Durmuş Yilmaz: Turkey's monetary and exchange rate policy for 2008

Speech by Mr Durmuş Yilmaz, Governor of the Central Bank of the Republic of Turkey, at the Central Bank of the Republic of Turkey, Ankara, 18 December 2007.

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General framework of the monetary policy

Overview of 2007

The Central Bank of the Republic of Turkey (the Central Bank) has continued to implement the monetary policy in 2007 based on the principles of inflation targeting regime. The Monetary Policy Committee (the Committee) meetings were held in line with the pre-announced annual timetable. Interest rate decisions were made public through press releases on the same day along with the rationale of decisions. Moreover, "Summary of the Monetary Policy Committee Meeting" including details of decisions and the assessments made during the meetings started to be published along with the English translation within eight working days following the meetings in 2007. Inflation Report, which is the main communication tool of the Central Bank, continued to be published quarterly. Furthermore, in order to increase the efficiency in management of expectations, Price Developments Report was also published within a very short time with a detailed analysis of inflation data following the announcement of monthly price developments.

Inflation in the first quarter of 2007, as foreseen, remained within the uncertainty band set around the path consistent with the target, whereas the decline in inflation stagnated in the last quarter due to both considerable increases in food prices, arising from drought as well as global conjuncture, and adjustments in administered prices. Thus, it has become obvious that the year-end inflation would remain outside the uncertainty band. Though the Central Bank has targeted the CPI inflation, it has pursued an effective communication strategy by referring to core measures at times of price movements beyond its control and pursued an effective communication strategy. In line with the positive outlook of inflation trend in prices excluding energy, food and administered prices, a measured rate cut cycle has been initiated in September 2007. Accordingly, the overnight borrowing rate was decreased by 175 basis points in total until the end of 2007, from 17.50 percent to 15.75 percent.

The Central Bank has made significant progress over the last two years in terms of communication policy, transparency and accountability. Despite the fact that inflation remained above the path consistent with the target due to a series of supply-side shocks over the past two years, the inflation expectations for the next 12 and 24 months indicate low levels such as 6.1 and 5.2 percent, which have not been experienced for many years in our economy. This shows that inflation targeting regime has highly succeeded in managing expectations. In the meantime, as the inflation expectations indicate figures above the medium-term target of 4 percent points, we think that there are many things to do towards disinflation. The Central Bank, not being content with what has been achieved so far, will continue to further increase the efficiency in expectations management in forthcoming periods.

The rest of this text provides the general framework of the monetary and exchange rate policy to be implemented in 2008. The first part addresses the strategic framework of the monetary policy, while the second part explains the exchange rate policy, foreign exchange auctions and guidelines for liquidity management.

Inflation targets

Inflation targets have been set as "point target" since 2006. The target has been defined as the end-year Consumer Price Index (CPI) inflation calculated by the annual percentage change of the Consumer Price Index (CPI) and the target horizon, has been set as 3 years in line with 3-year budget implementation. The Central Bank continues this practice in 2008 as well.

By considering the structural transformation of the economy, convergence process to the developed countries and the pricing behavior that remained from high inflationary period, a target of 4 percent has been considered appropriate for the medium-term as agreed with the government. Therefore, inflation targets for 2008 and 2009, which were previously announced as 4 percent, are maintained and the inflation target for 2010 has also been set as 4 percent.

The importance of Special CPI aggregates

Due to its comprehensive context coming from its definition, consumer price index can be exposed to temporary fluctuations. Core indicators allow for differencing out the price movements in items unaffected by monetary policy actions, and thus enable much better analysis of the main inflation trend. For instance, the impact of a significant increase in energy prices on consumer prices can be analyzed by using a price index excluding energy prices. Similarly, a temporary price increase arising from one-time movement in special consumption tax levied on tobacco products can also be identified by using special CPI aggregates excluding the item in consideration.

A series of supply-side shocks that have occurred over the last 2 years have underlined the importance of special CPI aggregates. The relevant indicators, which may also be called as "core" indices, have played an important role in the communication of monetary policy decisions in 2007.

Undoubtedly, it is not possible to define a single core indicator for inflation that can disregard all temporary effects observed in consumer prices. For instance, the Special CPI Aggregates issued by the Turkish Statistical Institute does not exclude *processed* food group. As we have experienced recently, the drought has a negative impact on core measures via processed food prices. In other words, although the main inflation trend has not worsened, the growth rate of special CPI aggregates can display increases stemming from processed food prices. Accordingly, the Central Bank has established an index excluding all food items and started to monitor this index closely.

From time to time, the Central Bank draws the attention to price movements in certain sub-groups of the CPI in order to increase efficiency of the communication of the monetary policy and to take sound decisions. For instance, in order to highlight the effects of the monetary policy tightening being implemented since mid-2006, the Central Bank has frequently referred in 2007 to the developments observed in sub-groups, such as services or durable consumption goods, whose prices are sensitive to monetary policy actions.

In summary, the Central Bank examines several variables including Special CPI Aggregates while assessing the main inflation trend, and can highlight different indicators at certain periods depending on the economic conjuncture. Understanding of the Central Bank's approach to core inflation by the public will allow for a sound assessment of the monetary policy actions and hence an improved efficiency of communication policies.

Uncertainty band and accountability

It is stipulated in Article 42 of the CBRT Law that "The Bank shall submit information to the Government in writing and inform the public disclosing the reasons of the incapability of achieving the determined targets in due time announced or the occurrence of the possibility of not achieving the targets and the measures to be taken thereof". While, it forms a basis for the accountability principle, the law does not specify the size of the deviation from the target that will require such an explanation. In other words, details of accountability mechanism are left to the Central Bank's own initiative. Therefore, the Central Bank has established an effective and enforceable accountability mechanism by setting a symmetrical uncertainty band of 2 percentage points in both directions around the point target.

As stated above, the inflation target has been defined over a very comprehensive CPI index. The CPI index also comprises of price items that are beyond the control of the monetary policy such as food, energy and administered goods. In emerging markets like Turkey, short-term fluctuations in exchange rates can lead to unpredictable temporary fluctuations in inflation as well. Since a sudden reaction of monetary policy to factors that are beyond its control will increase volatility in macroeconomic variables, inflation-targeting central banks adopt a medium-term approach and allow temporary fluctuations in inflation as long as the expectations are under control. In this framework, the primary objective of setting an uncertainty band is to establish a measurable criterion that will enable to determine to what extent the deviations from the point target will be tolerated with respect to the accountability principle.

In view of the above-mentioned factors, it has been decided to keep the uncertainty band at 2 percent for 2008 as well. In this context, the path consistent with the end-year target and the uncertainty bands defined for the end of each quarter of 2008 are given in Table 1.

Table 1: Inflation path consistent with the end-year target and the uncertainty band

	March	**June**	**September**	**December**
Uncertainty Band (upper limit)	9.10	8.50	8.30	6.00
Path Consistent with the Target	**7.10**	**6.50**	**6.30**	**4.00**
Uncertainty Band (Lower Limit)	5.10	4.50	4.30	2.00

In case of realizations of the end-of-quarter figures outside the band, the Central Bank shall submit an *open letter* to the Government disclosing the reasons of the deviation and the measures already taken and to be taken for convergence to the target, and share this letter with the public.

Recently, the Overview chapter of the Inflation Report has been restructured in line with accountability principle. Accordingly, the Central Bank has started using Inflation Report to share its view pertaining to inflation and monetary policy outlook and the necessary measures to be taken to keep inflation close to the target. Thus, besides being the main communication tool of the Bank, the Inflation Report has therefore assumed an important role with respect to accountability principle as well. Accordingly, there will be more references given to the Inflation Reports in the case of possible open letters in forthcoming periods. It is necessary for the communication policy of the Central Bank that the open letters and Inflation Report would be perceived as complementary factors.

Role of public sector in inflation targeting strategy

It should be reemphasized that the monetary policy should be supported by fiscal policy in order to be able to turn the downward trend in inflation into a long-term and lasting achievement. The fiscal policy can affect inflation through various channels. A particular channel, through which fiscal policy has direct effects on inflation, is the price and tax adjustments in the goods and services produced by the public sector. Making these adjustments in line with a pre-announced schedule or a pre-described rule would diminish uncertainties regarding inflation forecasts and thereby contribute to the reputation of inflation targeting regime.

The Central Bank sets inflation targets on the basis of the budget projections of public sector. Therefore, while updating the monetary policy stance, the trend of public sector expenditures, which is a very important component of total demand, is closely monitored. Moreover, keeping public sector wage adjustments consistent with the inflation target is very important as the private sector take these adjustments as a benchmark for their own wage adjustments.

Due to all these reasons mentioned above, the Central Bank closely monitors the income and fiscal policy implementations, and frequently emphasizes the importance of structural reforms that would enhance the quality of fiscal discipline and predictability of fiscal policies.

Transmission mechanism, inflation forecasts and monetary policy stance

Uncertainties regarding the impact of monetary policy implementations on inflation are an issue that central banks frequently underline in their monetary policy statements. In countries that are undergoing a structural transformation process like Turkey, the relationship between macroeconomic variables evolve over time, leading to a higher degree of uncertainty pertaining to monetary transmission mechanism compared to developed countries. Moreover, it is believed that Central Bank's sharing of its evaluations about the transmission mechanism would contribute to the expectations management.

The fact that the short-term interest rates have only shown a declining pattern for a long time with the disinflation process after 2001 and this trend coincided with transition to inflation targeting regime made it difficult to evaluate the transmission mechanism. Nevertheless, the monetary tightening, which have been made since the mid-2006 and the macroeconomic dynamics thereby, allow for important inferences regarding to the workings of the transmission mechanism. Upon the recent evaluations, it can be suggested that the effect of monetary policy tightening has lasted for one year on economic activity and for two years on inflation. The effect of monetary policy on private sector demand and inflation has become more evident in the last one-and-a-half years. Moreover, it has been affirmed that monetary policy can indeed control expectations. The sectors on which the monetary policy has been most influential have been consumer durables group and services sector. In fact, price dynamics of services and consumer durables sectors have contributed to disinflation process significantly.

To sum up, despite the fact that nearly half of the CPI is composed of energy, food, and administered goods prices, it is evident that monetary policy is still capable of keeping the main inflation trend under control via other items.

As stated also in the last two years' monetary policy statements, the inflation target would be changed only if *sharp and long-term deviations* from the target occur due to factors beyond the control of the monetary policy such that the medium-term targets no longer make sense. Within this framework, while considering the possibility that inflation might be exceeding the target for a while in the short run, the Central Bank maintains the 4 percent inflation target hinging on the evaluation that the general trend of inflation is downwards.

The forecasts presented in the Inflation Reports will continue to refer to two-year periods. In phases when inflation is above the target, the forecasts presented in the Inflation Report become more important. The forecasts inform the public about the path that inflation will follow while moving towards the medium term target. In other words, the reference value established for economic units is the inflation forecast in the short-run and the inflation target in the long-run.

Another message that inflation forecasts contain is the monetary policy stance. The answer sought while forming forecasts and monetary policy outlook in the Inflation Report is: "What is the monetary policy stance that will keep inflation close to the target in the medium-term?"

The *monetary policy stance* in this sense does not only consist of the current level of short-term interest rates. Monetary policy stance indicates the prospective path that short-term interest rates will follow in a period that extends from today to medium term. Sharing with the public the interest rate assumptions that form the basis of forecasts, though qualitatively, is a remarkable step towards enhancing the transparency and predictability principles that are essential for inflation targeting.

Communicating with the public about the possible Central Bank policies influences medium-term market interest rates via expectations and strengthens the transmission mechanism. However, it should be reminded once again that the monetary policy stance path pronounced in the Inflation Report is produced according to currently available information and that each new data release related to the medium-term inflation outlook would necessitate the revision of the future monetary policy stance. Under the inflation-targeting regime, revisions in the monetary policy stance are not an exception, but a rule. Thus, the monetary policy stance established according to currently available data should not be interpreted as a commitment. Any unforeseen change in the variables that affect inflation outlook calls for the re-definition of the monetary policy stance. What is important here is to share openly with the public the reasons of the monetary policy stance update. As a matter of fact, the Central Bank explains, via Inflation Reports and other policy instruments, why and how the monetary policy stance has been reviewed.

The main policy instrument of the Central Bank is short-term interest rates. The implementation and communication of the monetary policy decisions in the inflation-targeting regime will continue to be carried out through short-term interest rates. Moreover, as stated in previous policy documents, instruments such as reserve requirements or efficient liquidity management might be used, when deemed necessary.

The decision-making process and communication

The Monetary Policy Committee (the Committee) will continue to meet once a month in 2008 as well. Meetings will be held according to the previously set calendar and start at 13.00. After making a decision, summary of the decision and its rationale will be posted on the website of the Bank in a press release at 19.00 on the same day. English translation of the decision will be posted on the website on the same day.

To enhance the communication of monetary policy decisions, "Summary of the Monetary Policy Committee Meeting" will continue to be posted in both Turkish and English on the Bank's website within *eight working days* following the meeting.

The *Inflation Report*, which is the main communication tool of the monetary policy, will continue to be published quarterly, and the general evaluation of the Report will be presented to the public with a press conference. The *Financial Stability Report* will be published twice a year[1]. The "*Price Developments"* report will be published on the *working day* following the announcement of inflation data.

Beside these communication tools, speeches and presentations made by Central Bank autorities at the meetings in Turkey or abroad constitute an important pillar of the communication policy. Working papers, booklets and technical notes published along with the conferences and workshops organized by the Bank will be used as effective tools for communication policy.

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[1] The publication calendar for the Inflation Report and the Financial Stability Report along with the Monetary Policy Committee Meeting dates are presented in the Appendix.

Exchange rate policy and liquidity management

Exchange rate policy and foreign exhange buying auctions

Along with inflation targeting, the Central Bank will continue to implement floating exchange rate regime in 2008. As stated in the annual monetary and exchange rate policy announcements that have been published since 2002, the foreign exchange rate is neither a target, nor a policy tool in the floating exchange rate regime. Exchange rates are determined according to the supply and demand conditions in the market. The main factors affecting foreign exchange supply and demand are the monetary and fiscal policies implemented, international developments, economic fundamentals, and expectations.

Even if floating exchange rate regime has been adopted, keeping a strong foreign exchange reserves position is very important in emerging economies like Turkey to eliminate the unfavorable effects of potential internal and external shocks and to boost confidence in the country's economy. Moreover, the foreign debt payments of the Treasury should be settled and remittance accounts that comprise a significant part of the liabilities side of the Central Bank's balance sheet need to be gradually reduced in the long-term. Therefore, the Central Bank holds foreign exchange buying auctions to build up reserves at times where foreign exchange supply increases compared to foreign exchange demand.

With the aim of minimizing the impact on supply and demand conditions in the foreign exchange market, the Central Bank has been buying foreign exchange via foreign exchange buying auctions with pre-announced terms and conditions since 1 April 2002 and has been announcing annual auction programs since 2005. Even if the aim is running the auctions according to the pre-announced program, in case of significant developments exceeding the forecasts pertaining to foreign exchange supply, amendments to auction programs can be made with prior notice.

Thus,

i) The maximum amount to be purchased in daily foreign exchange buying auctions has been set as USD 45 million for 2007, with USD 15 million for auction amount and USD 30 million for optional selling amount,

ii) Then, the auction amount has been raised to USD 40 million as of 25 July 2007 with an assumption that the capital inflow to Turkey will follow a strong trend due to the end of the election process and positive expectations for macroeconomic policies,

iii) However, the auction amount has been lowered to USD 15 million as of 15 August 2007 due to the fact that the unfavorable developments in housing and credit markets in developing countries increased the volatilities in the Turkish markets as well as in other developing markets in the said period.

iv) The measures taken by central banks in order to alleviate the problems in housing and credit markets have relatively reduced the volatilities in these markets and increased the global risk appetite. Therefore, the maximum amount to be purchased in auctions has been set as USD 90 million with USD 30 million for auction amount and USD 60 million for optional selling amount from 9 October 2007 onwards.

As of 14 December 2007, the total amount of foreign exchange purchased via auctions in 2007 is USD 9.5 billion and there has not been any direct intervention in the foreign exchange market. The total amounts of foreign exchange purchased and sold by the Central Bank from 2002 onwards are shown year by year in the table below:

Table 2: The Central Bank's net foreign exchange purchases and sales (2002-2007; USD million)

Year	FX Buying Auctions	FX Selling Auctions	FX Buying Interventions	FX Selling Interventions	Total Net FX Buying
2002	795	-	16	12	**799**
2003	5,652	-	4,229	-	**9,881**
2004	4,104	-	1,283	9	**5,378**
2005	7,442	-	14,565	-	**22,007**
2006	4,296	1,000	5,441	2,105	**6,632**
2007*	9,494	-	-	-	**9,494**
Total	**31,783**	**1,000**	**25,534**	**2,126**	**54,191**

** As of 14 December 2007.*

Unless extraordinary differences are observed in foreign exchange liquidity conditions, foreign exchange buying auctions will continue in 2008 with the aforementioned amount that has been set as USD 90 million maximum with USD 30 million for auction amount and USD 60 million for optional selling amount. However, as was the case before, the developments related to foreign exchange supply will be closely monitored and in the event of unforeseen extraordinary developments, the Central Bank may, with prior notice, change the daily auction amount and/or optional selling amount in both directions and may suspend the auctions temporarily for shorter and longer periods.

On the other hand, the Central Bank will continue to closely monitor the volatility in exchange rates also in 2008 and will directly intervene in the market in the event of actual and potential excessive volatilities.

Banks will also be able to borrow foreign exchange in terms of USD and euro from the Central Bank within the predetermined limits with a one-week maturity in the Foreign Exchange and Banknotes Market-Foreign Exchange Deposit Market in the upcoming period. Moreover, the purchase/sale transactions of "foreign exchange against foreign exchange", "foreign exchange against foreign banknotes" and "foreign banknotes against foreign banknotes" conducted between the Central Bank and institutions authorized to operate in the Foreign Exchange and Banknotes Markets will continue.

In conclusion, within the framework of the current exchange rate regime and the exchange rate policy of the Central Bank, economic agents should take into account that they operate in an environment of exchange rate risk and that they should establish mechanisms that will ensure the efficient management of this risk.

Liquidity management

As an outcome of the Central Bank's foreign exchange purchases, the excess liquidity in the market continued in 2007, as well. The Central Bank continued to withdraw the excess liquidity in the market mainly via New Turkish Lira deposit transactions in the Interbank Money Market within the CBRT and repo transactions in the Repo and Reverse Repo Market of the Istanbul Stock Exchange, on an overnight basis. However, when the excess liquidity withdrawn via overnight operations increased, the Central Bank has started to issue liquidity bills from July onwards in addition to its overnight operations in order to increase the flexibility and efficiency of liquidity management. Overnight interest rates in the market were generally around the borrowing rate of the Central Bank, depending on the withdrawal of the excess liquidity by the Central Bank via overnight operations. Hence, the borrowing rate of the Central Bank has continued to be an indicator for money markets.

Based on the information currently available,

i) The increase in base money,

ii) Coupon and principle redemption by the Treasury to the Central Bank,

iii) Treasury's being net foreign exchange debt payer,

will have a lowering effect, while;

iv) The Central Bank's net foreign exchange purchases,

v) Interest payments to be made by the Central Bank for required reserves and excess liquidity absorbing transactions,

vi) The decline in Treasury cash accounts within the Central Bank

will have an increasing effect on the level of the liquidity in the market in 2008.

In view of the Treasury's financing program for 2008 and the Central Bank foreign exchange buying auction program for 2008, the excess liquidity in the market is expected to continue generally at reasonable levels in 2008. However, as was the case in previous years, the level of liquidity in the market may change significantly depending on the changes in Treasury's financing program as well as in foreign exchange buying amounts of the Central Bank and changes in Treasury cash accounts within the Central Bank.

As long as the excess liquidity in the market remains at reasonable levels, the Central Bank will continue to withdraw the excess liquidity in the market on an overnight basis, via New Turkish lira deposit transactions in the Interbank Money Market within the CBRT and repo transactions in the Repo and Reverse Repo Market of Istanbul Stock Exchange. Hence, overnight interest rates will continue to be at the level of the borrowing rate of the Central Bank. Thus, the overnight borrowing rate of the Central Bank will continue to be the benchmark interest rate with respect to the monetary policy.

In case of a permanent liquidity shortage in the market, the benchmark short-term interest rates will not be the borrowing rate of the Central Bank but the average interest rate of the repo auctions, which is the basic funding instrument. Therefore, in case of tightening in liquidity, the interest rate taken as a benchmark by the market would have increased merely due to the decline in liquidity. In order to avoid the negative impacts of such a situation, the Central Bank could lower its borrowing and lending interest rates – provided that the inflation outlook is stable – so as to encounter the pressure created by liquidity shortage on overnight interest rates. However, such an interest rate cut would only mean a technical arrangement stemming from the change in liquidity conditions. Therefore, such a move should not be perceived as loosening of monetary policy.

The Central Bank does not foresee any significant changes in the general framework of the liquidity management for 2008. Accordingly, 2008 liquidity management strategy will be as follows:

i) The Central Bank will continue to announce overnight borrowing and lending rates between 10:00-12:00 and 13:00-16:00 in the Interbank Money Market within the CBRT. In case of a liquidity shortage during the day, banks will be able to borrow at the Central Bank's lending rate against collateral within their limits. In the event of a fall in interest rates due to increasing liquidity, banks will be able to lend New Turkish Lira to the Central Bank at the Central Bank's borrowing rate without any limit.

ii) The Central Bank extended the transaction hours of Late Liquidity Window Facility from 16:00-16:30 to 16:00-17:00 and on the last working day of the required reserve provision to 16:00-17:15 as of July 9, 2007 in order to increase the flexibility and effectiveness of the liquidity management of banks. The Central Bank will continue to provide Late Liquidity Window Facility such that banks may borrow from the

Central Bank against collateral, and lend to the Central Bank without any limit within the hours mentioned above.

iii) In case of a temporary or permanent liquidity shortage, the Central Bank will continue to carry out its liquidity management through one-week repo auctions. When there is liquidity shortage in the market, the Central Bank will announce the amount of repo auction for that day on Reuters' "CBTF" page at 10.00. As long as no extraordinary fluctuations are observed in the market, the Central Bank, while determining the amount of the auctions, will endeavor to maintain the average auction interest rate;

    a) At maximum of 1 percentage point above the borrowing rate of the Central Bank announced for the intra-day transactions to reduce fluctuations in O/N interest rates, in cases where the liquidity shortage in the market is envisaged temporary and when the technical interest rate cut explained in paragraph 45 is not applied,

    b) Approximately at the mid point of the O/N borrowing and lending rates of the Central Bank, in cases where the liquidity shortage in the market is envisaged permanent and the technical interest rate cut explained in paragraph 45 is applied.

iv) The weekly repo auctions will be held at 11:00. and the results will be announced on Reuters' "CBTG" page no later than 11:30.The traditional method will be used in auctions; in other words, the successful bidders will be evaluated with their own interest rates.

v) In case of unforeseen excessive liquidity shortage during the day, which would exert excessive pressure on money market interest rates, the CBRT may announce "Intra-day Repo Auctions" in addition to the regular ones announced at 11:00.

vi) The primary dealer banks will be able to conduct repo transactions within the framework of open market operations, between 10:00-12:00 and 13:00-16:00.

vii) In case of an excessive increase in the liquidity surplus in the market, mainly the Central Bank liquidity bills with maturity up to 91 days, and when necessary New Turkish Lira deposit buying auctions with standard maturities of 1, 2 and 4 weeks and reverse repo auctions with maturities up to 91 days will be used actively, in order to enhance the effectiveness and flexibility of monetary policy and liquidity management strategy. However, the Central Bank will continue to focus on sterilizing the excess liquidity, which is at such a level that would bring the overnight interest rates in the money markets close to the Central Bank borrowing rates, through overnight transactions.

viii) In case of the emerge of extraordinary fluctuations in the market even at reasonable levels of excess liquidity, the Central Bank may allow the overnight interest rates to fluctuate between the Central Bank overnight borrowing and lending interest rates range by sterilizing the excess liquidity drained in overnight transactions through liquidity bills, New Turkish Lira deposit buying auctions and reverse repo auctions, in order to reduce the said fluctuations.

ix) In case of the emerge of a need to issue liquidity bills, information on auctions will be announced at Reuters' "CBTL" page at 10:00 one working day prior to the auction rather than on the same day, to provide investors a longer time for evaluation. Information on auctions will continue to be announced to banks and financial intermediaries by Electronic Fund Transfer (EFT) system. Liquidity bill auctions will be held at 11:00 with the value date of the following working day, and the results will be announced until 11:30 at Reuters' "CBTM" page. Auctions will be held by the traditional method.

x) Information on New Turkish Lira deposit buying auctions will be announced at Reuters' "CBTY" page; while information on reverse repo auctions will be announced at "CBTF" page at 10:00 on the same day.

In case of an accelerated credit expansion in the banking system in such an extent that would create inflationary pressure despite the active use of the said open market operations to drain the excess liquidity in the market, required reserves may also be used effectively to support liquidity management.

The Central Bank, the primary goal of which, entrusted to it by law, is to achieve and maintain price stability, will continue its practices to enhance the effectiveness of the monetary policy and liquidity management, also in 2008. Accordingly, the Central Bank may change not only its liquidity management strategy, but also the borrowing and lending interest rate margins in cases of unpredictable changes in market conditions and emergence of needs that may arise.

As always pointed out, the Central Bank deems the stability and development of financial markets as a supportive objective for the efficient implementation of the policies pertaining to price stability. Obviously, under the floating exchange rate regime, the Central Bank is able to implement the YTL liquidity policy in a more flexible manner than it can under a fixed currency peg regime and can act more promptly and flexibly to meet the YTL liquidity needs of the banking system. Also, the Central Bank can prevent excessive fluctuations in money market interest rates as long as they are consistent with the inflation target. Furthermore, the Central Bank provides the banking system with foreign exchange liquidity via short-term foreign exchange deposit auctions, albeit at limited amounts. However, it is worth mentioning once more that the banking system should not slacken risk management principles by simply relying on the more flexible and effective New Turkish Lira liquidity management and the foreign exchange liquidity facility of the Central Bank. On the contrary, the banking system should use risk management principles effectively.

Annex: calendar for 2008

MPC Meeting Dates	Inflation Report	Financial Stability Report
17 January, Thursday	31 January, Thursday	
14 February, Thursday		
19 March, Wednesday		
17 April, Thursday	30 April, Wednesday	
15 May, Thursday		30 May, Friday
16 June, Monday		
17 July, Thursday	28 July, Monday	
14 August, Thursday		
18 September, Thursday		
22 October, Wednesday	31 October, Friday	
19 November, Wednesday		28 November, Friday
18 December, Thursday		