestic borrowing at high interest rates increases the growth rate and the welfare level in the short run but puts the future at great risk.

The fast way out from the 1994 crisis is continuing: The 12.2 percent growth rate in the first quarter of 1996 has exceeded expectations.

In the first quarter of 1996, economic growth was well above expectations with a rate of 9.9 percent. One factor which contributed to the high rate of GNP growth was the expansionary economic policies which were put in action before the general elections of 24 December and carried on thereafter. The rise in interest rates at the beginning of the year was perceived by the private sector as a temporary aftereffect of the election period, and therefore did not produce the expected negative effects on production.

After the 1994 crisis, a strong expansionary period driven by high domestic demand, began in the second quarter of 1995. The growth rate was 12.6 percent in the second quarter of 1995, 10.7 percent in the third quarter, and 7.7 percent in the fourth. These high rates of economic growth constitute in fact a compensation to the reduction in real income in the crisis period. However, the production level required by the precrisis trend has still not been achieved.

The main stimulants of domestic demand is considered to be the rise in incomes as a result of the expansionary policies and the inflow of foreign resources. According to the estimations of the TÜSİAD Economic Research Division, the increase in investment was more than the increase in consumption in the first quarter. Investment expenditures increased at a faster rate than consumption expenditures in the private sector. In the public sector, on the other hand, despite the real contraction of investments, both current expenditures as well as salary and wage expenditures went up sharply. The private sector has increased its investment spending with the goal of preserving its competitive power within the Customs Union. In the January-March period of 1996, subsidised investments grew by 260 percent in comparison to the corresponding period of the last year and reached the level of TL 373 trillions. In the same period, total consolidated budget expenditures on investment underwent a real contraction of 16 percent, measured against their level in the January-March period of the previous year.

One indicator of the dynamism of domestic demand was the 12.6 percent growth rate of the commercial sector during the first quarter of the year, compared with its growth rate in the first quarter of the last year. The growth rate of the industrial sector, on the other hand, was an equally significant 8.8 percent. Still another sector which followed a remarkable upward trend was the transportation sector which grew by 7.3 percent.

Agriculture and construction were the two contracting sectors in the first quarter of 1996. In this period these two sectors repeated their poor performances of 1995. In the first quarter of 1995, the agriculture and construction sectors had contracted by 0.2 percent and 5.3 percent respectively, with respect to the same period of 1994. These two sectors continued to contract in the first quarter of 1996 by the respective rates of 2.8 percent and 1.4 percent.

The high discrepancy between the estimated and actual growth rates can be explained by the expansionary policies before and after the elections, as well as by the fact that the rise in interest rates at the beginning of the year was perceived as a temporary phenomenon by the market and it therefore exerted no negative impact on production and investment. However, two additional factors should be taken into account. One was the significant increase in import taxes despite the entry into the Customs Union. It is impossible to give a precise account of this issue because the import figures of the first quarter have not been made public as of July 1996. As the bulk of Turkey's imports come from EU countries, it had been initially predicted that there would have been a marked fall in the import taxes in the aftermath of the Customs Union. Notwithstanding this initial prediction, there occurred a 33.1 percent real increase in import taxes in the first period. For the first time since 1988, the import tax figure of the first quarter of a year exceeded that of the last period of the previous year. The second factor was a 119.2 percent rise in net factor income from abroad. The contribution of the import taxes and the net factor income from abroad to growth were, respectively, 1.3 and 1.7 points. These two items did thus constitute the 3 points of the 9.9 percent growth rate.

The expected expansionary policies of the new government will uphold the fast growth process in the remainder of the year. According to the monthly industrial production figures, industrial production has kept growing in the second quarter of the year. There occurred some monthly fluctuations in the annual growth rates as a result of the loss of working days during the religious holidays which occured in May in 1995 and in April in 1996. The 1.5 percent decline in industrial production in April was followed by a 15 percent rise in May, and the annual rate of increase for these two months averaged 6.5 percent. On the basis of the averages of the first five months, the annual rate of increase in industrial production has been 7.9 percent and the corresponding figure for the manufacturing industry has been 7.4 percent. The machinery industry, which includes durable consumer products, has achieved the highest growth rate of 30.3 percent among the subsectors of the manufacturing industry. Chemicals, which have the biggest share in the manufacturing industry, have grown by a mere 1.4 percent, foodstuffs by 8.2 percent and textiles by 7.0 percent. The capacity utilization ratios, though not as high as in the first quarter, nonetheless support the expectation that growth will continue in the second quarter.

Given the fact that the growth rate estimate for the first quarter fell far behind the actual value and the expectation that the new government will go on with expansionary policies, the GNP growth rates have been revised. In the 8th issue of the TÜSİAD Quarterly Economic Survey, the GNP growth rate was estimated as 3.3 percent; the estimate is now raised up to 8.0 percent.

Inflation is again on a rising trend...

The long-term inflation rate, which was about 60 percent before the 1994 crisis, could not be reduced to the precrisis level because no structural measures have been taken after the crisis. The inflation rate reached its maximum level of 156.8 percent in January 1995; it kept decreasing thereafter and fell down to 65 percent at the end of 1995, which was its lowest value in the postcrisis period. However, stimulated partly by the expansionary policies of the election period, the inflation rate began to rise again in the first months of 1996.

In the first six month-period, the growth in the wholesale price index (WPI) has turned out to be 43.7 percent and the increase in consumer prices has remained at 36.7 percent.

In this period, the prices of electricity and other public goods have been considerably raised with the resulting direct effect on inflation as well as on the prices of secondary products. The prices of the public manufacturing industry, which increased by 9.3 percent in the last quarter of 1995, have gone up by 30.6 percent in the first quarter of 1996 and by 16.5 percent in the second quarter. Similarly, electricity and gas prices increased by 1.8 percent in the last quarter of 1995, whereas they have risen up by 44.4 percent in the first quarter of 1996 and by 21 percent in the second quarter.

The prices of the private manufacturing industry, which have the biggest share in the WPI, have followed a more regular path in the same period. In the first six months, the increase in the private manufacturing prices has reached the level of 36.1 percent.

Agricultural prices, with over 10 percent average monthly increase during the January-April period, have risen by 51 percent in the first half of the year.

As a result of these developments, the WPI of the second three month period of the year has gone up by 15.6 percent. The increase in the April-June period, relative to the increase in the same period of the last year, has been 73.3 percent. This figure is fairly close to the inflation estimate given in the last issue of the TÜSİAD Quarterly Economic Survey. However, in anticipation of the continuation of the expansionary policies, the inflation estimates for the last two quarters of the year have been adjusted upward as being 81.8 percent and 97.4 percent, respectively. These estimates, together with the actual values of the first half of the year, yield an average 80.5 percent inflation rate forecast for 1996.

No structural solutions have been found to the problem of the public sector deficit and the main theme in the money markets has therefore remained unchanged: the provision of the cash requirements of the Treasury.

Developments in the money markets during the second quarter of the year, as in the previous periods, have been shaped by the cash requirements of the Treasury. In the 11 auctions made in this period, Treasury bonds in the amount of TL 1.1 quadrillions have been sold. In other words, at each transaction, bonds worth TL 100 trillions on average have been sold, and this required a transaction of TL 72 trillions. A transaction of this magnitude plays a decisive role in a market where the emission is TL 280 trillions and the Central Bank Money is about TL 500 trillions.

The founding of a new government at the beginning of March, and the optimistic expectations this gave rise to, resonated in the money markets in the form of an extension of the maturities and a fall in the interest rates throughout April and May. In the auctions held during the first quarter of the year the average annual simple interest rate had been 117 percent and the average maturity 141 days, whereas in second quarter the average interest rate fell to 98 percent and the average maturity extended to 164 days.

However, interest rates have started to rise again since the beginning of June as a result of the governmental crisis and the increasing cash requirement under the pressure of impending domestic debt repayments. The average compound interest rate has risen from its lowest level of 106 percent in May to 139 percent in mid-July. Despite the rise in interest rates, low amounts could be sold in the auctions held in mid-July.

Parallel to the trend of the interest rates, the real rate of interest of Treasury bonds, which was about 52 percent in February, began to decline by the beginning of March, fell to 22 percent in May, and went up to 28 percent in June.

In the second quarter of the year domestic borrowing became relatively easier because of the fall in interest rates and the prolongation of the maturities. As a result, not only have no shortterm advances from the Central Bank been used since the end of May, but also repayments have been made. With the repayment of the short-term advances to the Treasury, credits to the public sector decreased and net domestic assets declined from TL 546 trillions in March to TL 466 trillions in June.

The growth in the analytic balance-sheet of the Central Bank remained limited because no shortterm advances were used in the second quarter of the year.

The increase in total assets, which had been 20 percent in the first quarter of the year, remained at 15 percent in the second quarter.

During the January-March period the increase in Central Bank Money was brought about by the increases in credits to the public sector, whereas it resulted from the increases in net foreign assets during the April-June period. In the April-June period the international reserves of the Central Bank increased by $2 billions and reached the amount of $15.9 billions. As there was no rise in foreign exchange liabilities in dollar terms, the foreign assets of the Central Bank turned from a negative balance to a positive one. The Central Bank created reserve money corresponding to the foreign exchange it purchased. The increase in the reserve money totaled 19 percent in the second quarter. Particularly in April, at a time of massive repayments on domestic debt, increasing the emission and repaying the liabilities due to the Open Market Operations raised the liquidity level and helped the Central Bank to borrow at a lower interest rate.

Compulsory foreign exchange transfer ratio has been reduced in May to be able to slow down TL creation based on foreign exchange inflows.

Despite the decline in the interest rates there has been no upward movement in exchange rates above the rate of inflation. However, as of May and June, there has occurred a real depreciation in the value of the TL. In June, the real value of the Dollar with respect to the TL has been the same while that of the Mark has appreciated relative to their respective values at the end of 1993.

Foreign exchange deposits have remained around $21 billions since January, and have shown no significant change in the second quarter. As of the end of June foreign exchange deposits were in the amount of $21.8 billions. On the other hand, the FX deposits/M2Y ratio, which moves parallel to the exchange rates, from the level of 44 percent in June 1995, began to increase by the beginning of October, topped to 51.6 percent in December, and then again declined down to 50 percent.

In the second quarter of the year TL deposits have grown above the inflation rate in spite of the fact that the deposit interest rates on TL deposits have remained unchanged. The quarterly rate of increase in the deposits has been 27 percent. Measured with their value at the beginning of the year, the deposits have grown by a rate of 49 percent. What this figure shows is a 4 percent increase in real terms.

Deposit Bank Credits, on the other hand, showed a real increase throughout 1995 and have kept their high level since the beginning of the year.

Total credits (including Deposit Bank Credits, Central Bank Direct Credits, and Investment and Development Bank Credits) have contracted in real terms in the first half of the year.

The credit/deposit ratio has remained at 45 percent since the beginning of the year. This ratio, which is 7 to 8 points above its level in the same period of the last year, is still low compared to its value of 60 percent in the period preceding the crisis.

The real contraction in the money supply in the first quarter of the year has been replaced by a real expansion in the second quarter. Thus, currency in circulation has increased by 22 percent, and M2 has grown by 27 percent in parallel with the fast growth of time deposits.

The uncertainty of the interest policy of the new government which was founded at the end of June has driven the interest rates up while at the same time causing a decline in domestic borrowing. The problem of public sector financing has become severer as domestic borrowing decreased and decisions were taken to increase budget expenditures. In July, there has been a marked increase in the use of shortterm advances from the Central Bank for the purposes of public sector financing, and as a result cash credits to the public sector have gone up by 27.7 percent. Consequently, the increase in July alone has exceeded the total increase in the first half of the year. Credits to the public sector expanded by TL 79.7 trillions in the first half of the year, whereas in July they have gone up by TL 151.3 trillions. Parallel to the increase in domestic assets, reserve money has also enlarged by a rate of 7 percent in July. The Central Bank, on the other hand, driven by the goal of taking under control the swift expansion of liquidity in the markets, has engaged in open market operations. Liabilities due to open market operations, which totaled TL 26.1 trillions at the end of June, have moved up to TL 102 trillions by the end of July.

Foreign trade figures are still not known; but it is estimated that the foreign trade deficit will be accelerated by economic expansion and reach the annual value of $18 billions.

Though the first half of 1996 is long over only the foreign trade figures of January have been published. In the absence of the foreign trade figures it becomes impossible to arrive at a comprehensive evaluation of the economic balances and of the consequences of the Customs Union. In January exports were $1.733 millions, whilst imports reached $3.023 millions, resulting in a foreign trade deficit of $1.290 millions. According to the data supplied by our partner countries and by professional organizations, the foreign trade balance has continued to deteriorate. The dynamism of domestic demand in the first half of the year has constituted the root cause of the deterioration of the foreign trade balance, despite the fact that there has been no real appreciation of the exchange rates.

According to TÜSİAD estimates, in the first six months of the year exports have totaled $10.5 billions, imports $19.5 billions, and the foreign trade deficit $9 billions. Thus, the 12-month cumulative figure for exports is predicted at $22 billions, for imports at $40 billions, and for the foreign trade deficit at $18 billions.

It is estimated that, under the impact of a deteriorating foreign trade deficit, the current account balance has also yielded a deficit of about $2.4 billions in the first six months. In January, as a result of the increase in other invisible income, the current account balance gave a surplus of $277 millions.

On the other hand, foreign capital investments have declined, contrary to the initial expectations that they would have soared following the Customs Union. The $750 millions worth of foreign capital investment permits issued in the first six months of the year have shown a decrease of 39 percent compared with the same period of the last year. Only $136 millions of this total have been new investments.

The $3.5 billion reserve increase in the same period shows that the current account deficit has been financed, as in previous cases, by inflows of short term capital and portfolio investments.

The movement of the budget deficit in the first six months shows that the budget deficit/GNP ratio will reach the level of 9 percent in 1996.

In the first six months the budget deficit reached TL 475 trillion and the cash deficit reached 502 trillion. The reason behind the sharp real increase in the budget deficit with respect to the same period of the last year is that the 84 percent rise in budget revenues has fallen short of the 123 percent rise in budget expenditures. The two important items in budget expenditures, personnel expenditures and interest payments on domestic debt, have risen by 84 percent and 215 percent, respectively. In the January-June period, the primary budget balance showed a surplus of TL 133 trillions, interest payments amounted to TL 700 trillions.

It has become apparent that as a result of the expansionary policies, the TL 861 trillions budget deficit estimate for 1996 will be exceeded. The budget deficit is estimated to exceed TL 1.3 quadrillions. Though one factor for the widening of the budget deficit is the increase in personnel expenditures and budgetary transfers, the main factor consists of interest payments on domestic debt, whose share in total expenditures has risen from 28 percent in 1995 up to 41 percent in the first six months of 1996.

Shortterm borrowing has constituted the main source for the financing of the budget deficit. Since 21 August, 1995 the Treasury has not been able to borrow at 9 months or 12 months. In the January-June period, net repayments have been made on external debt and domestic debt with maturities longer than one year. In the first three months of the year shortterm advances from the Central Bank have been used, but during the months of April and May advances in the amount of TL 63 trillions have been paid back.

Despite the new government's frequent resort to Central Bank resources and its search for new resources, it can be said that foreign borrowing will remain limited and the budget deficit will be financed largely by means of domestic borrowing.

If the budget deficit figure for 1996 materializes as TL 1.3 quadrillions, the budget deficit/GNP ratio will set a new record with 8.7 percent.[1] One conclusion to be drawn from an analysis of the previous experiences is that significant deviations from the longterm average value of the budget deficit in one year gives way to considerable spending cuts in the following year. The unavoidable contractionary policies bring about a reduction in the growth rate and a loss in welfare. To ward off contractionary policies and the erosion of real incomes in 1997, structural measures that would block the inauspicious movement of the budget deficit must immediately be put in action.[2]

Economic policy in the second half of 1996 will be directed towards the financing of the budget and foreign trade deficits.

1996 started with growing budget and foreign trade deficits. Political instability in the first half of 1996 hindered the implementation of any serious economic measures. The new government established at the beginning of July will pursue policies to finance these two deficits.

While it has become clear that an expansionary fiscal policy will be followed, no efficient and feasible measures have yet been taken to finance the public

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[1] *The effects of the TL 1.3 quadrillion budget deficit on the macroeconomic variables are examined in Appendix 1.*

[2] *The movement of the budget deficit over the years in Turkey is analyzed in Apendix 2, within the framework of the structural budget approach.*

deficit which is on the rise. No measure, other than borrowing, stated in the resource program will make a significant contribution to the financing of the budget deficit in 1996. Foreign exchange indexed borrowing may have a positive effect on the markets in the short run, but it will not make the intended contribution to debt restructuring if it is not used as a part of a medium to long-term program.

Pursuant to the goal of checking the growth of the foreign trade deficit, measures have been taken that will increase the cost of imports and it has been announced that the exchange rate policy will not allow any real appreciation of the value of the TL. Using foreign credit has been made more costly and a Resource Utilization Support Fund deduction has been imposed on credit-financed imports which are not directed towards either investment or export. So long as the dynamism of domestic demand endures, the restraining power of these measures on the foreign trade deficit is bound to remain limited.

The wage and exchange rate policies and the rise in the interest rates will lead to an increase in the rate of inflation. It is a known fact that the increase in the inflation rate will in the long run exacerbate instability and decelerate growth. What is even more certain is that in the short run rising inflation will take back the increase in real income that has come with wage increases; it will push interest rates up; and it will reinforce the vicious cycle of exchange-interest-inflation rate. If the pessimistic expectations are to be proven wrong, it is imperative that the required measures be taken, particularly in view of the fact that inflation will settle on an upward trend in the last quarter of the year, that the last quarter will most probably witness a foreign exchange shortage because of the seasonal effects, and that the budget deficit will move up significantly in the last two months.

On the basis of these observations, it is recommended that the following measures be taken without delay: to make the finances of the public sector transparent; to impose mandatory economic constraints on the governments, such as upper limits on budget deficits; to discipline the financing of the public sector deficit; to introduce threeyear budgets; to make the Central Bank autonomous; to deepen the financial system; to make a tax reform that would increase tax revenues, expand the tax base and reduce the tax burden on the wage earners while not obstructing production and employment and not promoting the black economy; to redress the social security system which everyone accepts has gone bankrupt; to speed up privatization; and to render the build-operate-transfer system operational.

TABLE 1.1 MAIN ECONOMIC INDICATORS (1995-1996)
PRODUCTION AND PRICES

	1995						1996					
	July	August	Sept.	Oct.	Nov.	Dec.	Jan.	Feb.	March	April	May	June
INDUSTRIAL PRODUCTION INDEX (SIS, 1992=100)												
Annual % increase	19.8	13.5	5.9	2.2	10.9	15.7	12.1	1.8	12.4	-1.5	15.0	2.6
Monthly % increase	-1.7	2.1	1.9	0.3	8.9	0.6	-10.1	-17.4	16.5	-4.4	10.1	0.3
Monthly % increase (Seasonally Adjusted)	-5.3	2.7	-6.9	-3.1	9.1	0.3	-1.5	-7.0	10.1	-3.9	7.4	2.1
CAPACITY UTILIZATION RATIO (SIS, %)	83.4	82.6	84.3	80.7	79.4	81.4	79.7	78.1	75.2	76.9	83.5	80.9
WHOLESALE PRICE INDEX (SIS, 1994=100)												
Annual % increase	79.0	78.2	76.9	71.7	67.0	64.9	64.9	63.0	65.3	69.9	73.7	76.2
Monthly % increase	2.3	2.3	4.6	3.7	3.5	4.4	9.7	5.8	7.0	8.1	4.1	2.7
Monthly % increase (Seasonally Adjusted)	5.3	4.2	4.9	4.3	3.8	4.6	9.0	3.5	4.2	5.0	4.4	4.4
EXCHANGE RATE ($)												
TL/US$ (Monthly Average)	44,399	44,691	47,703	49,970	52,413	56,827	60,428	64,066	68,333	72,554	76,707	79,641
Annual % increase	43.4	46.8	40.6	42.9	44.4	51.5	50.1	56.2	63.9	71.8	78.3	85.0
Monthly % increase	3.1	5.2	2.2	4.8	4.9	8.4	6.3	6.0	6.7	6.2	5.7	3.8
INTEREST RATES (Yearly Simple Rate)												
Deposits (End of period)												
1 month	55.0	55.0	55.0	55.0	73.5	81.0	81.0	81.0	77.3	73.5	73.5	73.5
3 month	68.0	68.0	68.0	68.0	77.5	86.5	86.5	86.5	82.8	79.0	79.0	79.0
6 month	73.0	73.0	73.0	73.0	84.3	88.0	88.0	88.0	88.0	88.0	88.0	88.0
12 month	85.0	85.0	85.0	85.0	89.8	93.5	93.5	93.5	93.5	93.5	93.5	93.5
Treasury (Monthly Average)*												
3 month	69.0	68.5	92.7	96.3	98.9	120.3	131.1	104.6	94.2	-	82.5	91.8
6 month	85.8	81.0	93.9	-	-	-	134.0	111.4	101.9	102.5	97.4	99.7
9 month	-	83.2	-	-	-	-	-	-	-	-	-	-
12 month	105.0	99.8	-	-	-	-	-	-	-	-	-	-
Compound interest rate (all maturities)	98.3	92.1	117.0	130.6	135.6	183.7	201.5	148.4	126.8	127.2	114.6	126.1
Average maturity of papers sold (days, weighted by sales volume)	240	221	149	109	97	84	123	142	140	188	126	155

(. .): not available
(-): no auction
** include bills with irregular terms*

TABLE 1.2 MAIN ECONOMIC INDICATORS (1995-1996)
BALANCE OF PAYMENTS (*)

	1995 July	August	Sept.	Oct.	Nov.	Dec.	1996 Jan.	Feb.	March	April	May	June
FOREIGN TRADE												
Value (Current $ prices)												
Imports (Annual % increase)	79.1	68.9	59.7	56.0	59.0	59.6	45.4	*37.3*	*49.6*	*15.9*	*25.6*	*15.1*
Exports (Annual % increase)	13.4	15.2	1.8	16.0	24.2	3.9	12.7	*15.0*	*2.5*	*-7.0*	*3.2*	*-5.5*
Price Index (1989=100)												
Imports (Annual % increase)	21.0	19.7	17.7	11.2	-2.5	11.6	..	..	..	..	..	..
Exports (Annual % increase)	13.7	17.8	16.6	17.9	14.5	11.2	..	..	..	..	..	..
Quantity Index (1989=100)												
Imports (Annual % increase)	50.3	50.4	35.9	36.6	44.0	20.2	..	..	..	..	..	..
Exports (Annual % increase)	-7.7	1.9	-14.1	-8.5	6.9	-11.0	..	..	..	..	..	..
FOREIGN TRADE BALANCE ($ Million)												
Imports (Monthly)	2,876	3,192	3,066	3,213	3,574	4,319	3,013	*3,135*	*3,701*	*3,459*	*3,246*	*3,507*
Exports (Monthly)	1,790	1,748	1,750	1,937	2,059	2,396	1,733	*1,782*	*1,697*	*1,731*	*1,551*	*1,734*
Foreign Trade Balance (Monthly)	-1,086	-1,444	-1,316	-1,276	-1,515	-1,922	-1,280	*-1,353*	*-2,004*	*-1,728*	*-1,695*	*-1,773*
Imports (Last 12 months)	29,168	30,470	31,617	32,770	34,095	35,709	36,625	*37,477*	*38,704*	*39,178*	*39,840*	*40,301*
Exports (Last 12 months)	20,616	20,847	20,877	21,144	21,545	21,635	21,818	*22,050*	*22,090*	*21,960*	*22,009*	*21,908*
Foreign Trade Balance (Last 12 months)	-8,552	-9,623	-10,740	-11,626	-12,551	-14,074	-14,807	*-15,427*	*-16,614*	*-17,218*	*-17,831*	*-18,393*
BALANCE OF PAYMENTS ($ Million)												
Current Account Balance (Monthly)	-4	-183	212	-19	-877	-1,453	277	*-305*	*1,197*	*-332*	*-527*	*-407*
Current Account Balance (Last 12 months)	1,537	859	352	-6	-757	-2,339	-2,670	*-2,954*	*-3,992*	*-4,130*	*-4,398*	*-4,815*
Capital Account and Reserve Movements (Last 12 months)												
Net Foreign Direct Investment (Last 12 months)	629	598	665	639	592	772	760	*745*	*731*	*750*	*734*	723
Portfolio Invesmetment (Last 12 months)	74	752	1,110	1,363	1,072	1,723	2,624	*3,179*	*4,223*	*4,506*	*5,450*	5,897
Net Long-Term Capital (Last 12 months)	-389	-209	-225	-370	-419	-96	-126	*-118*	*135*	*-372*	*-263*	-272
Net Short-Term Capital (Last 12 months)	2,797	3,481	4,138	4,390	3,744	2,306	2,401	*1,523*	*1,380*	*1,267*	*1,128*	900
Net Errors and Omissions (Last 12 months)	3,389	3,067	2,554	3,150	2,572	2,292	1,215	*1,280*	*483*	*1,659*	*718*	*753*
Reserve Changes** (Last 12 months)	-8,037	-8,551	-8,594	-9,166	-6,804	-4,658	-4,204	*-3,655*	*-2,960*	*-3,680*	*-3,369*	-3,186

(*) : *Figures in italics are TÜSİAD estimates*

(**): *Positive sign indicates decrease in reserves*

(..): *Not available, balance of payments figures are relased as of January 1996, while cumulative capital account figures are relased as of June 1996.*

TABLE 1.3 MAIN ECONOMIC INDICATORS (1995-1996) CONSOLIDATED BUDGET

	1995						1996					
	July	August	Sept.	Oct.	Nov.	Dec.	Jan.	Feb.	March	April	May	June
Monthly (Billion TL)												
Revenues	123.278	124,391	121,960	155,679	146,722	148,121	157,629	123,937	141,081	169,534	274,727	207,014
Expenditures	113,546	130,391	98,287	100,323	271,383	310,745	225,453	137,727	133,686	133,971	614,102	304,424
Primary Balance (Current price)	35,364	42,459	29,978	63,643	16,149	-62,056	25,898	15,943	18,667	39,019	98,173	26,564
Budget Balance (Current price)	9,732	-6,000	23,673	55,356	-124,661	-162,624	-67,824	-13,790	7,395	35,563	-339,375	-97,410
Budget Balance (At 1994 prices)	5.229	-3,153	11,890	26,807	-58,307	-72,893	-27,706	-5,322	2,667	11,866	-108,739	-30,384
Budget Balance (Cur. price billion $)	0.219	-0.129	0.496	1.108	-2.378	-2.862	-1.122	-0.215	0.108	0.490	-4.424	-1.223
Financing	-14,908	40,514	9,886	-7,280	21,970	121,217	91,497	105,012	98,644	136,411	-2,763	73,680
Foreign Borrowing (Net)	-14,165	-15,958	26,433	-14,976	-14,677	28,005	-16,256	-17,201	-21,949	-1,017	37,220	-6,814
Domestic Borrowing (Net)	12,256	28,250	-5,573	-3,770	-14,247	-3,874	-11,326	-18,456	-53,695	-62,592	-15,577	470
Short-Term Borrowing	6,269	5,284	-3,840	31,953	30,485	77,866	251,967	85,954	171,350	197,075	-21,143	52,922
Central Bank (Net)	-5,843	-11,058	31,473	1,424	11,938	58,263	10,472	16,326	41,985	-12,113	-51,748	-6,195
Treasury Bills (Net)	12,112	16,342	-35,313	30,529	18,548	19,602	241,495	69,628	129,365	209,188	30,605	59,117
Other	-19,268	22,938	-7,134	-20,487	20,409	19,219	-132,888	54,715	2,937	2,944	-3,261	27,103
Last 12 months (Billion TL)												
Revenues	1,106,400	1,154,215	1,204,331	1,282,026	1,347,502	1,403,071	1,478,377	1,520,264	1,569,951	1,653,071	1,793,023	1,895,073
Expenditures	1,300,277	1,351,186	1,367,790	1,383,637	1,594,210	1,720,647	1,869,308	1,883,126	1,907,806	1,880,953	2,373,278	2,574,038
Primary Balance (Current price)	263,886	277,609	284,870	326,602	315,727	258,539	257,401	255,139	242,180	292,217	343,046	349,801
Budget Balance (Current price)	-193,877	-196,971	-163,459	-101,611	-246,708	-317,576	-390,931	-362,862	-337,855	-227,936	-580,255	-679,965
Budget Balance (At 1994 prices)	-128,610	-129,042	-108,410	-76,207	-150,480	-157,210	-188,640	-167,636	-154,473	-100,455	-216,397	-248,045
Budget Balance (Cur. price billion $)	-4.944	-4.981	-4.194	-2.901	-5.843	-6.258	-7.518	-6.712	-6.181	-3.930	-8.656	-9.932
Financing	192,408	223,400	218,657	191,901	206,431	294,256	366,866	441,175	515,170	585,070	588,084	673,880
Foreign Borrowing (Net)	-144,761	150,486	-107,768	-112,832	-121,211	-81,238	-86,323	-94,947	-95,925	-98,812	-38,098	-31,355
Domestic Borrowing (Net)	24,395	70,213	73,205	87,059	75,713	85,657	75,289	56,880	-40,547	-156,008	-158,830	-148,134
Short-Term Borrowing	341,619	297,282	263,261	244,023	257,303	291,941	496,952	539,246	710,267	911,702	857,213	886,142
Central Bank (Net)	28,219	11,168	48,376	40,771	43,757	94,723	108,734	126,169	164,281	117,481	84,453	84,942
Treasury Bills (Net)	313,400	286,114	214,885	203,252	213,547	197,218	388,218	413,077	545,986	794,221	772,760	801,218
Other	-28,845	6,391	-10,041	-26.349	-5,374	-2,105	-119,053	-60,005	-58,627	-71,815	-72,202	-32,773

TABLE 1.4 MAIN ECONOMIC INDICATORS (1995-1996)
MONEY SUPPLY

	1995						1996					
	July	August	Sept.	Oct.	Nov.	Dec.	Jan.	Feb.	March	April	May	June
(Annual percentage change)												
M1	85.7	87.7	81.4	73.8	76.0	65.7	76.3	90.8	79.9	85.5	64.4	62.7
Currency in circulation	95.2	83.2	81.5	78.7	89.5	81.6	81.7	88.5	71.6	115.3	50.6	55.7
Currency+coins	91.1	81.4	78.0	79.5	87.6	86.6	81.7	95.1	74.7	107.9	58.1	57.0
Cash in vault (-)	59.9	66.1	55.8	88.6	69.8	117.7	82.5	154.2	92.9	59.4	133.9	64.9
Commercial sight deposits	70.3	98.5	81.2	57.1	44.9	54.4	68.6	97.8	89.5	54.7	86.3	74.5
Saving sight deposits	96.2	88.8	84.1	88.2	88.8	56.4	88.0	81.6	89.1	70.0	62.6	74.5
Other sight deposits	54.8	76.4	72.3	87.9	93.5	46.3	49.0	103.0	84.8	33.2	109.4	42.7
Central Bank deposits	-15.4	-39.8	378.4	-89.4	-80.7	-72.4	-82.8	-62.3	-66.3	-23.5	-54.3	844.7
M2	87.4	100.8	100.1	97.4	101.9	97.7	103.9	100.5	87.5	91.7	86.7	86.3
Commercial time deposits	97.4	141.6	141.5	148.4	189.5	197.3	187.4	126.3	105.0	126.3	150.2	127.4
Saving time deposits	88.6	108.5	111.1	112.3	114.9	117.8	123.6	114.2	96.4	94.8	95.5	95.7
Other time deposits	87.9	99	103.9	98.6	99.8	91.4	76.6	70.8	68.3	89.4	92.7	101.1
Certificates of deposits	36.4	56.4	55.8	80.0	70.5	49.6	47.5	35.6	21.0	16.4	20.0	10.0
M2Y	91.8	94.4	92.0	86.1	93.7	106.5	97.4	96.2	96.2	100.7	102.2	104.9
Foreign exchange deposits (TL)	97.7	86.7	83.0	75.0	85.5	115.5	91.3	91.7	105.3	110.9	120.9	128.4
Foreign exchange deposits ($)	36.6	26.8	28.0	24.5	27.2	35.6	25.6	23.1	21.9	20.3	22.5	23.4
TL/USD Buying Rate	44.7	47.3	43.0	40.6	45.8	58.9	52.2	55.8	68.5	75.3	80.4	85.1
M3Y	92.1	95.1	93.0	88.1	93.3	106.8	102.2	97.3	97.2	101.2	101.2	105.0
M3	88.2	101.7	101.5	100.5	100.6	98.6	113.1	102.3	90.0	93.2	86.1	87.6
Foreign exchange deposits (TL)	97.7	86.7	83.0	75.0	85.5	115.5	91.3	91.7	105.3	110.9	120.9	128.4
Credit Stock	78.8	88.8	95.3	92.6	96.5	119.4	108.1	118.2	128.7	117.0	97.7	119.6
Central Bank Direct Credits	-12.4	-5.1	1.9	-2.6	-13.7	30.9	30.4	64.6	72.8	31.8	27.7	33.4
Deposits Bank Credits	109.0*	117.9	126.5	125.3	136.1	149.9	132.1	135.5	146.1	142.7	132.2	132.3
Invest. and Develop. Bank Credits	49.1	47.1	51.7	49.9	57.4	62.4	66.5	75.6	81.7	87.1	96.8	105.4

* *Adjusted for changes in data definition between 1.7.1994-1.7.1995*

TABLE 2 GROSS DOMESTIC PRODUCT (EXPENDITURE BASED)

(At 1987 Prices)	Growth Rate			% Share			Annual Growth Rate (%)					
	1993	1994	1995	1993	1994	1995	1995-1	1995-2	1995-3	1995-4	1996-1	1996-2
Private Final Consumption Expenditure	8.4	-5.3	7.6	69.5	69.0	69.0	-4.6	12.2	13.0	8.4	..	..
Food-Beverages	3.3	-0.7	7.4	25.6	26.7	26.6	-0.5	10.4	10.6	7.1	..	..
Durable Goods	23.2	-29.3	20.0	10.1	7.5	8.4	-18.9	39.8	50.8	30.6	..	..
Semi-Durable&Non-Durable Goods	7.0	-12.6	11.6	11.6	10.6	11.0	-11.0	18.5	25.6	16.8	..	..
Energy-Transportation-Communication	14.7	4.2	1.7	9.9	10.9	10.3	0.9	5.6	2.7	-1.9	..	..
Services	8.6	5.2	2.7	6.5	7.1	6.8	2.9	7.6	3.9	-3.3	..	..
Ownership of Dwelling	2.6	2.8	2.1	5.7	6.2	5.9	2.2	2.0	2.0	2.2	..	..
Government Final Consumption Expenditure	5.4	-3.5	6.7	7.6	7.7	7.6	7.1	9.6	2.3	7.8	..	..
Compensation of Employees	1.8	0.8	2.5	4.6	4.8	4.6	2.7	2.9	2.7	1.8	..	..
Purchases of Goods&Services	11.4	-10.0	13.7	3.0	2.8	3.0	22.2	25.5	1.5	13.7	..	..
Gross Fixed Capital Formation	24.9	-15.9	8.3	30.1	26.5	26.7	-15.1	14.2	11.1	22.1	..	..
Public Sector	3.5	-34.8	-16.9	8.0	5.5	4.2	-37.5	-1.4	-15.2	-17.3	..	..
Machinery&Equipment	3.7	-63.9	3.2	3.1	1.2	1.1	-21.8	4.7	3.5	17.4	..	..
Building Construction	11.4	-35.7	4.2	1.5	1.0	1.0	-7.7	34.6	1.6	-2.2	..	..
Other Construction	0.1	-8.2	-30.5	3.4	3.3	2.1	-53.8	-12.8	-26.1	-34.1	..	..
Private Sector	35.0	-9.1	14.9	22.1	21.1	22.5	-11.4	17.4	18.1	38.8	..	..
Machinery&Equipment	60.5	-22.5	28.1	12.2	9.9	11.9	-23.8	33.3	45.1	73.8	..	..
Building Construction	12.8	7.6	3.0	9.8	11.1	10.6	4.5	4.1	3.4	-0.6	..	..
Change in Stocks	-	-	-	1.6	-3.2	1.4	-	-	-	-	..	..
Exports of Goods & Services	7.7	15.2	6.7	18.4	22.2	22.1	19.9	12.2	2.3	-1.8	..	..
Imports of Goods & Services	35.8	-21.9	30.0	-27.1	-22.2	-26.8	-2.6	37.7	41.4	48.0	..	..
Gross Domestic Product (Expenditure based)	7.7	-4.7	7.5	100.0	100.0	100.0	-0.8	14.3	9.0	7.0	..	..
Statistical Discrepancy	-	-	-	1.6	0.8	0.6	-	-	-	-	..	..
Gross Domestic Product (Production based)	8.0	-5.5	7.3	-	-	-	-1.5	13.5	9.6	6.4	..	..

(..): Not available

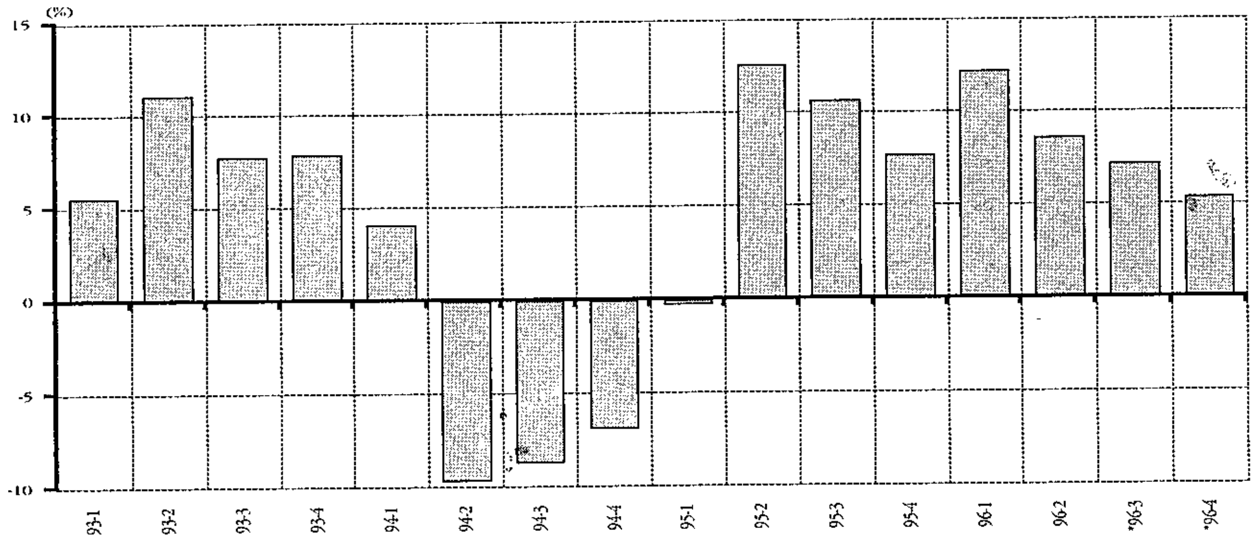
TABLE 3 TÜSİAD ESTIMATES

	94-1	94-2	94-3	94-4	94	95-1	95-2	95-3	95-4	95	96-1	96-2	96-3	96-4	96
	Realization					Realization					Estimate				
(25 Jan. 1996)															
Growth Rate	4.1	-9.7	-8.7	-6.9	-6.1	-0.3	12.6	10.7	7.7	8.1	3.1	1.4	3.9	4.4	3.3
Inflation	67.8	133.9	128.3	141.3	120.7	149.9	82.0	79.8	70.3	88.5	**64.4	74.5	78.6	80.2	75.1
(25 July 1996)															
Growth Rate	4.1	-9.7	-8.7	-6.9	-6.1	-0.3	12.6	10.7	7.7	8.1	**12.2	**8.6	7.2	5.4	8.0
Inflation	67.8	133.9	128.3	141.3	120.7	149.9	82.0	79.8	70.3	88.5	**64.4	**73.3	81.8	97.4	80.5

*** Realization*

GNP GROWTH RATE

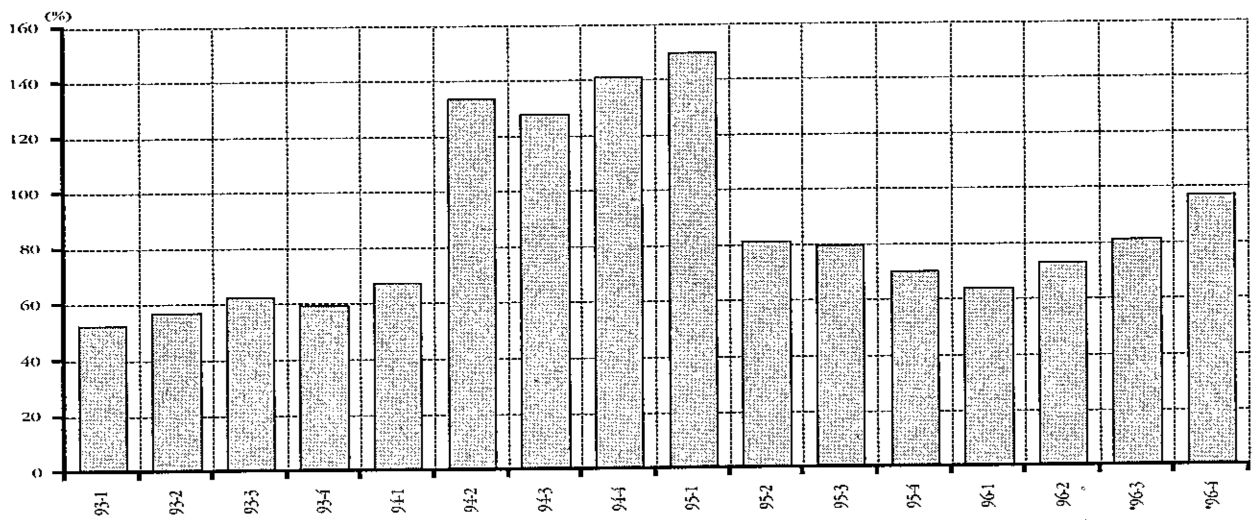
GRAPH 1



** Estimate*

WHOLESALE PRICE INDEX
(Average Annual Percentage Change)

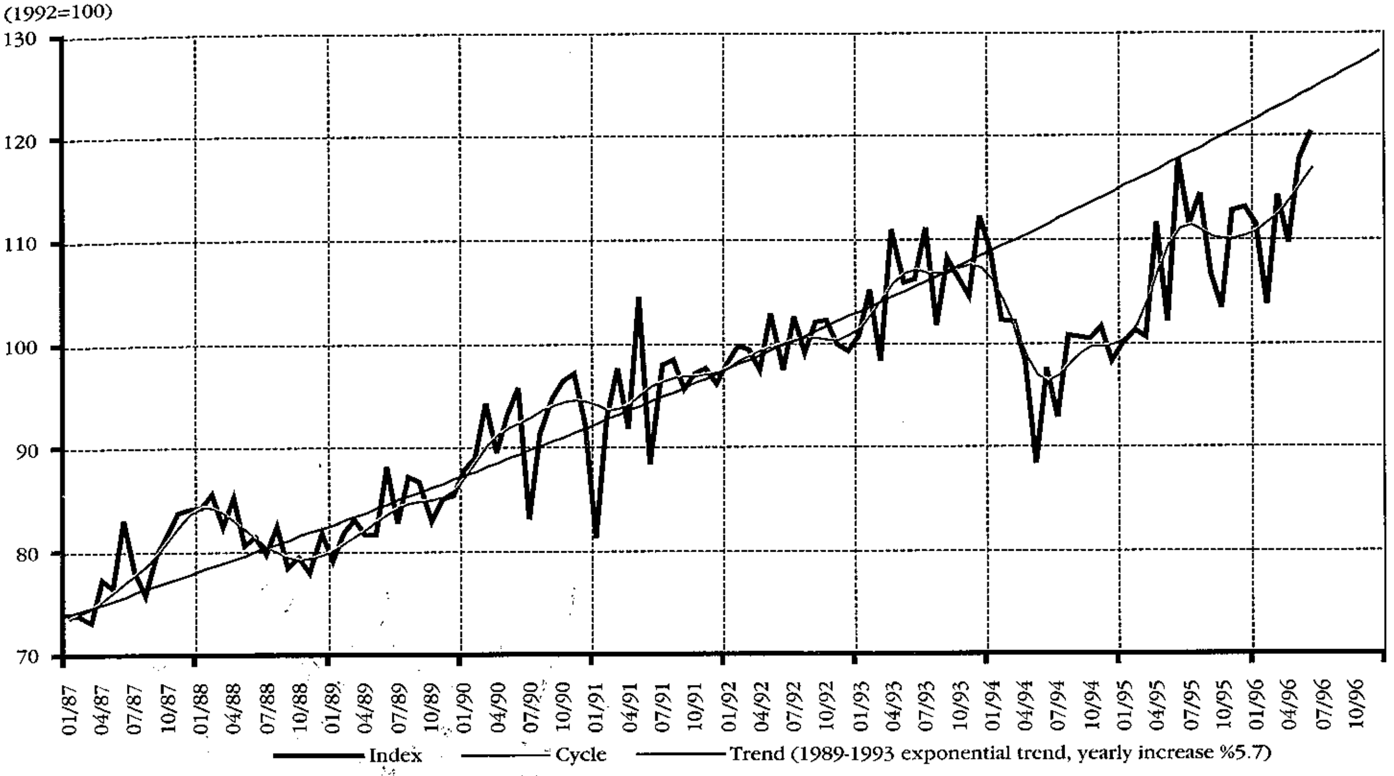
GRAPH 2



** Estimate*

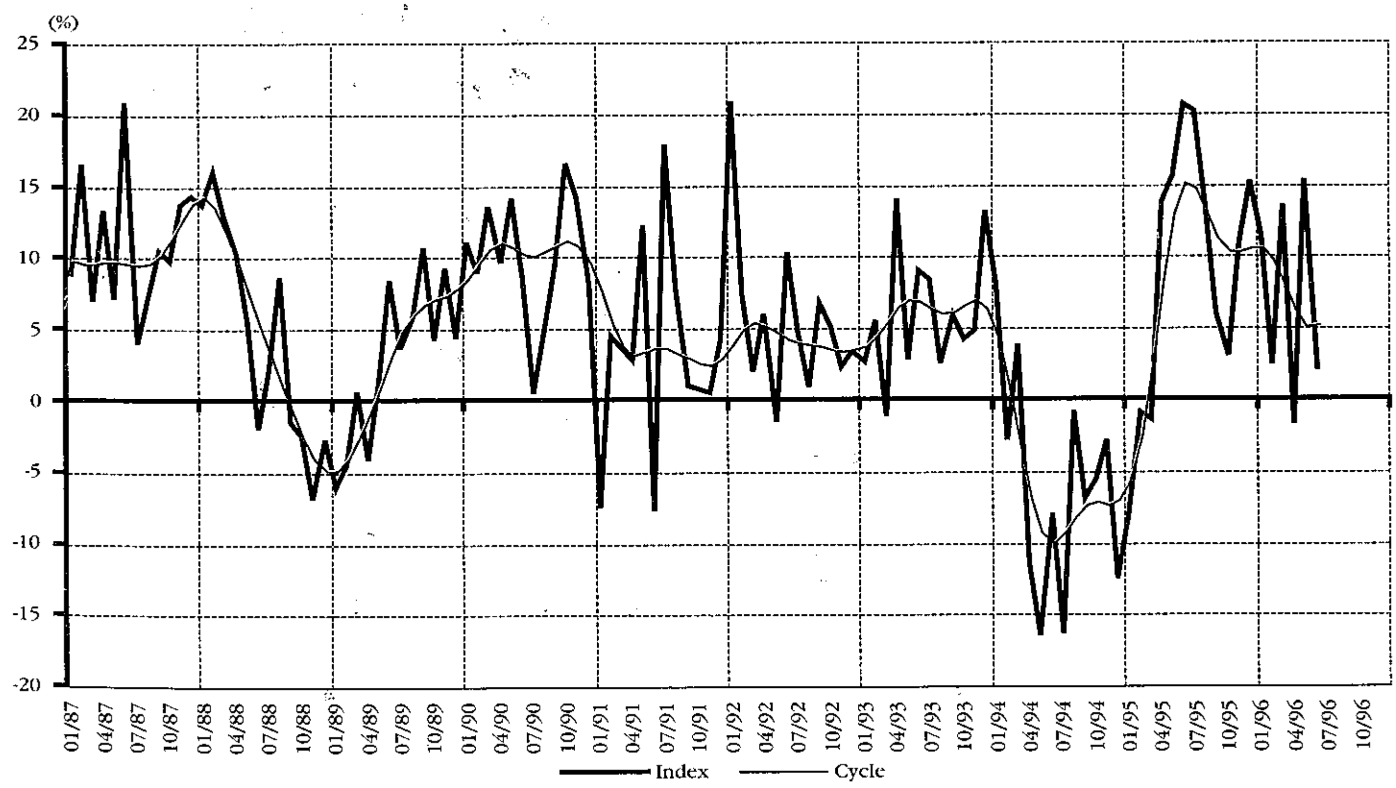
SEASONALLY ADJUSTED INDUSTRIAL PRODUCTION INDEX (Level)

GRAPH 3

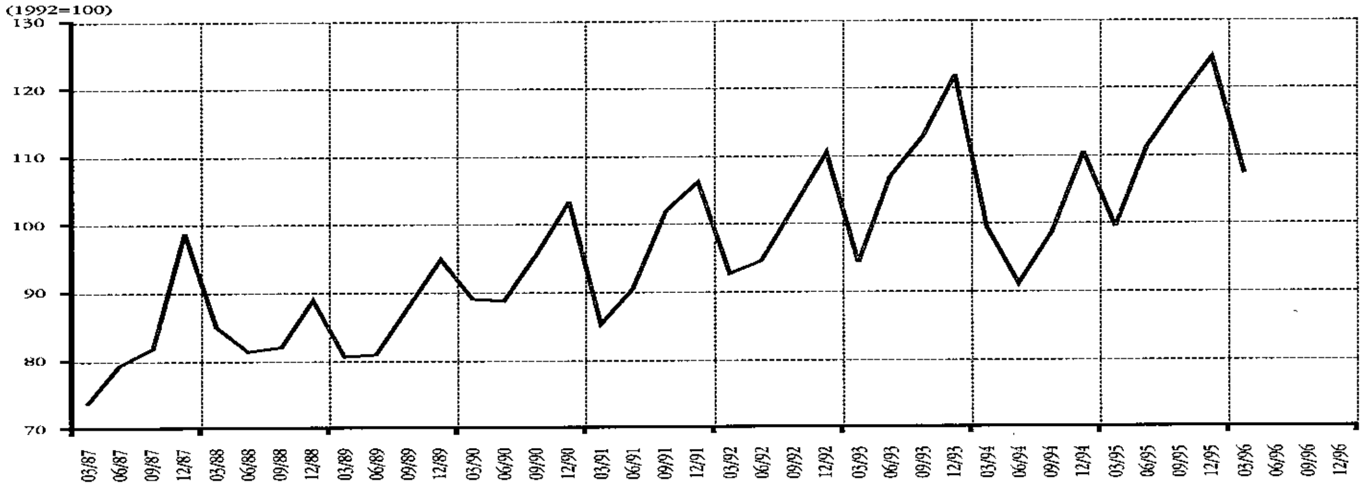


SEASONALLY ADJUSTED INDUSTRIAL PRODUCTION INDEX (Annual Percentage Increase)

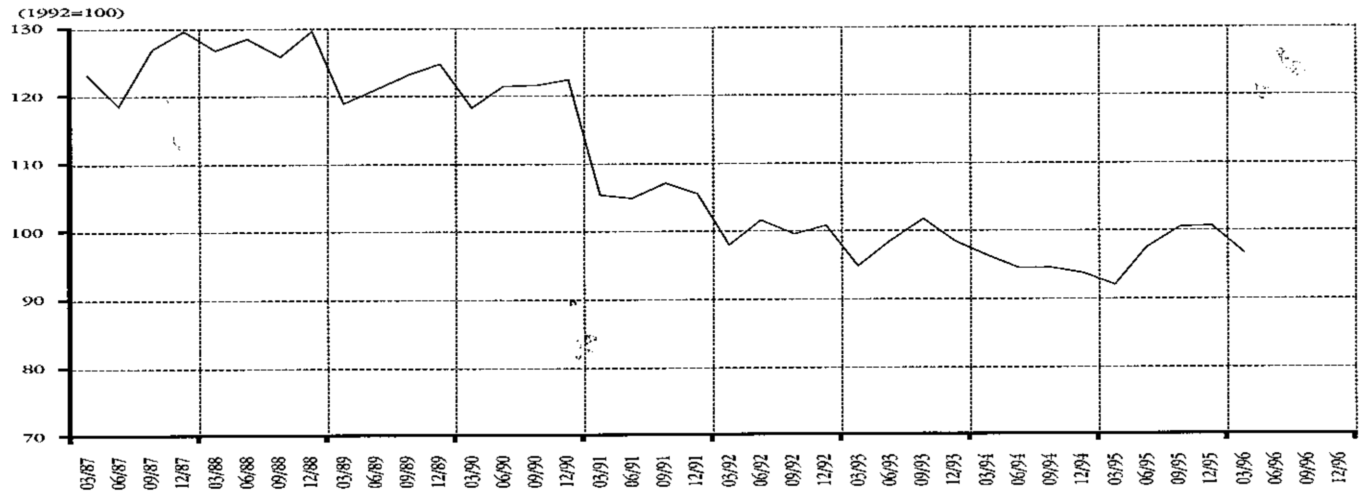
GRAPH 4



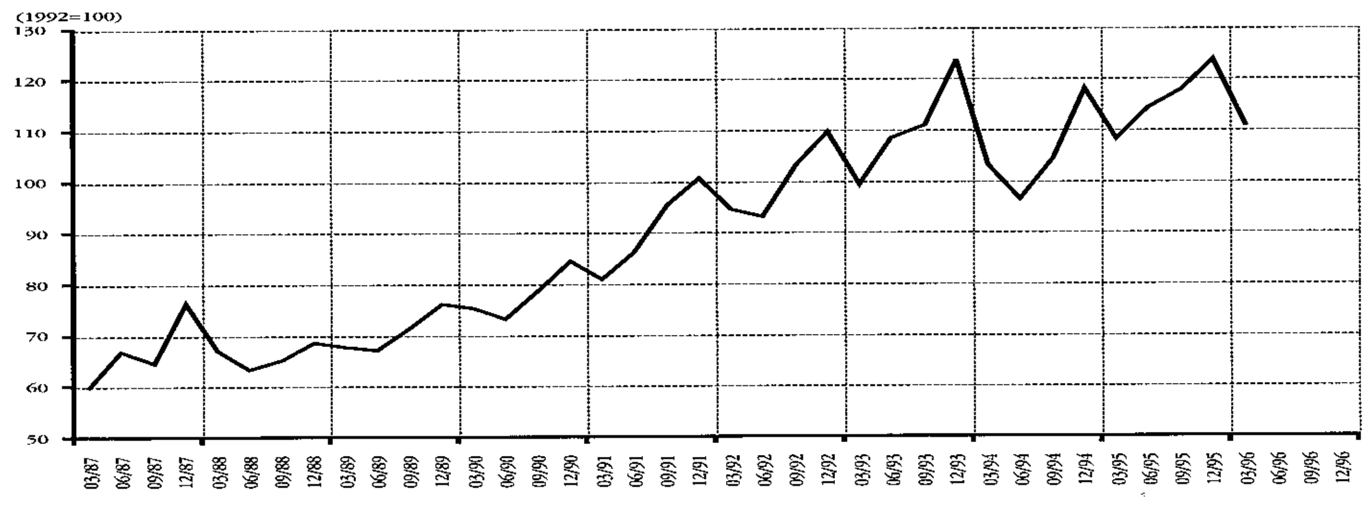
MANUFACTURING INDUSTRY QUARTERLY PRODUCTION INDEX GRAPH 5



PRODUCTION WORKERS IN MANUFACTURING INDUSTRY INDEX GRAPH 6

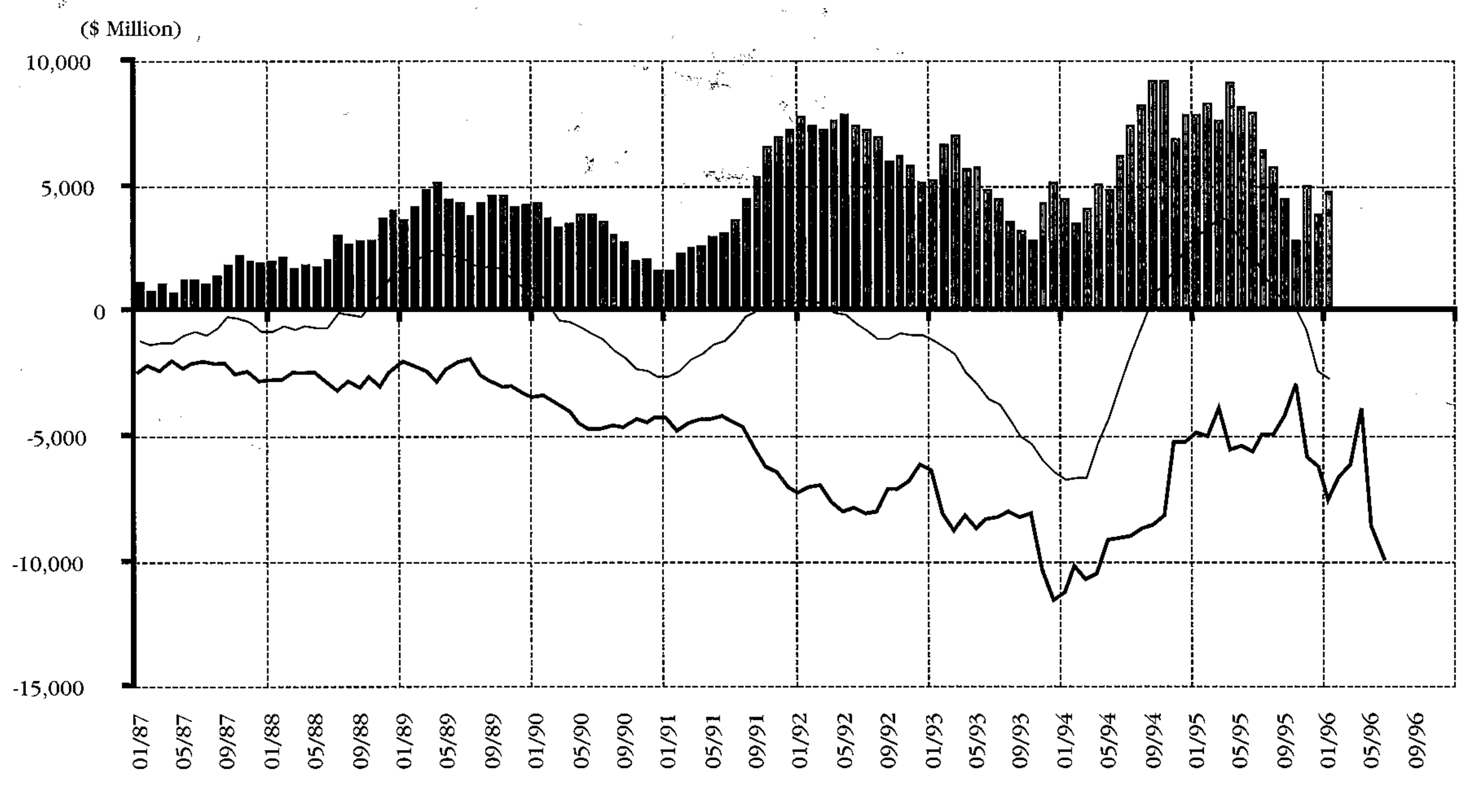


MANUFACTURING INDUSTRY PRODUCTIVITY INDEX GRAPH 7



GRAPH 8

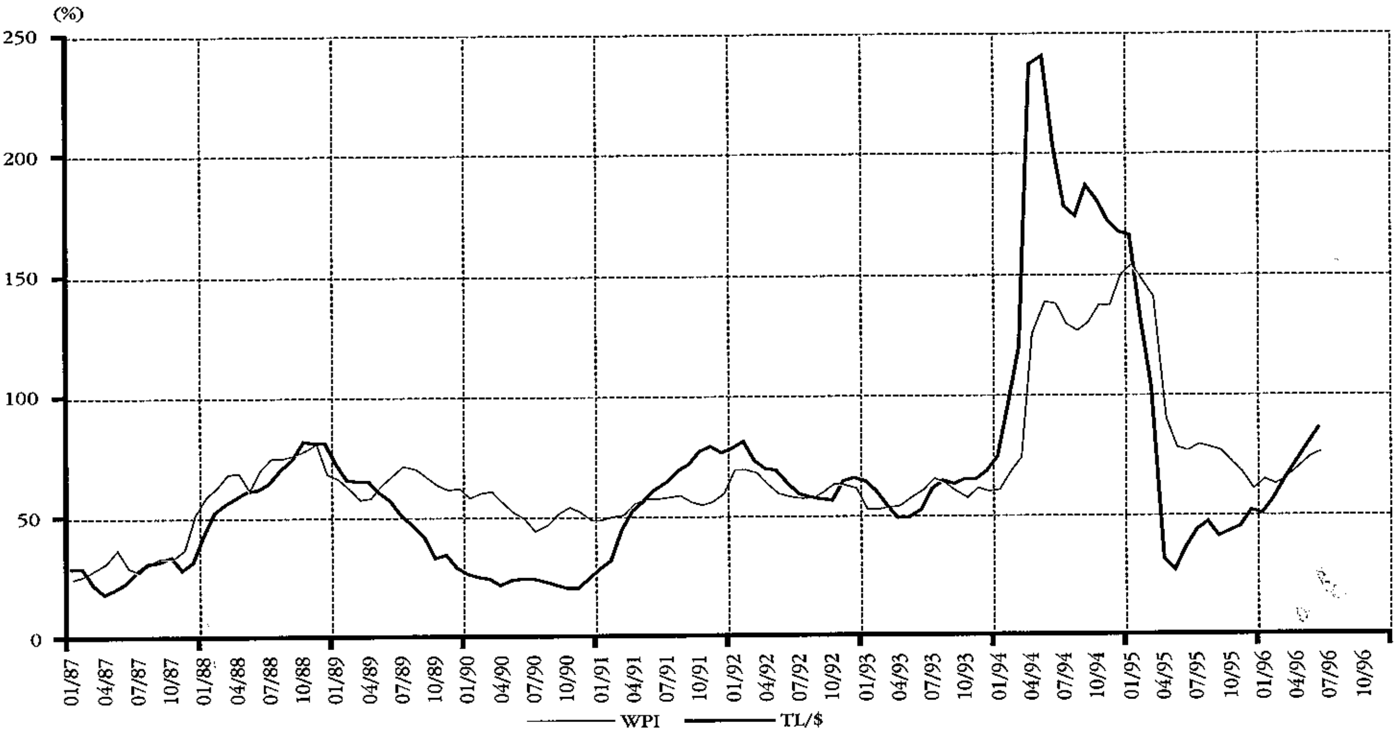
SAVING - INVESMENT BALANCE (*)
(Cumulative for the last 12 months)



(*) Consolidated budget balance is used as a proxy for the public sector saving gap due to lack of monthly data on the latter. Private sector saving surplus figures are calculated as the sum of budget deficit and current account balance.

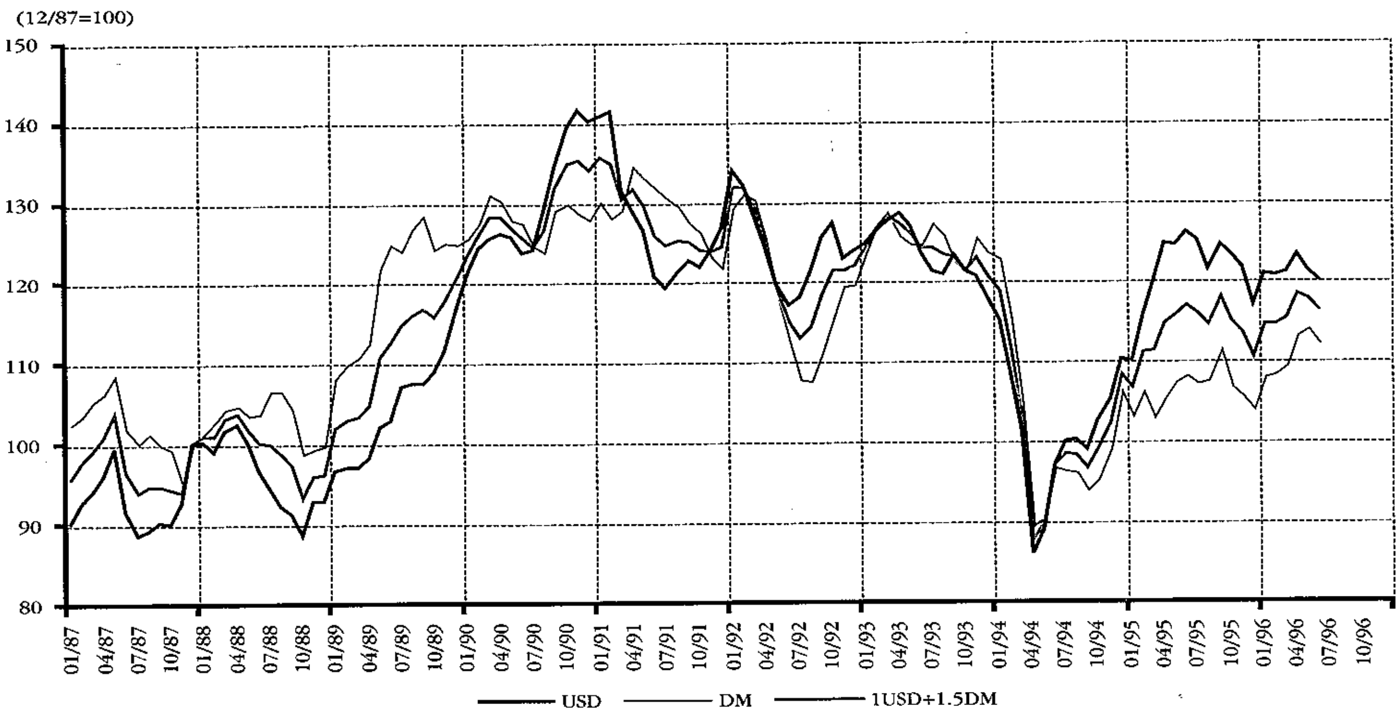
WHOLESALE PRICE INDEX AND MONTHLY AVERAGE US DOLLAR EXCHANGE RATE (Annual Percentage Change)

GRAPH 9



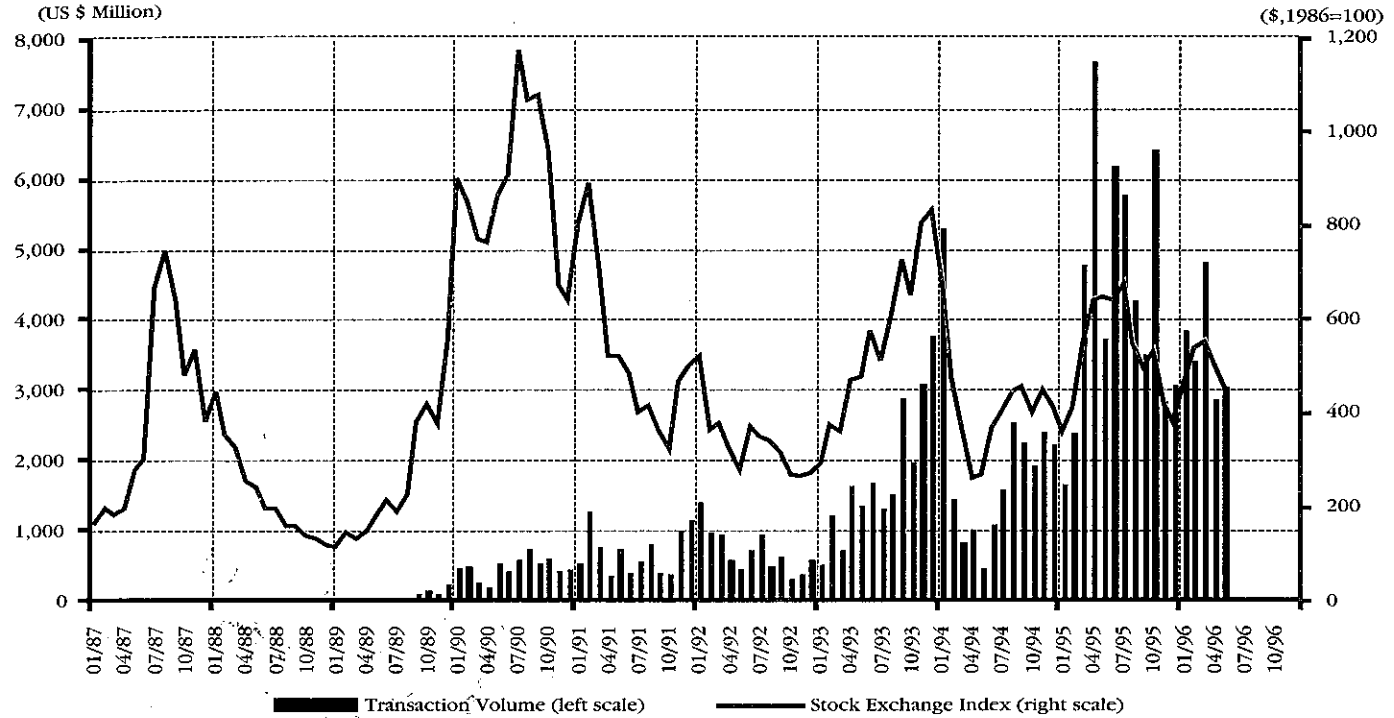
REAL EXCHANGE RATE INDEX

GRAPH 10



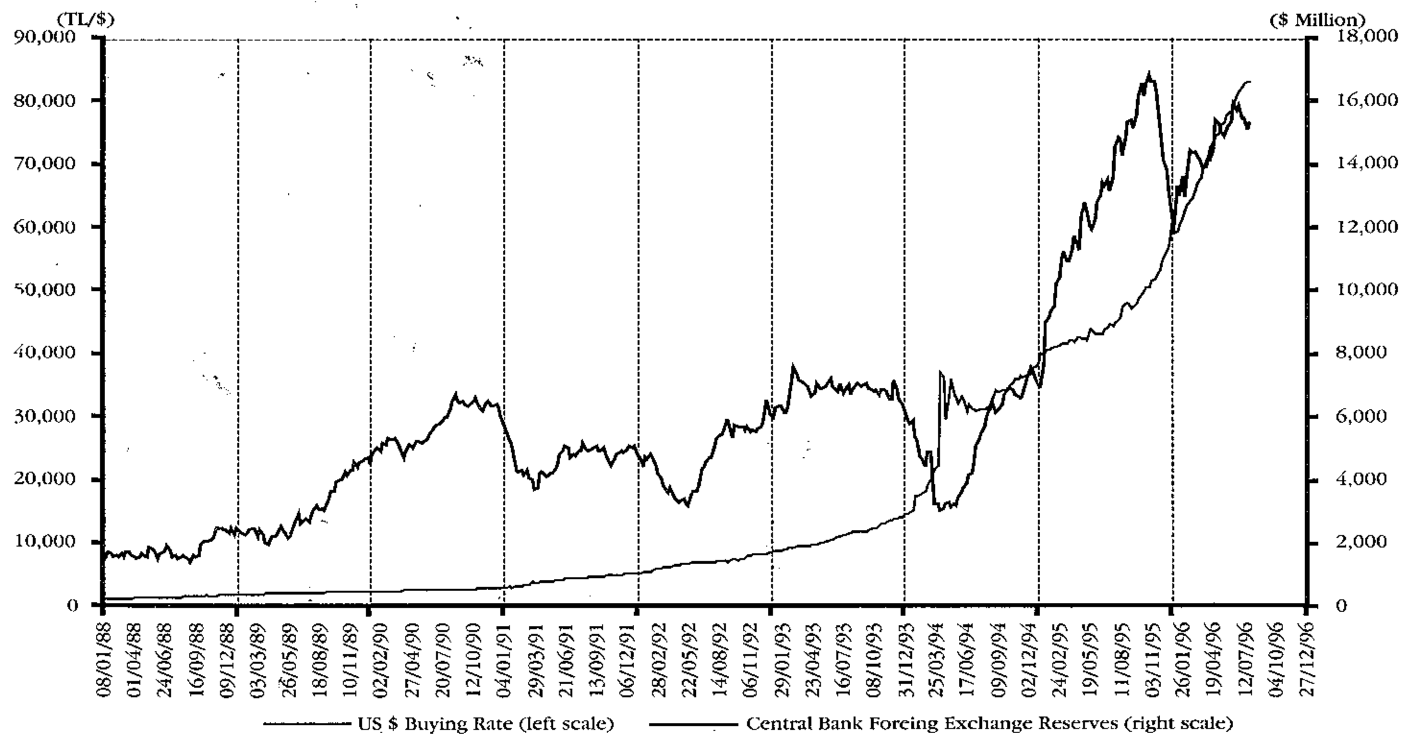
STOCK EXCHANGE INDEX AND TRANSACTION VOLUME

GRAPH 11



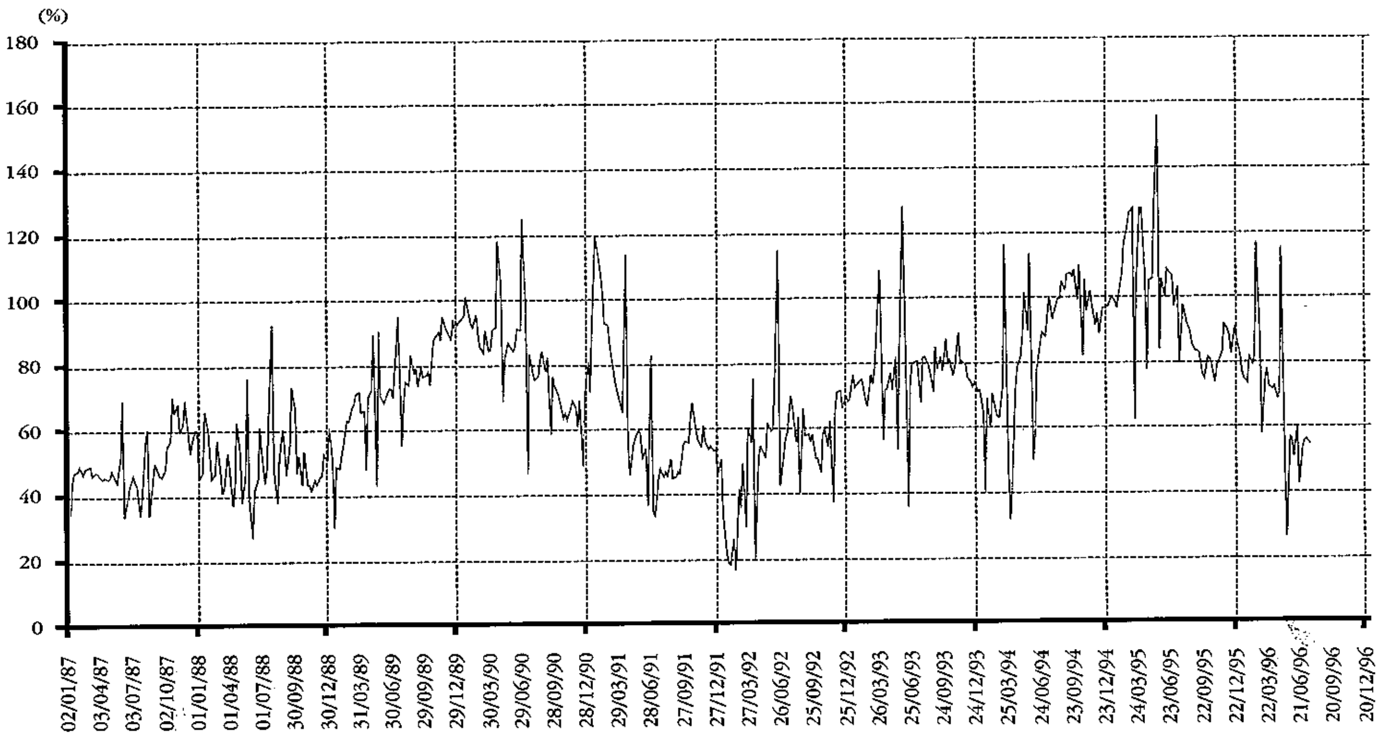
CENTRAL BANK FOREIGN EXCHANGE RESERVES & US DOLLAR NOMINAL EXCHANGE RATE

GRAPH 12



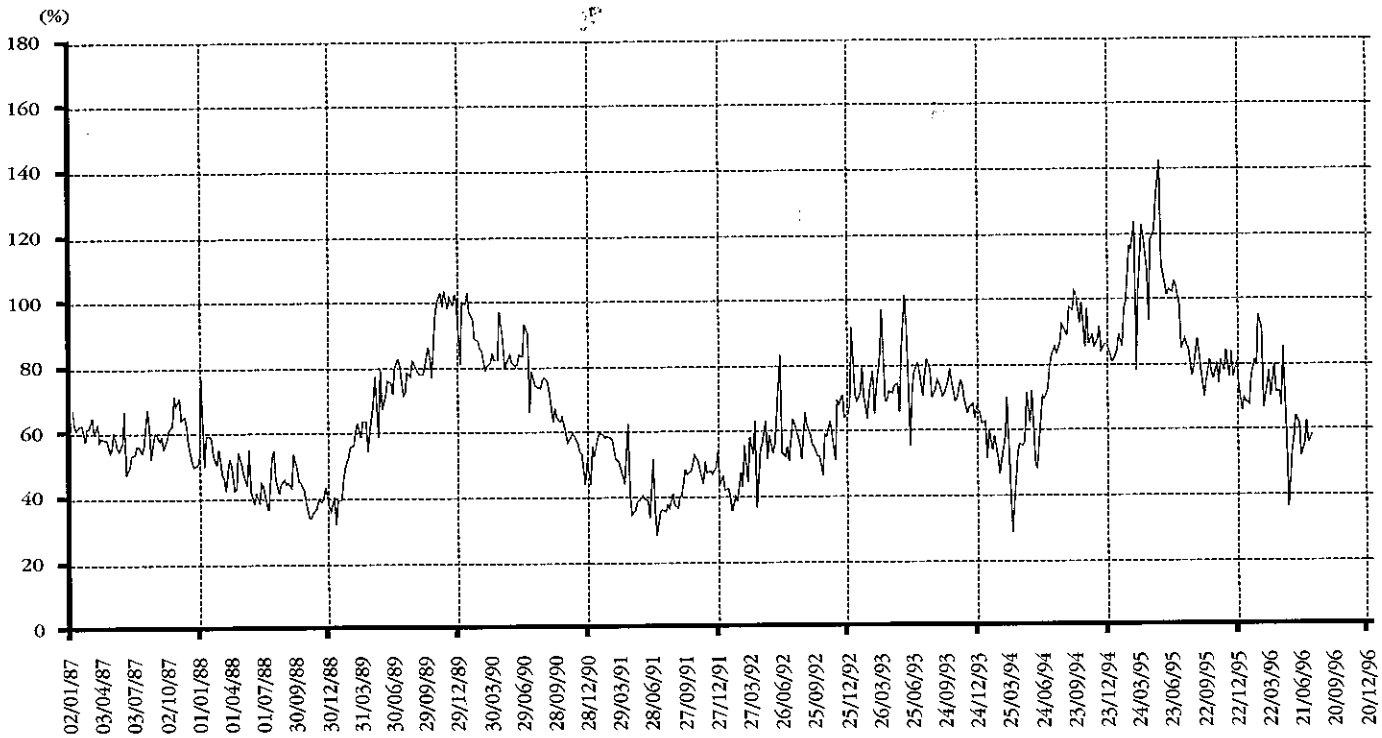
CURRENCY IN CIRCULATION (Annual Percentage Increase)

GRAPH 13



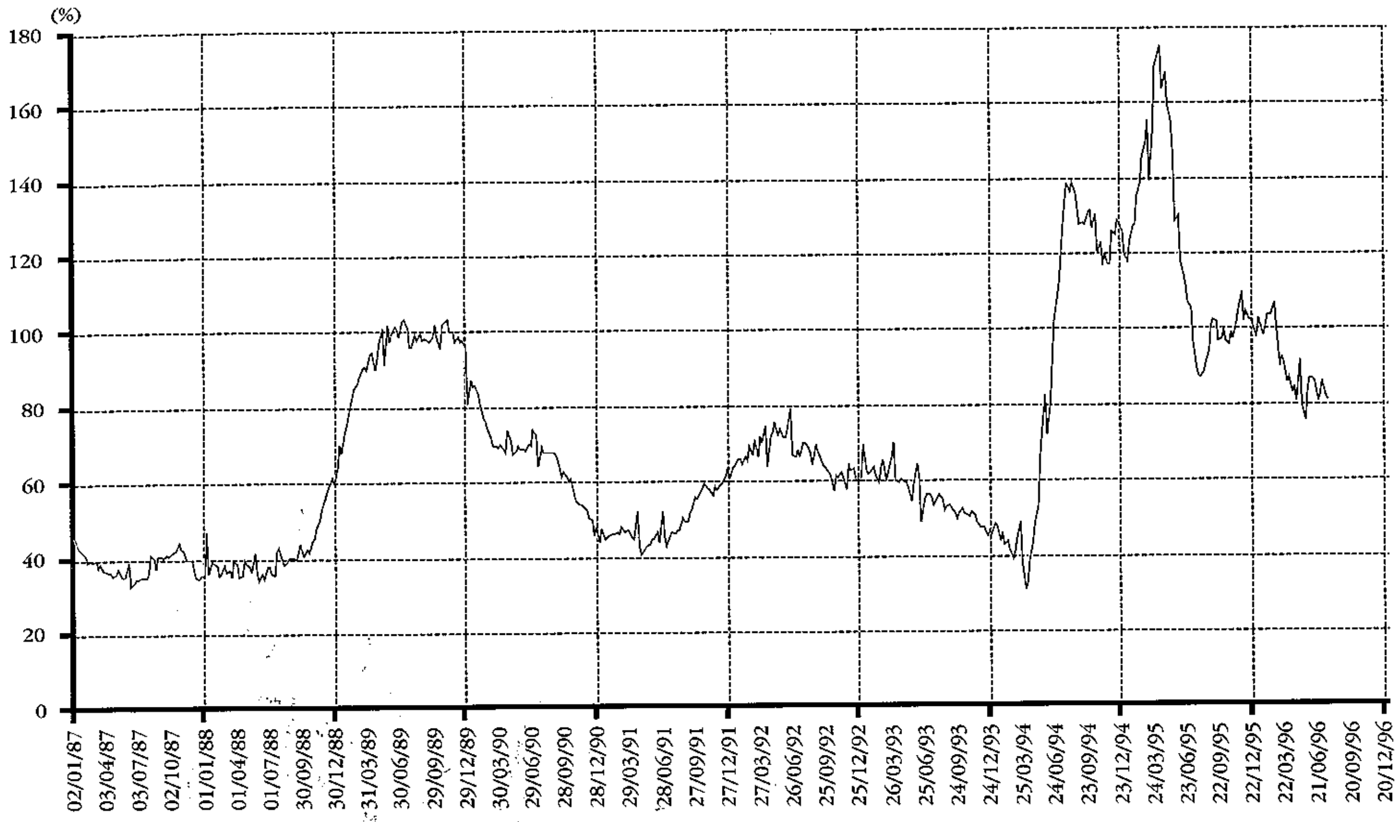
M1 (Annual Percentage Increase)

GRAPH 14



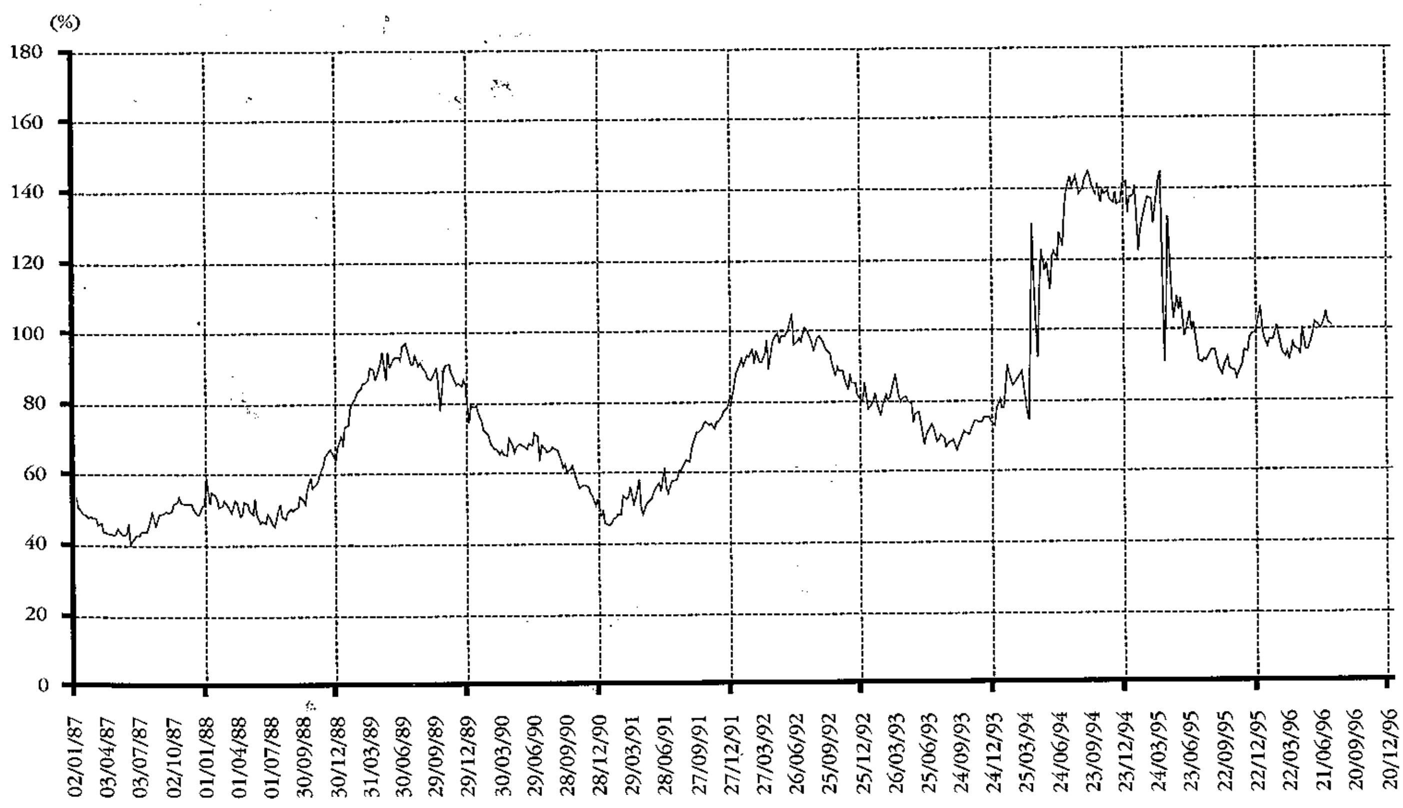
M2 (Annual Percentage Increase)

GRAPH 15



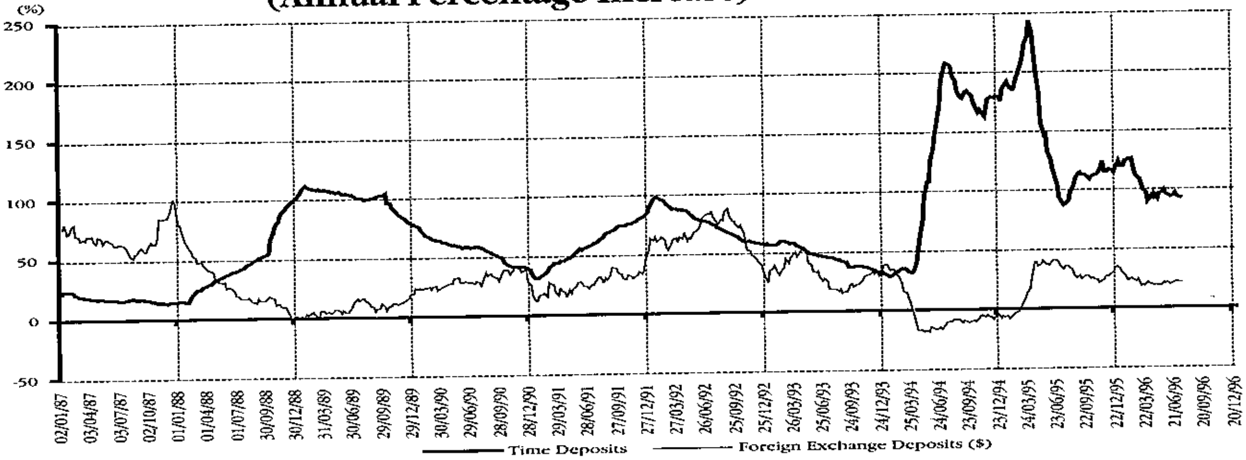
M2Y (Annual Percentage Increase)

GRAPH 16



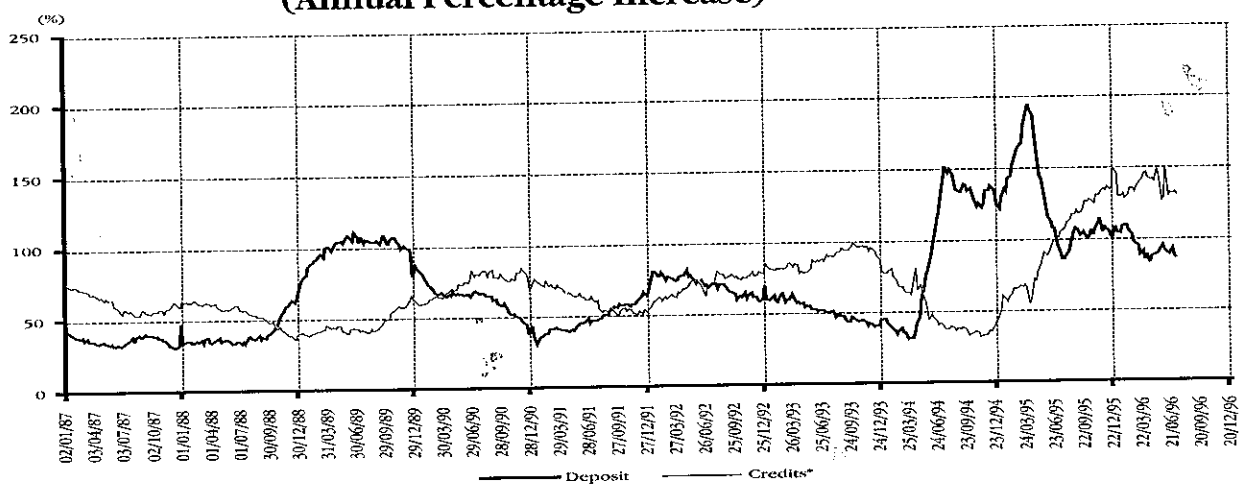
TIME DEPOSITS & FOREIGN EXCHANGE DEPOSITS (Annual Percentage Increase)

GRAPH 17



DEPOSIT BANK CREDITS* & DEPOSITS (Annual Percentage Increase)

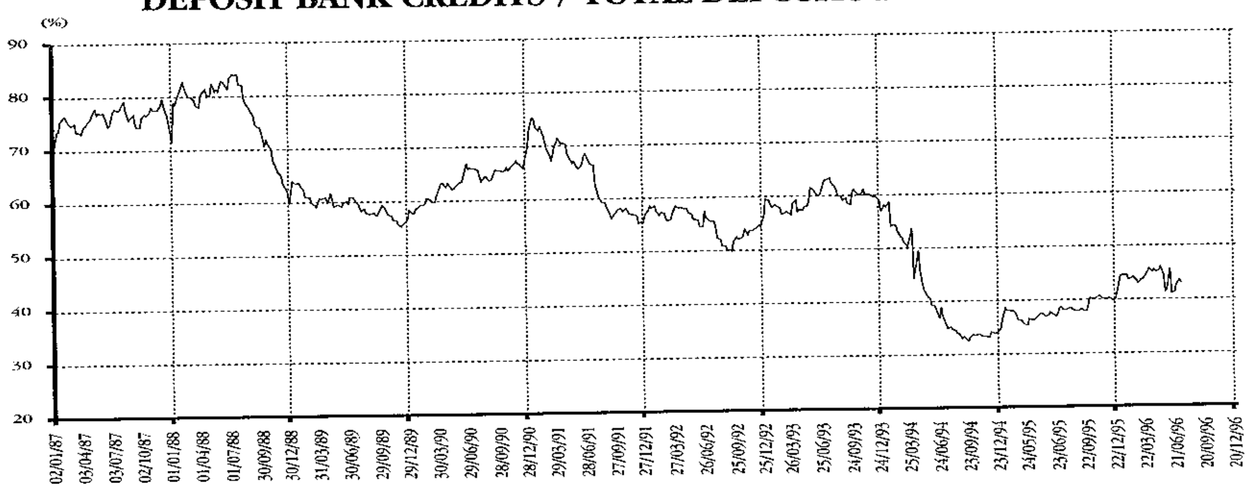
GRAPH 18



* *Adjusted for changes in data definition between 1.7.1994 - 1.7.1995*

DEPOSIT BANK CREDITS*/ TOTAL DEPOSITS RATIO

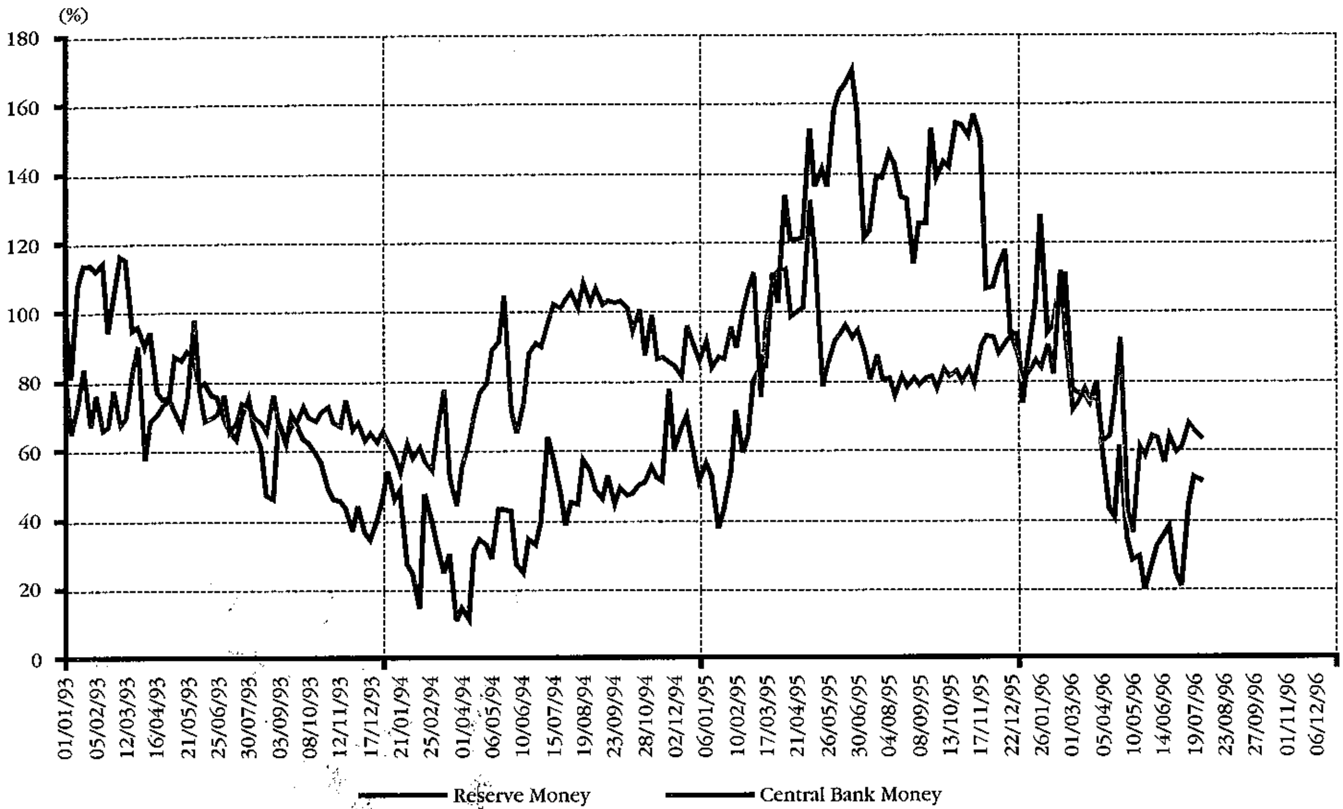
GRAPH 19



* *Adjusted for changes in data definition. Total deposits include Foreign Exchange Deposits in M2Y.*

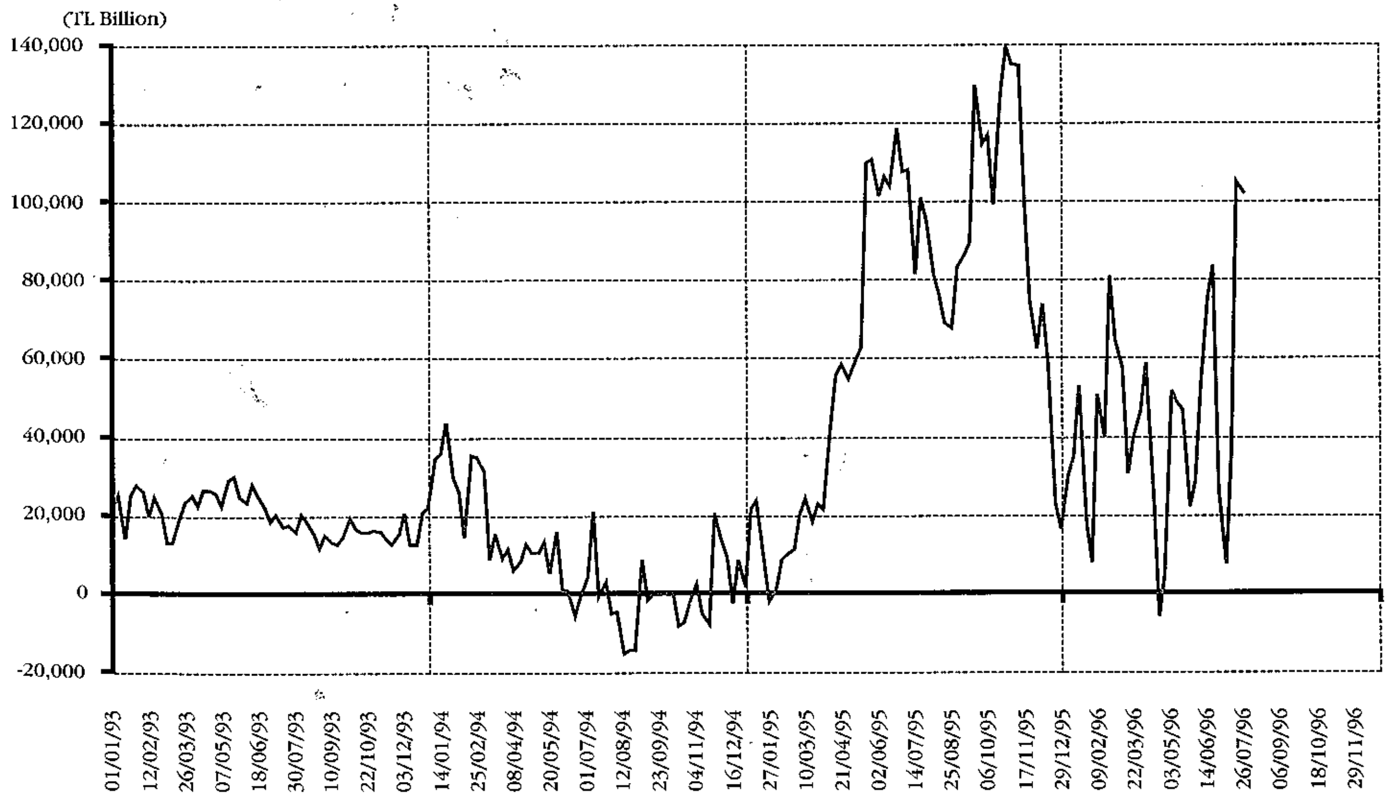
CENTRAL BANK MONEY AND RESERVE MONEY
(Annual Percentage Increase)

GRAPH 20



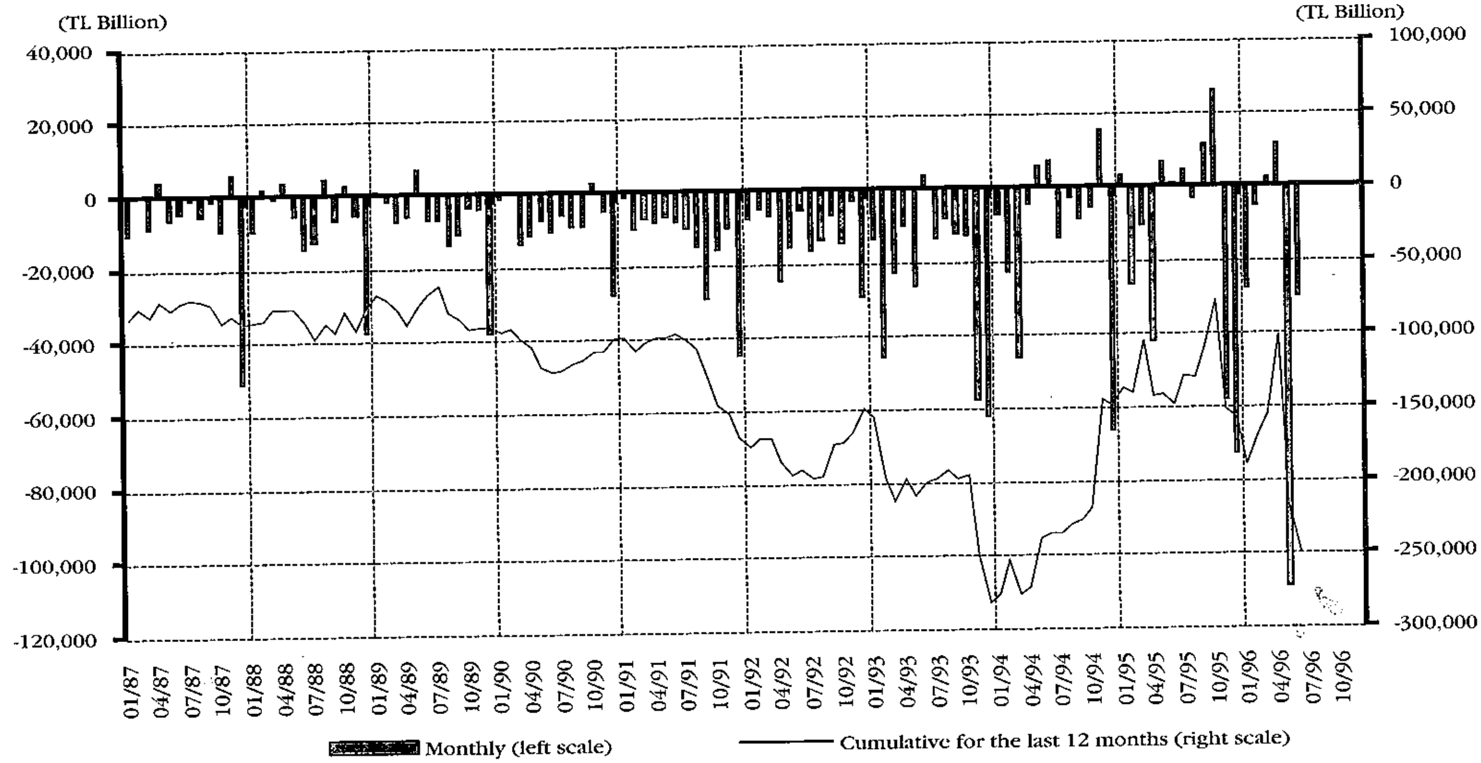
LIABILITIES DUE TO OPEN MARKET OPERATIONS

GRAPH 21



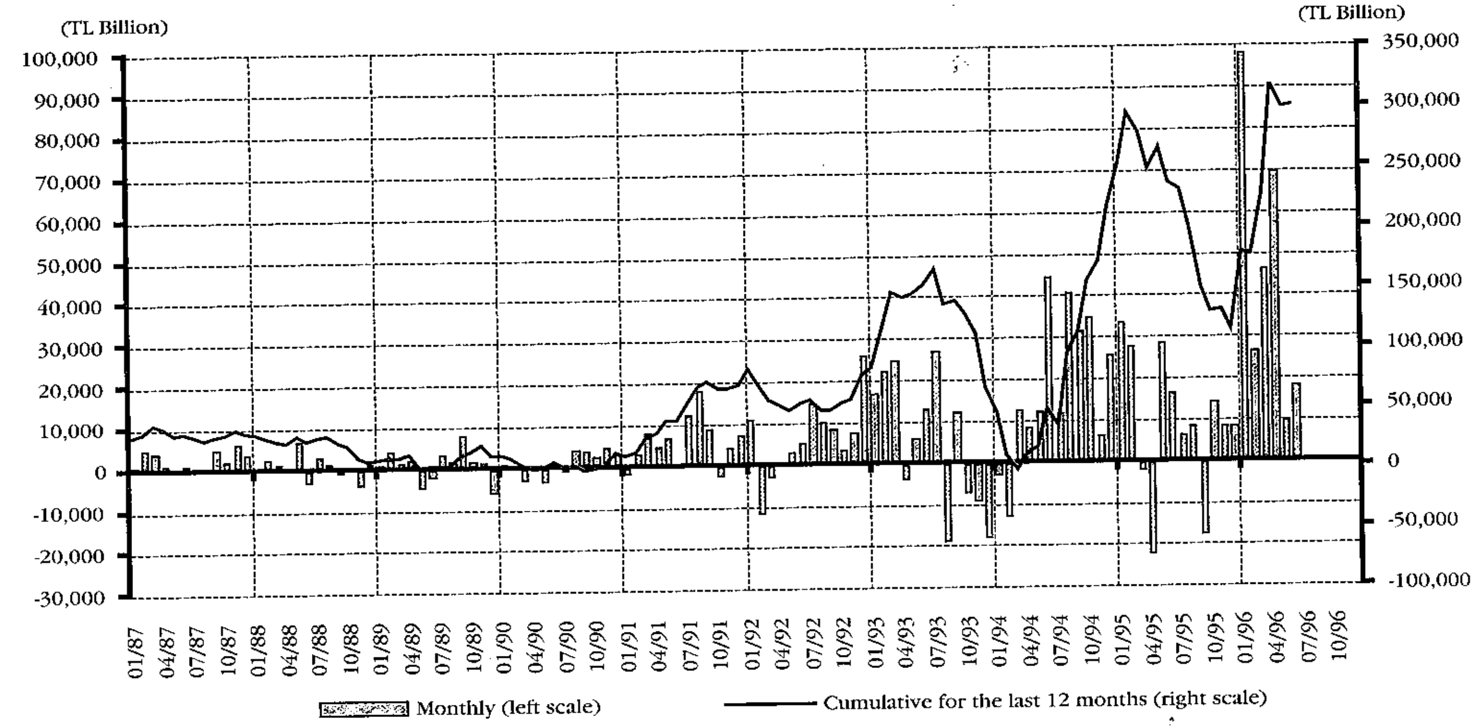
GRAPH 22

CONSOLIDATED BUDGET DEFICIT (At 1994 Prices)



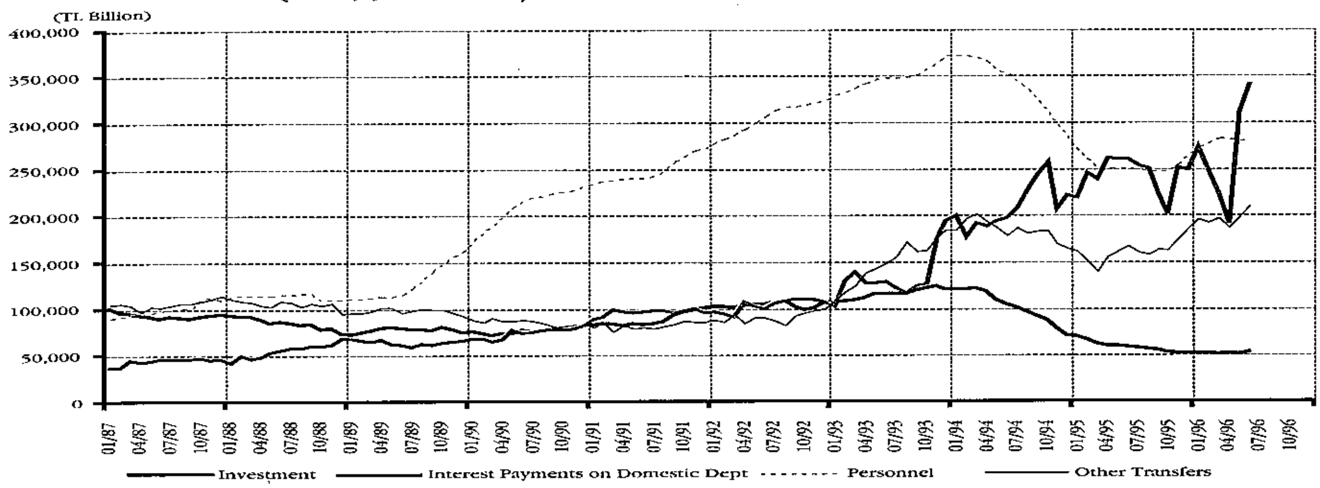
GRAPH 23

BORROWING BY TREASURY BILLS (NET) (At 1994 Prices)



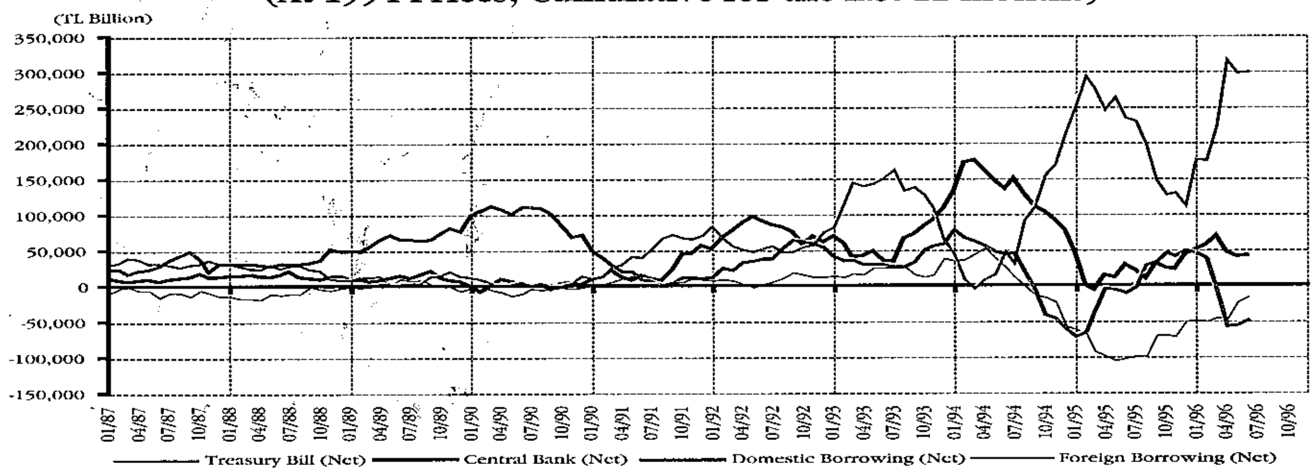
CONSOLIDATED BUDGET EXPENDITURES (At 1994 Prices, Cumulative for the last 12 months)

GRAPH 24



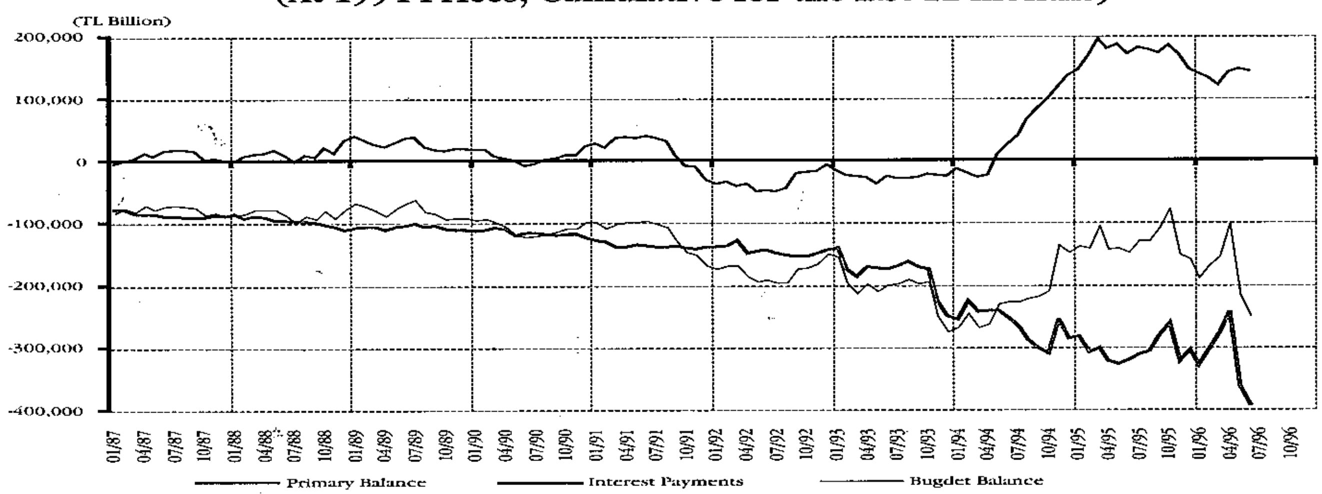
CONSALIDATED BUDGET FINANCING (At 1994 Prices, Cumulative for the last 12 months)

GRAPH 25



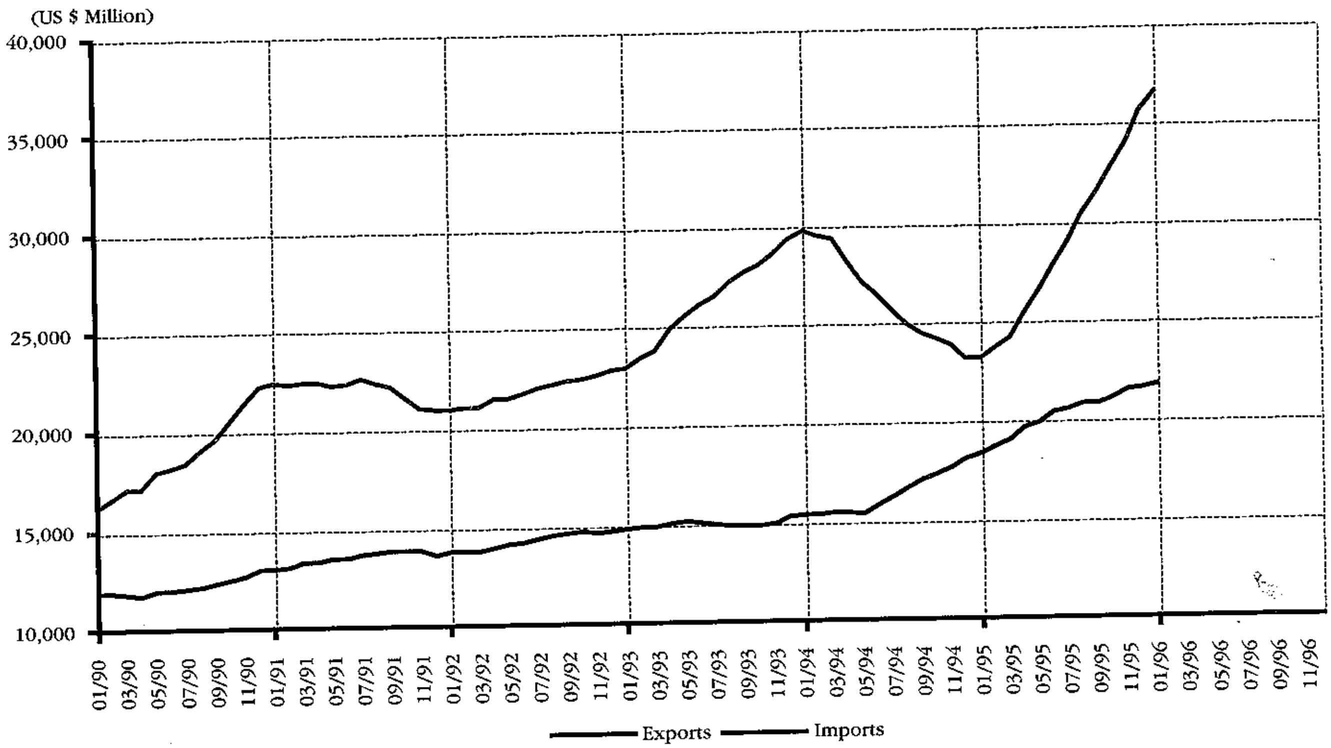
CONSOLIDATED BUDGET DEFICIT (At 1994 Prices, Cumulative for the last 12 months)

GRAPH 26



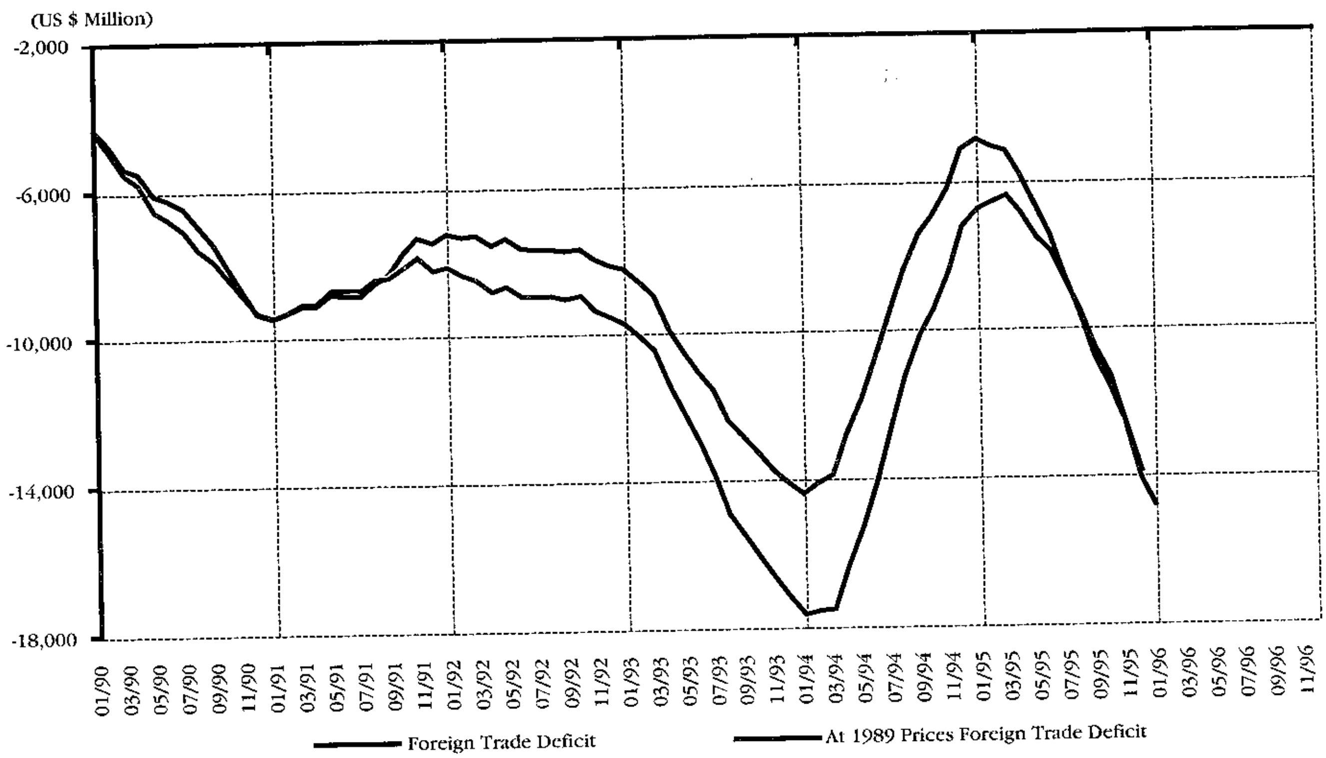
GRAPH 27

NOMINAL EXPORTS AND IMPORTS
(Cumulative for the last 12 months)



GRAPH 28

FOREIGN TRADE DEFICIT
(Cumulative for the last 12 months)

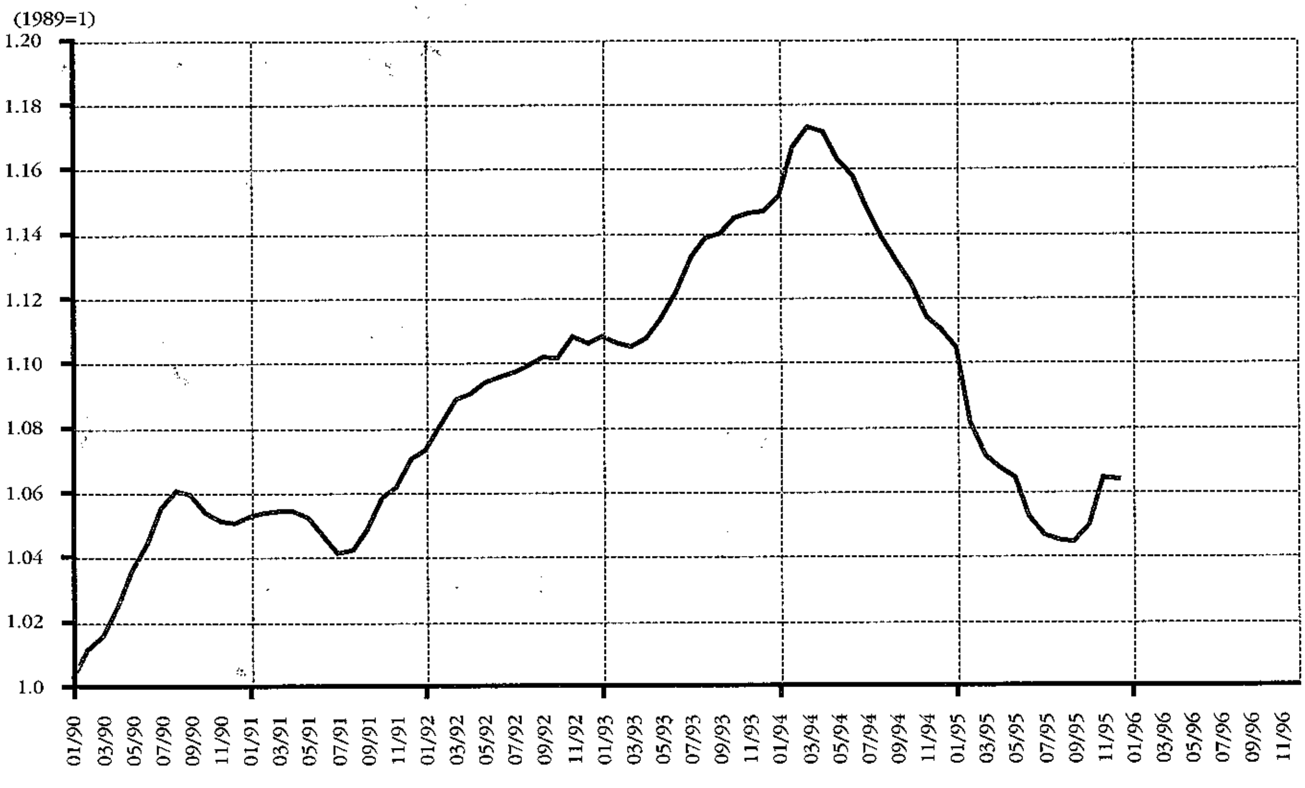


FOREIGN TRADE PRICE INDEX (Cumulative for the last 12 months)

GRAPH 29

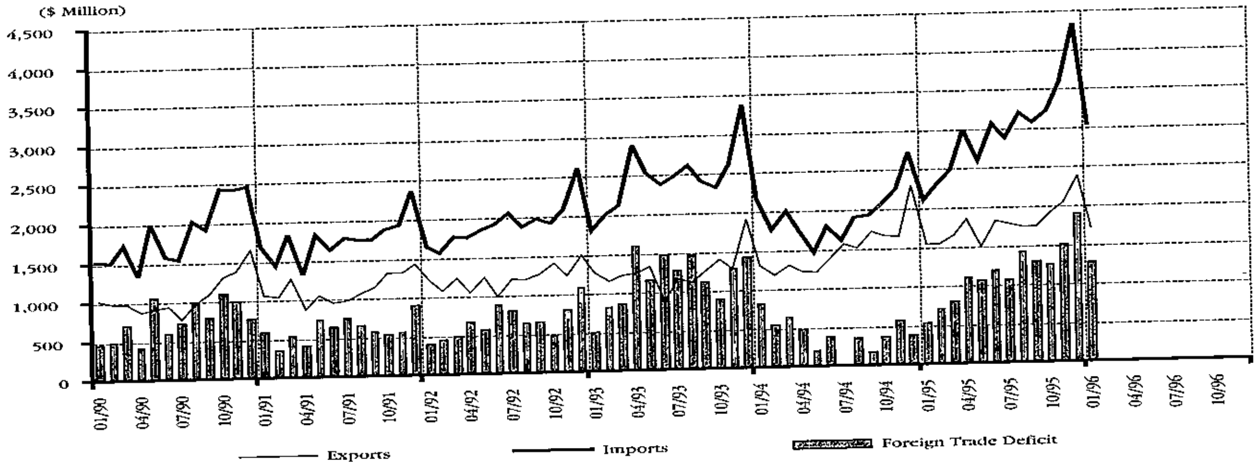
TERMS OF TRADE (Annual Average)

GRAPH 30



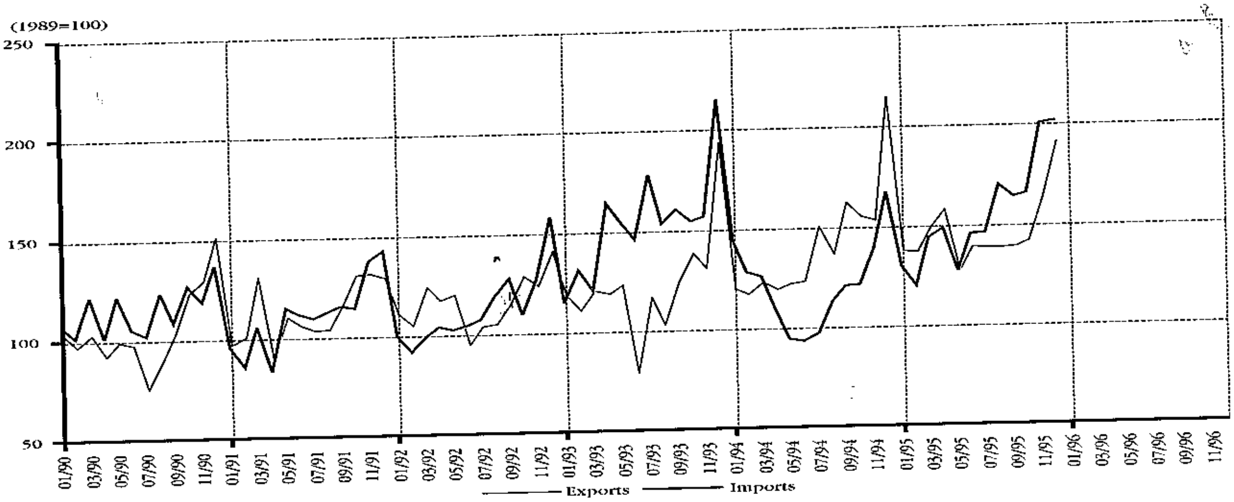
FOREIGN TRADE

GRAPH 31



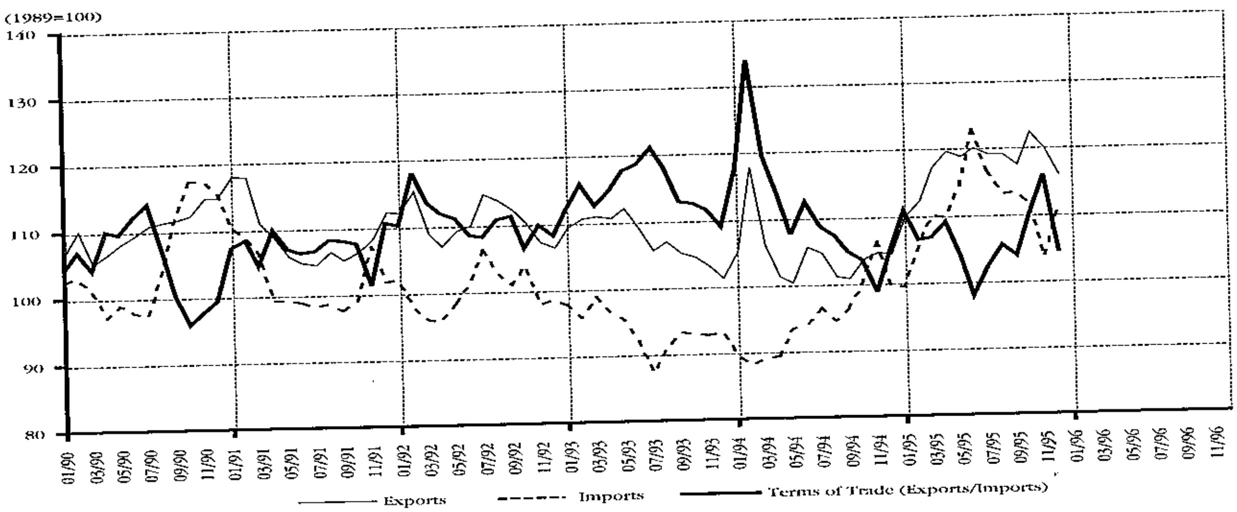
FOREIGN TRADE QUANTITY INDEX

GRAPH 32



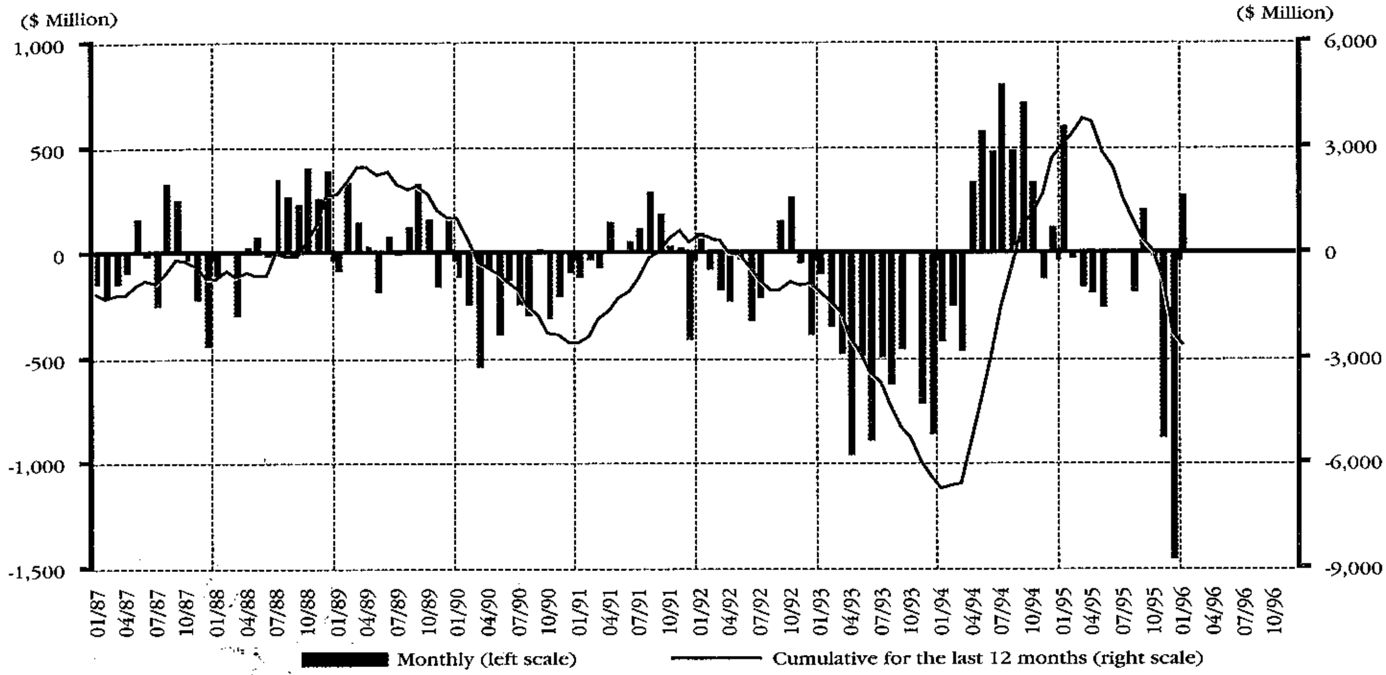
FOREIGN TRADE PRICE INDEX

GRAPH 33



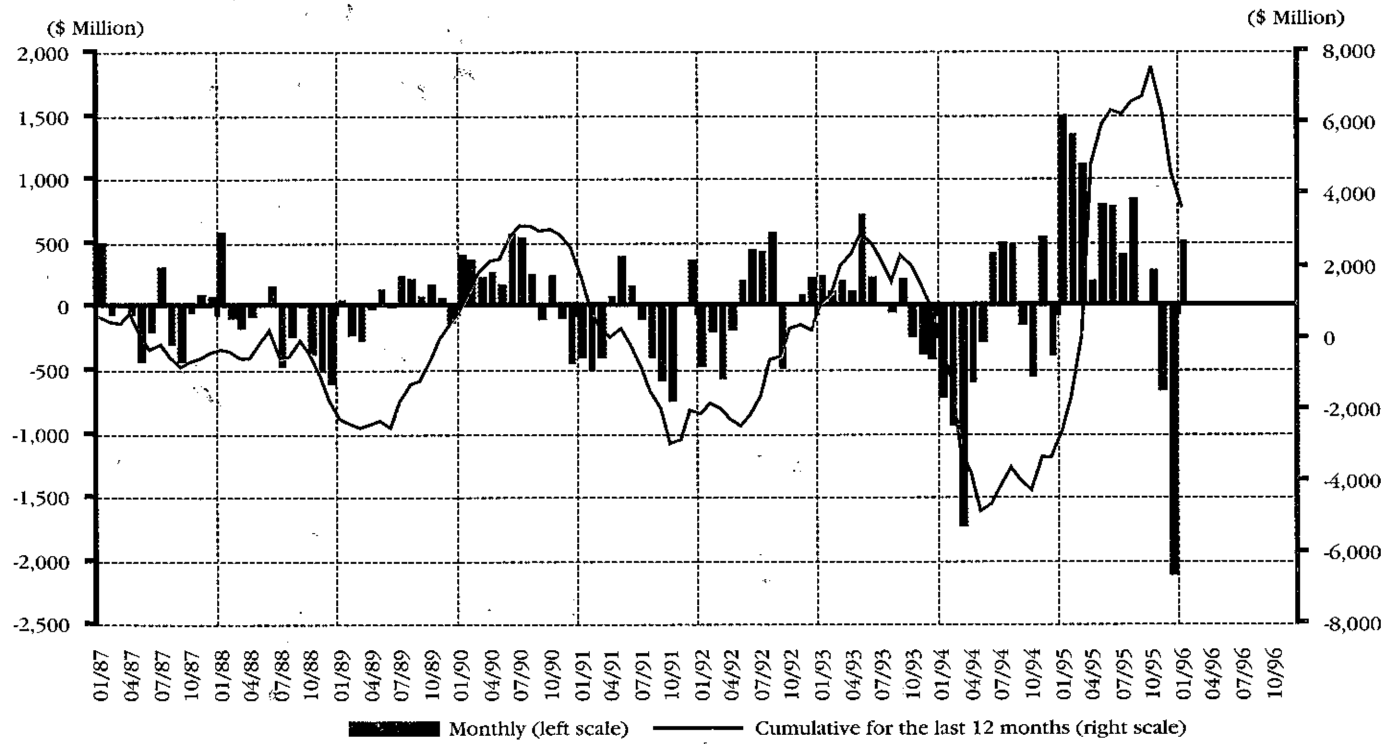
CURRENT ACCOUNT BALANCE

GRAPH 34



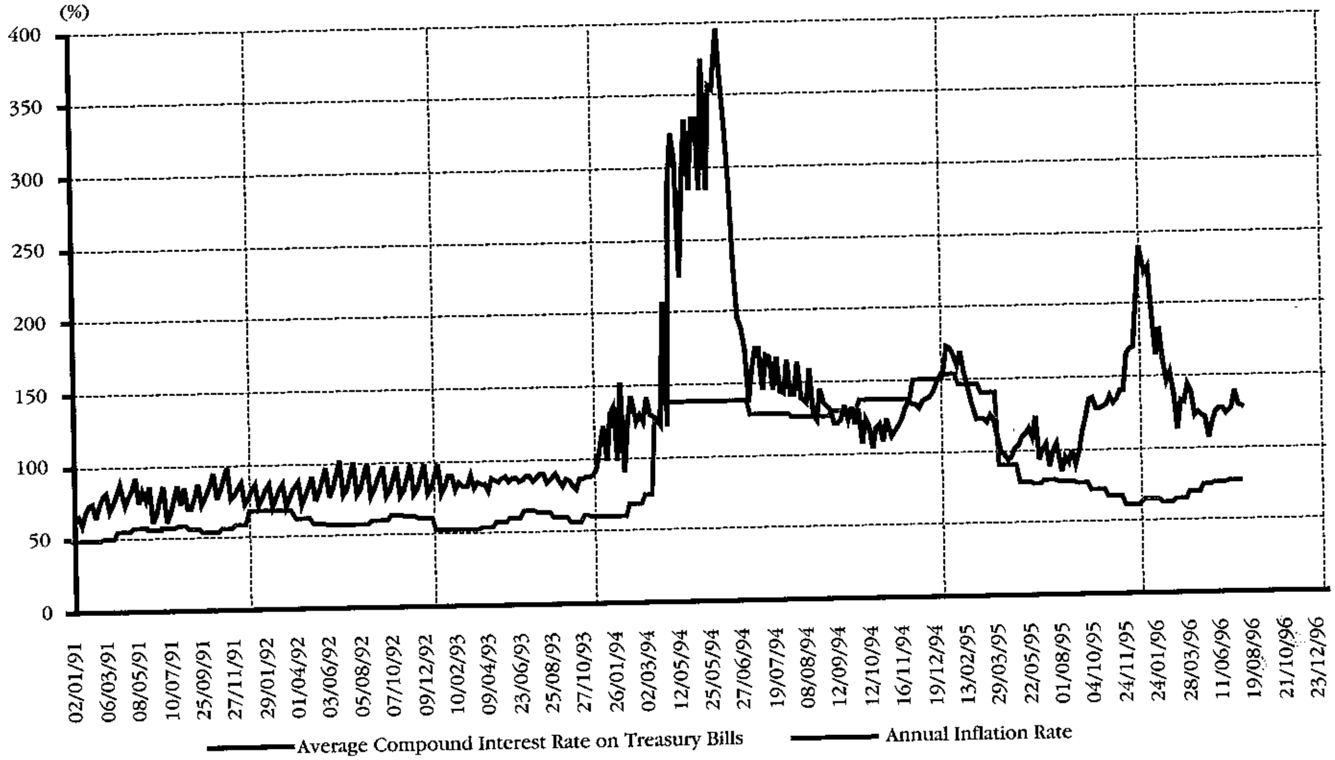
TOTAL OF SHORT-TERM CAPITAL AND NET ERRORS AND OMISSIONS

GRAPH 35



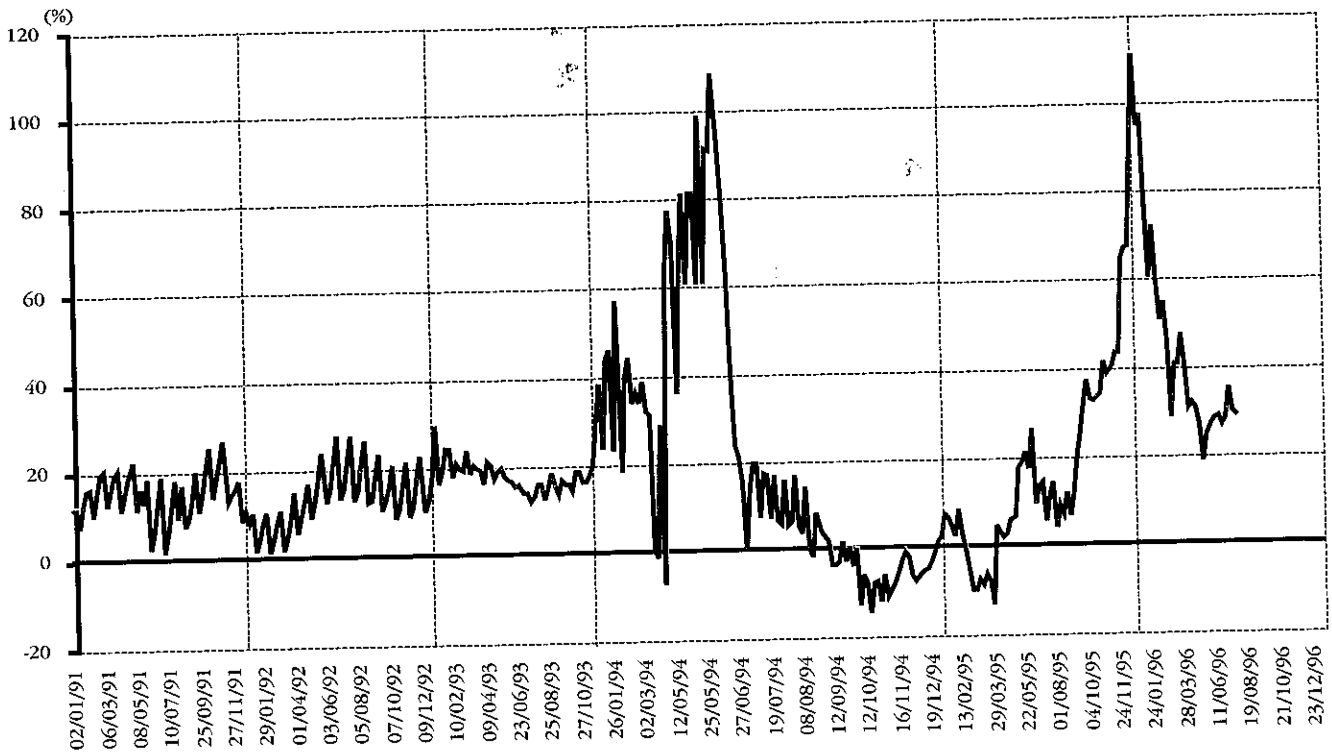
AVERAGE YEARLY NOMINAL INTEREST RATE

GRAPH 36



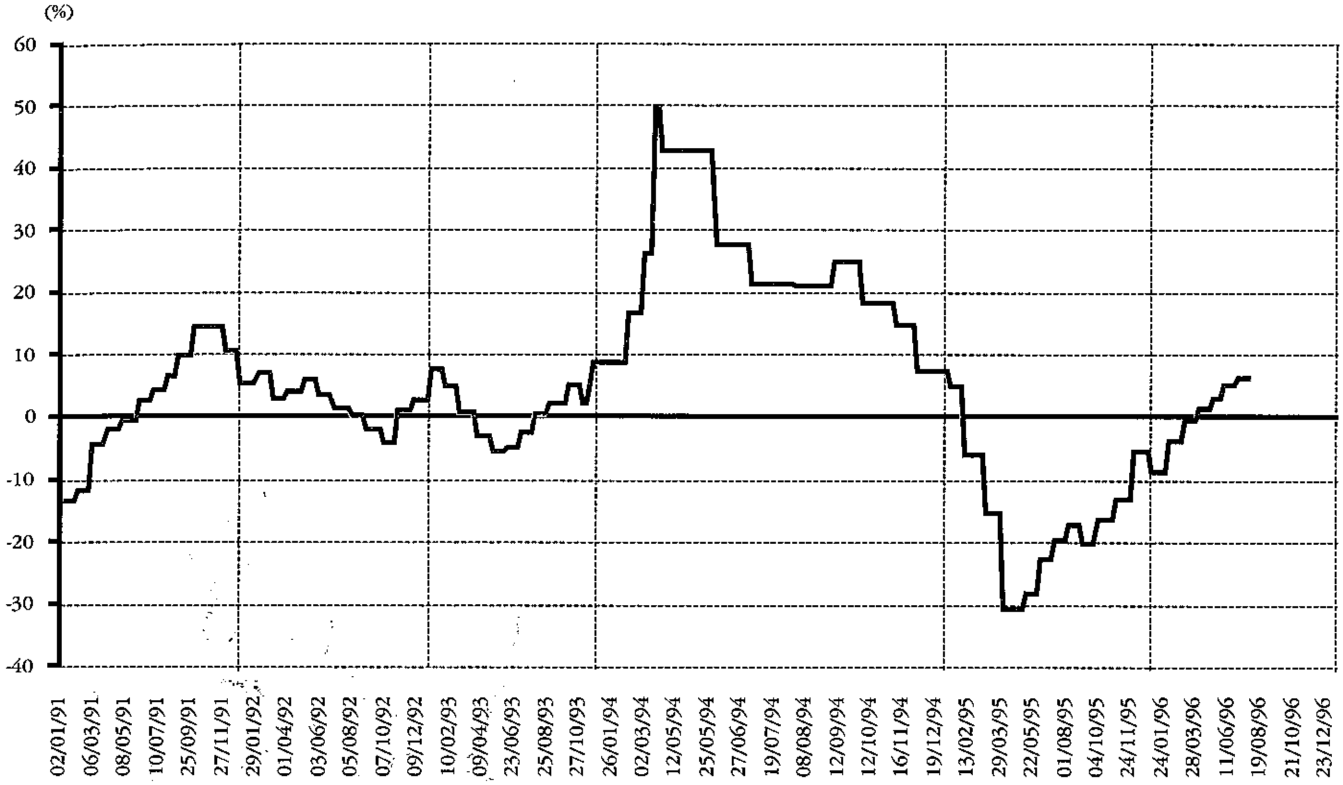
REAL INTEREST RATE ON GOVERNMENT PAPER (*)

GRAPH 37



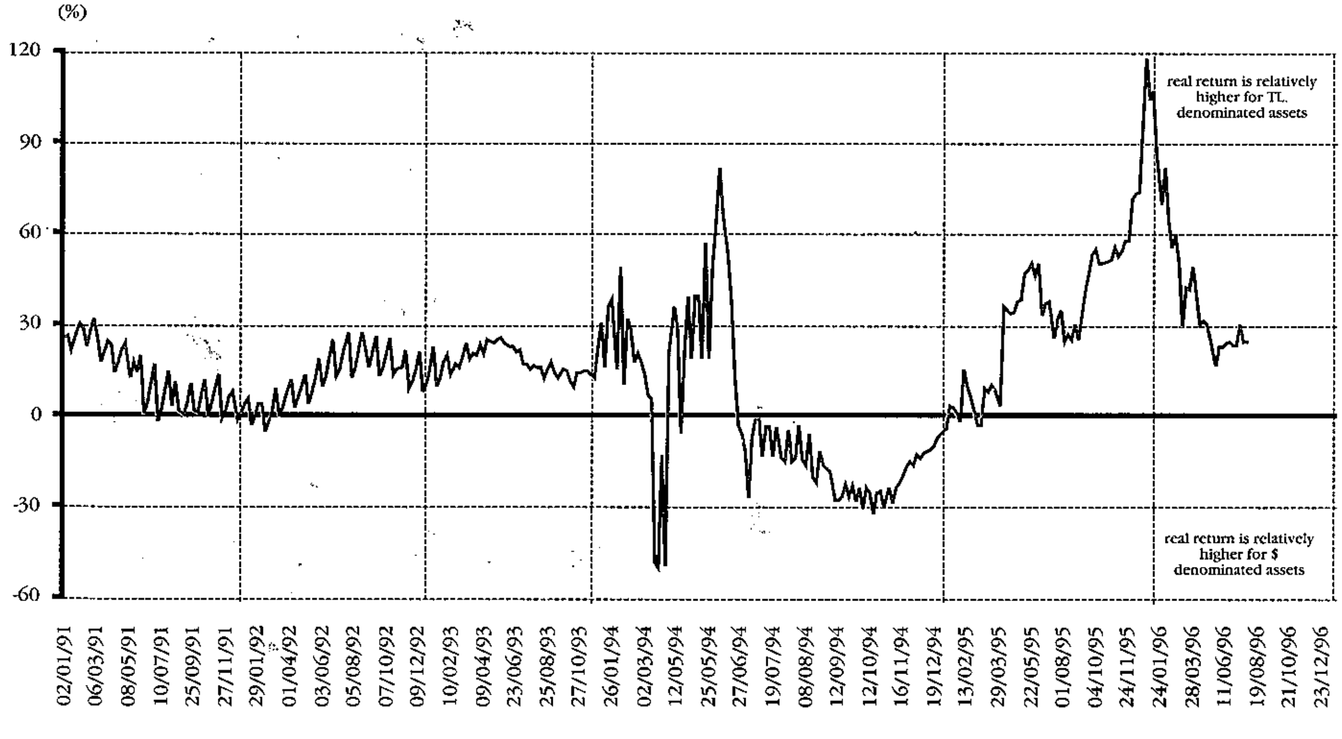
(*) Real interest rate is computed as: $\{(1+i)/(1+\dot{p})-1\} \times 100$.
i: Average compound rate of interest on government paper (for all maturities), $\dot{p}$: inflation rate $\{(pt/p(t-12)-1\}$

REAL RATE OF RETURN ON US $ (*) GRAPH 38



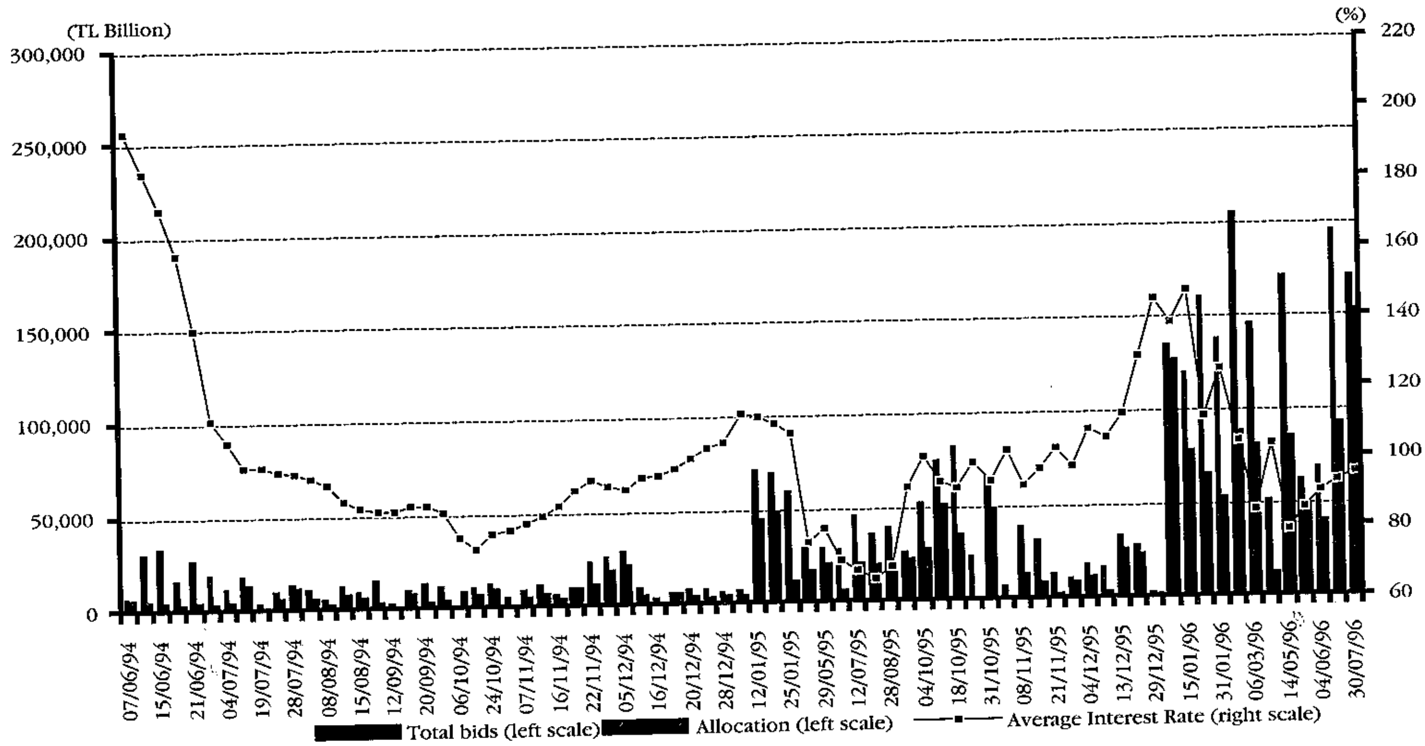
(*) Real rate of return is calculated as the yearly increase of index (TL/$) / WPI (1994=100)

REAL INTEREST RATE MINUS REAL RATE OF RETURN ON US $ GRAPH 39



TREASURY AUCTIONS (3 Months Maturity) (*)

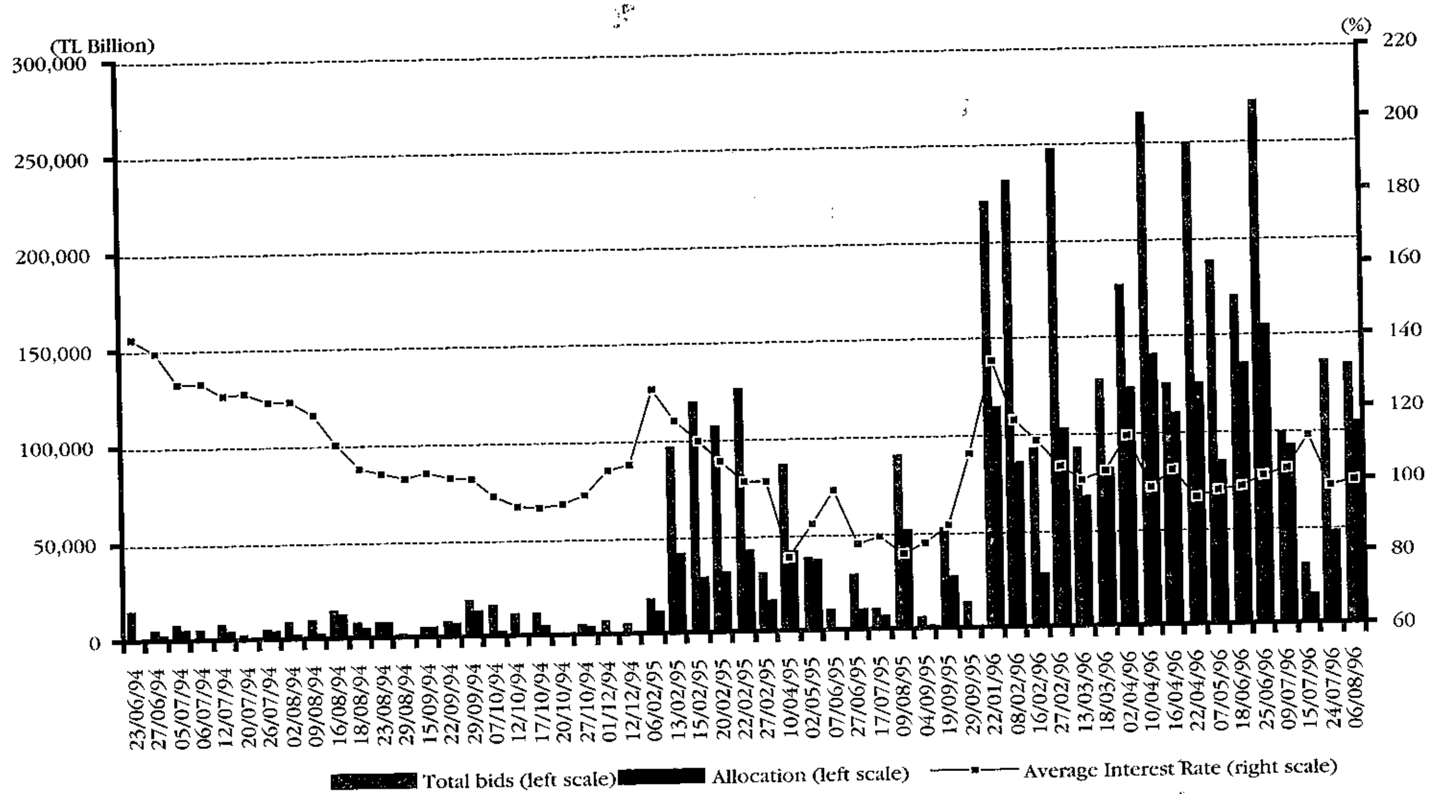
GRAPH 40



(*) Includes bids with irregular terms.

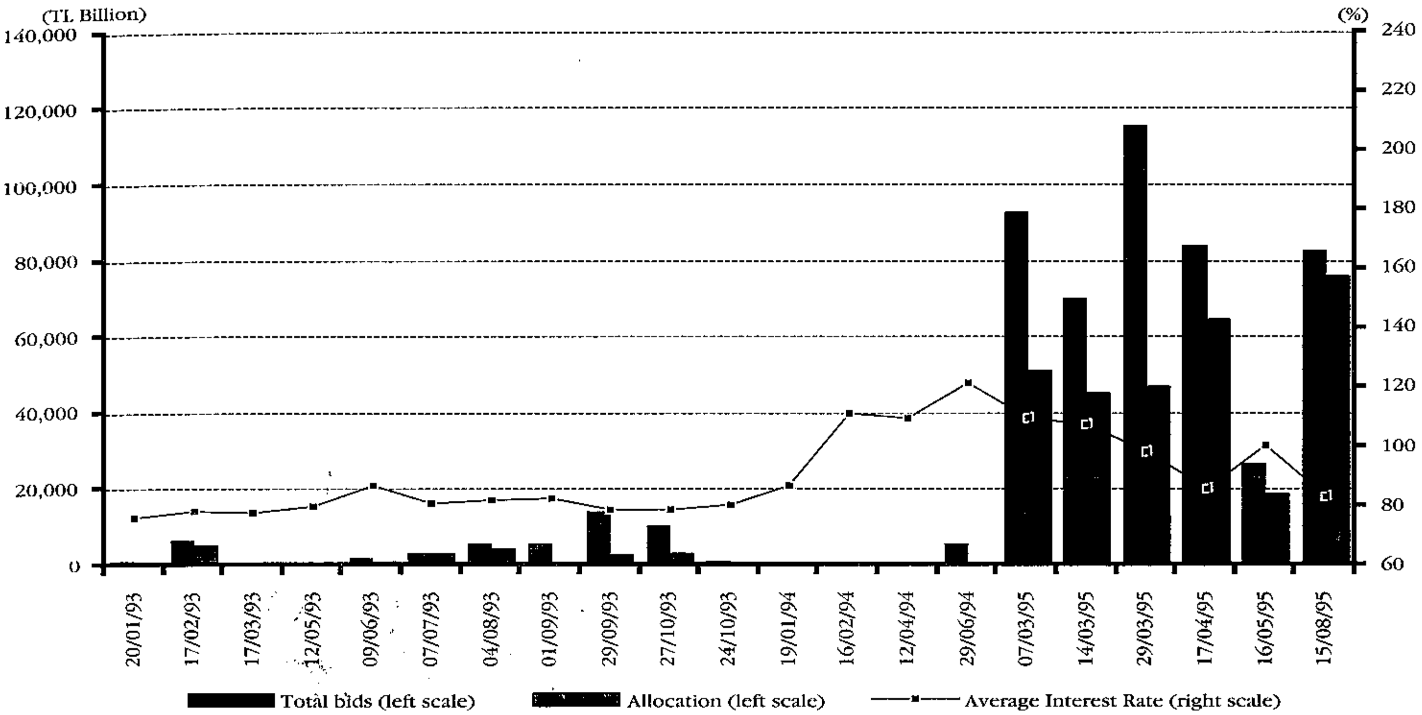
TREASURY AUCTIONS (6 Months Maturity) (*)

GRAPH 41



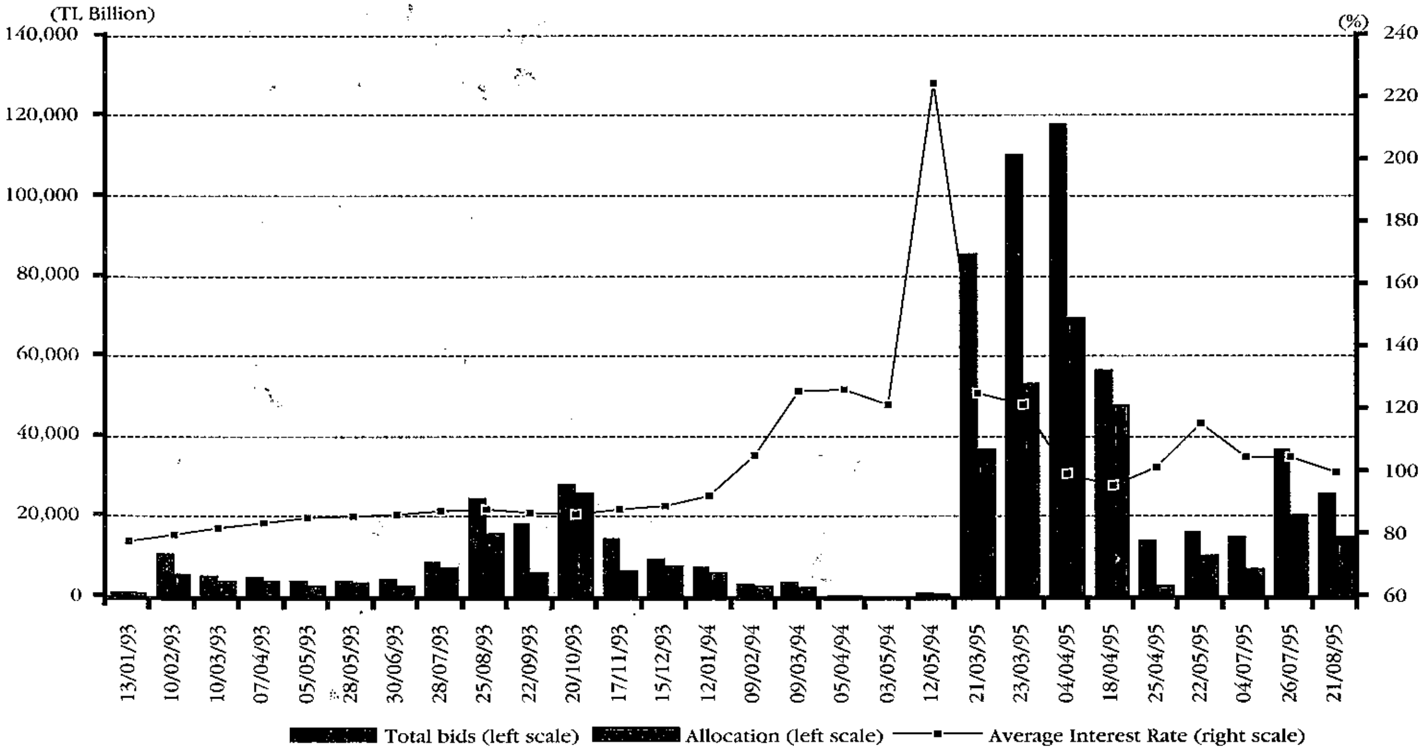
(*) Includes bids with irregular terms.

TREASURY AUCTIONS (9 Months Maturity) (*) GRAPH 42



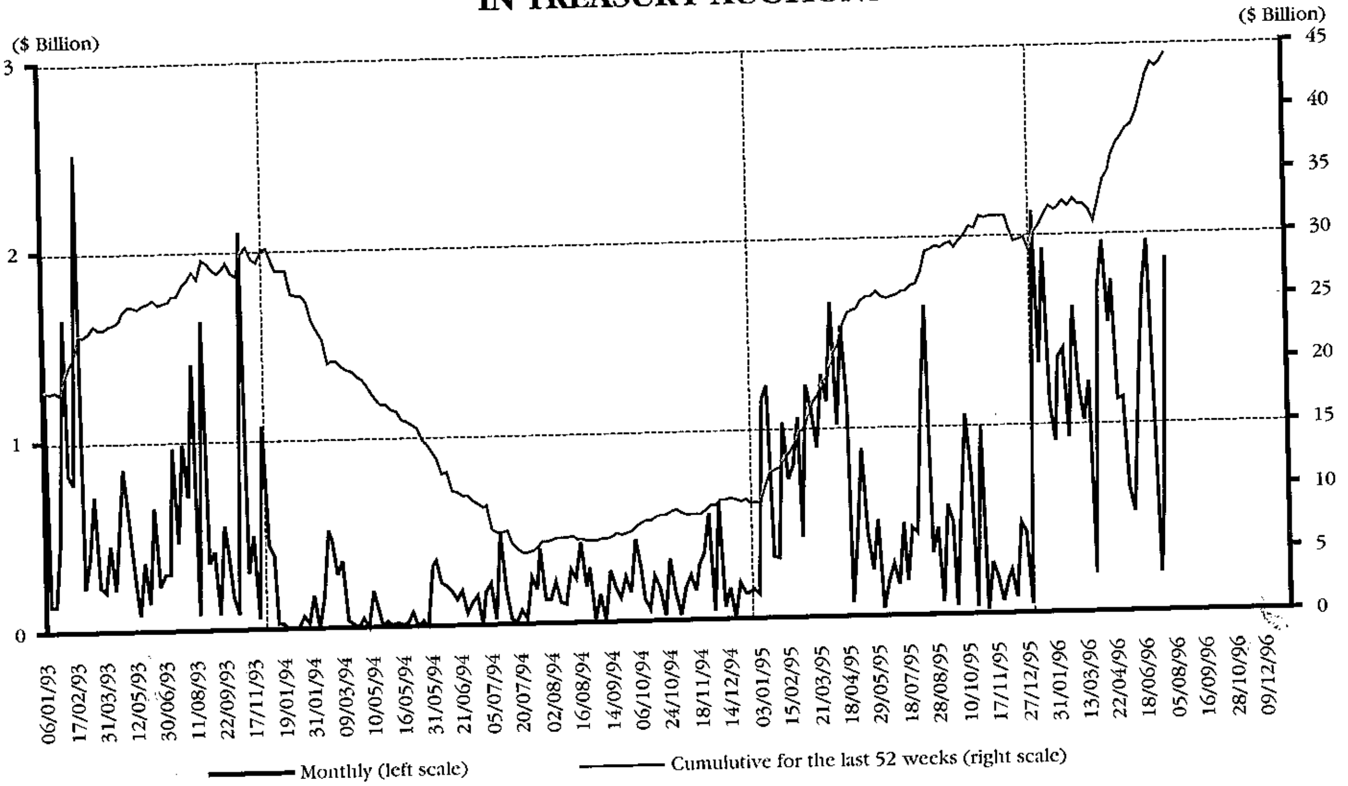
(*) Includes bids with irregular terms.

TREASURY AUCTIONS (12 Months Maturity) GRAPH 43



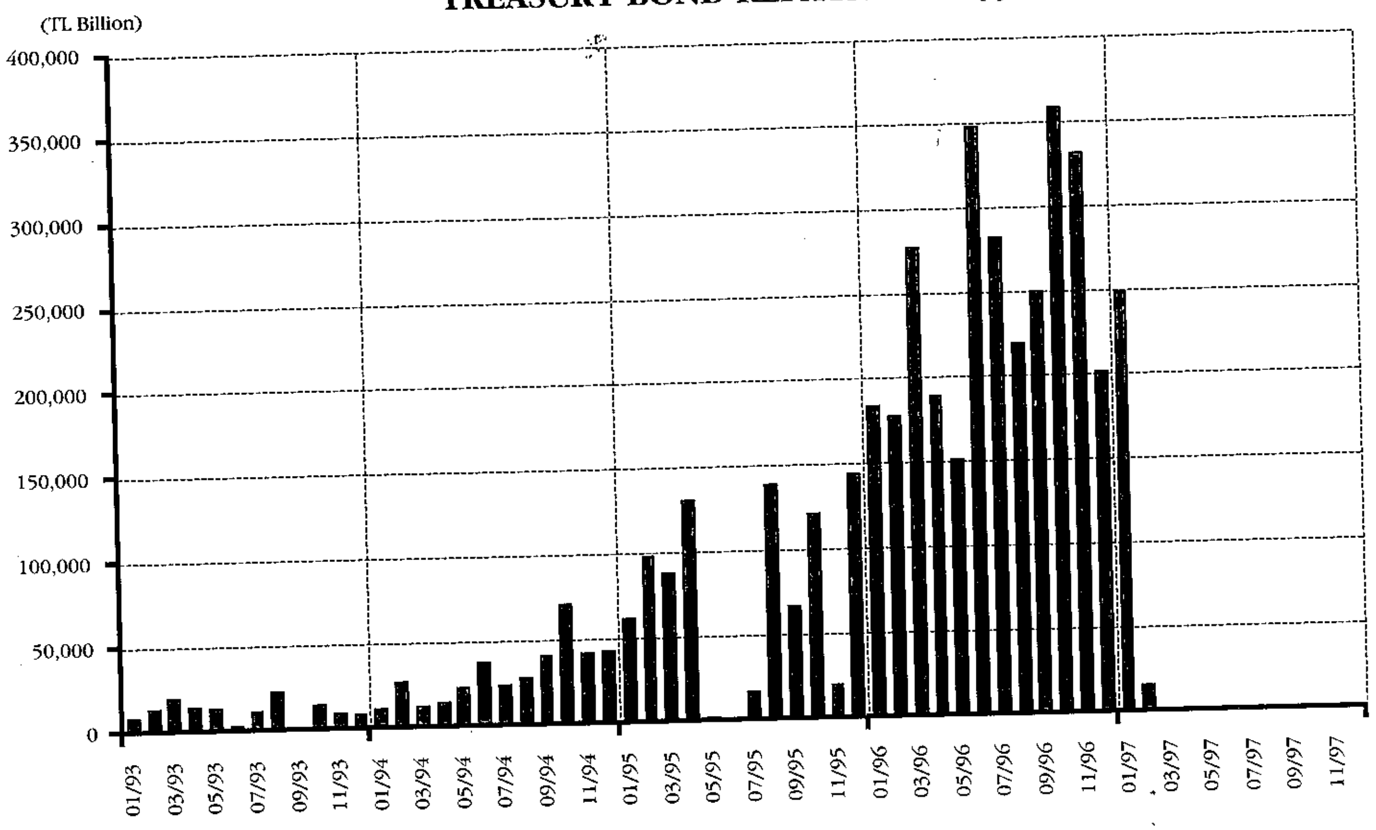
GRAPH 44

THE AMOUNT OF GOVERNMENT PAPERS SOLD IN TREASURY AUCTIONS



GRAPH 45

TREASURY BOND REPAYMENTS (*)



(*) As of end of July 1996

APPENDIX 1

MACROECONOMIC SCENARIO: THE CONSEQUENCES OF EXPANSIONARY MONETARY AND FISCAL POLICIES

The Turkish economy has been living with macroeoconomic instability for a long time. In the last 7 to 8 years various stabilization programs were put in action. These stabilization programs were generally aimed at producing shortrun solutions to the problems, but could not last long because of political reasons, and they were all replaced by populist policies shortly after their induction. Although difficulties have been dealt with in the shortterm, longterm solutions to structural problems have always been postponed and instability has reemerged in an even more acute form.

The measures that were taken in response to the 1994 crisis were also short-lived, and expansionary policies made a comeback before the elections of December 1995. As a result, by the beginning of 1996, budget and foreign trade deficits were again growing very fast, inflation was on the rise, and growth rate was following a very unsteady path.

The last issue of TÜSİAD's Quarterly Economic Survey included a study entitled as "A Macroeconomic Scenario for Stable Growth in the 1996-1998 Period". This study, which laid down the main contours of an attainable process of stable growth for the coming threeyear period, was prepared on the assumption that the budget deficit would be around TL 811 trillions in 1996 and that there would be less use of shortterm advances for the financing of budget deficits. The study calculated the values of certain macroeconomic variables so that a 6 percent longterm growth rate could be achieved at the end of the threeyear period. However, the study's assumptions for 1996 were invalidated by a number of economic policies that were pursued in the first half of the year. It became apparent that problems will remain unsolved as in the previous years and that the new government will stick to expansionary policies.

In the first and second quarters of 1996 the growth rate reached the high levels of 12.2 and 8.6 percent respectively, while growth in exports for the same period were much lower than expected. This indicates that the high growth rate in GDP was caused by an expansion in domestic demand. As of September 1996, policies to reduce this rise in the domestic demand have not been introduced. Therefore it can be expected that high growth rates will continue in the foreseeable short-term.

Starting from these estimates, a new scenario was prepared to trace the developments in the macroeconomic variables of the previous scenario until the end of 1996. A three-block constrained Bayesian Vector Autoregression model is run under these assumptions and the results are summarized in Table A.1.1.

The results indicate that 1996 will witness a GNP growth rate of approximately 8.0 percent, an average annual inflation rate of 81 percent, an end-of-year inflation rate of around 100 percent, exports in the amount of $23.0 billions, imports totaling $41.9 billions, and a foreign trade deficit of $18.9 billions.

These results differ significantly from the results of the previous scenario. In this new scenario, the inflation rate turns out to be higher because of the 65 percent higher consolidated budget deficit in comparison to the first scenario and the assumption that Central Bank resources will be more intensely utilized for the financing of the deficit. The 75.1 percent inflation rate estimate of the first scenario has been recalculated as 80.5 percent in the new one. With the acceleration of monetary expansion in the second half of the year, the inflation rate is forecasted to accelerate as well and go up to 100 percent at the end of the year. In view of the expansionary policies, the 3.3 percent GNP growth rate estimate of the first scenario is recomputed as 8.0 percent, imports are anticipated to increase faster, exports are expected to increase at a slower pace, and the foreign trade deficit is predicted to be higher.(1)

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(1) The GNP figures for the first quarter of 1996 have been revised and those for the second quarter have been published after this report was prepared. Due to the time constraint these figures have only been taken into consideration in this part of the report.

TABLE A1.1 AN EXPANSIONIST POLICY SCENARIO FOR 1996

Level	94-1	94-2	94-3	94-4	94	95-1	95-2	95-3	95-4	95	96-1	96-2	96-3*	96-4*	96*
GNP (1987 prices)	19,017	19,982	29,960	22,773	91,733	18,967	22,490	33,162	24,531	99,150	21,281	24,424	35,566	25,865	107,136
RESERVE MONEY (TL Billion)	309,575	418,651	533,707	545,822	451,939	614,285	797,754	935,180	999,731	836,737	1,108,395	1,365,309	1,628,433	1,826,121	1,482,065
BUDGET REVENUES (TL Billion)	111,525	173,198	216,935	251,782	753,440	255,767	327,153	369,629	451,522	1,404,071	422,647	651,275	761,073	988,156	2,823,151
BUDGET EXPENDITURES (TL Billion)	162,798	163,118	243,865	329,594	899,375	309,707	386,265	342,224	682,451	1,720,647	496,866	1,052,497	1,059,771	1,596,633	4,205,767
IMPORT (USD Billion)	5,713	4,715	5,393	6,785	22,606	6,623	8,422	9,330	10,812	35,187	9,533*	9,987*	10,876	11,483	41,879
EXPORT (USD Billion)	3,914	3,894	4,889	5,693	18,390	4,821	5,306	5,373	6,474	21,974	5,298*	5,121*	5,604	6,957	22,980
REAL EXCHANGE RATE (WPI/USD)	0.363	0.304	0.334	0.356	0.339	0.386	0.419	0.421	0.405	0.408	0.405	0.408	0.405	0.399	0.404
REAL INT. RATE (3 mon. T.B./WPI)	4.3	-13.8	13.6	2.2	1.6	1.5	5.3	11.3	13.2	7.8	5.6	3.1	9.8	4.0	5.6
WPI (1994=100)	64.3	99.0	107.8	129.0	100.0	158.4	179.4	191.8	214.5	186.0	260.4	310.8	348.7	423.4	335.8

Annual Percentage Increase

	94-1	94-2	94-3	94-4	95-1	95-2	95-3	95-4	96-1	96-2	96-3*	96-4*
GNP	4.1	-9.7	-8.7	-6.9	-0.3	12.6	10.7	7.7	12.2	8.6	7.2	5.4
RESERVE MONEY	47.8	77.4	99.6	85.9	98.4	90.6	75.2	83.2	80.4	71.1	74.1	82.7
BUDGET REVENUES	85.6	10.2	40.1	98.2	129.3	88.9	70.4	79.3	65.2	99.1	105.9	118.9
BUDGET EXPENDITURES	77.3	70.1	128.8	69.0	90.2	136.8	40.3	107.1	60.4	172.5	209.7	134.0
IMPORT	-3.7	-39.5	-32.2	-16.1	15.9	78.6	73.0	59.4	43.9*	18.6*	16.6	6.2
EXPORT	5.1	9.5	34.5	21.2	23.2	36.3	9.9	13.7	9.9*	-3.5*	4.3	7.5
REAL EXCHANGE RATE	-14.2	-28.2	-18.1	-11.6	6.5	37.9	25.8	13.8	4.8	-2.7	-3.9	-1.4
WPI	67.8	133.9	128.3	141.3	146.6	81.2	78.0	66.3	64.4	73.3	81.8	97.4

Annual Average Percentage Increase

	1988	1989	1990	1991	1992	1993	1994	1995	1996*
GNP	1.5	1.6	9.4	0.3	6.4	8.1	-6.1	8.1	8.0
RESERVE MONEY	61.0	74.8	47.9	46.0	62.5	72.9	79.6	85.1	77.1
BUDGET REVENUES	68.4	78.4	80.7	74.8	81.1	100.5	109.4	86.4	101.1
BUDGET EXPENDITURES	64.4	81.2	75.4	92.0	70.4	119.3	83.8	91.3	144.4
IMPORT	1.1	16.7	41.1	-7.0	9.9	29.0	-24.1	55.7	19.0
EXPORT	15.6	-1.2	10.6	4.9	9.0	4.8	17.8	19.5	4.6
REAL EXCHANGE RATE	3.4	8.8	24.0	-1.9	-2.1	-0.7	-18.1	20.2	-0.9
WPI	70.4	64.0	52.3	55.3	62.1	58.4	120.7	86.0	80.5

* *Estimate*

APPENDIX: 2

STRUCTURAL BUDGET AND CYCLICAL EFFECTS

The structural budget balance is a method that is used to better evaluate the size of the public sector deficit and the impact of fiscal policies on domestic demand. The basic idea behind this method is to measure the budget deficit independently of the fluctuations in economic activity. Thus, the method makes it possible to distinguish between the structural and cyclical components of budget revenues and expenditures.[1]

The actual budget deficit involves the effects of the business cycles. The structural budget balance refers to the adjusted levels of budget revenues and expenditures for movements in the cyclical output gap. Cyclical budget deficit, on the other hand, is measured as the difference between actual and structural budget deficits, and it can be interpreted as an indicator of whether fiscal policy, in comparison to a "neutral" budget deficit, is expansionary or contractionary in the short run.

If the actual budget deficit is more (less) than the structural budget deficit, i.e. if the cyclical effect is positive (negative), then budgetary policy can be said to be expansionary (contractionary). Similarly, if the annual change of cyclical effect is positive (negative), this is indicative of an expansionary (contractionary) fiscal impulse.

In this study, the actual budget deficits in the 1975-1996 period were decomposed into structural balances and cyclical effects. The computations reveal that in the 1989-1996 period, the cyclical effect has always been positive. In other words, in this particular period, the actual budget deficit has always been higher than the structural budget deficit. The main reason behind the rise of the budget deficit/GNP ratio has been the sharp increase of the share of the consolidated budget expenditures in GNP as opposed to a much slower growth of the respective share of the budget revenues. The remarkable increase of the share of the consolidated budget expenditures in GNP, on the other hand, can be attributed directly to the policy of domestic borrowing and the resulting payments of massive amounts as interest on domestic debt. It should be noted that there occurred a significant decrease in the budget deficit/GNP ratio shortly after the

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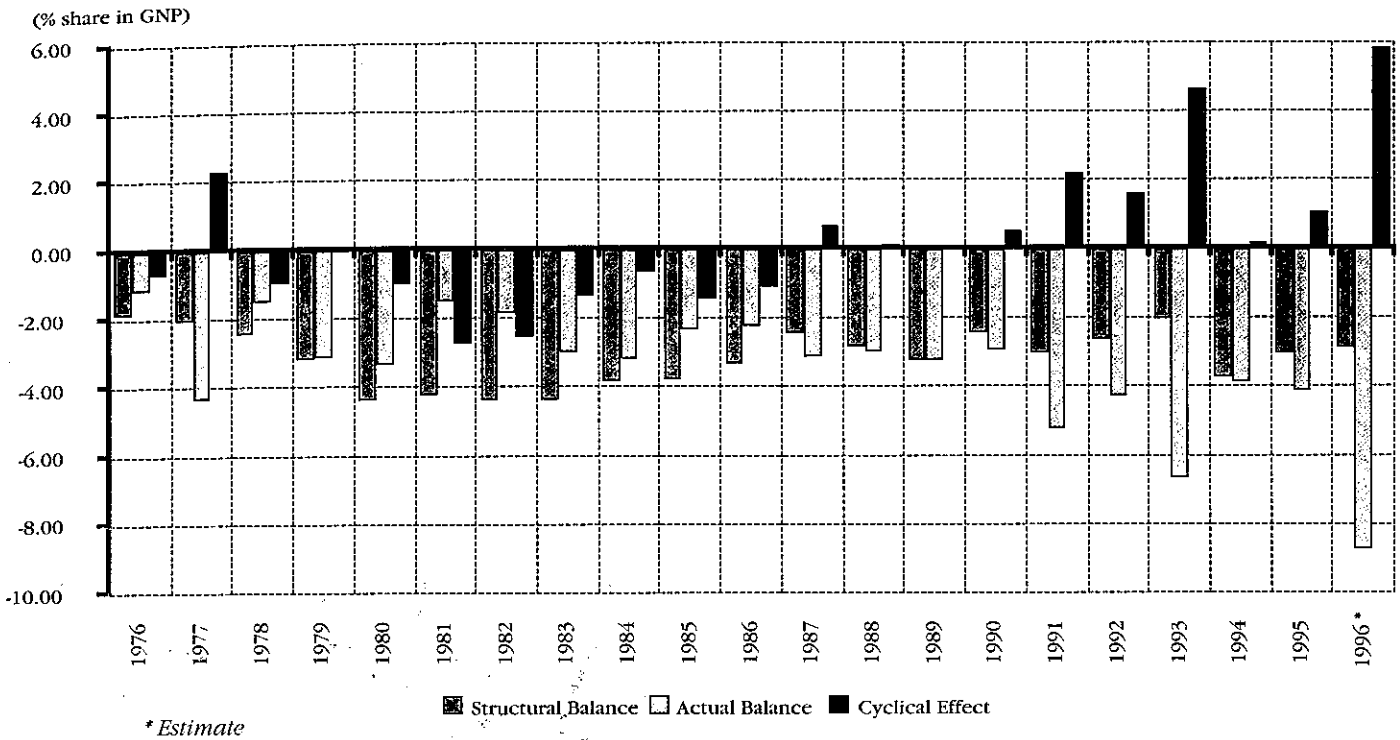
[1] *According to the method followed in this study, the actual budget deficit is separated into two components: structural balance and cyclical effect. The figure for structural balance is equal to the difference between structural revenues and structural expenditures. For any given year, structural budget expenditures are found by multiplying the potential GNP figure of this year by the expenditure/GNP ratio of a base year. Structural budget revenues, on the other hand, are calculated by multiplying the actual GNP figure of a given year by the revenue/GNP ratio of a base year. Cyclical effect is computed by subtracting the actual budget balance from the structural budget balance. In this study, 1989 is taken as the base year. The potential production level is calculated with the use of the exponential growth rate obtained from the real production figures of the 1975-1995 period. Because of the assumptions of the computation method, the figures for cyclical effects should be read not as absolute magnitudes but as indicators of direction and intensity.*

1994 crisis. However, as the cyclical effect turned out to be positive both in 1994 and 1995, one can conclude that the budget deficit could not be reduced sufficiently because of high interest payments and inadequate revenue-raising measures.

The fiscal impulse, which shows the annual changes in the cyclical effect, has a self correcting nature. After a period of expansionary fiscal policy, there arises a need for making a considerable adjustment in the budget, and as a result the fiscal impulse turns negative and a serious recession or economic crisis sets in. Moreover, it is observed that the intensity of a contractionary fiscal impulse, which occurs in reaction to an expansionary fiscal impulse, increases in time. During the period under investigation, the fiscal impulse was higher than 3 percent in only two years, 1977 and 1993. The 3 percent expansionary fiscal impulse of 1977 gave way to a 3.3 percent contractionary fiscal impulse in 1978. The 3 percent expansionary effect of 1993, on the other hand, resulted in a 4.5 percent contractionary effect in 1994. In 1996, if the real growth rate becomes 5.2 percent, the deflator increases by 85 percent, and the budget deficit reaches the predicted amount of 1.3 quadrillions, then the budget deficit ratio will set a new record with 8.7 percent and the cyclical impulse will rise to 4.8 percent. In other words, in 1996 budgetary policies will give rise to an expansionary effect unseen in the last 20 years. This record high expansionary effect of 1996 will bring about a considerable contractionary effect in 1997. So much so that, expenditure-cutting and revenue-raising measures, much more demanding than the ones that were taken in 1994, will have to be put in effect.

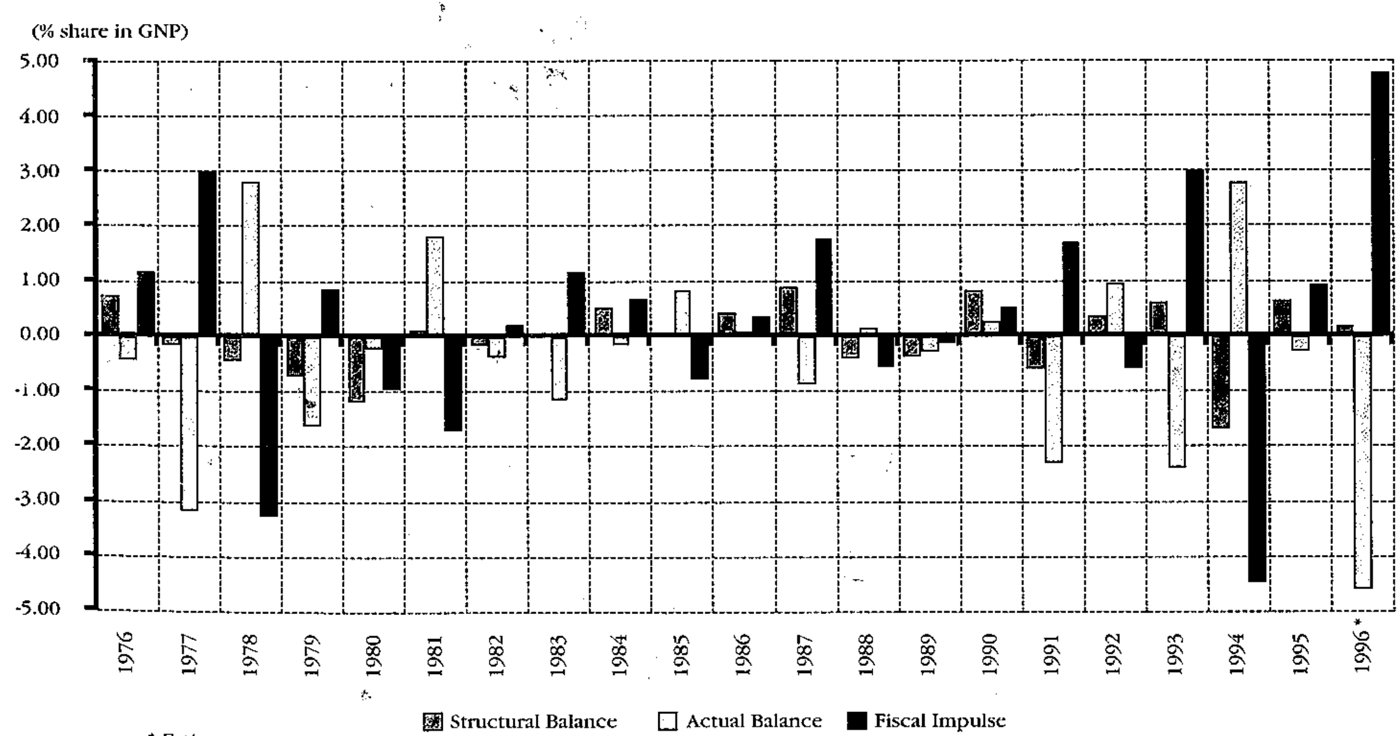
The general conclusion that can be drawn from the method which has been used in this study to determine the short-run impact of fiscal policy on domestic demand is the following: If increases in consolidated budget expenditures with the aim of raising the level of social welfare are not backed up by parallel increases in budget revenues, they will result in ever-widening budget deficits; moreover, expansionary policies cannot possibly be implemented over a few successive periods. Excessive expansionary policies in one year necessarily give way to severe belt-tightening measures in the next year. If expenditure-cutting and revenue-raising measures are not taken without delay, a very dear price will have to be paid in 1997 for the expansionary effect of 1996.

CONSOLIDATED BUDGET DEFICIT **GRAPH A2.1**
STRUCTURAL BALANCE - ACTUAL BALANCE = CYCLICAL EFFECT



** Estimate*

CHANGES IN THE CONSOLIDATED BUDGET DEFICIT **GRAPH A2.2**
STRUCTURAL BALANCE - ACTUAL BALANCE = FISCAL IMPULSE



** Estimate*

TABLE A2.1 THE CONSOLIDATED BUDGET STANCE CYCLICAL EFFECT AND FISCAL IMPULSE

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
(TL Billion)											
GNP	691	868	1,108	1,646	2,877	5,303	8,023	10,612	13,933	22,168	35,350
Real GNP	46,275	50,438	51,944	52,582	52,324	50,870	53,317	54,963	57,279	61,350	63,989
GNP Deflator (1987=100)	1.49	1.72	2.13	3.13	5.50	10.42	15.05	19.31	24.32	36.13	55.24
Potential GNP	670	803	1,035	1,581	2,888	5,696	8,554	11,417	14,963	23,122	36,775
Real Potential GNP	44,854	46,661	48,540	50,494	52,528	54,643	56,844	59,133	61,514	63,991	66,568
Budget Revenues	107	144	187	310	506	939	1,445	1,492	2,374	3,375	5,158
Budget Expenditures	112	154	235	335	596	1,116	1,565	1,690	2,792	4,078	5,988
Budget Deficit	-5	-10	-48	-25	-90	-177	-120	-198	-418	-703	-830
Annual Percentage Increase											
GNP		25.62	27.65	48.56	74.79	84.32	51.29	32.27	31.29	59.10	59.46
Real GNP		9.00	2.99	1.23	-0.49	-2.78	4.81	3.09	4.21	7.11	4.30
GNP Deflator (1987=100)		15.25	23.95	46.75	75.65	89.59	44.35	28.31	25.99	48.55	52.89
Potential GNP		4.03	4.03	4.03	4.03	4.03	4.03	4.03	4.03	4.03	4.03
Real Potential GNP		19.89	28.94	52.66	82.72	97.23	50.16	33.48	31.06	54.53	59.04
Percentage Share in GDP											
Budget Revenues	15.48	16.59	16.88	18.83	17.59	17.71	18.01	14.06	17.04	15.22	14.59
Budget Expenditures	16.21	17.74	21.21	20.35	20.72	21.04	19.51	15.93	20.04	18.40	16.94
Budget Deficit	-0.72	-1.15	-4.33	-1.52	-3.13	-3.34	-1.50	-1.87	-3.00	-3.17	-2.35
Cyclical Effect (Percentage Share in GDP)											
Structural Balance	-2.61	-1.87	-2.03	-2.46	-3.19	-4.37	-4.23	-4.39	-4.36	-3.85	-3.80
Budget Deficit	-0.72	-1.15	-4.33	-1.52	-3.13	-3.34	-1.50	-1.87	-3.00	-3.17	-2.35
Cyclical Effect	1.89	-0.72	2.30	-0.94	-0.06	-1.03	-2.74	-2.53	-1.36	-0.67	-1.45
Fiscal Impluse (Absolute Changes in Shares)											
Structural Balance		0.74	-0.16	-0.43	-0.73	-1.18	0.13	-0.16	0.03	0.52	0.05
Budget Deficit		-0.43	-3.18	2.81	-1.61	-0.21	1.84	-0.37	-1.13	-0.17	0.82
Fiscal Impulse		1.17	3.02	-3.25	0.88	-0.97	-1.71	0.21	1.17	0.69	-0.78

Table A2.1 cont.

	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996 *
(TL Billion)											
GNP	51,185	75,019	129,175	230,370	397,178	634,393	1,103,605	1,997,323	3,887,903	7,644,206	14,877,154
Real GNP	68,315	75,019	76,108	77,347	84,592	84,887	90,322	97,677	91,732	99,150	104,306
GNP Deflator (1987=100)	74.92	100.00	169.73	297.84	469.52	747.34	1,221.86	2,044.82	4,238.33	7,709.74	14,262,99
Potential GNP	51,885	72,038	127,191	232,186	380,764	630,468	1,072,290	1,866,786	4,025,127	7,616,774	14,658,460
Real Potential GNP	44,69,249	72,038	74,939	77,957	81,096	84,362	87,759	91,293	94,970	98,794	102,773
Budget Revenues	7,154	10,444	17,587	31,396	56,573	99,085	178,070	357,333	751,615	1,403,071	2,650,000
Budget Expenditures	8,312	12,791	21,447	38,871	68,355	132,401	225,398	490,438	902,454	1,720,647	3,950,000
Budget Deficit	-1,158	-2,347	-3,860	-7,502	-11,782	-33,316	-47,328	-133,105	-150,839	-317,576	-1,300,000
Annual Percentage Increase											
GNP	44.79	46.56	72.19	78.34	72.41	59.73	73.96	80.98	94.66	96.62	94.60
Real GNP	6.76	9.81	1.45	1.63	9.37	0.35	6.40	8.14	-6.09	8.09	5.20
GNP Deflator (1987=100)	35.63	33.47	69.73	75.48	57.64	59.17	63.49	67.35	107.27	81.91	85.00
Potential GNP	4.03	4.03	4.03	4.03	4.03	4.03	4.03	4.03	4.03	4.03	4.03
Real Potential GNP	41.09	38.84	76.56	82.55	63.99	65.58	70.08	74.09	115.62	89.23	92.50
Cyclical Effect (Percentage Share in GDP)											
Budget Revenues	13.98	13.92	13.61	13.62	14.24	15.62	16.14	17.89	19.33	18.35	17.80
Budget Expenditures	16.24	17.05	16.60	16.87	17.21	20.87	20.42	24.55	23.21	22.51	26.60
Budget Deficit	-2.26	-3.13	-2.99	-3.26	-2.97	-5.25	-4.29	-6.66	-3.88	-4.15	-8.74
Fiscal Impluse (Percentage Share in GDP)											
Structural Balance	-3.35	-2.46	-2.87	-3.26	-2.43	-3.02	-2.65	-2.03	-3.72	-3.06	-2.88
Budget Deficit	-2.26	-3.13	-2.99	-3.26	-2.97	-5.25	-4.29	-6.66	-3.88	-4.15	-8.74
Cyclical Effect	-1.09	0.67	0.12	0.00	0.53	2.23	1.64	4.63	0.16	1.09	5.86
Absolute Changes in Shares											
Structural Balance	0.45	0.89	-0.41	-0.39	0.82	-0.59	0.37	0.62	-1.69	0.65	0.19
Budget Deficit	0.09	-0.87	0.14	-0.27	0.29	-2.29	0.96	-2.38	2.78	-0.27	-4.58
Fiscal Impulse	0.36	1.76	-0.55	-0.12	0.53	1.70	-0.59	2.99	-4.47	0.93	4.77

* *Estimate*