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Statement by Mr. Hosseini and Mr. Boostani on Turkey
(Preliminary)
Executive Board Meeting
May 27, 2021

We thank staff for the well-written paper and Mr. Azal and Mr. Dogan for their insightful Buff statement. We commend the authorities for their swift response to the health crises and supporting activity. The real growth rate remained positive in 2020 and is projected to surge in 2021. However, the pandemic aggravated pre-existing vulnerabilities and disproportionally affected female, youth, low-skill and refugee population. We agree with staff that the economic outlook is uncertain specially because of large shifts in monetary positions. Also, the risk of new COVID-19 outbreak, in the absent of broad vaccination, is still present. We concur with the thrust of the staff appraisal and policy recommendations and would like to limit ourselves to the following comments for emphasis.

1. **The authorities' firm monetary policy stance would be instrumental in helping to anchor inflation expectations credibly and guiding the inflation rate down to target**. Moreover, we agree with staff that a firm monetary stand that in short term targets higher ex-ante real interest rate would serve to bring inflation down, while leaving the premature measure would damage the policy credibility. Regulatory measures that constrain the growth of bank credit, especially by the state-owned banks, would also improve the effectiveness of monetary policy.

The Central Bank of Republic of Turkey has a strong track record in policy formulation and implementation and an effective policy framework. The policy and operational independence of the central bank is critical for the creditability of monetary policy. Against this background, the introduction of a new committee for achieving price stability may entail coordination costs and risks to the credibility of the monetary authorities.

2. **Fiscal support, especially to vulnerable and disproportionally affected groups, should continue until the crisis abates and potential scarring minimizes**. Although growth in Turkey in 2020 was higher than peers, it was un-even. Employment declined and an additional 1.5 million people were pushed into poverty. We agree with staff on the need for a comprehensive medium-term fiscal consolidation plan in the medium term when the pandemic subsides, while keeping in focus the protection of the vulnerable population through well-calibrated and targeted measures.

3. **There are risks to the financial sector**. High dollarization, worsening FX position of state-owned banks, and high external financing needs, against the background of low official reserves, make the financial system vulnerable to FX shocks. Monetary policy normalization in funding economies and/or changes in foreign investors' sentiments towards emerging markets in general, and Turkey in particular, could also pose downside risks.

4. **Structural reforms are required in order to achieve strong, inclusive, and sustainable growth**. We noted positively the authorities' intention to introduce a comprehensive New Reform Program aimed at promoting sustained and equitable growth, increasing productivity and strengthening governance. We echo the staff's view that to achieve these objectives enhancing labor market flexibility, supporting viable non-financial corporations and, on a longer horizon, strengthening the business environment should be prioritized.

With these remarks, we wish the authorities every success in their policy efforts.