The Effect of Consumer Loans on the Current Account Balance in Turkey (2005-2011)

Asst. Prof. Figen Özülke
Okan University
School of Applied Sciences
Department of Accounting and Financial Management
Tuzla Campus
Istanbul, 34959
Turkey
e-mail: figen.ozulke@okan.edu.tr

Abstract
The Turkish financial sector and banking system showed a highly positive performance during the global financial crisis. The Turkish Banking System differs from those in the USA and the EU in that it has a higher capital adequacy ratio and liquidity, and it has not carried any risks resulting from derivatives. Despite this strong structure, with the effect of global conditions, loan volume decreased and non-performing loans increased from the last quarter of 2008 to the third quarter of 2009 in Turkey. In 2009, the unemployment rate reached 16.1% while non-performing consumer loans and credit cards reached their peak. Economic recovery started in late 2009. In 2010, consumer loans increased by 35%, and in the same year, Turkey became the sixteenth biggest economy of the world. The monetary expansion in the domestic market caused a rapid increase in consumption. In the first quarter of 2011, growth in gross domestic product broke all records to reach 11%. Yet, growth was dependant on imports, and within the same time frame, the current account deficit has risen rapidly. This paper aims to explain the relationship between consumer loans and current account balance and discuss possible measures for the limitation of consumer loans.

Keywords: consumer loans, current account balance, financial crisis, Turkey
JEL codes: E44, F32, G21

1. Introduction

The consumption behaviors of individuals vary by disposable income and borrowing facilities available. Income, interest rates and inflation figures play an important role in shaping consumption preferences. Lower interest rates result in higher levels of borrowing and, on the part of the consumers, a stronger demand for consumer loans. Consumer loans are financial instruments that facilitate the realization of consumption demands by financing individuals' expenses. An increase in the amount of consumer loans thus has a positive effect on growth. However, if the increase in the amount of consumer loans also increases the demand for imported goods, it has a negative impact on the balance of trade and results in a higher current account deficit. The latest global crisis has clearly shown that fluctuations in interest rates as a result of macro-economic developments have a big impact on the volume and risk level of consumer loans.

The global crisis emerged at the end of a long period and was accompanied, in each stage of its development, by remarkable figures. The center of the crisis was the financial sector in the US, from where it first spread to the European Union across the Atlantic, and then to the whole world. Problems concerning the performance of subprime mortgages in the US financial sector meant huge losses for those international financial institutions that issued and bought collateralized debt obligations (CDOs) backed by subprime mortgages. This led to the bankruptcy of some major US- and EU-based financial institutions operating in the international arena, and resulted in a deep crisis in global economy due to a liquidity crunch and an abrupt end to credit supply and global flow of funds.

2. Development of the Global Crisis

The burst of the high-tech stock market bubble in the first half of the year 2000 dealt a severe blow to US stock markets. Following this shock, developed economies gave signals of an upcoming recession towards 2001. In this period, the Federal Reserve in the US and central banks in Japan and Europe started to lower interest rates. Following the FED's cuts, interest rates dropped from 6.25% in May 2000 to 1.75 in December 2001. The federal policy followed in this period also aimed to facilitate economic growth by stimulating the construction sector. Banks started to borrow short term money at low rates and give long-term loans, especially in the form of mortgages. Low interest rates and the increase in asset prices led consumers to borrow above their means. Credit growth rates in the US and EU increased rapidly and saving rates decreased. The ratio of household credit debt to disposable income increased to 136% in 2007 from 98% in 2000 in the US, to 180% from 120% in the UK, and to 91% from 71% in the European Union (Erdönmez, 2009).

The increase in global liquidity supply, which was a result of expansionary monetary policies based on low interest rates, led investors to seek high yield investment tools. Collateralized debt obligations backed by mortgages emerged as attractive investment opportunities in this period. The volume of CDOs rapidly increased, accompanied by an increase in the risk associated with the pool of mortgages that backed these securities, which was due to inter-bank competition, product diversification, and failure to follow due procedures for a sufficient and objective risk assessment prior to lending. However, credit rating agencies continued to give triple-A status to these instruments, mostly based on past performance and a failure to take notice of the current make up of the portfolios, and regulatory and supervisory institutions failed to create effective control mechanisms, both of which played a role in the rapid surge in the trading volume of derivative products. Under normal conditions, mortgage holders had the option of paying back by selling the collateral for their loans. However, this expectation ignored possible decreases in asset prices and changes in macro-economic variables (Poole, 2010).

Interest rates remained low until mid-2004. With the second half of 2004, FED started to increase interest rates due to the inflationist pressures on the economy. This had a big impact on low-income households who had adjustable rate mortgages. The demand for houses, on the other hand, started to decline from early 2005 onwards. The decrease in the demand brought house prices down. After peaking in 2006, house prices decreased by about 30% (Glick and Lansing, 2010). Thus, low-income families no longer had the option of paying off their debt by selling their houses. Problems in payments resulted in an increase in the number of foreclosures. All of this led to a flight from derivative products, which meant a liquidity crunch and huge losses on the part of the financial institutions that issued these instruments. In July 2007, two subprime hedge funds managed by Bear Stearns collapsed. From this point onwards, financial markets witnessed large scale turbulence. The US-based investment bank Lehman Brothers went bankrupt on September 15, 2008, marking the beginning of the most severe stage of the global crisis. The financial crisis that originated in developed economies created a domino effect and turned into a global crisis. Stock markets all over the world collapsed and the flow of funds to developing countries stopped. The significant decrease in demand that followed brought commodity prices down, increased unemployment rates, and slowed the global rate of growth.

Large amounts of capital injections to financial institutions in the US and Europe were followed by central banks cutting interest rates and the implementation of expansionary monetary policies designed to stimulate economic activity. However, this created burdens that were too heavy for the macroeconomic balances of many countries to sustain. In the three years since, global problems of unemployment, low trade volumes, budget deficits and current account deficits have been deepened even further. In the Euro zone, Greece, Portugal, Spain and Italy have serious problems with the financing of public spending, and face ever higher borrowing costs. The US economy faces a serious threat of recession. The US government announced that it plans to increase public spending by investing in infrastructure, as one of the measures designed to stimulate job growth.

3. The Turkish Economy during the Development of the Global Financial Crisis

Due to chronic high inflation, a fragile banking sector, and heavy public domestic debt stock, the Turkish economy entered the 21st century with a tight monetary policy and a stand-by agreement with the IMF that included a program based on a three-year currency peg. As the program was being implemented, the increase in imports as a result of the appreciation of the real exchange rate raised concerns that the current account deficit would increase. When, contrary to expectations, the program failed to provide a rapid decrease in inflation, the credibility of the program diminished, and domestic debt interest rates increased. In November 2000, the Central Bank of the Republic of Turkey (CBRT) intervened in the liquidity squeeze in the market by providing funding on a scale that exceeded the program's goals. However, when these funds turned into a demand for foreign currency, official reserves significantly declined. Interest rates rapidly increased in November and December. At the end of 2000, a supplementary reserve facility provided by the IMF calmed the markets.

The unanticipated political crisis that erupted in February 2001 shattered the confidence in the program and resulted in a strong demand for foreign currency. Interest rates increased as a result of the liquidity squeeze created by the demand for foreign currency. CBRT sold USD 5 billion within two days in compliance with the exchange rate commitment, USD 1.5 billion on February 20, 2001, and USD 3.5 billion on February 21, 2001 (CBRT, 2001). Taking the degradation of the banks' payment system and high interest costs into consideration, CBRT announced on February 22, 2001, a switch to a floating exchange rate regime. In May 2001, the "Program for Transition to a Strong Economy" started to be implemented within the framework of the stand-by agreement with the IMF, which aimed to improve the government's budgetary performance and to restructure the banking system. Firms operating in the financial and real sectors, especially those that had open positions, faced large devaluations and high interest burdens in the process of transition to a floating exchange rate regime, which devastated the balance sheets of many companies. The 2001 crisis resulted in an increase in the financial liabilities of the state as a result of the government debt securities issued to finance the so-called 'duty losses' of state enterprises, large amounts of outflows on the capital account of balance of payments, historic contraction of the economy, and a significant increase in unemployment.

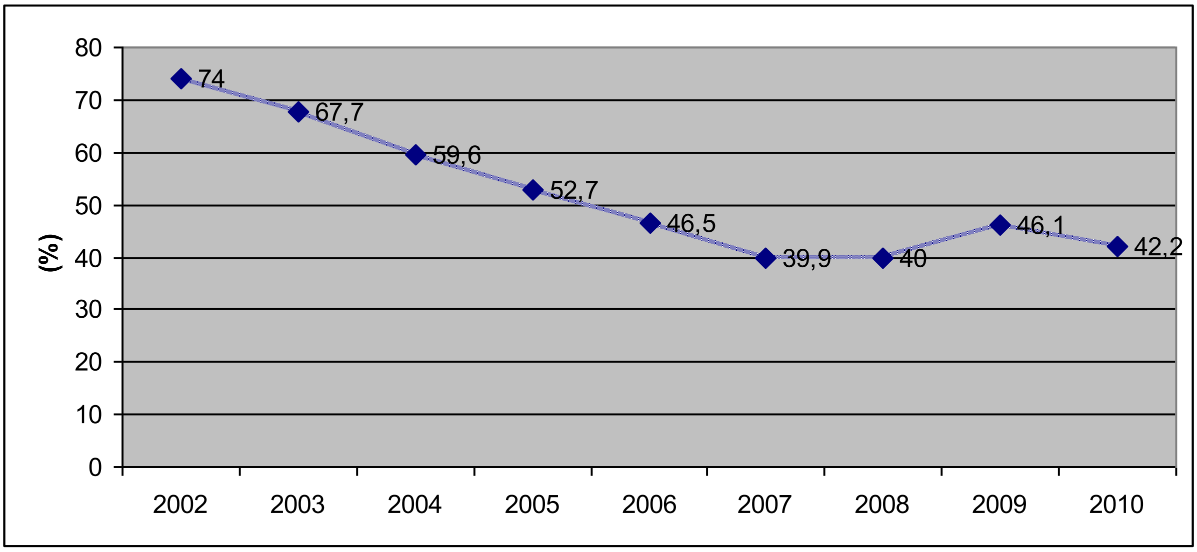
Table 1: Macroeconomic Indicators of the Turkish Economy (1999-2011)

Indicator / Year	Growth Rate %	CPI %	Unemp-loyment %	Capacity Utilization %	GDP Billion $	CBRT Reserves Billion $	Internal Debt Billion $	External Debt Billion $
1999	-3.4	68.8	7.4	73.1	247.5	24.2	42.4	103.1
2000	6.8	39.0	6.5	76.1	265.4	23.1	54.2	118.6
2001	-5.7	68.5	8.4	71.7	196.7	19.8	84.8	113.6
2002	6.2	29.7	10.3	76.2	230.5	28.1	91.7	129.5
2003	5.3	18.4	10.5	78.5	304.9	35.1	139.3	144.1
2004	9.4	9.3	10.8	81.5	390.4	37.6	167.3	160.9
2005	8.4	7.7	10.6	80.3	481.5	52.4	182.4	169.9
2006	6.9	9.7	9.9	81.0	526.4	63.3	178.9	207.8
2007	4.7	8.4	10.3	81.8	658.8	76.4	219.2	249.5
2008	0.7	10.1	11	78.1	742.1	74.2	181.7	277.0
2009	-4.8	6.5	14	68.9	617.6	74.8	219.2	268.2
2010	8.9	6.4	11.9	72.5	735.8	85.9	234.9	289.5
2011	8.8*	6.6***	9.2*	76.1***	203.6*	99.4*	239.7**	298.8**

Source: Turkish Statistical Institute (TURKSTAT), Central Bank Of The Republic Of Turkey (CBRT) (*June 2011, ** March 2011, ***August 2011)

Despite the improvements observed, since 2002, in growth, inflation, capacity utilization, public sector borrowing requirement and CBRT reserves, and the political stability that followed the elections in late 2002, the growing economy failed to create enough jobs. External debt increased by 180% in the period 1999 to 2010. The share of the private sector in external debt increased from 46.6% to 65.2%, whereas the share of the public sector decreased by 18 percentage points in the same period. As of 2011, $193 billion of the gross external debt stock originated from the private sector, of which $70.5 billion is short term. (Undersecretariat of Treasury, 2011)

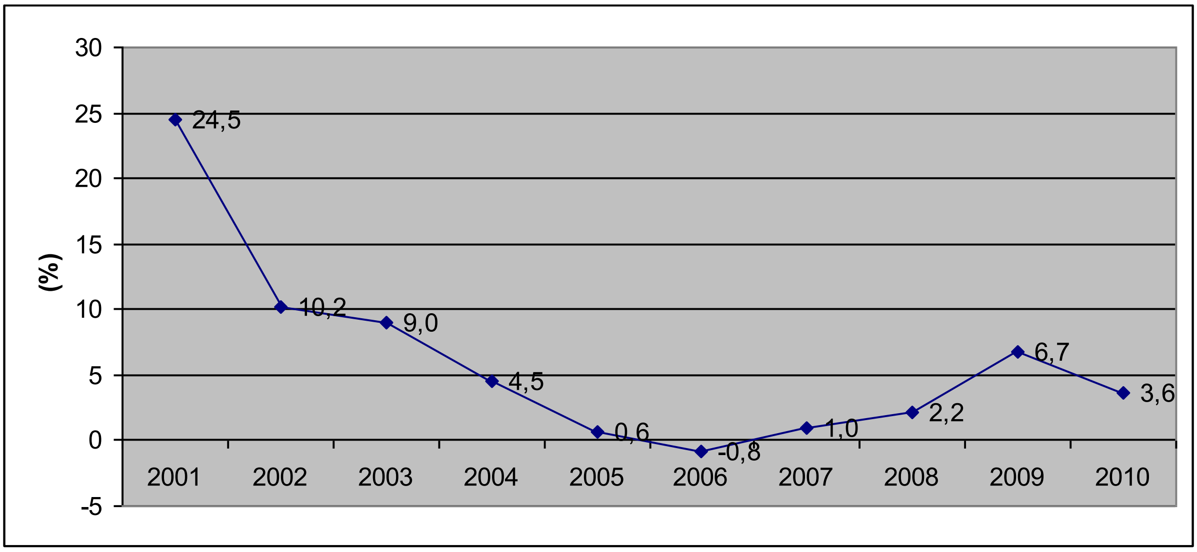
Figure 1: General Government Nominal Debt Stock Defined By EU Standards/GDP(%)



Source: Undersecretariat of the Treasury

Maastricht criteria set the ceiling for public debt stock at 60% of the GDP. However, as of 2010, the average figure was 80% for the 27 EU member states, 142.8% in Greece, 119% in Italy, and 93% in Portugal. In Germany, which is considered to be the locomotive of the Euro zone, this figure is 83.2% (Undersecretariat of Treasury, 2011). Figure-1 shows that Turkey has continuously met EU criteria for public debt stock, since 2004.

Figure 2: General Government Budget Deficit Defined By EU Standards /GDP(%)



Source: Undersecretariat of Treasury

Maastricht criteria set the ceiling for the ratio of the budget deficit to GDP at 3%. Turkey has met this criterion starting with 2005, but in 2009, when the effects of the global crisis were felt, and in 2010, in which Turkey had general elections, the budget deficit increased somewhat above this limit. In Ireland, which was significantly affected by the global crisis, the budget deficit was 32.3% in 2010, and was 8.3% in Greece and 9.2% in Spain. In 2010, the US had a budget deficit of 10.5%, the UK had a budget deficit of 9.6%, and Germany had a budget deficit of 4%.

The effects of the global crisis were deeply felt in Turkey in the last quarter of 2008. The negative impact of the crisis on macroeconomic indicators continued throughout 2009. In this period, the rate of unemployment in Turkey was the second highest among EU countries, after Spain. From 2010 onwards, the revival in internal consumption had a positive impact on major indicators. However, the revival in consumption, supported by a large increase in loans, was accompanied by a significantly larger current account deficit. International financial circles and the IMF identify the current account deficit as the most important threat for the Turkish economy.

4. Monetary Policy of the CBRT during and after the Crisis

During the global crisis, CRBT held foreign currency auctions to provide liquidity to the market and to keep credit channels open, decreased interest rates by 1025 basis points from November 2008 to the end of 2009, decreased the ratio of required reserves from 6% to 5% for TL deposits and from 11% to 9% for deposits in foreign currencies, and provided additional liquidity to financial markets via weekly repos. As the effects of the global crisis diminished, starting with the last quarter of 2009, these extraordinary measures were gradually abandoned.

In 2010, paralleling the relative improvement of the external demand and the rapid increase in domestic demand, the economy started to grow at a high rate. In this period, international capital flows were re-directed to developing economies. In the period April-November 2010, CBRT announced a “Crisis Exit Strategy” and started to implement quantitative tightening.

In the last quarter of 2010, CBRT started to implement a new policy mix to protect financial stability and to limit the current account deficit. The components of this policy mix were an increase in required reserves, and a larger interest rate corridor (the difference between overnight lending and borrowing interest rates). From November 2010 onwards, the ratio of required reserves for TL deposits was rapidly increased between 16% and 5% based on the maturity of the deposits, and between 11.5% and 8.5% for foreign currency deposits (Başçı, 2011). These measures aimed to extend maturities of short term deposits and capital movements, and to limit credit expansion by increasing the costs of resources.

Credits and Current Account – CBRT Modeling

Current Account Deficit=Credit Growth-Deposit Growth+Public Sector Borrowing Requirement+Other*

2011 Credit Growth Rate (Annual Change)	**2011 Current Account Deficit (Percent of GDP)**
15%	1.2
20%	3.3
25%	5.4
30%	7.5
35%	9.6

2011 Assumptions;

Growth;	4.5%
Inflation;	5.3%
PSBR;	2%
Deposits/GDP;	57.4%
Deposit Growth;	16.1%

Source: Central Bank Of The Republic Of Turkey (CBRT, December/2011)

A modeling made by the CBRT at the end of 2010 showed that a 5% increase in annual credit growth rate increased the current account deficit by 2.1 percentage points. On the basis of the formulae and assumptions informing this model, the Banking Regulation and Supervision Agency (BRSA) took additional measures in July 2011. These measures are expected to decrease credit growth to 25% by the end of the year. However, the current account deficit is still expected to be a two-digit figure for 2011, even if the anticipated credit contraction takes place.

Paralleling the CBRT policy, the BRSA increased required reserves for consumer loans other than auto and housing loans, which are usually without collateral, to limit the increase in household borrowing rates. NBRSA policy increased required reserves for

- banks in which the ratio of consumer loans to all loans exceeds 20%, banks in which the ratio of non-performing consumer loans -other than auto and housing loans- to all loans exceeds 8%,
- banks that provide consumer loans with maturity dates longer than one year, and
- loans for which initial payment plans are revised to provide additional time for borrowers.

Lowering of the US credit rating from July 2011 onwards, the political crisis the US government faced in raising the debt ceiling, the increase in Greece’s risk of default, the increases in borrowing costs which Italy and Spain had to face due to high levels of public sector debt, and the doubts concerning the equity and liquidity adequacies of commercial banks in EU countries increased the risk of a new financial crisis. As of September 2011, CBRT restarted holding foreign currency auctions, narrowed the interest rate corridor and took measures to provide liquidity for the market with the purpose of alleviating the effects of the fluctuations in currency, commodity and capital markets on financial stability.

5. Literature

The process of globalization entailed the liberalization of the flow of goods, services and capital all over the world. As a result, problems in national economies affected the whole world, proportionate in size to the share and activity of the economy in question in global markets. In this context, sustainability of the balance of payments of individual countries, which is a result of the commodity, service and capital exchanges with the outside world, emerges as a vital issue. Current account deficits, in particular, are perceived as early indicators of financial and currency crises (Labonte, 2005). In the Turkish case, crises in 1994 and 2000 were followed by the stronger regulation of the financial sector and large devaluations.

Studies on the current account deficit in the literature show that the so-called twin deficits of current account deficit and budget deficit move together (Bussiére, Fratzscher and Müller, 2004), current account deficit is accompanied by an increase in interest rates (Freund, 2000), and current account deficit emerges when there is a decrease in total savings as a result of increased demand (Freund, 2000).

The increase in demand, which eventually leads to a larger current account deficit, is financed by an increase in the volume of bank credits. If the increase in credit volume is accompanied by ineffective regulation and supervision of the financial sector, it leads to banking crises (Ito and Kruger, 2001). Demirgüç-Kunt and Detragiache (1998) show that current account deficits emerge as a result of private sector credit expansion, and result in banking crises and currency crises.

Büyükkarabacak and Krause (2009) argued that a singular focus on credit expansion, which is said to cause current account deficit, is insufficient, and examined the shares of commercial and consumer loans in the total credit volume and their respective effects on current account deficit. They found that commercial loans go into production because they are used for investment goods and raw materials, and have a positive effect on net exports. Consumer loans, on the other hand, were found to have a negative effect on net exports. The authors suggest that policy makers not monitor credit expansion per se, but developments concerning the make-up of credits.

In their study on the composition of commercial and consumer loans, Büyükkarabacak and Valev (2010) found that the expansion of consumer loans was a significant early indicator of banking crises, but the expansion of commercial loans played a relatively smaller role in the development of banking crises.

6. Model and Data

Using secondary data analysis, this study aims to examine the effects, on a basic dataset, of other datasets developed for different purposes, and to explore the issue with the help of the new data formed by merging different datasets.

Statistics periodically published by the Turkish Statistical Institute (TurkStat), Undersecretariat of Treasury, Central Bank of the Republic of Turkey, and the Banking Regulation and Supervision Agency formed the basis of the datasets used. Data for 2011 are for different periods, indicated under each table.

Data on loans were taken from the "Monthly Interactive Bulletin" published by the BRSA. This bulletin is prepared using the interim financial statements that banks file each month, and covers both domestic and overseas branches of the banks. Data provided in non-consolidated form by the banks are published in the bulletin after consolidation.

7. Current Account Deficit and the Development of Consumer Loans in Turkey

In 1980, Turkey abandoned the import substitution model of industrialization and started to follow a policy of a liberal, outward-oriented economy which encouraged exports and foreign capital investments. Following the liberalization of capital movements in 1989 and the resulting convertibility of the Turkish Lira, the current account gained a greater significance. In periods with high growth rates, real appreciation of the TL, and increased amounts of short-term capital inflows, the current account deficit increased. In periods of crisis, current account surpluses were also recorded due to large devaluations and a small volume of imports paralleling slower growth rates (as in 2001).

Table 2: Current Account Balance (1999-2011)

Indicator / Year	Exports (FOB) Billion $	Change (%)	Imports (FOB) Billion $	Change (%)	Ratio of Exports to Imports (%)	Foreign Trade Deficit Billion $	Service Balance Billion $	Current Account Deficit Billion $	Current Account Deficit/ GDP (%)
1999	29.0	-5.8	38.8	-13.4	74.4	-9.8	7.5	-0.9	-0.4
2000	30.8	6.2	52.9	36.3	58.2	-22.1	11.4	-9.9	-3.7
2001	34.7	12.6	38.1	-28.0	91.1	-3.4	9.1	3.8	1.9
2002	40.7	17.3	47.1	23.6	86.4	-6.4	7.9	-0.6	-0.3
2003	52.4	28.7	85.9	82.4	61.0	-13.5	10.5	-7.5	-2.5
2004	68.5	30.7	91.3	6.3	75.0	-22.7	12.8	-14.4	-3.7
2005	78.4	14.5	111.4	22.0	70.4	-33.1	15.2	-22.3	-4.6
2006	93.6	19.4	134.7	20.9	69.5	-41.1	13.6	-32.2	-6.1
2007	115.4	23.3	162.2	20.4	71.1	-46.8	13.3	-38.4	-5.8
2008	140.8	22.0	193.8	19.5	72.7	-53.0	17.3	-41.9	-5.6
2009	109.6	-22.2	134.5	-30.6	81.5	-24.9	16.7	-14.0	-2.3
2010	120.9	10.3	177.3	31.8	68.2	-56.4	14.7	-47.7	-6.5
2011*	81.3	18.7	135.7	43.1	59.9	-54.4	8.1	-50.6	-

Source: Turkish Statistical Institute (TURKSTAT) (*)July 2011

Table 2 reports the main items of the current account in the period 1999-2011 on the basis of data provided by the Turkish Statistical Institute. The table shows that the current account deficit of Turkey results from the foreign trade deficit. The rapid increase in export revenues fails to finance the surge in imports, and thus the current account deficit remains as an important element of risk for the economic outlook. Foreign trade balance is directly affected both by the dependency ratio of the main components of export products, and by fluctuations in the prices of oil and commodities and exchange rate fluctuations in the global economy. Economic fluctuations in EU countries, which are a traditional export market for Turkish firms, also affect exports negatively.

The service balance decreases the current account deficit thanks to surpluses in tourism revenues and construction and transportation services. However, tourism revenues are subject to rapid changes due to political and economic developments. Turkey experiences serious fluctuations in its tourism revenues as a result of political instability and wars in the Middle East, exemplified during the Gulf Crisis and the Iraq War.

Ratio of exports to imports

The ratio of exports to imports decreases significantly in periods of high growth. This is due to the increase in energy imports, which is the main input in production and increases together with economic activity. Energy, in the form of natural gas, coal and oil, is the largest item on Turkey's import bill. Increases in energy prices and the depreciation of the TL result in hikes in the energy bill, and negatively affect the current account deficit. Energy imports in the seven months from January to July 2011 increased by 42.4% compared to the same period last year, and reached USD 29.581 billion (TURKSTAT), which makes up 22% of total imports.

Table 3: Classification of Imports by Type of Commodity (%)

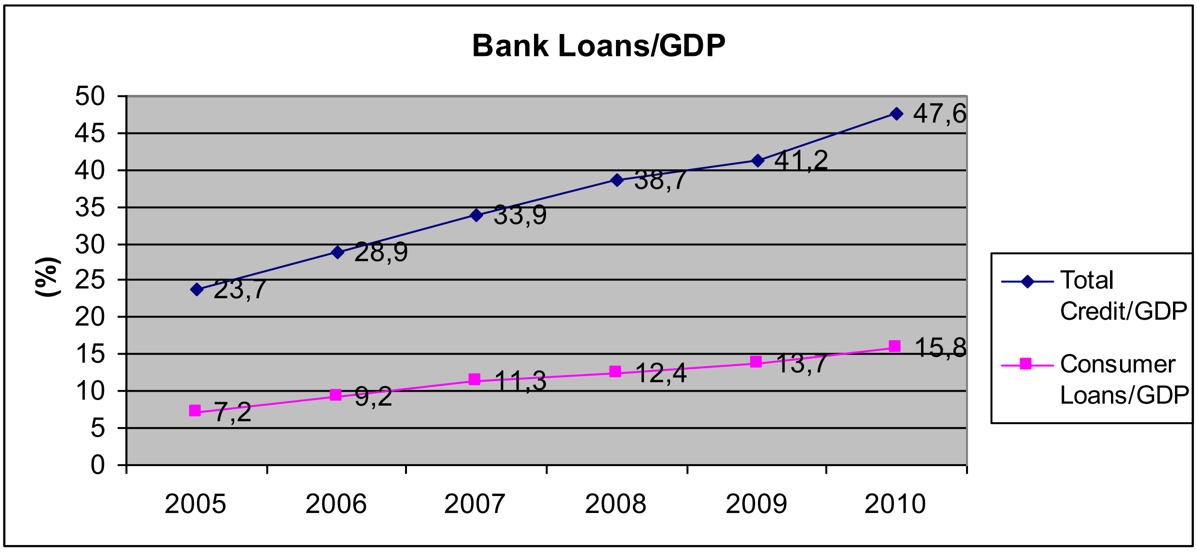
Year	Capital Goods	Intermediate Goods	Consumption Goods	Others
1999	21.5	66	11.9	0.7
2000	20.9	66.1	12.7	0.4
2001	16.8	73.2	9.2	0.8
2002	16.3	73	9.5	1.2
2003	16.3	71.7	11.3	0.7
2004	17.8	69.3	12.4	0.5
2005	17.4	70.1	12	0.5
2006	16.7	71.4	11.5	0.4
2007	15.9	72.7	11	0.4
2008	13.9	75.1	10.6	0.3
2009	15.2	70.6	13.7	0.5
2010	15.5	70.8	13.3	0.3
2011*	15.6	71.4	12.7	0.3

Source: Turkish Statistical Institute (TURKSTAT) *July/2011

An examination of the classification of imports by commodity type in the period 1999-2010 shows that there is a trend towards less capital goods to more intermediate goods. In 1999, capital goods made up 21.5% of all imports, whereas this figure declined to 15.5% in 2010. The share of intermediate goods, on the other hand, increased 5% in the same period, and became 70.8% in 2010. Imports of consumption goods decreased in crisis years to 9.2% in 2001 and 10 10.6% in 2008. These declines parallel consumers' behavior of cutting their expenses during periods of depression. In terms of absolute figures, imports of consumption goods increased from $4.8 billion in 1999 to $24.7 billion in 2010, a 4.13 fold increase. In the same period, imports of intermediate goods increased 3.9 fold, and imports of capital goods increased 2.3 fold.

The increase in the imports of consumption goods is financed, on the part of the consumers, both by disposable income and by consumer loans. On BRSA's reports, the category of consumer loans consists of housing loans, vehicle loans, personal loans and credit card loans. Total credit volume in Turkey, and the share of consumer loans in this volume, has increased rapidly in recent years. Figure 3 shows that the ratio of consumer loans to GDP were 15.8% in 2010. In the UK, this figure was 110% in 2010 (PWC, 2011).

Figure 3: Bank Loans/GDP



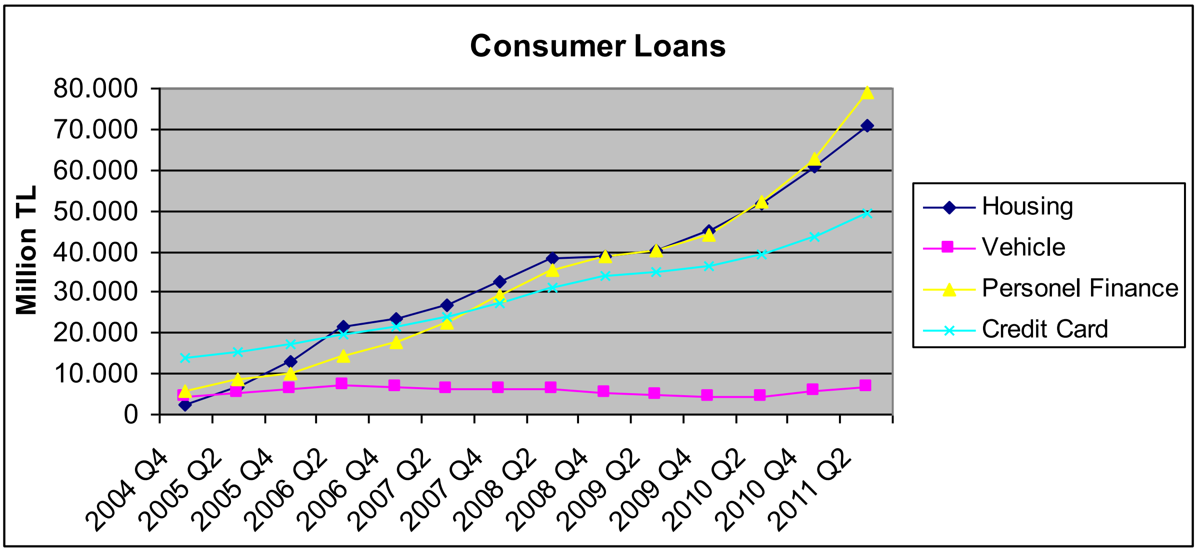
Source: Banking Regulation and Supervision Agency

In 2005, consumer loans totaled TL 46.7 billion; credit card loans made up 36.9% of this amount, housing loans made up 27.9%, personal loans made up 21.3%, and vehicle loans made up 13.8%. As of June 2011, consumer loans totaled TL 205.5 billion; credit card loans made up 24% of this amount, housing loans made up 34.5%, personal loans made up 38.4%, and vehicle loans made up 3.2%. Figure 4 shows the development of the composition of consumer loans by loan type in the period under study.

There was a rapid increase in housing loans from 2005 to the second half of 2008. Both the Housing Development Administration and the private sector increased their activities in the construction sector, which led to an increase in the number of building permits. A total of 114,254 building permits were given in 2005, 114,204 in 2006, and 106,659 in 207 (TURKSTAT, 2011). From the second half of 2008, when the global crisis was at its peak, to the end of 2009, the rate of increase in housing loans slowed down. The number of building permits given has also declined in this period. A total of 95,193 permits were given in 2008, and 92,342 in 2009. Starting in early 2010, however, there was another surge in housing loans, with the number of building permits given in 2010 reaching 128,837 (TURKSTAT, 2011).

In absolute terms, the amount of vehicle loans remained the same in the period under study, and its share in total consumer loans decreased by about 10 percentage points. However, imports of passenger cars made up about 25% of all imports of consumption goods, and significant increases were observed in 2010 and in 2011. An analysis of the increase in imports of passenger cars needs to examine the role of non-bank financial institutions -consumer financing firms and fleet rental firms- as well.

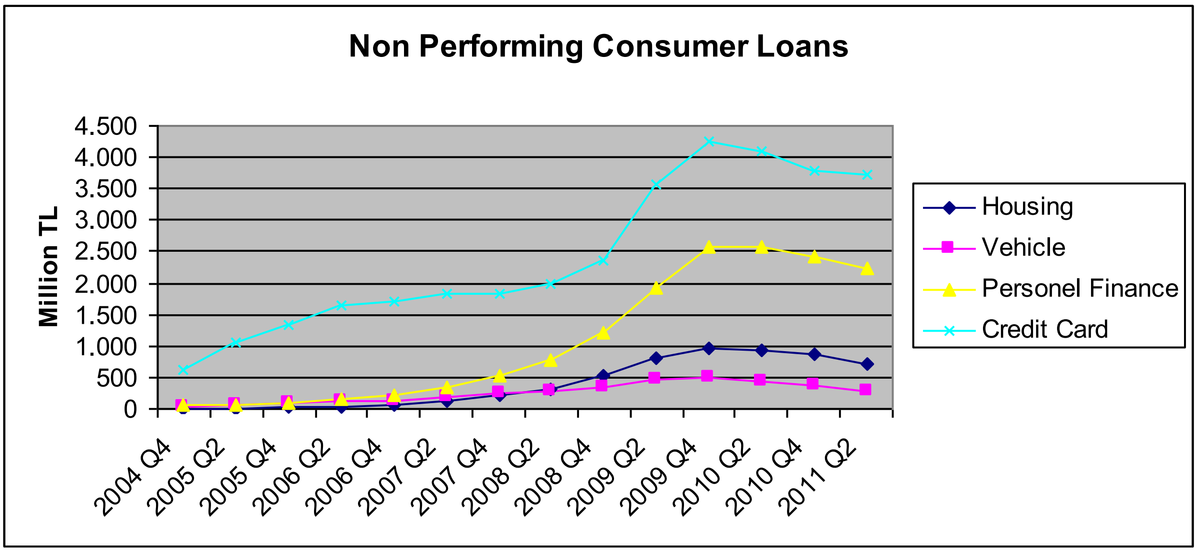
Figure 4: Composition of Consumer Loans



Source: Banking Regulation and Supervision Agency

Among all consumer loan types, personal loans recorded the fastest increase in the period under study. The rate of increase in total consumer loans was 18.3% in 2011, whereas personal loans increased by 22.4%. The question of which expenses are financed by personal loans and credit card loans is an important one in terms of macroeconomic indicators. The concern that the increase in consumer loans may have negative effects on current account deficit, frequently voiced in the discussions on Turkey's current account deficit, is based on the possibility that personal loans and credit card loans may increase the demand for imported goods. We do not have reliable measures of the items on which personal loans are spent. However, we do know that credit card loans are used mostly in purchases of food, clothing and fuel. Thus, we do not have sufficient data to claim that credit card loans make a significant impact on the current account deficit. Similarly, we do not have reliable figures to back up the claim that personal loans are used to finance purchases of imported goods.

Figure 5: Composition of Non-Performing Consumer Loans



Source: Banking Regulation and Supervision Agency

Data on non-performing consumer loans show that there was an increase in the volume of non-performing loans from the second half of 2008 to the end of 2009. At the end of 2009, the ratio of non-performing consumer loans to all consumer loans reached 6.4%. In June 2011, this figure declined to 3.4%. Credit card loans come first in the list of non-performing loans, followed by personal loans.

8. Conclusion

This article presented data on the structure and development of current account deficit and consumer loans in Turkey. Based on these data, the following conclusions can be made:

ı. In the aftermath of the global financial crisis, the most important factor threatening financial stability in Turkey is the current account deficit. Public sector borrowing rates comply with Maastricht criteria. A significant improvement has been recorded in the budget balance in the last 10 years. In recent years, part of this improvement came from the taxes on imports, which are on the increase.

ıı. The source of the current account deficit in Turkey is the foreign trade balance. Turkey is dependent on imports for its energy, and energy is the largest item on Turkey's import bill. This triggers an increase in the current account deficit in times of economic expansion.

ııı. The improvement in Turkey's economic activity in the aftermath of the global crisis and the strong growth performance was based mostly on a revival in domestic demand.

ıv. In the last five years, consumer loans played an important role in the financing of domestic demand. From the last quarter of 2009 onwards, loans gained momentum once again. Despite the surge in consumer loans, both the ratio of consumer loans to GDP and household debt ratio are well below those in developed economies.

v. Although there has been no marked increase in the last 10 years in the share of consumption goods in all imports, both the appreciation of the TL and the increase in loans in an environment of high liquidity have the potential to increase the demand for imported goods. However, there are no definitive findings on how much of the expansion in consumer loans is used to purchase imported goods. For example, imports of passenger cars increased from 2010 to 2011, but there was no corresponding increase in the same period in vehicle loans. Credit card loans, on the other hand, are used mostly to purchase food and fuel. We do not have sufficient information on how personal loans are spent, but it has been argued that at least some are used to finance current household debts.

Some of the studies in the literature argue that credit expansion leads to an increase in current account deficit, but we do not have sufficient data to back up the claim that the high current account deficits Turkey ran in 2010 and 2011 were caused by credit expansion in general or the expansion in consumer loans. CBRT failed to provide sufficient explanation concerning the assumptions of its model or the dataset used. In an environment of extraordinary fluctuations in outside economic conditions, rigid implementation of measures that will cause sudden drops in total credit volume could have a negative impact on economic activity based on domestic demand, and may result in a decline in production or contraction in employment. In addition, local currencies underwent a significant depreciation from August 2011 onwards, due to the outflow of funds from developing economies as a result of outside economic conditions. In the nine months from January to September 2011, TL lost 19.8% of its value.

At a time when speculations abound on a new economic crisis originating from the public sector debt stock of the US and EU countries, a more flexible policy mix concerning credit channels would be wiser in terms of effects on macroeconomic indicators.

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