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EBS/84/42

CONFIDENTIAL

March 7, 1984

To: Members of the Executive Board

From: The Secretary

Subject: Turkey - Request for Stand-By Arrangement

Attached for consideration by the Executive Directors is a paper on a request from Turkey for a stand-by arrangement equivalent to SDR 225 million. A draft decision appears on page 19. The letter of intent will be circulated shortly.

It is proposed to bring this subject to the agenda for discussion on Wednesday, April 4, 1984.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Tyler (ext. 75175) or Mr. Kopits (ext. (5)8814).

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

TURKEY

Request for Stand-By Arrangement

Prepared by the European Department and
The Exchange and Trade Relations Department

(In consultation with other Departments)

Approved by Brian Rose and Subimal Mookerjee

March 6, 1984

I. Introduction

A mission consisting of G. Tyler (Head, EUR), G. Kopits (EUR), J. Bonvicini (ETR), M. Z. Khan, P. Thomsen, and, as secretary, C. Nguyen (all EUR) was in Ankara during January 6-24, 1984 to review the current stand-by, which is scheduled to end in mid-June 1984, and to discuss a possible program for a new one-year stand-by arrangement, which the authorities requested. The Turkish representatives included officials of the Under Secretariat of the Treasury and Foreign Trade, the Ministry of Finance and Customs, the State Planning Organization, and the Central Bank of Turkey. There were meetings with the Deputy Prime Minister in charge of Economic Affairs, the Minister of Finance and Customs, and the Governor of the Central Bank. Turkey continues to avail itself of the transitional arrangements under the provisions of Article XIV.

Following the completion of a three-year stand-by arrangement with Turkey in the amount of SDR 1,250 million (416.7 percent of previous quota), all of which was purchased over June 1980 to May 1983, the Executive Board approved a one-year stand-by arrangement in an amount of SDR 225 million (75 percent of the previous quota) on June 24, 1983 (EBS/83/98) and at that time Turkey made the first of four equal purchases. Although formally meeting the performance criteria attached to the second purchase, Turkey did not request it. Subsequently, some performance criteria for December 1983 were not met. Following the election of a new Government, new wide-ranging economic policies were introduced. As of March 31, 1984, the estimated Fund holdings of Turkish liras subject to repurchase amount to 338.7 percent of Turkey's new quota of SDR 429.1 million.

In a letter from the Minister of State and Deputy Prime Minister to the Managing Director (to be circulated later), Turkey requests the cancellation of the existing stand-by arrangement and its replacement by a new one-year stand-by arrangement in an amount equivalent to SDR 225 million (52.4 percent of the new quota). Financing of the proposed stand-by would be entirely from ordinary resources. Purchases would be available in four equal tranches with the first available following approval of the stand-by arrangement, and the remaining three at the end of July 1984, October 1984, and February 1985. The resulting Fund holdings of Turkish liras, assuming that repurchases are effected on schedule are shown in Table 1 (Appendix II). A waiver of the limitation of Article V, Section 3(b)(iii), of the Articles of Agreement would be required.

Since January 1, 1980, the World Bank has approved four structural adjustment loans (SAL) for a total amount of US$1,180.3 million, including US$300.8 million as part of SAL IV approved June 27, 1983, of which US$1,080.3 million has been disbursed. The World Bank is currently reviewing the second tranche of SAL IV for disbursement of the remaining US$100 million, and appraising a fifth structural adjustment loan.

II. Performance Under the 1983 Stand-By Arrangement

Between 1980 and 1982 the external current account deficit declined from 6 1/4 to 2 1/4 percent of GNP and domestic inflation fell from more than 100 percent a year to below 30 percent. In addition, real GNP rose by more than 4 percent in both 1981 and 1982, after declining by some 1 1/2 percent over 1979-80. On June 24, 1983 the Fund approved a one-year stand-by arrangement with Turkey in support of a financial program aimed at consolidating the progress achieved over the previous three years. The 1983 program envisaged a narrowing of the current account deficit in 1983 to 1 1/4 percent of GNP, domestic growth of 4 3/4 percent, and an annual inflation rate of some 20 percent. These objectives were to be achieved principally through monetary and fiscal discipline, and flexible exchange and interest rate policies.

The results were disappointing. Fiscal policy was basically on target. The consolidated budget deficit was kept to 0.5 percent of GNP, as programmed, and transfers to the State Economic Enterprises (SEEs) were limited to the amount permitted under the program; however, the target on the public sector borrowing requirement was not achieved because of unexpectedly heavy short-term borrowing by the SEEs. In particular, monetary management deteriorated severely as nominal interest rates were reduced at a time of renewed inflationary pressures and Central Bank credit expanded rapidly after midyear. The ceiling on the net domestic assets of the Central Bank was exceeded after September (and would have been exceeded in September in the absence of special transactions between the Agricultural Bank and the Central Bank). Not surprisingly, the failure of monetary policy was a major cause of an acceleration in inflation to an annual average rate of 31 percent and it accomodated an increase in the current account deficit to almost 3 1/2 percent of GNP in 1983 instead of the expected reduction.

The ceiling on net Central Bank credit to the public sector and the limits on contracting of public and publicly guaranteed foreign debt of 1- to 12-year maturity and on the increase in outstanding short-term foreign debt were observed.

The authorities took some measures to implement structural reforms of the banking system and the SEEs by passing the necessary legislation. While this legal framework was a necessary beginning to the process of implementing the reforms, the major steps of implementation remain to be taken.

In summary, the 1983 program failed, principally because the authorities were unwilling to implement an effective monetary policy. The outcome was a sharp deterioration in both the domestic and external sectors, including an aggravation of the foreign debt position which put the economy in a worse position than it was in 1982.

III. Developments in 1983 and Prospects for 1984

1. Domestic economy

During 1983 the growth of consumption and fixed investment more than offset a continuing decline in stocks, so that domestic demand grew by 3.5 percent. Private consumption, which had begun to recover in 1982, continued to increase, as the effects of some reduction in real wages and agricultural incomes appeared to be offset by the impact of negative real interest rates. Fixed private investment continued to expand, increasing its share of total investment from 38.9 percent in 1982 to 39.3 percent in 1983. Although export volume rose rather more than projected, the real foreign balance made a negative contribution to growth in 1983 as remittances declined and the volume of imports overshot targets. Consequently, growth of real GNP slowed down to 3.2 percent in 1983 from 4.6 percent in the previous year (Table 2). Agricultural output declined by almost 1 percent in 1983 due to drought. Industrial production continued to expand, albeit at a slightly lower rate than during 1982.

In 1983 the annual average increase in wholesale prices was about 31 percent compared with an increase of 25 percent in 1982 (Table 3). By end-year, prices were around 40 percent higher than a year earlier (Chart 1). The chief explanatory factor was a relatively expansionary monetary policy, which accommodated price increases stemming from a further deterioration in the terms of trade and a rise in domestic demand. There were revisions to a number of wage settlements, including a supplementary wage adjustment in November for some public sector employees, which led to average wage increases (net of income tax) of nearly 30 percent for the year in that sector. Private sector wages lagged behind and are estimated to have increased by 20 percent. Further adjustments in public sector wages are planned for 1984 in addition to the proposed income tax rebate for all wage earners designed to compensate them for their relatively high effective income tax liability.

The official forecasts envisage a 4.5 percent increase of real GNP in 1984 with the growth of domestic demand leveling off. The foreign sector is expected to contribute positively to overall growth. On the production side, the impetus to growth is expected to come from agricultural production, which is forecast to increase by about 3.5 percent assuming normal weather conditions, while other sectors are projected to continue expanding at about the same level as in 1983. The GNP deflator is projected to be held slightly below 30 percent and, by December 1984, wholesale prices are expected to be less than 25 percent higher than a year earlier. These projections are predicated on a monetary policy that will be substantially tighter than in 1983, and fiscal policies that will lead to a further improvement in public sector performance. These policies, combined with continued flexibility in exchange rate policy, aim to reverse the deterioration that occurred in the balance of payments in 1983.

2. Balance of payments and external debt

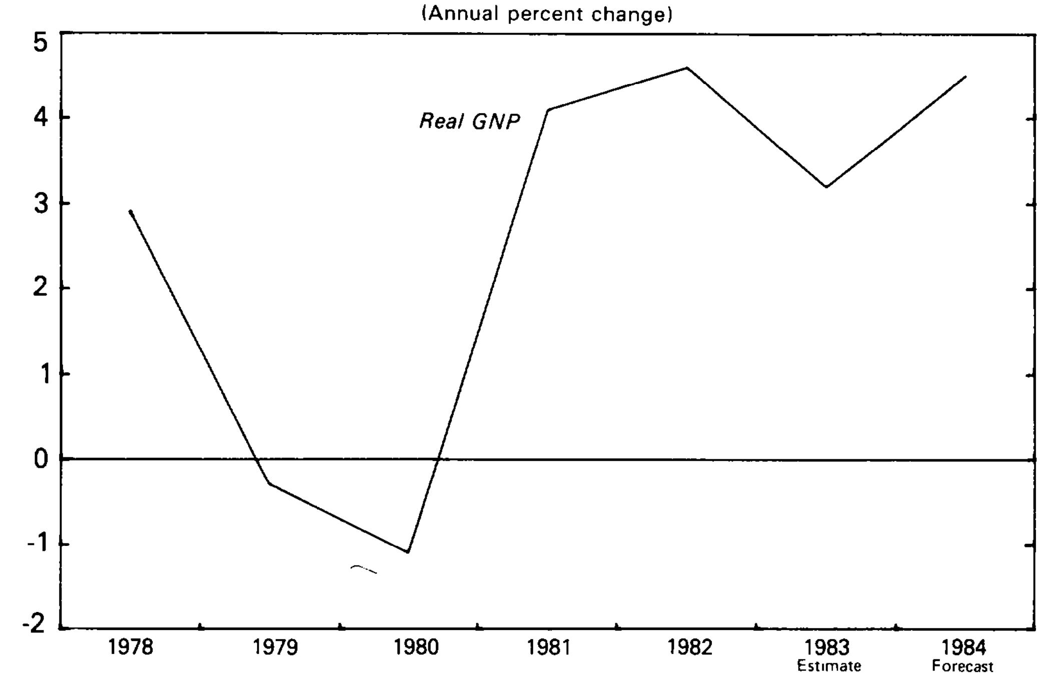
a. Balance of payments

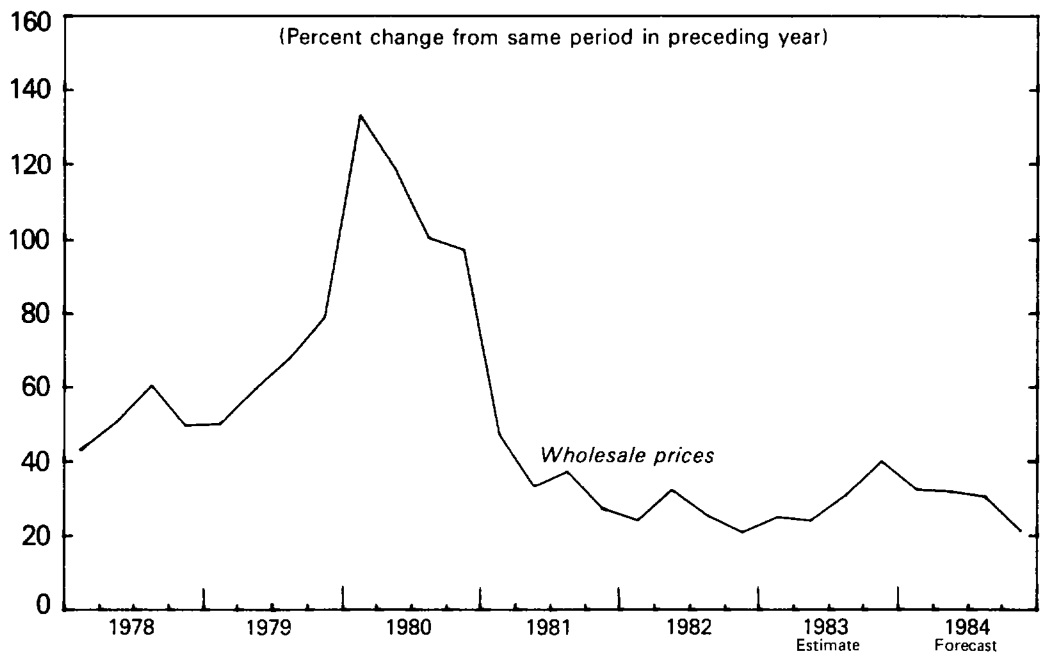
The external payments situation deteriorated in 1983 and the current account deficit, which had been projected to decline to US$0.6 billion from US$1.3 billion in 1982 (or from 2 1/4 to 1 1/4 percent of GNP), rose to an estimated US$1.8 billion (3 1/2 percent of GNP). Although net capital inflow (including errors and omissions) was higher than expected, the overall balance was a deficit of some US$0.3 billion in 1983, against a projected surplus of US$0.4 billion (Table 4).

The deterioration in 1983 reflected a weakening of the trade balance and a significant decline in workers' remittances; other invisible transactions were basically as projected. With the value of exports stagnating in response to the continued decline of agricultural prices and to sluggish demand in some major Middle Eastern countries, the trade deficit rose slightly to US$3.2 billion. A further increase of 13 percent in export volume in 1983--reflecting to a large extent the improved competitiveness of Turkish manufactured exports in European markets--was largely offset by an estimated 10 1/2 percent decline in prices, especially of agricultural goods (Table 5). The value of imports rose by 2 percent, despite a 12 percent drop in the price of imported crude oil, as volume increased by 9 percent. The terms of trade deteriorated for the fifth consecutive year. The unexpectedly sharp slowdown in workers' remittances (from US$2.2 billion in 1982 to US$1.6 billion in 1983) was caused by the recession in host countries, the weakening of host countries' currencies relative to the U.S. dollar, the decline in real interest rates in Turkey, and end-year rumors of a depreciation of the Turkish lira. About one fifth of the decline in remittances was offset by increased transfers through deposits in special savings accounts with the Dresdner Bank, recorded as short-term capital inflow.

In 1983, net medium- and long-term capital inflow fell to about one half of the level in 1981 and 1982, as special official assistance programs started to be scaled down and the disbursement of project credits was slower than anticipated. Net short-term capital inflows (including errors and omissions) more than doubled, reaching US$1.0 billion, including

CHART 1
TURKEY
GROWTH AND INFLATION





Sources: State Planing Organization, Ministry of Commerce, and Fund staff estimates.

US$0.5 billion of "Dresdner" 1/ and convertible Turkish lira deposits. Other registered short-term capital movements--which in 1982 accounted for a combined outflow of nearly US$400 million--showed a net inflow of US$100 million, primarily because of the normalization of trade financing. At the end of 1983, gross official international reserves amounted to US$1.1 billion, equal to six weeks of merchandise imports.

Assuming a growth in export volume of 17 percent and a slight recovery in the terms of trade, the balance on merchandise trade is projected to improve somewhat in 1984, after allowing for an increase in non-oil imports by 12 percent as a result of a major trade liberalization recently enacted. Workers' remittances are expected to increase moderately, principally in response to higher domestic interest rates and the liberalization of the exchange system. The net result is a projected reduction in the current account deficit to US$1.0 billion (2 1/4 percent of GNP). In the staff view, the assumptions underlying the projections are reasonable only on the basis that domestic demand is kept under strict control and that the competitive position of the export sector continues to improve. Moreover, the outlook for exports could be adversely affected by developments in some Middle East markets and the import liberalization could generate a higher level of imports than currently projected. Net medium- and long-term capital inflow is expected to rise, with an acceleration of both the execution of projects with foreign financing and the anticipated use of IBRD funds under SAL IV and V. The forecast allows for US$500 million of financial credits from banks and some increase in private foreign capital inflow. Net short-term capital inflow is expected to remain at about last year's level, with about half "Dresdner" deposits. Gross official reserves are projected to rise by some US$600 million, equal to nine weeks of imports by the end of the year.

b. <u>External debt</u>

According to preliminary data, Turkey's total external disbursed debt rose by 4.0 percent over the first nine months of 1983, and at the end of September amounted to US$18.3 billion (35.4 percent of GNP). During this period, medium- and long-term external debt rose by only 2.3 percent as the dollar value of debt to official bilateral creditors--the bulk of which are OECD countries--declined after 1982, partly reflecting the exchange rate impact on outstanding balances in currencies other than dollars and lower special official aid. Much of the rise in medium- and long-term debt was accounted for by net Fund purchases and disbursements of IBRD loans. After declining since the end of 1979, medium-term debt to foreign commercial banks also rose over the first nine months of 1983 reflecting increased market borrowing to replace special official assistance. Medium-term debt to commercial banks accounts for 22 percent of total medium- and long-term foreign debt.

1/ Workers can make foreign exchange deposits in the Dresdner Bank, which acts as the agent of the Central Bank of Turkey. The deposits are recorded as liabilities of the Central Bank.

Most of the 15.5 percent increase in short-term foreign debt in January-September 1983 was in the form of "Dresdner" deposits. The latter have increasingly been the vehicle for transferring workers' remittances to Turkey and to date they have been a very stable form of foreign liability, although this could, of course, change if confidence in the Turkish balance of payments deteriorated. Excluding these and deposits under the convertible Turkish lira deposits scheme, outstanding short-term foreign debt was basically unchanged, reflecting caution on short-term foreign borrowing. Currently, short-term foreign debt represents less than 15 percent of total foreign debt, compared with almost 50 percent at the end of 1978.

Debt service payments on existing debt are shown in Table 7; projections which take into account new borrowing and examine the relationship between external viability and domestic growth possibilities are discussed in Appendix IV. The ratio of debt service payments (excluding amortization of short-term debt) to exports of goods and services should decline to 29 percent in 1984, after rising from 24 to 31 percent between 1981 and 1983. In 1985, however, gross debt repayments jump sharply as rescheduled debt falls due for repayment and remain high in subsequent years. As a result, the debt service ratio is projected to increase to nearly 33 percent in 1985. Projections on the debt service burden beyond 1985 become increasingly sensitive to a number of assumptions. Assuming that export growth remains close to 10 percent per year in real terms and there is no substantial reduction in access to foreign capital from the levels foreseen for 1984, the debt service ratio would decline to 24 percent to 26 percent by 1988; such a result would be consistent with acceptable growth rates of domestic output, provided import elasticity declines. However, the medium-term scenarios suggest that, to obtain the rates of increase of domestic output that the authorities wish, even if export growth was close to 10 percent per year, would require a large and increasing level of medium- and long-term borrowing. It is questionable whether the market would supply this level of new funds and in any case the debt service ratio would remain high. On this line of reasoning, the authorities may well find themselves obliged to accept less growth and more adjustment over the medium term.

Progress has been achieved in the recording and management of external debt; however, problems still remain (see SM/83/114, 6/6/83). A program for systematic classification and reporting procedures and for computerization of foreign debt statistics is being carried out with technical and financial assistance from the World Bank and the Fund.

IV. Economic Policies

1. Overview

During 1980-82, Turkey implemented successfully a stabilization program based primarily on demand management and increased flexibility in commodity and factor prices--notably interest rates and the exchange sight deposit rate accentuated, by a cut in the withholding tax rate from 25 percent to 20 percent. By contrast, the effective yield of CDs became comparatively lower as the applicable withholding tax rate was raised to 30 percent. Despite the fact that the rate of inflation began to climb again during 1983, in July, the spread between time and sight deposit yields was narrowed further as interest rates on time deposits and CDs were lowered by an additional 5 percentage points. Thus, in the second half of the year, deposit rates became negative in real terms; the result was a decline in the demand for time deposits. Concomitantly, many borrowing rates were reduced. The restructuring of interest rates was accompanied by the unification of a wide variety of reserve requirement and liquidity ratios, and the completion of reform legislation aimed at strengthening the financial position of banks (see SM/83/114, 6/6/83). The reform, although important in itself for longer-run efficiency, did not provide immediate relief to banks in financial difficulty.

Unable to attract sufficient time deposits, as real interest rates became negative (by mid-December 1983, the real effective yield on 6- to 12-month deposits had fallen to minus 9 percent, from 10 percent a year earlier), several banks had to ask for special assistance from the Central Bank. The banking system's dependence on Central Bank credit was increased because it was required to provide substantial credits to some enterprises facing financial difficulties. All told, in the course of 1983 the Central Bank extended special credits to commercial banks totaling LT 70 billion, and discounted about LT 140 billion in commercial bills for private enterprises--many of them in the export sector. By the end of the year the net domestic assets of the Central Bank were LT 155 billion or 13 percent above target (Table 8). Despite a small unanticipated increase in net foreign liabilities, the year-end expansion in reserve money reached 36 percent, as against a targeted annual growth rate of 25 percent. The increase in broad money was above the rise in estimated money demand, which was depressed by slower growth of real output and negative real interest rates, resulting in a significant liquidity overhang in the second half of the year.

As a first step to correct the monetary disequilibrium and in view of the reluctance of the large banks to increase interest rates to positive real levels, the new Government authorized the Central Bank to establish deposit rates and review them at least every three months. On December 19, 1983, deposit rates were raised substantially, and a wider choice of shorter maturities and more frequent interest payments was introduced, along with a uniform interest rate on all sight deposits (Table 9). Also, effective January 1, 1984, all withholding tax rates on interest income were cut to 10 percent, raising the after-tax real yields on 6-month time deposits and CDs from minus 9 percent to plus 1 percent. Banks were freed to determine general lending rates. Owing in part to the reduction in the transactions tax from 15 to 3 percent, the nominal effective nonpreferential cost of borrowing has leveled off at around 60 percent.

rate. Public finances and incomes policy were strengthened and monetary policy was tightened. Price controls were abolished in the private sector and relaxed for the SEEs. The exchange rate was adjusted continuously to offset the inflation rate differential with major trading partners. Financial incentives were given to exporters, while the multiple exchange rate practices and certain import restrictions were phased out.

In 1983, the picture changed. While the authorities maintained a competitive exchange rate and broadly adhered to fiscal restraint, credit creation was allowed to get out of hand and sharp cuts were made in interest rates. However, at the end of the year, confronted both with an upsurge in inflation and a serious deterioration in the external payments situation, the newly elected Government moved to institute corrective action; it increased interest rates, depreciated the lira, and began to moderate monetary growth.

Important structural reform legislation was enacted in 1983 to enhance the efficiency of the banking system and the SEEs. At the beginning of 1984, a far-reaching liberalization of the trade and payments system was implemented. Further structural measures are to be introduced, particularly to develop financial markets.

2. Monetary policy

a. Recent developments

Since 1980 the authorities have actively used monetary instruments for stabilization, as well as to mobilize financial resources. Net domestic credit of the Central Bank of Turkey has been subject to quantitative ceilings, with the objective of limiting the growth of money supply to levels consistent with realistic output and price targets. Interest rates were determined by commercial banks, and competition between them for deposits resulted in real positive interest rates by the middle of 1981. This, along with the introduction of negotiable certificates of deposit (CDs), led to the revival of financial intermediation reflected in a steady rise in the real demand for broad money, as the rise in quasi-money holdings more than offset the decline in narrow money balances (Chart 2). However, excessive competition among some banks and other financial intermediaries for deposits and the consequent large increases in interest rates eventually led to the "Kastelli" crisis in mid-1982, and left many banks in a strained liquidity position. In response, the authorities permitted an increasing rate of credit expansion and widespread nonobservance of legal reserve requirements in the second half of 1982.

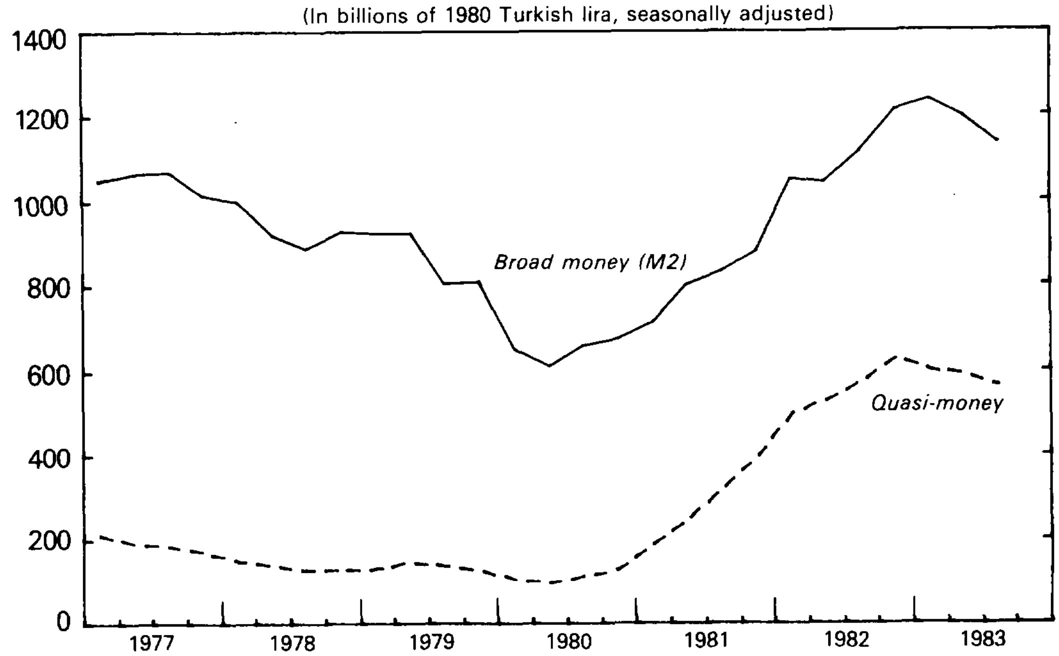
Following the deceleration in the rate of inflation and with official encouragement, in January 1983 nominal interest rates were reduced to 40 and 45 percent (from 50 percent), respectively, on 6- to 12-month deposits and 1-year deposits, as well as on comparable CDs, but raised to 20 percent (from 5 percent) on personal sight deposits. In effective terms, the fall in time deposit rates was dampened, and the rise in the

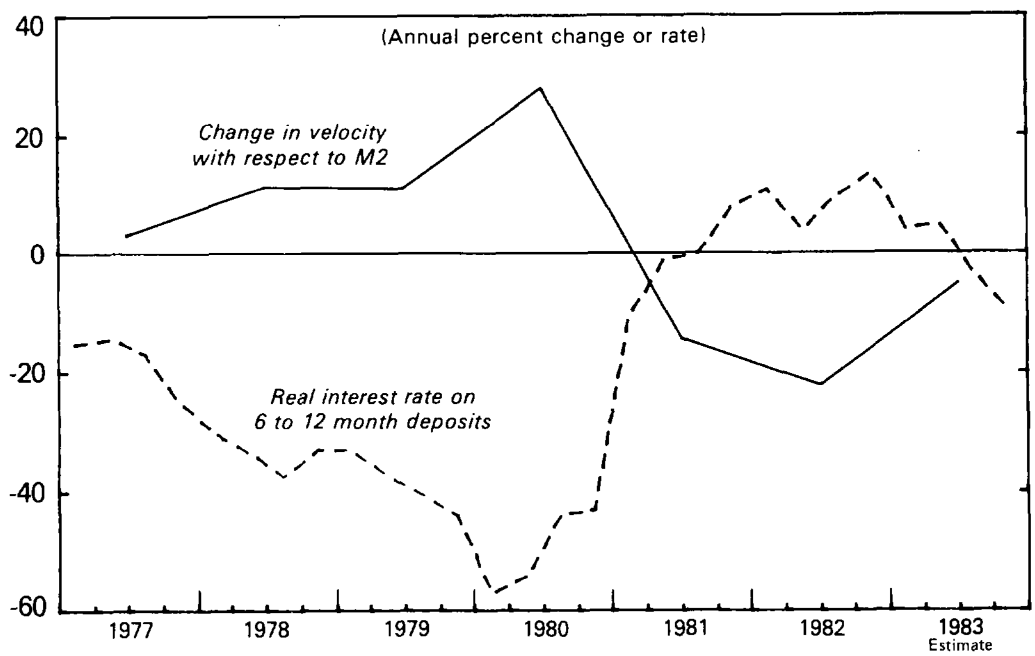
CHART 2

TURKEY

SELECTED MONETARY INDICATORS

(In billions of 1980 Turkish lira, seasonally adjusted)





Sources: Turkish authorities, and Fund staff estimates.

With the objective of phasing out the direct availability of Central Bank credit for export and certain investment purposes, preferential reserve requirement ratios were introduced for such credits extended by commercial banks. Meanwhile, in line with the differentiation of interest rates on bank deposits, reserves against time and commercial deposits earn an annual interest rate of nearly 40 percent, compared with a 6 percent rate on reserves against sight deposits; previously, 18 percent was paid on all reserves.

b. The 1984 program

The monetary program has been formulated on the basis of the official targets of 4.5 percent real growth, an average price increase of 29 percent, and a sharp increase to 6 percent in the average real effective interest rate on time deposits--to result from a decline in the rate of inflation during the year. In the absence of excess liquidity at the start of the program period, and of structural measures that may affect money demand, staff estimates suggest that the assumed macro-targets and real deposit rates would lead to a 38 percent average growth in the demand for broad money and thus to a 2 1/2 percent decline in income velocity. However, the program envisages a 31 percent annual increase in broad money (compared with a 41 1/2 percent increase last year), which implies a 2 1/2 percent rise in velocity. The reason for the latter is that the program allows for the absorption of the liquidity overhang by the second quarter, and provides a safety margin (i) to dampen the possible adverse consequence of the external liberalization measures on the balance of payments and (ii) to adjust for the increased efficiency in the use of financial resources due to the intended development of an interbank money market--for which the stage has been set with the cut in the transactions tax rate.

Lacking direct control on overall domestic bank credit, the targeted monetary expansion is to be attained through ceilings on the net domestic assets of the Central Bank. Net foreign assets of the Central Bank are forecast to rise by some US$320 million during the year (they fell by US$18 million in 1983). Thus, the Bank's net domestic assets are not to increase by more than LT 285 billion (compared with LT 343 billion in 1983). The average growth of reserve money is projected at 28 1/2 percent (46 percent in 1983), assuming a further increase to 2.35 in the reserve money multiplier (2.30 percent average in 1983). Net credit to the public sector is not to exceed LT 100 billion. The Government will consult with the Fund if the reserve money multiplier or the Central Bank's net foreign asset position deviate significantly from their assumed levels.

3. Public finances

The public sector borrowing requirement decreased from 6.0 percent of GNP in 1982 to 4.7 percent in 1983, continuing the decline from 12.0 percent in 1980 (Chart 3). This was possible because the borrowing requirement of the SEEs was reduced through higher sale prices and a reduction in their investment relative to GNP, and because the Government cut expenditure by more than the reduction in revenue. In 1984, the public sector borrowing requirement (PSBR) is expected to fall below 3.5 percent 1/ of GNP mainly due to a further improvement in the operational performance of the SEEs and the emergence of a small surplus in the consolidated budget.

a. The consolidated budget

In 1983, the decrease in revenue relative to GNP was again more than offset by a relative decrease in expenditure (Table 10). The budget deficit is estimated to have been as low as 0.5 percent of GNP in 1983, compared with 1.2 percent in 1982 and 4.6 percent in 1980. The cash account was in surplus in 1983 (0.4 percent of GNP) because of an increase in deferred payments. 2/ In 1984, the budget is projected to show a small surplus.

Total revenue decreased as a ratio of GNP from 21.2 percent in 1981 to 20.2 percent in 1982 and 19.0 percent in 1983. Underlying this trend is an increase in tax arrears, to more than LT 350 billion at the end of 1983, (3 percent of GNP) and a decrease in personal income tax liabilities relative to GNP. The downward revision of income tax rates designed to reduce the high average income tax rates that emerged when inflation accelerated and tax schedules remained unchanged lowered personal income tax revenues from 8.8 percent to 7.5 percent of GNP between 1981 and 1983. For 1984, the new Government has already announced changes that will result in a tax loss of LT 120 billion in 1984, of which LT 80 billion is due to a reduction in the transactions tax. However, other measures will raise an additional LT 180 billion. Improved tax collection and the sale of goods confiscated by the customs authorities, are expected to yield LT 130 billion. Initially, the authorities believed that a substantially larger amount might be raised by these means but they agreed that it would be prudent to opt for the lower figure, given the likely speed with which collections can be improved. An additional LT 50 billion will be raised through changes in the production tax, in motor vehicle fees, and in income taxation. Despite these measures, revenues will decrease to 18.3 percent of GNP in 1984. The new Government intends to reverse this development through major improvements over the next few years in the assessment and collection of taxes.

Total expenditures decreased from 21.4 percent of GNP in 1982 to 19.4 percent in 1983, continuing the decline from 24.0 percent in 1980.

1/ This assumes short-term borrowing of LT 330 million by the SEEs. Measures already taken to increase SEE prices and expected revenue and expenditure increases should reduce short-term borrowing significantly below the above amount. At present, the authorities' cannot quantify the net effect of the changes.

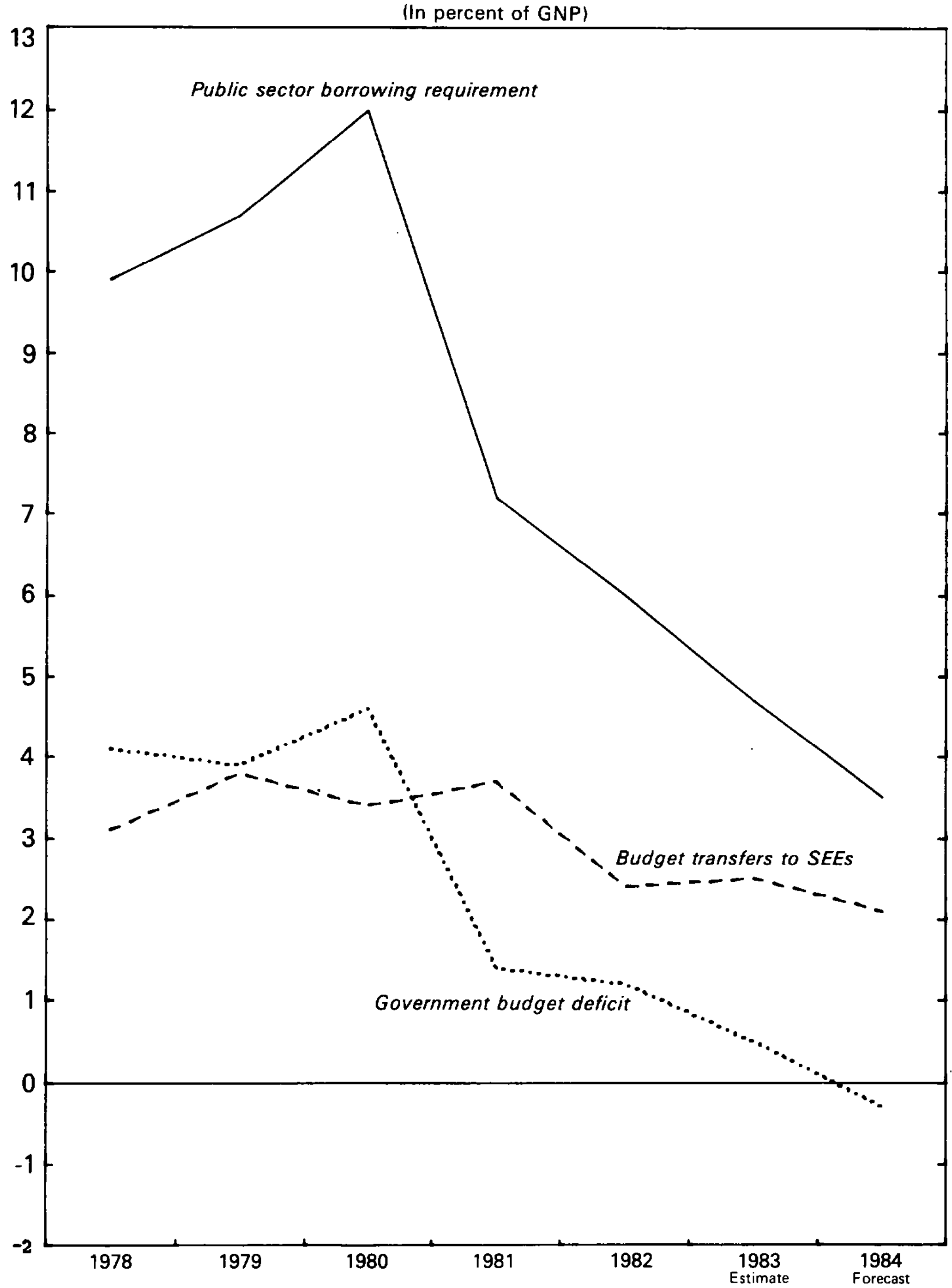
2/ The budget balance is shown on an accrual basis. However, while expenditures are recorded on an accrual basis, revenues are on a cash basis.

CHART 3

TURKEY

SELECTED PUBLIC SECTOR INDICATORS

(In percent of GNP)



Sources: Turkish authorities, and Fund staff estimates.

As in previous years, the decrease was mainly on account of personnel expenditures and transfer payments; investment expenditures increased substantially, due to increased investment in energy and infrastructure. In 1984, total expenditures are expected to decrease to 18 percent of GNP, taking into account reductions of LT 303 billion in appropriations that the new Government has decided upon. In addition, the Government has contingency plans for further expenditure cuts of LT 75 billion, which it will implement if necessary. As in earlier years, the decrease in expenditure in real terms is concentrated on personnel expenditures and transfer payments. Transfers to the SEEs will be limited to LT 330 billion in 1984, a real decrease of about 20 percent, taking into account that four enterprises that had been classified as decentralized government agencies in 1983 are now classified as SEEs.

b. State Economic Enterprises

The flexible, market-oriented pricing policy introduced in 1980, under which the SEEs mainly set prices in accordance with market principles, was maintained in 1983. Major price changes were announced in late 1983, but in the future small but more frequent changes in prices will be made. The SEEs' use of their pricing autonomy is reflected in the fact that, despite the unexpected acceleration in the rate of inflation during 1983, the deficit on the current operations relative to GNP increased only marginally and mainly on account of an increase in the duty losses that occur when the sale prices are deliberately set by the Government below cost for social reasons (Table 11). The efforts to improve the efficiency of the SEEs through structural measures were stepped up in 1983 (SM/83/114, 6/6/83).

The authorities continued to control SEE investment for demand management purposes and to reduce SEE involvement in manufacturing activities traditionally handled by the private sector. In 1983, the SEEs were again instructed to give priority to improved operational performance. In addition, a monetary ceiling was imposed on fixed investments except for those in the energy sector, where investment was subject to physical control. While this did not prevent the outlays for fixed investment from exceeding the earlier projection, these fell from 6.1 percent of GNP in 1982 to 5.8 percent in 1983, continuing the slow decrease since 1980. With the fairly rapid slowdown in the accumulation of stocks continuing, total investment was 6.9 percent of GNP in 1983, compared with 7.8 percent in 1982, and 10.4 percent in 1980. The financing requirement of the SEEs decreased to 6.8 percent, continuing the decline from 10.7 percent in 1980 that has contributed significantly to the decrease in the PSBR. In 1984, the profitability of the SEEs is to increase and both total and fixed investment are to decline further as percentages of GNP. The total financing requirement is forecast to decline to 5.9 percent of GNP.

4. External policies

A flexible exchange rate policy has been a key to strengthening external competitiveness. Since May 1981, the exchange rate has been adjusted frequently in small steps, based on relative price movements in Turkey and abroad and movements in other exchange rates. On the basis of an export-weighted basket, the real effective exchange rate of the Turkish lira remained broadly unchanged during 1983 (Chart 4).

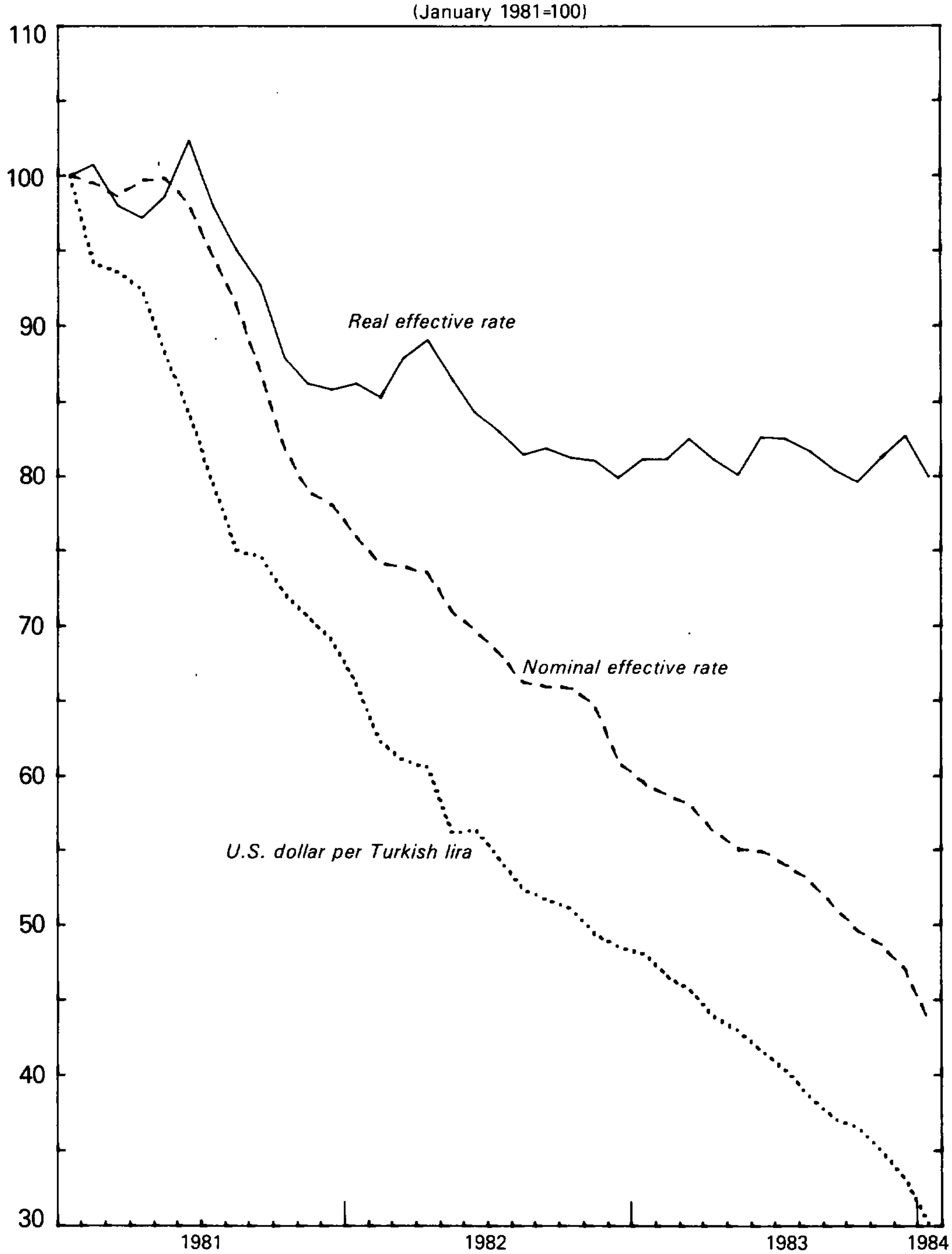
Since the beginning of 1984, and as part of a series of measures aimed at liberalizing the exchange and trade system, the mechanics of exchange rate determination have been modified to add more flexibility to the system. 1/ Under the new system, the official exchange rate is still determined daily by the Central Bank on the basis of other exchange rates and changes in domestic relative to foreign prices; actual transactions, however, take place at a rate which is set by commercial banks and is allowed to fluctuate within a band of $\pm$ 6 percent 2/ around the official rate. In practice, the above modification led to an effective one-step depreciation of the Turkish lira of about 6 percent early in 1984 since the banks depreciated their rates by the maximum amount permitted by the new margin. This and the continued adjustment of the official exchange rate resulted in a depreciation of the lira vis-à-vis the U.S. dollar of about 10 percent between end-1983 and end-January 1984.

Commercial banks have been given greater freedom to perform foreign exchange operations on their own account, being required to sell to the Central Bank only 20 percent of foreign exchange purchased; in addition, most foreign exchange operations have been transferred to commercial banks. The surrender requirement on export earnings has been lowered from 100 to 80 percent and that on invisible receipts has been eliminated; retained foreign exchange earnings may be deposited in foreign exchange accounts or transferred to other parties without restriction. Limitations on travel have been greatly reduced. The long-standing requirement that--in the case of imports with letters of credit--payment in Turkish liras be made when opening the letter of credit has been abolished. Foreign investment regulations have been simplified, and investment abroad by Turkish residents under any form can be undertaken with official authorization up to specified limits. Barriers on foreign borrowing by banks and enterprises have been considerably reduced. The authorities view these changes as a first major step toward the complete elimination of exchange controls over the medium term.

1/ Even though a number of exchange and trade measures were announced on December 29, 1983, foreign exchange operations were suspended until January 2, 1984. A detailed explanation of changes in the exchange and trade system is presented in Appendix III.

2/ Since early in February, a wider band (8 percent) is allowed for transactions in banknotes.

CHART 4
TURKEY
EXCHANGE RATE DEVELOPMENTS
(January 1981=100)



Sources: IMF, *International Financial Statistics,* and staff estimates.

Measures have been taken to open up the economy to foreign competition. On January 1, 1984 the import regime was considerably simplified and import restrictions sharply reduced. All goods may now be imported, except when explicitly prohibited or restricted; the new import regime 1/ contains: (i) a list of prohibited goods; (ii) a list of goods subject to licensing by the Undersecretariat of Treasury and Foreign Trade; and (iii) a list of goods ("Fund List") freely importable but subject to the payment of a specific tax besides customs duty. The bulk of items included in this list are luxury consumer goods. 2/ Imports of all goods not included in any of the above lists are freely permitted. On the basis of preliminary data on the value of import authorizations in 1983, about 75 percent of goods imported under special authorization (restricted imports) last year are now freely importable. Restricted imports in 1983 were about 70 percent of total imports. In addition, administrative procedures have been greatly simplified. Import guarantee deposits--ranging from 1 to 15 percent--remained basically unchanged. It had been intended to eliminate them at the end of 1983. The authorities wish to postpone this step to end-1984 because they believe it will be helpful to be able to monitor import orders under the greatly liberalized import system. To strengthen the negotiating position of Turkish enterprises vis-à-vis state trading agencies of countries where foreign trade is nationalized, imports from such countries may only be made by public sector agencies for their own needs, or by private firms with an annual export volume of at least US$50 million. Export procedures have been simplified and the number of goods subject to licensing has been narrowed. To improve resource allocation, the rates of tax rebates granted to exporters are scheduled to be reduced to 80 percent of their current level by April 1, 1984, and to 55 percent by September 1, 1984.

Custom tariffs and production tax rates have been changed. Duties on basic raw materials now generally range up to 15 percent, those on intermediate and semifinished goods vary between 10 and 30 percent, and on finished products between 30 and 40 percent. The authorities intend to continue the program of phasing out import licensing and replacing it with a rationalized tariff structure.

The Government remains cautious with respect to foreign borrowing. Limits have been established on the contracting of new nonconcessional public and publicly guaranteed foreign borrowing in the maturity range of 1-12 years. 3/ Even though short-term borrowing is not currently a source

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1/ More details of the number of tariff items in each list is given in Appendix III.

2/ Most of the proceeds from these surcharges are to be earmarked for the Housing Fund.

3/ Fund purchases and possible commitments for certain long-range projects (e.g., the Ataturk Dam) are excluded. Any contractions for such projects will be examined in the midterm review.

of concern, the increase in outstanding short-term debt of the nonfinancial public sector and the banking system will be limited to no more than US$500 million between end-1983 and end-1984. 1/

V. Proposed New Stand-By Arrangement and Performance Criteria

The new program is based on a set of policies having the same general character as those successfully implemented in 1980-82, involving firm demand management and continued structural reforms. A principal feature of the program is a substantial tightening of monetary policy through a return to positive real interest rates and a sharp reduction in lending by the Central Bank. Further improvement is planned in the fiscal sector, including a surplus in the consolidated budget and reduced reliance by the SEEs on budget transfers. On the structural side, the operations of the SEEs are being reorganized, with emphasis on more efficient management and flexible pricing policies. The external sector has been extensively liberalized and a flexible exchange rate policy is to ensure that the sector is competitive. The success of the program will, of course, depend upon the determination of the Government in implementing policies. In this regard, the staff notes that important elements in the program--particularly increases in interest rates and exchange rate action--have already been put in place.

The following performance criteria, of which the quantified components are set out in Table 12, are applicable for the proposed stand-by arrangement:

(1) Limits on the net domestic assets of the Central Bank with subceilings on Central Bank credit to the public sector through June 30, 1984, with indicative limits thereafter. Limits for the second half of 1984 will be established at a midterm review. These limits are combined with avoidance of new deficiencies in reserve requirement obligations of banks and the maintenance of the reserve requirements of commercial banks at existing levels of 25 percent for general deposits, 20 percent for deposits equivalent to export credits, and 15 percent for deposits equivalent to certain medium- and long-term investment credits.

(2) A limit on budgetary transfers to the SEEs.

(3) A limit on the contracting of new nonconcessional public or publicly guaranteed external debt, excluding purchases from the Fund, in the maturity range of more than 1 year and up to and including 12 years for the period ending December 31, 1984; a limit on the increase in 1984 of outstanding short-term debt of the nonfinancial public sector and the banking system, excluding normal trade credits, and certain foreign liabilities of the banking system such as those that are reserve-related and savings schemes for workers abroad.

1/ "Dresdner" deposits and similar deposits of workers abroad are excluded, as are pre-export credits through commercial banks and some minor Central Bank liabilities.

(4) The continuation of a flexible exchange rate policy under which the Central Bank will determine the buying rate of the lira applicable to nonbank transactions daily in the light of developments in international currency markets and in domestic relative to foreign prices, with the aim of improving further the existing external competitiveness.

(5) The elimination by December 31, 1984 of import guarantee deposits.

(6) The standard performance criterion on trade and payments restrictions.

A midterm review by the Fund in the second half of 1984 will examine developments and progress in implementing the program and at that time credit ceilings for the second half of the year will be established as performance criteria. Purchases subsequent to August 31, 1984 will be subject to the completion of the review.

VI. Staff Appraisal

Since the beginning of 1980, Turkey has been engaged in a sustained effort to stabilize the economy, supported by Fund stand-by arrangements. Until 1983, there was substantial success in stabilizing the economy and progress, although less so, in the gradual introduction of longer-term structural changes. In 1983, however, there was a serious setback, especially in price developments and the balance of payments. In December 1983, a newly elected Government took office. Since then it has re-established the stabilization effort, because it believes that a strengthening and a reorientation of policies will set the basis for sustained economic growth in an environment of domestic and external stability. The Government believes that further structural reforms are necessary and has already introduced significant new measures in the trade and payments system. To support its efforts, the Government requests the cancellation of the existing stand-by arrangement and its replacement by a new arrangement. The authorities have taken this course because of the failure in 1983 to implement the stand-by program and because the new policies represent such a substantial change from those that were advanced in support of the current stand-by arrangement.

The economic outturn in 1983 was clearly unsatisfactory. The sharp upward trends in the rate of inflation and the current account deficit of the balance of payments reversed the improvement that had taken place in these crucial areas in the preceding years. The deterioration can primarily be ascribed to a weakening of monetary policy. Partly because of domestic political reasons, the authorities did not carry out the credit policies established at the beginning of the year and by the end of the year monetary aggregates substantially exceeded targets. At the same time, real interest rates on deposits became sharply negative, reducing the demand for money and leaving a liquidity overhang at the end of the year. Fiscal policy was more successful and continued the trend of recent years under which the budget deficit, budget transfers to the SEEs, and the PSBR have declined as percentages of GNP. However, it remains disappointing that budget revenues continued to lag below expectations, despite the fact that in 1983 nominal incomes and expenditures were well above the original projections. The financial results of the SEEs were relatively encouraging and the determination of the new Government that they should implement more realistic pricing policies should be helpful.

The external accounts in 1983 deteriorated substantially, as the terms of trade again moved against Turkey, principally because of lower prices for primary commodity exports. Moreover, the volume of imports rose more than programmed and net invisible receipts declined as workers' remittances fell. Export receipts were relatively flat, reflecting weaker Middle East markets and lower prices. However, the growth in export volume was encouraging, particularly as exports to the industrial countries, where competition is strong, rose quite sharply, suggesting that Turkish exports remained competitive as a result of the flexible exchange rate policy.

Policies for 1984 are substantially different from those of 1983. The Government believes that a gradual increase in the domestic growth rate can be achieved only if inflation can be brought down sharply and the current account deficit reduced by a sustained rise in exports. These results are to be obtained through substantial progress in the direction of establishing a more market-oriented economy and a more open external sector, supported by appropriate incentives for exports and tight demand policies. In addition, the Government is convinced that a continuation of structural changes is necessary to improve economic efficiency. The staff fully supports this philosophy, which is in line with the views frequently expressed in the Executive Board and staff reports. For most of the postwar period, the Turkish economy had been inward-looking and based on import substitution in a highly protected domestic market, at the expense of an efficient and competitive export sector. The welcome change can, however, give rise to short-run problems that will require the authorities to be agile in their management of policy in the coming months. The new freedom to import could easily lead to a surge of imports, especially if domestic demand is not contained, and export growth could slow down if competitiveness is not maintained. Turkey cannot afford any further setback in the area of external adjustment. Indeed, an even larger decline than programmed in the current account deficit would be helpful in view of the substantially higher level of foreign debt repayments in the period 1985-87. Sustained improvement in the external accounts is necessary not only to contain gross borrowing requirements but also to maintain the supply of new loans through increasing confidence of foreign lenders. The authorities recognize that adequately tight demand management and external competitiveness are essential to success; the staff and the authorities intend to remain in close contact in the period immediately ahead in order to ensure that appropriate adjustments are made, if necessary, to financial policies to achieve these ends.

Fiscal policies aim at continuing the trend of reducing the relative size of the public sector and at bringing the consolidated budget into surplus. The SEEs are also to continue their improvement through pricing policy and better management, which should be reflected, inter alia, in further reduction in the real level of budget transfers. The staff believes these aims are achievable, although they will require resolute action that may necessitate politically difficult decisions. It is clear, for example, that budget policy can succeed only if the specified revenue measures are implemented effectively.

Monetary policy has been strengthened by the substantial increase in nominal interest rates, resulting in a welcome return to positive real levels, which in turn will increase significantly the demand for money. The intention to re-examine interest rates at least quarterly in the light of price developments and other relevant factors is to be welcomed. The credit program for 1984 further assumes that an improvement in the external sector will provide a substantial part of the liquidity requirements of the banking system with a correspondingly sharp reduction in the growth of Central Bank lending. The credit targets assume a further increase in the reserve money multiplier. The monetary projections are inevitably difficult to make in a year when virtually all elements of the sector are to change, when the rate of inflation is to be reduced sharply, and when there are necessarily some uncertainties about liquidity inflow through the balance of payments. Firm targets for monetary aggregates have been made for the first half of 1984 and incorporated as performance criteria in the stand-by arrangement. Developments for the second half will be examined again in the context of a midterm review. In the meantime, the staff has arranged to be in close contact with the authorities throughout the year, especially in the first half when the danger of a surge of imports cannot be ignored and when the first indications of a reversal of the adverse trends of 1983 should be appearing.

The extent of the move to external liberalization is major by any standard. Import liberalization is now the rule, not the exception; invisible transactions are now considerably freer and controls on both capital inflow and outflow have been eased. In addition, the systems of tariffs and import duties are being simplified and rationalized. The counterpart of this new freedom must be a sustained growth of exports. Action already taken has led to an important depreciation of the real effective exchange rate and the staff welcomes the intention of the authorities to continue with a flexible exchange rate policy. The liberalization substantially exceeds that foreseen when the current stand-by arrangement was approved in June 1983. In the light of this, the staff can accept the intention to extend the import deposit requirement, on the understanding that it will be eliminated by the end of 1984.

The medium-term foreign debt picture has changed since the last Board discussion to the extent that the worse-than-forecast current account result in 1983 increased future servicing. The manageability of the debt service obligations requires a sustained and substantial increase in exports; if this condition is met, a satisfactory growth of domestic output should be attainable, given that there has been an encouraging improvement in the way in which foreign lenders view Turkey. However, if that condition is not met, the authorities may well face the need to restrain domestic growth more than they wish in order to maintain external viability. Given that the scenarios already assume a quite rapid export growth, albeit at a slightly decelerating pace, it is quite possible that the authorities may have to accept less growth and more adjustment over the medium term.

The amount of the proposed stand-by arrangement is SDR 225 million (52.4 percent of quota) to be available in four equal installments, the final two conditional upon a midterm review. The proposed amount takes into account the outstanding use of Fund credit and allows for possible further Fund financing under present access limits. In the staff view, the amount of access is warranted by the strong adjustment measures already adopted and envisaged in the program, in particular the liberalization of the trade and payments system, and the need to increase the import coverage of reserves, which were less than six weeks at the end of 1983.

In the light of the foregoing, the following draft decision is proposed for adoption by the Executive Board:

I. Stand-By Arrangement

1. The Government of Turkey has requested a stand-by arrangement for the period of one year beginning April 1984 for an amount equivalent to SDR 225 million.

2. The Fund approves the stand-by arrangement attached to EBS/84/42 (3/7/84).

3. The Fund waives the limitation in Article V, Section 3(b)(iii).

4. In accordance with the request of the Government of Turkey, the stand-by arrangement approved by the Fund on June 24, 1983 is cancelled as of April .., 1984.

Table 1. Turkey: Selected Economic and Financial Indicators, 1981-84

	Actual 1981	Actual 1982	Estimate EBS/83/98 1983	Revised estimate 1983	Projection 1984
			(Annual percentage change, unless otherwise specified)		
National income and prices					
GNP at constant prices	4	4 1/2	4 3/4	3 1/4	4 1/2
GNP deflator	42	27 1/4	20	30	29
Wholesale prices	36 3/4	25 1/4	20	30 1/2	29
External sector (in U.S. dollars)					
Exports, f.o.b.	61 1/2	22 1/4	15	1	17 1/4
Imports, c.i.f.	13	-1	7 1/2	1 3/4	7 3/4
Non-oil imports, c.i.f.	25	1/2	13 1/2	7 1/2	14
Export volume	68 3/4	34	10 1/2	12 3/4	16 3/4
Import volume	11 1/2	7 3/4	7	9 1/4	8 3/4
Terms of trade (deterioration -)	-5 1/4	-3	3 1/4	-4	1 1/4
Nominal effective exchange rate (depreciation -)	-21	-25	...	-22	...
Real effective exchange rate (depreciation -)	-8	-11 3/4	...	-3 1/1	...
Government budget 1/					
Revenue, excluding grants	62	26 1/2	25 1/2	26	29 1/2
Total expenditures	39 1/2	25 3/4	21 1/2	22	24 1/2
Money and credit					
Domestic credit 2/	34 1/4	12 1/4	20 1/2	26 1/4	23
Public sector (net)	30 3/4	10	12 1/2	8 1/2	15 3/4
Private sector	39 1/2	15 1/4	35	53	30 1/2
Broad money (M2)	72 1/2	69 3/4	...	42	31 1/2
Velocity (GNP relative to M_2)	-14 1/4	-22	...	-5	2 1/2
Interest rate on time deposits 3/	37 1/2	37 1/2	32	30	37
			(In percent of GNP)		
Public sector borrowing requirement	7 1/4	6	4 1/4	4 3/4	3 1/2
Central government budget balance	-1 1/2	-1 1/4	-1/2	-1/2	1/4
Central government cash balance	--	-1 1/2	-3/4	1/2	1/4
Domestic financing	--	2	1 1/4	1/2	1 1/4
Foreign financing	--	-1/2	-1/2	-1	-1 1/2
Financing requirement of SEEs	9 1/2	7 1/4	6 1/4	6 3/4	6
Gross domestic investment	24 1/2	20	22 1/2	20 1/2	20 1/2
Gross domestic savings	20 1/2	17 3/4	21 1/4	16	18 1/2
External current account deficit	4	2 1/4	1 1/4	3 1/2	2 1/4
External debt, at year-end	28 1/2	33	...	35 4/	44 1/2
Debt service ratio 5/(in percent of foreign exchange earnings)	23 1/2	26 3/4	25	31	28 3/4
Interest payments (in percent of foreign exchange earnings)	15	16	12 3/4	15 1/2	13 1/2
		(In millions of SDRs, unless otherwise specified)			
Overall balance of payments	-55	251	350	-243	633
Gross official reserves (weeks of imports)	8	6	...	6	9
External payments arrears, at year-end	320	--	--	--	--

Sources: Turkish authorities; IMF Executive Board papers; and staff estimates.

1/ For 1981, fiscal-year data (March-February); for 1982, these data refer to the ten-month period March-December scaled up by 1.2; and for 1983 and 1984, calendar year.
2/ December over December of previous year; refers to domestic credit of Central Bank.
3/ Average effective interest rate on 6- to 12-month deposits.
4/ As of end-September 1983.
5/ After debt relief.

Table 2. Turkey: National Expenditure and Production

	Actual 1982	Actual 1980	Actual 1981	Actual 1982	1983 Estimate in EBS/83/98	1983 Preliminary Outturn	Forecast 1984
	(In billions of liras)	(Percentage change in volume from preceding year)					
Consumption	7,134.7	-3.4	0.6	3.5	4.3	4.2	3.9
Public	939.4	8.8	0.8	2.1	3.6	3.4	3.9
Private	6,195.3	-5.1	0.6	3.7	4.4	4.3	4.0
Fixed investment	1,646.9	-10.0	1.7	3.4	5.9	4.2	5.0
Public	1,005.5	-3.7	9.4	2.2	5.2	3.2	4.5
Private	641.4	-17.3	-8.8	5.4	7.0	5.7	5.7
Stockbuilding 1/	127.7	(3.9)	(0.7)	(-0.9)	(-0.1)	(-0.7)	(-0.2)
Total domestic demand	8,909.3	-1.2	1.6	2.4	4.3	3.5	3.5
Foreign balance 1/	-187.5	(0.2)	(2.5)	(2.1)	(0.4)	(-0.4)	(1.0)
GNP	8,721.8	-1.1	4.1	4.6	4.8	3.2	4.5
	(Share of GNP, in percent)						
Agriculture	19.3	1.7	0.1	6.5	3.4	-0.8	3.5
Industry	25.2	-5.9	7.2	4.6	5.5	6.6	6.6
Construction	4.1	0.8	0.4	0.5	) 4.9 (Construction and Services)	0.4	) 3.5 (Construction and Services)
Services	44.6	-0.3	5.4	4.6		3.7	
GDP at factor cost	93.2	-1.0	4.2	4.8	4.7	3.1	4.4
GNP at market prices	100.0	-1.1	4.1	4.6	4.8	3.2	4.5

Sources: State Planning Orgnaization; and IMF staff estimates.

1/ Contribution, in percentage points, to growth in GNP.

Table 3. Turkey: Price Developments

(Percent change over average for corresponding period of preceding year)

	Wholesale Prices 1/	Consumer Prices 2/		Implicit GNP Deflator
		General	Istanbul	
1978	52.6	...	45.3	43.7
1979	63.9	...	58.7	71.1
1980	107.2	...	110.2	103.8
1981	36.8	...	36.6	42.0
1982	25.2	...	30.9	27.3
1983	30.6	31.4	30.1	30.0 3/
1984 Forecast	29.0	...	...	29.0
1982 Q1	26.1	...	31.2	...
Q2	30.2	...	34.4	...
Q3	24.7	...	27.6	...
Q4	22.4	...	30.5	...
1983 Q1	24.6	29.0	27.6	...
Q2	25.8	29.7	25.1	...
Q3	31.8	30.5	29.5	...
Q4	39.0	35.8	38.1	...

Sources: Turkish authorities; and IMF staff estimates.

1/ Ministry of Commerce.
2/ State Institute of Statistics (new index 1978-79 = 100).
3/ Estimate.

Table 4. Turkey: Balance of Payments, 1981-84

(In millions of U.S. Dollars)

	1981	1982	1983 Estimate EBS/83/98	1983 Current estimate	1984 Projection
Trade balance	-4,230	-3,097	-2,800	-3,200	-2,900
Exports, f.o.b.	4,703	5,746	6,600	5,800	6,800
Imports, c.i.f.	-8,933	-8,843	-9,400	-9,000	-9,700
Balance on services and transfers	1,888	1,844	2,155	1,440	1,890
Workers' remittances	2,490	2,187	2,250	1,550	1,900
Interest payment (before debt relief)	-1,443	-1,565	-1,370	-1,420	-1,350
Tourism	277	262	275	300	325
Other services and transfers (net)	564	961	1,000	1,010	1,015
Current balance	-2,324	-1,252	-645	-1,760	-1,010
Capital account (long- and medium-term)	1,196	1,119	710	505	825
Project and suppliers' credits	642	754	875	600	900
Program loans	480	495	350	250	350
Private foreign capital 1/	129	90	130	130	175
Petroleum loans	--	25	--	--	--
Loans from banks	-35	20	235	285	500
Eurocurrency loans	(--)	(45)	(255)	(300)	(500)
Other	(-35)	(-25)	(-20)	(-15)	(--)
Special assistance under the auspices of the OECD	315	487	100	320	200
Debt repayments (before debt relief)	-1,185	-1,502	-1,980	-2,080	-1,880
Debt relief	850	750	1,000	1,000	580
Principal	(600)	(650)	(930)	(930)	(580)
Interest	(250)	(100)	(70)	(70)	(--)
Short-term credits, errors and omissions	1,057	410	325	995	850
Of which: Dresdner Bank deposits	108	344	...	440	400
SDR allocations	24	--	--	--	--
Overall balance	-65	277	390	-260	665
Financing	65	-277	-390	260	-665
Net use of Fund resources	335	205	135	190	-45
Increase in net official reserves other than arrears and IMF (-)	-270	-482	-525	70	-620

Sources: Turkish authorities; and Fund staff estimates.

1/ Includes imports with waiver.

Table 5. Turkey: Foreign Trade

	1980	1981	1982	Estimate 1983	Projection 1984
	(In millions of U.S. dollars)				
Exports, f.o.b.	2,910	4,703	5,746	5,800	6,800
Imports, c.i.f.	7,909	8,933	8,842	9,000	9,700
Oil and oil products	3,856	3,871	3,748	3,522	3,455
Non-oil	4,053	5,062	5,094	5,478	6,245
	(Percent change from previous year)				
Total exports					
Value	28.7	61.6	22.2	0.9	17.2
Price	16.1	-4.2	-10.8	-10.4	0.5
Volume	10.1	68.7	37.0	12.7	16.7
Total imports					
Value	56.0	12.9	-1.0	1.8	7.8
Price	58.0	1.2	-8.1	-6.8	-0.8
Volume	-1.3	11.6	7.7	9.2	8.7
Oil imports					
Value	125.9	0.4	-3.2	-6.0	-1.9
Price	83.2	14.6	-9.6	-12.0	-5.3
Volume	23.3	-12.4	7.1	6.8	3.6
Non-oil imports					
Value	20.6	24.9	0.6	7.5	14.0
Price	51.0	-10.9	-7.0	-3.0	2.0
Volume	-20.1	40.2	8.2	10.8	11.8
Terms of trade	-26.5	-5.3	-2.9	-3.9	1.3

Source: State Planning Organization

Table 6. Turkey: Outstanding External Disbursed Debt, 1979-83

(In millions of U.S. dollars; end of period)

	1979	1980	1981	1982	Preliminary Sept. 1983
			(By maturity)		
Total outstanding disbursed debt 1/	14,234	16,227	16,841	17,638	18,337
Medium- and long-term	10,638	13,722	14,667	15,474	15,838
Short-term	3,596	2,505	2,174	2,164	2,499
			(By borrower)		
Medium- and long-term					
Government 1/ (including SEEs)	7,047	10,197	11,199	12,170	12,438
Central Bank	3,232	3,307	3,227	3,074	3,157
Private sector	359	218	241	230	243
Short-term					
Government (including SEEs)	40	25	63	73	50
Central Bank	1,104	1,448	1,154	1,031	1,318
Private sector	2,452	1,032	957	1,060	1,207
			(By lender)		
Medium- and long-term					
Multilateral agencies	2,445	3,242	3,857	4,550	5,004
IMF	630	1,054	1,322	1,455	1,625
IBRD, IDA, IFC	1,180	1,438	1,783	2,115	2,436
European Investment Bank	471	447	427	420	400
European Resettlement Fund	148	253	287	384	414
Islamic Development Bank	16	35	23	117	73
OPEC Fund	--	15	15	40	40
Int. Fund for Agric. Development	--	--	--	19	16
Bilateral lenders	4,370	6,026	6,712	7,115	6,736
OECD countries	3,976	5,253	5,901	6,146	5,805
OPEC countries	55	392	449	587	524
Other countries	339	381	362	382	407
Commercial banks	3,464	3,436	3,257	3,229	3,505
Private lenders	359	1,018	841	580	593
Short-term					
Islamic Development Bank	40	25	63	73	50
Bilateral lenders	308	620	459	68	22
Commercial banks 2/	575	608	407	335	439
Private lenders 2/	2,673	1,252	1,245	1,688	1,988
Of which: deposits of citizens abroad 3/	(961)	(908)	(946)	(1,402)	(1,713)
			(By type of credit)		
Medium- and long-term					
Project and program credits	6,815	9,268	10,569	11,665	11,740
Eurocurrency loans	659	763	651	720	1,035
Rescheduled debt					
Convertible Turkish lira deposits	2,269	2,137	2,077	1,996	1,996
Bankers' credits	429	429	429	429	429
Third party reimbursement claims	107	107	100	84	45
Suppliers' arrears (NGTAs)	--	800	600	350	350
Private credits	359	218	241	230	243
Short-term					
Public sector					
Bankers' credits	18	10	--	--	2
Third party reimbursement claims	--	--	--	--	--
Overdrafts	244	254	69	48	157
Dresdner Bank program	344	365	473	817	1,064
Petroleum credits	308	620	459	68	22
Other 4/	230	224	216 5/	171	127
Private sector					
Convertible Turkish lira deposits	617	543	473	585	649
Acceptance credits	435	377	230	276	304
Pre-export financing	--	112	254	199	174
Suppliers' arrears (NGTAs)	1,400	--	--	--	--
			(In percent)		
Memorandum item:					
Ratio of total outstanding debt to GNP					
Including IMF	20.1	27.8	28.6	33.1	35.4
Excluding IMF	19.2	26.0	26.3	30.4	32.3

Source: Data provided by the Turkish authorities.
1/ Includes purchases from IMF.
2/ Includes acceptance credits and pre-export financing, which are estimated to be distributed equally between commercial banks and private lenders.
3/ Dresdner Bank program and convertible Turkish lira deposits.
4/ Includes short-term credits from Islamic Development Bank.
5/ Includes pre-export financing of $38 million.

Table 7. Turkey: Projected Debt Service Payments on Existing Medium- and Long-Term Debt, 1983-88 1/

(In millions of U.S. dollars)

	1984	1985	1986	1987	1988
International organizations,					
excluding IMF	439	497	586	666	680
Principal	207	264	316	366	405
Interest	232	233	270	300	275
Bilateral lenders					
OECD countries	834	822	747	688	607
Principal	601	624	579	548	495
Interest	233	198	168	140	112
Other countries	165	123	143	149	141
Principal	115	78	101	114	111
Interest	50	45	42	35	30
Commercial banks	656	1,093	396	843	760
Principal	302	793	669	684	667
Interest	354	300	227	159	93
Private sector	83	135	105	92	82
Principal	49	107	82	74	67
Interest	34	28	23	18	15
Debt service payments,					
excluding IMF	2,177	2,670	2,477	2,438	2,270
Principal	1,274	1,866	1,747	1,786	1,745
Interest	903	804	730	652	525
IMF 2/	386	403	443	405	280
Repurchases	221	263	336	339	248
Charges	165	140	107	66	32
Debt service payments,					
including IMF	2,563	3,073	2,920	2,843	2,550
Principal	1,495	2,129	2,083	2,125	1,993
Interest	1,068	944	837	718	557
Memorandum item:					
Debt relief	580	150	--	--	--
Principal	580	150	--	--	--
Interest	--	--	--	--	--

Sources: Data provided by the Turkish authorities; and Fund staff estimates.

1/ Projections are based on disbursed and undisbursed external debt as of September 30, 1983. The projections assume LIBOR of 10 percent for dollars, 5.25 percent for deutsche marks, and 3.25 percent for Swiss francs.

2/ Based on purchases outstanding as of November 30, 1983. SDR amounts converted to U.S. dollars at the rate of SDR 1 = US$1.05.

Table 8. Turkey: Monetary Developments and Program

	December 1982	EBS/83/98 Program 1/ December 1983	Actual December 1983	Proposed 1984 program: Performance criteria 1/ March	Performance criteria 1/ June	Indicative targets September	Indicative targets December
	(In billions of Turkish lira at end of period) 2/						
Broad money (M2)	2,306	... 3/	3,018	3,280	3,480	3,730	3,940
Reserve money	943	1,181	1,282	1,396	1,481	1,587	1,677
Central Bank's net foreign assets	-39	11	-43	-24	-8	41	67
Central Bank's net domestic assets	982	1,170	1,325	1,420	1,489	1,546	1,610
Credit to public sector, net	585	657	634	680	696	714	734
Credit to private sector	395	533	604	653	706	745	789
Other items, net	2	-20	87	87	87	87	87
	(Percent change from corresponding period of previous year)						
Broad money (M2)	62	... 3/	31	31	31	31 1/2	30 1/2
Reserve money	47	25	36	31	32	23	31

Sources: Turkish authorities; and Fund staff estimates.

1/ Ceilings apply to net domestic assets and credit to the public sector.
2/ All figures refer to last Friday of the month, except next to last Friday in December.
3/ Program target was formulated in terms of M2A (equivalent to M2 less certificates of deposits).

Table 9. Turkey: Selected Interest Rates

(In percent per annum)

	End-December 1980	End-December 1981	End-December 1982	January 1 1983	June 1 1983	January 1 1984
Central Bank						
Interest on required reserves						
Sight deposits	10	20	12	18	18	6
Time deposits	16	26	18	18	18	39.6
Discounts and advances						
Short-term rates						
General	26	31.5	31.5	31.5	28	49.5
Agriculture	19.5	20	18	18	18	24.2
Exports	17.8	27	31.5	31.5	26.5-30	35
Long-term rate						
General	28.5	32.8	32.8	32.8	32.8	32.8
Commercial banks						
Deposit rates						
Personal sight deposits	5	5	5	20	20	5
Other sight deposits	0	0	0	0	0	5
Time deposits (6 to 12 months)	15	50	50	40	35	47
Time deposits (12 months)	33	50	50	45	40	45
"Scheduled" lending rates						
Short-term rates						
General	31	36	36	36	32	50
Agriculture	22	22	20	20	20	27.5
Exports	22	27	31.5	31.5	26.5-30	35
Long-term rates						
General	36	41	41	41	34	52
Agriculture	24	24	22	22	22	28
Memorandum items:						
Effective 6-month deposit rate 1/	12	37.5	37.5	32	28	42
Effective cost of borrowing 2/						
Long-term, general	75	74	70	...	...	60
Exports	25	32	40	...	...	...

Sources: Central Bank of Turkey; and Fund staff estimates.

1/ After deduction of withholding tax.

2/ Estimates include, in addition to the "scheduled" rate, net contribution to Interest Rate Rebate Fund, transactions tax, bank commission, and required compensatory balances.

Table 10. Turkey: Consolidated Central Government Budget 1/

(In billions of Turkish liras)

	1980	1981	1982	1983 Estimate EBS/83/98	1983 Current Estimate	1984 Projection
Revenues	857	1,389	1,466	2,205	2,217	2,870
Direct taxes	471	768	826	1,242	1,155	...
Indirect taxes	279	423	477	738	757	...
Nontax revenues	107	199	162	225	305	...
Expenditures	1,063	1,482	1,552	2,265	2,270	2,825
Personnel	335	390	425	630	640	770
Other current	162	255	275	425	425	580
Investment	107	290	338	530	525	715
Transfers to SEEs	213	214	233	292	292	330
Other transfers	186	333	281	388	388	430
Budget balance	-206	-93	-87	-60	-53	45
Increase in accounts payable, net	16	86	-29	-30	95	--
Cash balance	-190	-7	-116	-90	42	45
Financing	190	7	116	90	-42	-45
Foreign borrowing, net	7	12	-45	-50	-104	-230
Domestic borrowing, net	183	-5	161	140	62	185
Central Bank	109	53	32	35	70	85
Other	74	58	129	105	-8	100
Memorandum items:						
(In percent of GNP):						
Revenues	19.3	21.2	20.3 2/	20.2	19.0	18.3
Expenditures	24.0	22.6	21.5 2/	20.8	19.4	18.0
Of which:						
Transfers to SEEs	(4.8)	(3.3)	(2.2) 2/	(2.7)	(2.5)	(2.1)
Budget balance	-4.6	-1.4	-1.2 2/	-0.6	-0.5	0.3
Cash balance	-4.3	-0.1	-1.6 2/	-0.8	0.4	0.3

Source: Turkish authorities; and staff estimates.

1/ For 1980 and 1981, fiscal year data (March-February); for 1982, the data refer to ten 10-month periods March-December only; for 1983 and 1984, calendar year.

2/ For comparative purposes, the 10-month data have been multiplied by 1.2, but transfers to the SEEs have been estimated separately.

Table 11. Turkey: Operations of the State Economic Enterprises

(In billions of Turkish lira)

	1980	1981	1982	1983 Estimate EBS/83/98	1983 Current Estimate	Projection 1984 1/
Sales revenues	1,146	1,767	2,650	3,285	3,403	4,940
Current expenditures	1,184	1,800	2,640	3,297	3,455	4,900
Wages and salaries	238	314	370	470	458	645
Purchases of goods and services	898	1,390	2,135	2,248	2,785	3,983
Taxes	15	41	57	80	104	126
Other	33	55	78	99	108	146
Profit on current operations	-38	-33	10	-12	-52	40
Capital expenditures	459	616	684	752	809	1,091
Fixed investment	281	406	533	625	678	863
Increases in stocks	178	210	151	127	131	228
Depreciation	23	28	48	80	67	126
Overall surplus	-474	-621	-626	-684	-794	-925
Total financing	474	621	626	684	794	925
Budgetary transfers	149	241	205	292	292	330
Transfers from Price Stabilization Fund	30	74	76	79	97	120
Borrowing from Central Bank	50	32	31	8	-3	-7
State Investment Bank	16	16	59	14	28	76
Foreign borrowing 2/	67	122	104	120	139	76
Short-term borrowing	161	136	151	171	241	330
Memorandum items:						
Duty losses 3/	75	111	107	109	175	212
Profit on current operations after compensation for duty losses	37	78	117	97	123	252
			(In percent of GNP)			
Profit on current operations	-0.9	-0.5	0.1	-0.1	-0.4	0.3
Profit on current operations after compensation for duty losses	0.8	1.2	1.3	0.9	1.1	1.6
Total investment	10.4	9.4	7.8	6.9	6.9	6.0
Fixed investment	6.3	6.2	6.1	5.7	5.8	5.5
Overall surplus	-10.7	-9.5	-7.2	-6.3	-6.8	-5.9

Sources: Turkish authorities; and staff estimates.

1/ Four government enterprises that had been classified as decentralized government agencies in 1983 are classified as SEEs in 1984.
2/ Including lira counterpart of IBRD structural adjustment loans.
3/ Losses resulting from the retention of price controls by the government for social reasons.

Table 12. Turkey: Quantitative Performance Criteria

	Net Domestic Assets of the Central Bank	Net Central Bank Credit to the Public Sector
	Limit	
	(In billions of Turkish liras)	
A. Credit ceilings		
1984 January-March 1/	1,400	675
March 2/	1,420	680
April-June 1/	1,459	685
June 2/	1,489	696
July-September 1/3/	1,540	705
September 2/3/	1,546	714
October-December 1/3/	1,578	725
December 2/3/	1,610	734
	Limit	
B. Budgetary transfers to SEEs		
1984 January-December	330	
	Limit	
	(In billions of U.S. dollars)	
C. Contracting of new nonconcessional public and publicly guaranteed foreign borrowing with a maturity range of more than 1 year and up to and including 12 years		
1984 January-December	1.5	
D. Increase in outstanding foreign borrowing of the nonfinancial public sector and banking sector of up to and including one year		
Change end-December 1983 to end-December 1984	0.5	

Source: IMF staff.
1/ Average of last reporting date in each month.
2/ Average of each weekly reporting date during the month.
3/ Targets, not performance criteria. Latter will be established at mid-term review.

Table 13. Turkey: Synthesis of Main Program Relationships and Assumptions

	Preliminary Outcome 1983	Projection 1984
	(In millions of U.S. dollars)	
Increase in foreign reserves (-)	70	-620
Net purchases from IMF	190	-45
Overall external deficit (+)	260	-665
Plus capital inflows	1,500	1,675
Current account deficit	1,760	1,010
Plus exports	5,800	6,800
Plus net invisibles	1,440	1,890
Program imports	9,000	9,700
	(Annual percentage change, unless otherwise indicated)	
Total value of imports	1 3/4	7 3/4
Import prices	-6 3/4	-3/4
Import volume	9 1/4	8 3/4
Real GNP	3 1/4	4 1/2
GNP deflator	30	29
Nominal GNP	34	34 3/4
Velocity of M2	-5	2 1/2
Broad money (M2)	42	31 1/2
Reserve money	46	29
Reserve money multiplier (level)	2.30	2.35
Effective interest rate on 6- to 12-month deposits (average annual rate)	30	37
	(In billions of Turkish liras)	
Change in reserve money	339	395
Change in Central Bank net foreign assets	-4	110
Change in NDA of Central BAnk	343	285

Source: IMF staff.

Turkey: Stand-By Arrangement

Attached hereto is a letter dated ...., 1984 from the Minister of State and Deputy Prime Minister of Turkey, requesting a stand-by arrangement and setting forth the objectives and policies that the authorities of Turkey intend to pursue for the period of this stand-by arrangement, and understandings of Turkey with the Fund regarding a review that will be made of the progress in realizing the objectives of the program and of the policies and measures that the authorities of Turkey will pursue for the remaining period of this stand-by arrangement.

To support these objectives and policies, the International Monetary Fund grants this stand-by arrangement in accordance with the following provisions:

1. For the period of one year from April .., 1984, Turkey will have the right to make purchases from the Fund in an amount equivalent to SDR 225 million, subject to paragraphs 2, 3, 4, and 5 below, without further review by the Fund.

2. a. Purchases under this arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 56.25 million until July 27, 1984, the equivalent of SDR 112.5 million until October 26, 1984, and the equivalent of SDR 168.75 million until February 22, 1985.

b. None of the limits in (a) above shall apply to a purchase under this stand-by arrangement that would not increase the Fund's holdings of Turkey's currency in the credit tranches beyond 25 percent of quota.

3. All purchases under this stand-by arrangement shall be made from ordinary resources.

4. Turkey will not make purchases under this stand-by arrangement that would increase the Fund's holdings of Turkey's currency in the credit tranches beyond 25 percent of quota:

a. during any period in which the data at the end of the preceding period indicate that:

(i) the limit on net domestic assets of the Central Bank referred to in paragraph 13 of the attached letter and specified in the table annexed to that letter; or

(ii) the limit on net Central Bank credit to the public sector referred to in paragraph 13 of the attached letter and specified in the table annexed to that letter had not been observed; or

b. if the limit on budgetary transfers to State Economic Enterprises referred to in paragraph 15 of the attached letter is not observed; or

c. if the understandings with regard to the exchange rate of the lira referred to in paragraph 8 of the attached letter are not observed; or

d. if the understandings with regard to the maintenance of the reserve requirement ratio of the commercial banks and the avoidance of new deficiencies in reserve requirements, both referred to in paragraph 13 of the attached letter are not being observed; or

e. if the limit on the contracting of new nonconcessional public and publicly guaranteed external debt in the maturity range of more than 1 and up to and including 12 years described in paragraph 9 of the attached letter is not observed; or

f. if the limit on the increase in outstanding foreign debt of the nonfinancial public sector and the banking system of up to and including one year described in paragraph 9 of the attached letter is not observed; or

g. during the period after August 15, 1984 until the policies of the program have been reviewed by the Fund and suitable performance criteria with respect to net domestic assets of the Central Bank and net Central Bank credit to the public sector for the second half of 1984 have been established in consultation with the Fund as contemplated by paragraph 16 of the attached letter, or, after such performance criteria have been established, while they are not being observed; or

h. after December 31, 1984, if the understanding with regard to import guarantee deposits described in paragraph 10 of the attached letter is not observed; or

i. during the entire period of this stand-by arrangement if Turkey

(i) imposes or intensifies restrictions on payments and transfers for current international transactions; or

(ii) introduces multiple currency practices; or

(iii) concludes new bilateral payments agreements which are inconsistent with Article VIII; or

(iv) imposes or intensifies import restrictions for balance of payments reasons.

When Turkey is prevented from purchasing under this stand-by arrangement because of this paragraph 4, purchases will be resumed only after consultation has taken place between the Fund and Turkey and understandings have been reached regarding the circumstances in which such purchases can be resumed.

5. Turkey's right to engage in the transactions covered by this stand-by arrangement can be suspended only with respect to requests received by the Fund after (a) a formal ineligibility, or (b) a decision of the Executive Board to suspend transactions, either generally or in order to consider a proposal made by an Executive Director or the Managing Director, formally to suppress or to limit the eligibility of Turkey. When notice of a decision of formal ineligibility or of a decision to consider a proposal is given pursuant to this paragraph 5, purchases under this arrangement will be resumed only after consultation has taken place between the Fund and Turkey and understandings have been reached regarding the circumstances in which such purchases can be resumed.

6. Purchases under this stand-by arrangement shall be made in the currencies of other members selected in accordance with the policies and procedures of the Fund, and may be made in SDRs if, on the request of Turkey, the Fund agrees to provide them at the time of the purchase.

7. Turkey shall pay a charge for this stand-by arrangement in accordance with the decisions of the Fund.

8. a. Turkey shall repurchase the outstanding amount of its currency that results from a purchase under this stand-by arrangement, in accordance with the provisions of the Articles of Agreement and decisions of the Fund, including those relating to repurchases as Turkey's balance of payments and reserve position improves.

b. Any reductions in Turkey's currency held by the Fund shall reduce the amounts subject to repurchase under (a) above in accordance with the principles applied by the Fund for this purpose at the time of the reduction.

9. During the period of the stand-by arrangement, Turkey shall remain in close consultation with the Fund. These consultations may include correspondence and visits of officials of the Fund to Turkey or of representatives of Turkey to the Fund. Turkey shall provide the Fund, through reports at intervals or dates requested by the Fund, with such information as the Fund requests in connection with the progress of Turkey in achieving the objectives and policies set forth in the attached letter.

10. In accordance with paragraph 16 of the attached letter, Turkey will consult the Fund on the adoption of any measures that may be appropriate at the initiative of the Government or whenever the Managing Director requests consultation because any of the criteria in paragraph 4 above have not been observed or because he considers that consultation on the program is desirable. In addition, after the period of the stand-by arrangement and while Turkey has outstanding purchases in the upper credit tranches, the Government will consult with the Fund from time to time, at the initiative of the Government or the request of the Managing Director, concerning Turkey's balance of payments policies.

Turkey: Fund Relations
(As of March 31, 1984, unless otherwise indicated for specific items)

I. Membership Status

(a) Date of membership: March 11, 1947

(b) Status: Article XIV

(A) Financial Relations

II. General Department (General Resources Account)

(a) Quota: SDR 429.1 million

(b) Total Fund holdings of Turkish liras: SDR 1,850.14 million (431.2 percent of quota)

(c) Fund credit: SDR 1,453.31 million (338.7 percent of quota)
Of which: Under tranche policies: SDR 1,417.50 million (330.3 percent of quota)
CFF: SDR 35.81 million (8.3 percent of quota)

(d) Reserve tranche position: SDR 32.3 million

III. Current Stand-By

(a) Current stand-by
(i) Duration: from June 24, 1983 to June 23, 1984
(ii) Amount: SDR 225 million
(iii) Utilization: SDR 56.25 million
(iv) Undrawn balance: SDR 168.75 million

(b) Previous stand-by arrangements approved during the last ten years:
(i) Two-year stand-by arrangement in the amount of SDR 300 million approved on April 24, 1978. Utilization: SDR 90 million; cancelled on July 19, 1979.
(ii) One-year stand-by arrangement in the amount of SDR 250 million approved on July 19, 1979. Utilization: SDR 230 million; cancelled on June 17, 1980.
(iii) Three-year stand-by arrangement in the amount of SDR 1,250 million approved on June 18, 1980. Fully disbursed; completed as planned.

IV. SDR Department

(a) Net cumulative allocation: SDR 112.3 million (as of February 26, 1983).

(b) Holdings: SDR 0.03 million.

(B) Nonfinancial Relations

V. Exchange rate arrangement: flexibly managed floating exchange rate. Unapproved exchange practices subject to Article VIII, Sections 2 and 3: bilateral payments agreement with Iran.

VI. Last Article IV consultation and the request for the current stand-by arrangement was discussed by the Board on June 24, 1983 (EBS/83/98); the Board approved the stand-by arrangement and a waiver of Article V, Section 3(b)(iii). Turkey is on the 12-month consultation cycle.

VII. Technical assistance:

CBD: An advisor provided since July 1983 for one year to assist in the development of an external debt management system in cooperation with the World Bank. A second advisor was made available for three months to provide statistical support in the same area.

Table 14. Turkey: Fund Position During Period of Arrangement

	Estimated outstanding on March 31, 1984	Apr.-June 1984	July-Sept. 1984	Oct.-Dec. 1984	Jan.-Mar. 1985
		(In millions of SDRs)			
Transactions under tranche policies (net) 1/		19.49	5.51	6.99	-6.99
Purchases		56.25	56.25	56.25	56.25
Ordinary resources		(56.25)	(56.25)	(56.25)	(56.25)
Borrowed resources		(--)	(--)	(--)	(--)
Repurchases		36.76	50.74	49.26	63.24
Ordinary resources		(13.74)	(13.75)	(13.75)	(13.75)
Supplementary finance resources		(23.02)	(36.99)	(35.52)	(49.49)
Transactions under special facilities (net) 2/		-8.95	-8.95	-8.95	-8.95
Purchases		--	--	--	--
Repurchases		8.95	8.95	8.95	8.95
Total Fund credit outstanding (end of period)	1,453.31	1,463.85	1,460.41	1,458.45	1,442.50
Under tranche policies 1/	1,417.50	1,436.99	1,442.50	1,449.49	1,442.50
Special facilities 2/	35.81	26.86	17.91	8.96	--
		(As percent of quota)			
Total Fund credit outstanding (end of period)	338.7	341.2	340.3	339.9	336.2
Under tranche policies 1/	330.3	334.9	336.1	337.8	336.2
Special facilities 2/	8.4	6.3	4.2	2.1	--

Source: International Monetary Fund.

1/ Ordinary and borrowed resources.
2/ Compensatory financing facility.

Changes in Turkey's Exchange and Trade System

On December 29, 1983 operations in foreign exchange were suspended until January 2, 1984 and a series of changes in the exchange and trade system were announced. Further measures were enacted during January 1984, as the authorities clarified--and sometimes rectified slightly--some of the original measures. The following are the most important changes.

1. Exchange arrangement

Under the new system, the official exchange rate for the Turkish lira continues to be established daily by the Central Bank of Turkey on the basis of developments in foreign currency markets and in domestic relative to foreign prices. However, no transactions take place at this rate. Commercial banks are authorized to set up their own buying and selling exchange rates within a band of ± 6 percent 1/ around the official or "central" rate of the Central Bank; the spread between the buying and selling rates of a commercial bank cannot exceed 2 percent. To ensure the smooth functioning of the new system, the Central Bank has introduced an interbank market for foreign exchange. An interbank rate (set on the basis of the rates of the leading commercial banks) is announced on several occasions during the day by the Central Bank; the interbank buying and selling rates are set with a spread of one percent. Transactions between the Central Bank and the commercial banks take place at the interbank buying and selling rates, which also serve as indicators for transactions between commercial banks. In addition, transactions between the Central Bank and the nonbank sector (including the Government) take place at buying and selling rates set between the buying and selling rates of the interbank market and of the leading commercial banks. As an example, on January 16, 1984 exchange rates in terms of U.S. dollar were as follows:

1. Central Bank - central rate: LT 294.20 = US$1

2. Central Bank (interbank rate) - buying: LT 306.90 = US$1
   selling: LT 310.57 = US$1

3. Central Bank (other transactions) - buying: LT 306.90 = US$1
   selling: LT 311.20 = US$1

4. Commercial banks - buying: LT 305.96 = US$1
   selling: LT 312.08 = US$1.

2. Administration of control and general provisions on foreign and domestic currency

The administration of exchange and trade controls has been centralized in the Undersecretariat of Treasury and Foreign Trade. Some of

1/ Since early February, a wider band of ± 8 percent is permitted for transactions in bank notes.

its functions in the area of exchange regulations have been delegated to the Central Bank. Prior import authorization by different Ministries has been eliminated.

The ban on the use of foreign currencies in transactions has been lifted. Commercial banks are entitled to perform on their own account any foreign exchange operation not reserved explicitly for the Central Bank, and limits on the bank's foreign exchange position have been abolished. Commercial banks are required under the new system to sell to the Central Bank the equivalent of only 20 percent of all foreign exchange purchases. Turkish residents are now entitled to hold foreign exchange, to open accounts denominated in foreign exchange in commercial banks, and to dispose freely of those holdings. The limit on the import of Turkish bank notes and coins has been eliminated, and that on the export of Turkish bank notes and coins has been raised from the equivalent of US$100 to US$1,000.

3. Imports and import payments

Since the beginning of 1984, all goods are freely importable, except those explicitly prohibited or subject to licensing; by comparison, previously only goods included in two lists (Liberalized list I and Fund list) could be freely imported. The 1984 import regime contains three lists: (1) the first list, or "Negative" list, containing items under 207 tariff lines (originally 220, but items under 13 tariff lines were later on excluded), consists of articles whose importation is prohibited; it is mostly composed of foodstuffs, leather and leather goods, textiles and clothing, and other finished products. Except for narcotics, weapons and ammunitions, the importation of goods included in this list may be authorized on a case-by-case basis when used in production for export; (2) the second list, containing items under 423 tariff lines (originally 369, but items under 54 tariff items were added after mid-January), is composed of goods which can be imported only with specific licensing by the Undersecretariat of Treasury and Foreign Trade; it mostly includes raw materials, parts, intermediate goods and tools for industry, and some electrical equipment; and (3) the third list of "Fund" list, containing items under 90 tariff lines (originally 77, but increased in mid-January) consists of goods whose importation is free after payment of a specific levy in addition to custom duties; it is made up of luxury consumer goods. The importation of all goods not included in any of the above lists is freely permitted with payment of custom duties. On the basis of preliminary data on the value of import authorizations in 1983 (US$8.5 billion), 1/ about 75 percent of imports which under the previous import regime were subject to specific licensing are now freely importable. Import licensing procedures were simplified; all licenses are now granted by the Undersecretariat of Treasury and Foreign Trade and access to foreign exchange is open to duly registered importers once the import authorization--in the case of restricted imports--is approved, and the

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1/ The difference between import authorizations and actual imports in 1983 is primarily due to an excessive level of import authorizations for crude oil in 1982, part of which were used in crude oil imports of 1983.

corresponding prior import deposit (up to 15 percent of import value) is made. In the case of imports of freely importable goods made by exporters with own foreign exchange funds deposited with commercial banks, the prior import deposit is not required. Restrictions on means of import payment were reduced in conjunction with the expanded role of commercial banks in foreign trade operations. The requirement to prepay in local currency the equivalent of the foreign exchange for which a letter of credit has been opened--as well as the requirement to deposit 20 percent of the local currency counterpart of the consignment at the time of applying for an import license in the case of payment against goods--was eliminated. Regulations for imports with waiver were also simplified. On the other hand, imports from countries where foreign trade is nationalized may only be carried out by the public sector (for its own needs), or by companies with an annual volume of exports of at least US$50 million.

Import duties and production tax rates were also modified. Custom duties now generally range up to 15 percent in the case of raw materials, between 10 and 30 percent for intermediate and semifinished products, and between 30 and 40 percent for finished goods. Higher duties apply in the case of a number of luxury consumer goods.

4. Payments for invisibles

Access to foreign exchange for invisible payments was also liberalized considerably, and a number of transactions are now handled by commercial banks without need for specific Central Bank authorization. The following operations remain subject to specific licensing by the Central Bank: business expenses of Turkish firms abroad, transfers related to copyrights for scientific and artistic works (up to US$10,000 may be provided in advance), proceeds of foreign air transportation companies, payments expenses, revenues of foreign consulates, and government expenses. All other transactions may be carried out by commercial banks, in some cases within general limits established by the Central Bank.

Limitations on tourist travel--one trip per person every two years (two trips per person per year to Cyprus)--were eliminated. All resident Turkish nationals may now travel abroad without proof of exchange allocation by commercial banks. Banks are allowed to allocate up to US$1,000 per person per trip 1/ for tourist travel, and US$2,000 per person per trip for business travel. Foreign citizens residing in Turkey may be allocated up to US$200 per person per trip for travel abroad.

5. Exports, export receipts, and receipts from invisibles

Regulations concerning exports were simplified, and the list of exports subject to license was reduced to only 11 items. As a means of facilitating exports to countries where foreign trade is nationalized, export companies allowed to import from those countries are permitted

1/ US$500 per person per trip for travelers under 18 years of age. Also, no foreign exchange is allocated for travel to the Turkish Republic of North Cyprus.

to engage in barter trade on a voluntary basis. Tax rebates granted to exports are scheduled to be reduced to 80 percent of present rates as of April 1, 1984 and to 55 percent as of September 1, 1984.

The surrender requirement of foreign exchange earnings was reduced from 100 percent to 80 percent of receipts in the case of merchandise exports, and was altogether eliminated in the case of receipts from invisibles. Foreign exchange not surrendered may be deposited with commercial banks or freely transferred to other parties.

6. Capital

Regulations on foreign investment in Turkey were simplified. Investments abroad by Turkish residents (in cash or kind) up to US$2 million may take place with authorization of the Undersecretariat of Treasury and Foreign Trade; higher accounts may be authorized by the Council of Ministers.

The ability of commercial banks to borrow abroad has been expanded, and banks are now allowed to open foreign exchange deposit accounts as well as convertible lira deposit accounts in favor of residents and non-residents. Interest and other costs in foreign exchange operations are fully negotiable, and the transfer abroad of such costs are to be financed from the bank's own resources. Exchange rate and interest rate guarantee schemes for specific types of foreign borrowing were eliminated. The Central Bank will continue to supervise foreign borrowing operations of banks.

Turkey: Medium-Term Scenarios for External Debt and Balance of Payments

1. Summary and implications

In order to evaluate the compatibility of an adequate medium-term growth rate and a viable external debt and payments position, several alternative scenarios have been simulated over the period 1984-88 on the basis of a computational model. 1/ The results of three alternative scenarios are presented in Table 15: an "adjustment" scenario predicated on an external current account brought into equilibrium by 1988; a "growth" scenario that assumes a 5.5 percent yearly real GNP growth rate considered necessary to prevent an increase in the unemployment rate; and a mixed scenario that combines features of the two other scenarios through a considerably less ambitious external adjustment process.

The scenarios suggest that largely as a result of slippages in the 1983 economic performance, Turkey's medium-term outlook has deteriorated significantly in comparison with similar scenarios prepared last year. Under any plausible scenario, in 1985 the debt service ratio will be close to 33 percent given the bunching of maturities from previous debt rescheduling agreements. At the end of 1988, even with full adjustment to current account balance, the debt outstanding will be above US$20 billion, while the debt service ratio would remain at 24 percent. Alternatively, adherence to a 5.5 percent target growth rate would lead to a rise in the current account deficit to US$1.3 billion, and an external indebtedness of US$24 billion--reflecting an increase in real terms.

Admittedly, these calculations are merely illustrative, in view of data limitations, as well as assumptions regarding the structure of the economy over the scenario period. However, by the same token, they have certain implications precisely in the area of structural reform. In particular, it can be argued that the trade-off between growth and external equilibrium could be relaxed significantly over the medium term through a stepped-up outward orientation of the economy. To this end, in addition to reliance on existing policy measures aimed at maintaining adequate prices for tradables, it would be helpful to strengthen incentives for direct foreign investment that would both enhance Turkey's export capacity, reduce its import dependence and in the short-run probably require minimal additional debt service. Also, a concerted policy effort should be directed to cut the oil import bill through appropriate conservation and investment programs in the energy sector.

2. Major assumptions

The starting point for each scenario is the balance of payments projection for 1984. Assumptions regarding import and export prices and the interest rate (in U.S. dollar terms) are consistent with those used for the medium-term World Economic Outlook exercise. Import prices are

1/ For an earlier application to Turkey and a discussion of the underlying methodology, see SM/83/98 (5/20/83).

assumed to increase 3.5 percent and export prices 5 percent in 1985, and converge at a 4 percent world inflation rate thereafter, while the interest rate on new borrowing and on existing adjustable-rate debt (equivalent to LIBOR plus 1.5 percentage points) is expected to decline from 11.5 percent in 1985 to 9.5 percent in 1986-87, and further to 8.5 percent in 1988.

The growth rate in the volume of merchandise exports is projected to fall from almost 17 percent in 1984 to 12 percent in 1985 and then taper off to 8 percent by 1988, as it may become increasingly difficult to realize gains in market shares in the absence of added structural changes. At the same time, the output elasticity of imports is assumed to decrease from almost 2 in 1984 to 1.6 in 1985, and to decline by 0.1 annually from 1986 onwards, reflecting movements to a longer-term propensity to import. Workers' remittances are projected to rise by the assumed international inflation rate.

As for the capital account, future official credits are to be amortized in four equal yearly installments following a five-year grace period, whereas new commercial borrowing is repayable in four yearly installments, after a three-year grace period. Yearly disbursement of official medium- and long-term debt is maintained at US$0.2 billion and project credits at US$0.9 billion after 1984. Net short-term inflows are kept constant at US$0.8 billion per year. Direct private investment is expected to almost double to US$0.4 billion between 1984 and 1988. Finally, international reserves are targeted to increase steadily--except in 1985, to accomodate the bulge in debt service obligations--in order to maintain a stock more or less equivalent to two months of merchandise imports (the size of which depends on the scenario under consideration). The remaining financing requirement is to be met with program loans from commercial sources.

Table 15. Turkey: Medium-Term External Debt and Payments Scenarios, 1983-88

(In millions of U.S. dollars, unless otherwise specified)

	1983	1984	1985	1986	1987	1988
"Adjustment" scenario						
Current account balance	-1,760	-1,010	-800	-400	-200	--
Interest payments	1,420	1,350	1,588	1,557	1,617	1,522
Amortization of medium- and long-term debt	1,256	1,522	2,129	2,083	2,196	2,280
Gross medium- and long-term borrowing	1,821	2,127	1,729	1,483	1,396	1,480
Total debt outstanding at year-end	18,600	20,055	20,555	20,755	20,755	20,755
Debt service ratio (in percent of foreign exchange earnings)	30.9	28.6	32.6	28.5	26.8	24.2
Export volume growth (annual percentage change)	12.7	16.7	12.0	10.0	9.0	8.0
Import volume growth (annual percentage change)	9.2	8.7	5.6	5.3	6.1	6.3
Real GNP growth (annual percentage change)	3.2	4.5	3.5	3.5	4.4	4.8
"Growth" scenario						
Current account balance	-1,760	-1,010	-1,056	-1,050	-1,194	-1,294
Interest payments	1,420	1,350	1,603	1,612	1,750	1,739
Amortization of medium- and long-term debt	1,256	1,522	2,129	2,083	2,196	2,344
Gross medium- and long-term borrowing	1,821	2,127	1,985	2,133	2,390	2,838
Total debt outstanding at year-end	18,600	20,055	20,811	21,661	22,655	23,949
Debt service ratio (in percent of foreign exchange earnings)	30.9	28.6	32.8	28.9	27.7	26.0
Export volume growth (annual percentage change)	12.7	16.7	12.0	10.0	9.0	8.0
Import volume growth (annual percentage change)	9.2	8.7	8.0	8.2	7.7	7.2
Real GNP growth (annual percentage change)	3.2	4.5	5.0	5.5	5.5	5.5
Mixed scenario						
Current account balance	-1,760	-1,010	-950	-800	-750	-600
Interest payments	1,420	1,350	1,597	1,590	1,695	1,641
Amortization of medium- and long-term debt	1,256	1,522	2,129	2,083	2,196	2,318
Gross medium- and long-term borrowing	1,821	2,127	1,879	1,883	1,946	2,118
Total debt outstanding at year-end	18,600	20,055	20,705	21,305	21,855	22,455
Debt service ratio (in percent of foreign exchange earnings)	30.9	28.6	32.7	28.8	27.3	25.2
Export volume growth (annual percentage change)	12.7	16.7	12.0	10.0	9.0	8.0
Import volume growth (annual percentage change)	9.2	8.7	7.1	7.2	6.6	6.1
Real GNP growth (annual percentage change)	3.2	4.5	4.4	4.8	4.7	4.7

Sources: Data provided by the Turkish authorities; and Fund staff estimates.

Turkey: Summary of the Economic Program Under the Proposed Stand-By Arrangement

1. Overall objectives

a. An increase in real GNP of 4.5 percent in 1984 compared with a growth of 3.2 percent in 1983.

b. The rate of inflation, as measured by the change in wholesale prices over the preceding 12 months, is expected to decline to under 25 percent by the end of 1984 compared with 41 percent in December 1983.

c. The current account deficit of the balance of payments is to be reduced from US$1.8 billion (3 1/2 percent of GNP) in 1983 to US$1.0 billion (2 1/4 percent of GNP) in 1984.

2. Principal elements

a. Public sector finance

The public sector borrowing requirement is to be reduced from 4.7 percent of GNP in 1983 to well below 3.5 percent in 1984. The Central Government's consolidated budget deficit is projected to move from the equivalent of 0.5 percent of GNP in 1983 to a surplus of 0.3 percent in 1984 and no further accumulation of arrears is expected. A number of measures have been announced by the Government that will result in a projected net revenue increase of LT 60 billion. On the expenditure side, the Government will ensure a reduction relative to the original budget for 1984 of LT 303 billion. Furthermore, the Government has drawn up contingency plans for further cuts in expenditure of LT 75 billion, which it will implement in the event that the outcome in 1984 shows signs of being less favorable than expected.

With regard to the SEEs, the profit on current operations is expected to amount to at least 0.3 percent of GNP, compared to a deficit of 0.4 percent in 1983; an even larger surplus is likely to result from price increases in addition to those already built into the 1984 program, as well as from additional savings. Budgetary transfers to the SEEs are limited to LT 330 billion, equivalent to a decrease of about 20 percent in real terms.

b. Monetary policy

The monetary program is designed to bring about a deceleration in the average rate of growth of reserve money from 46 percent in 1983 to 29 percent in 1984, and a reduction in the growth of broad money to 31 1/2 percent in 1984 from 42 percent in 1983, assuming a reserve money multiplier of 2.35 for 1984. Net domestic assets of the Central Bank and net Central Bank credit to the public sector are subject to quarterly ceilings. The program also assumes for 1984: (i) an increase in net foreign assets of the Central Bank of about US$320 million; and (ii) no new buildup of reserve requirement deficiencies, and unchanged reserve requirement ratios. In addition, after-tax interest rates on time deposits are to remain positive in real terms; specifically, the real effective yield on 6- to 12-month deposits and certificates of deposit is assumed to average 6 percent during 1984.

In the second half of the year, further steps (in addition to the recent cut in the transactions tax rate) will be taken to develop an interbank money market.

c. External policies

A key element in the program is the pursuit of a flexible exchange rate policy to support the balance of payments and export objectives.

A program will be devised over 1984 as to the timing and form in which remaining quantitative import restrictions are to be eliminated in the period through 1988. Advance import deposit requirements are to be eliminated by the end of 1984.

The Government will follow cautious external debt management policies. Limits on both short-term and medium- and long-term (1-12 years) foreign borrowing are performance criteria under the program. In addition, the debt reporting mechanism will be further improved, with technical assistance from the World Bank and the Fund.

d. Review

There will be a review with the Fund after mid-1984, which will provide detailed targets and policies for the second half of the year and set the performance criteria for the remainder of the program. The third and fourth purchases cannot be made until after the review is contemplated.