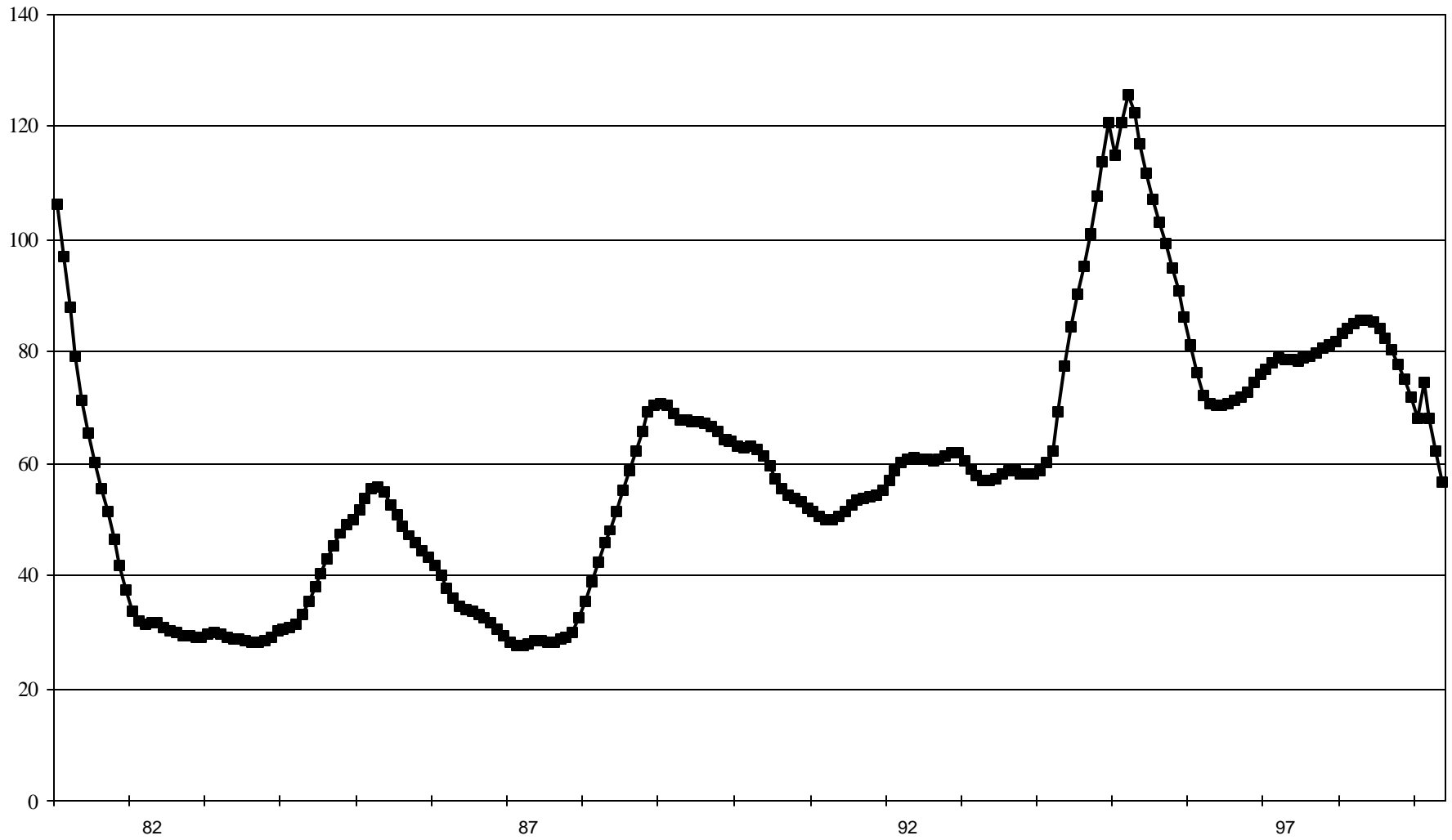


Is Turkey Winning the Fight Against Inflation?

Dani Rodrik

September 13, 2000

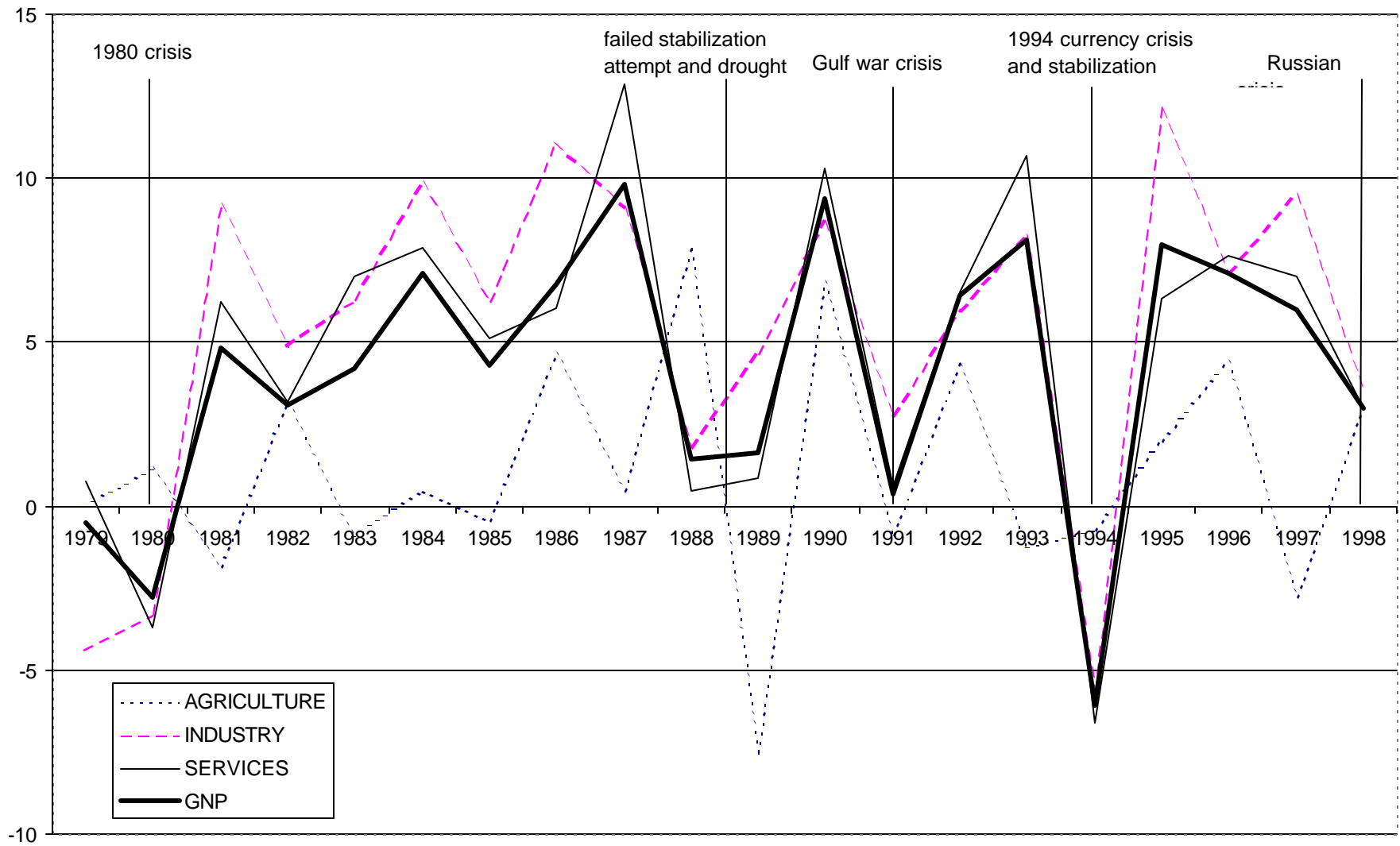
Inflation since the early 1980s

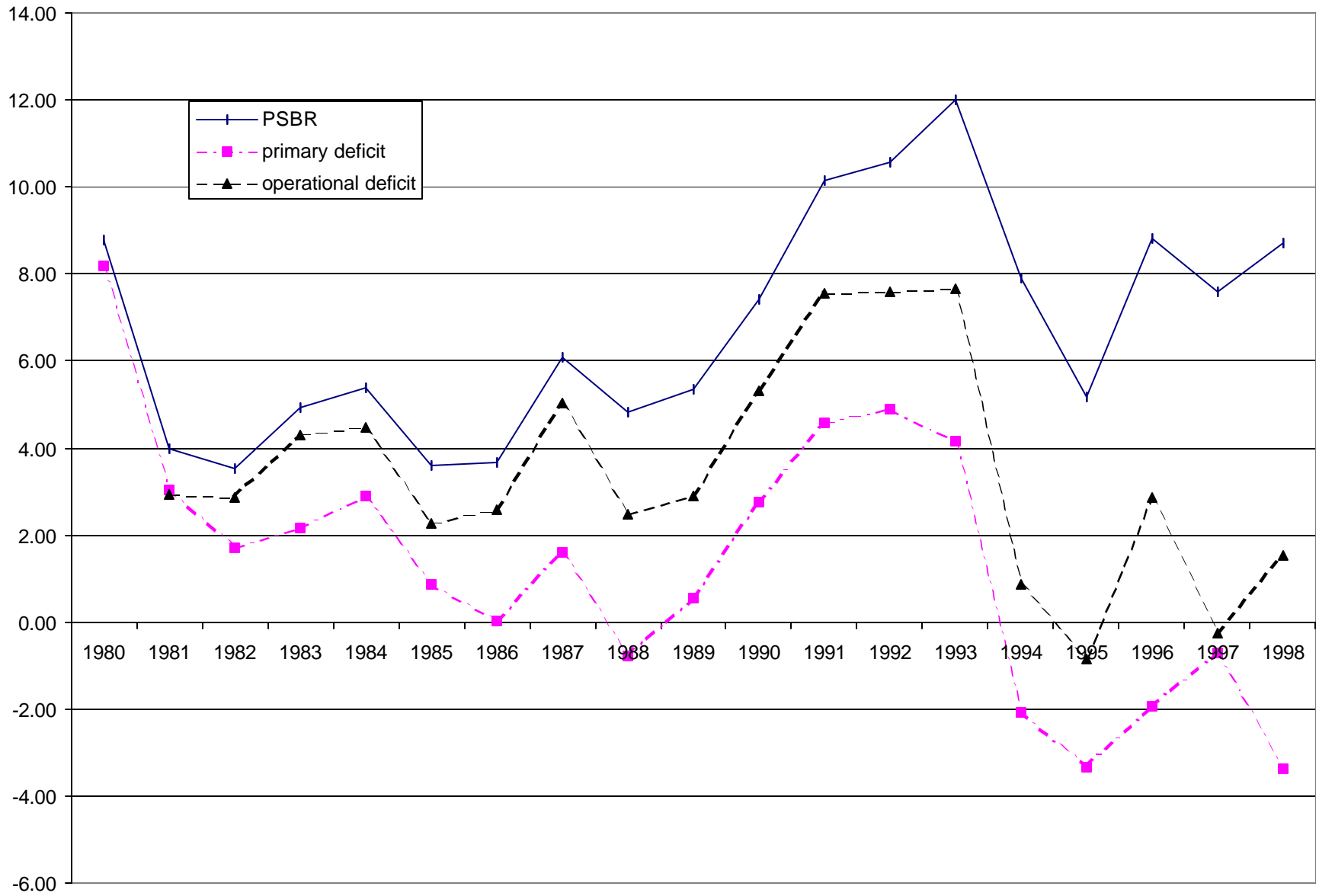


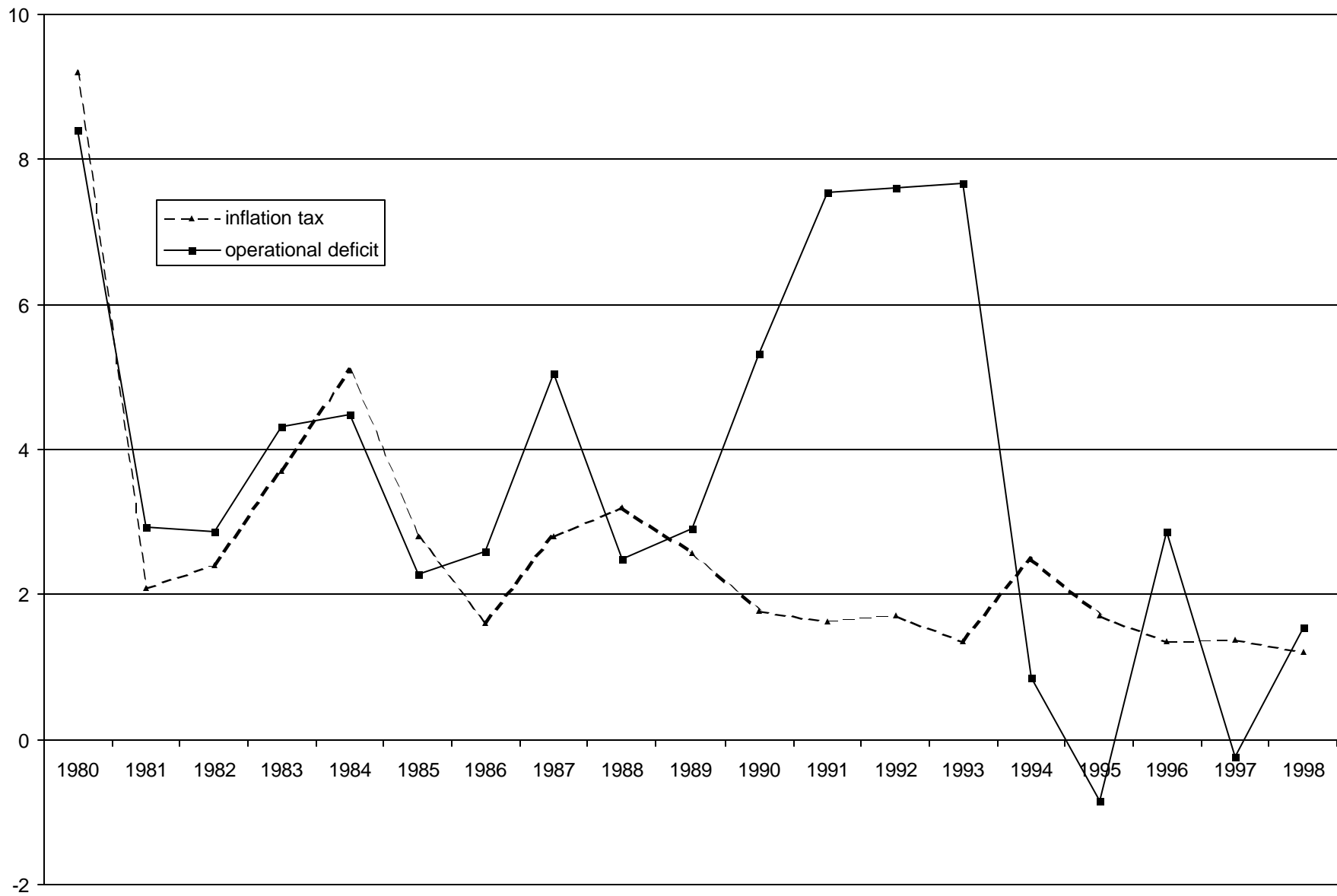
Annual inflation rates in 1999

Belarus	294 %
Angola	248
Congo, Dem. Rep.	200
Russia	86
Turkey	65
Zimbabwe	60
Ecuador	55

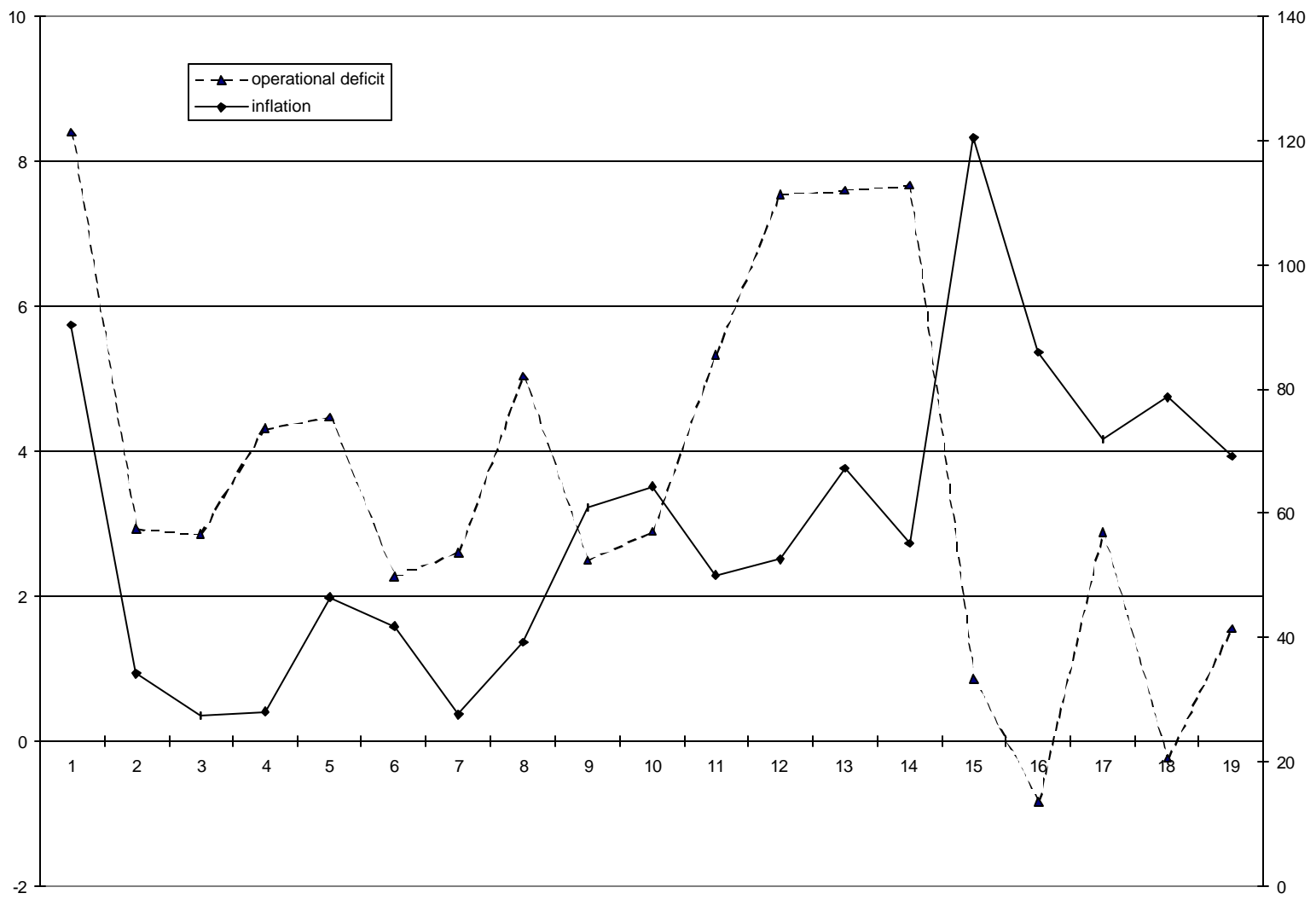
Growth rates of GNP by sector







Inflation and Deficits



Inertial Inflation

$$p_t = ap_{t-1} + by_t$$

a large

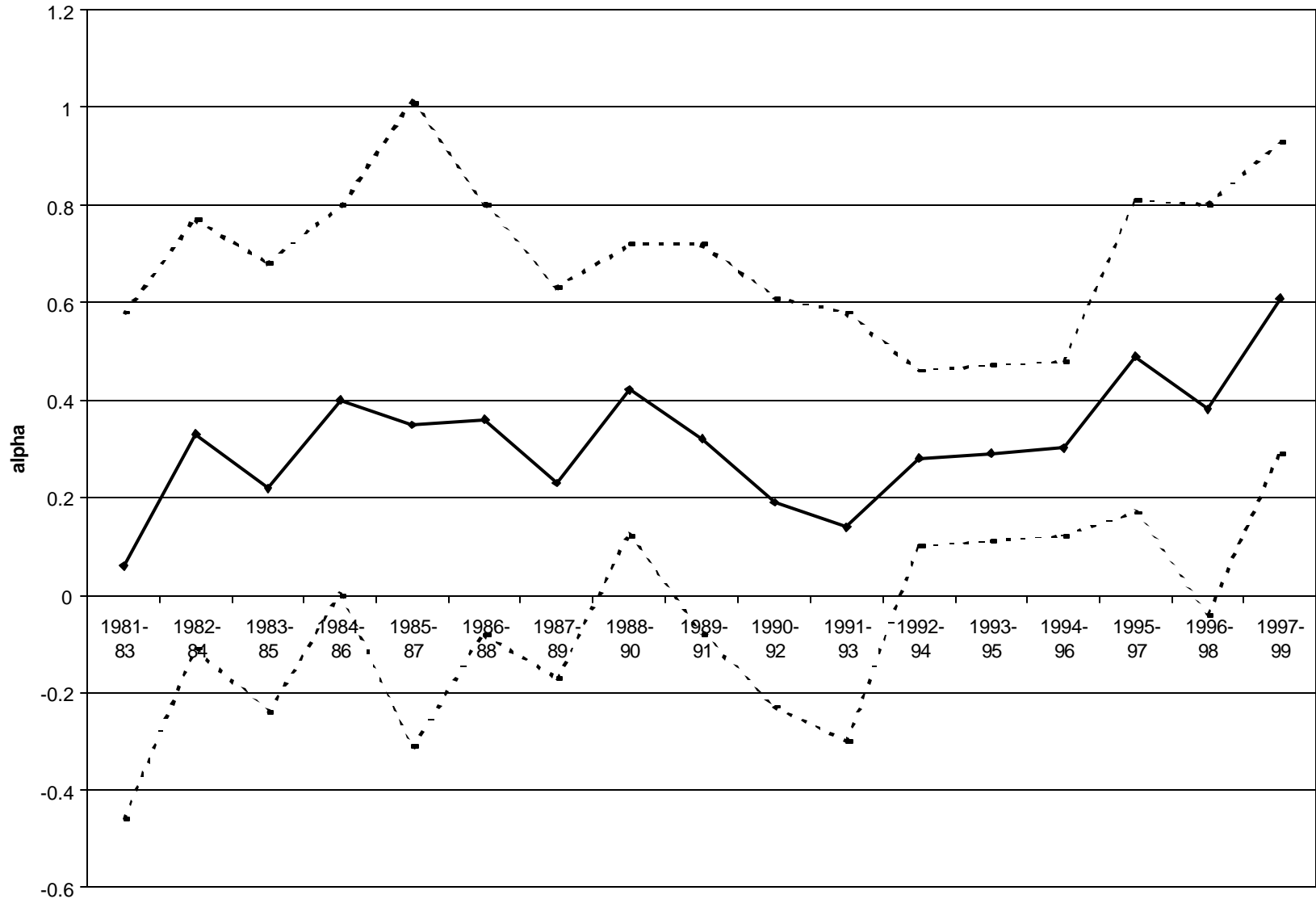
b small

Determinants of price movements in inertial inflation:

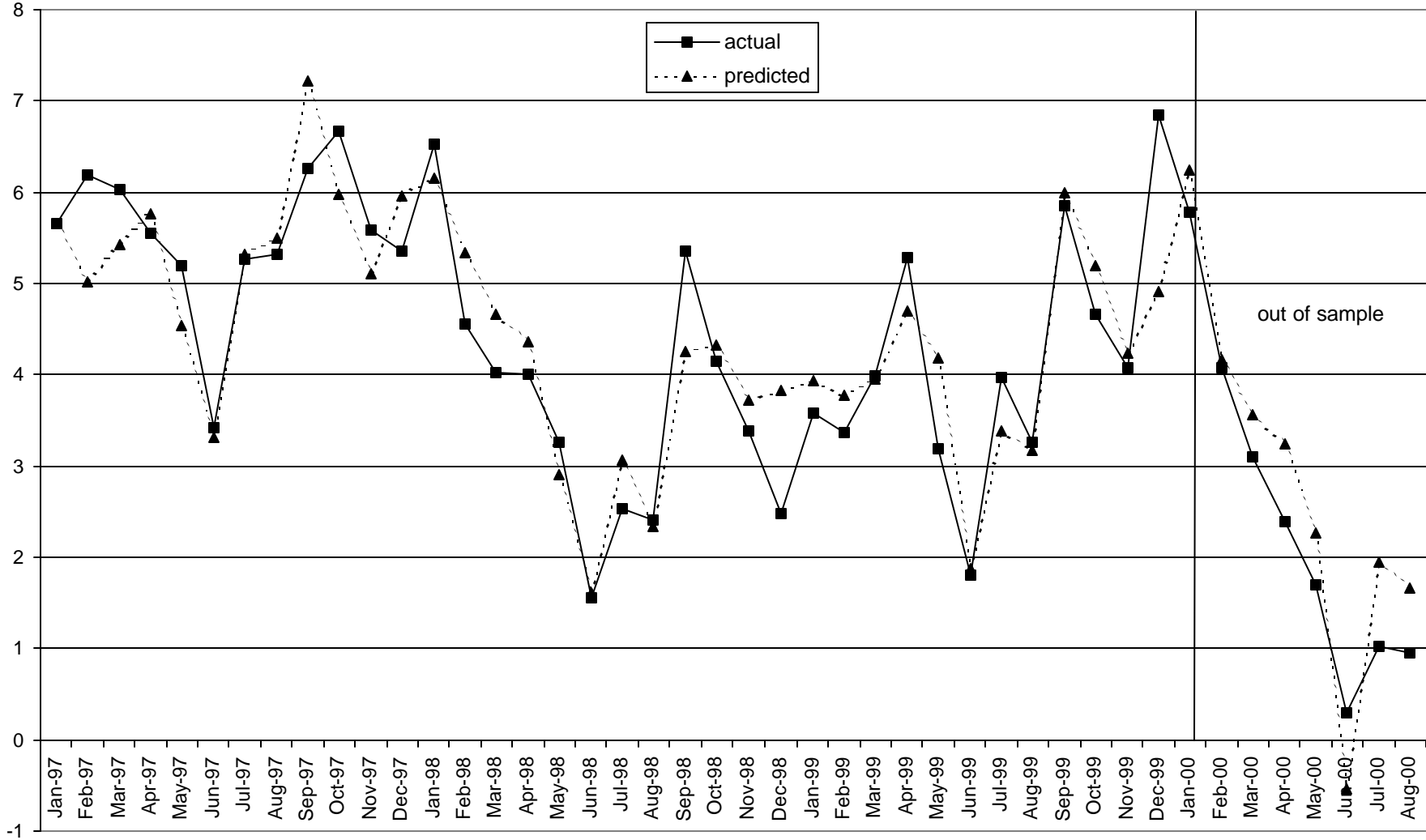
$$p_t = \alpha p_{t-1} + \gamma \hat{e}_t + \text{seas. effects}$$

	wpi	cpi	wpi-priv	wpi-priv. man.
alpha	0.61*	0.53*	0.73*	0.56*
gamma	0.33**	0.26***	0.20	0.41*
R-squared	0.79	0.79	0.86	0.90

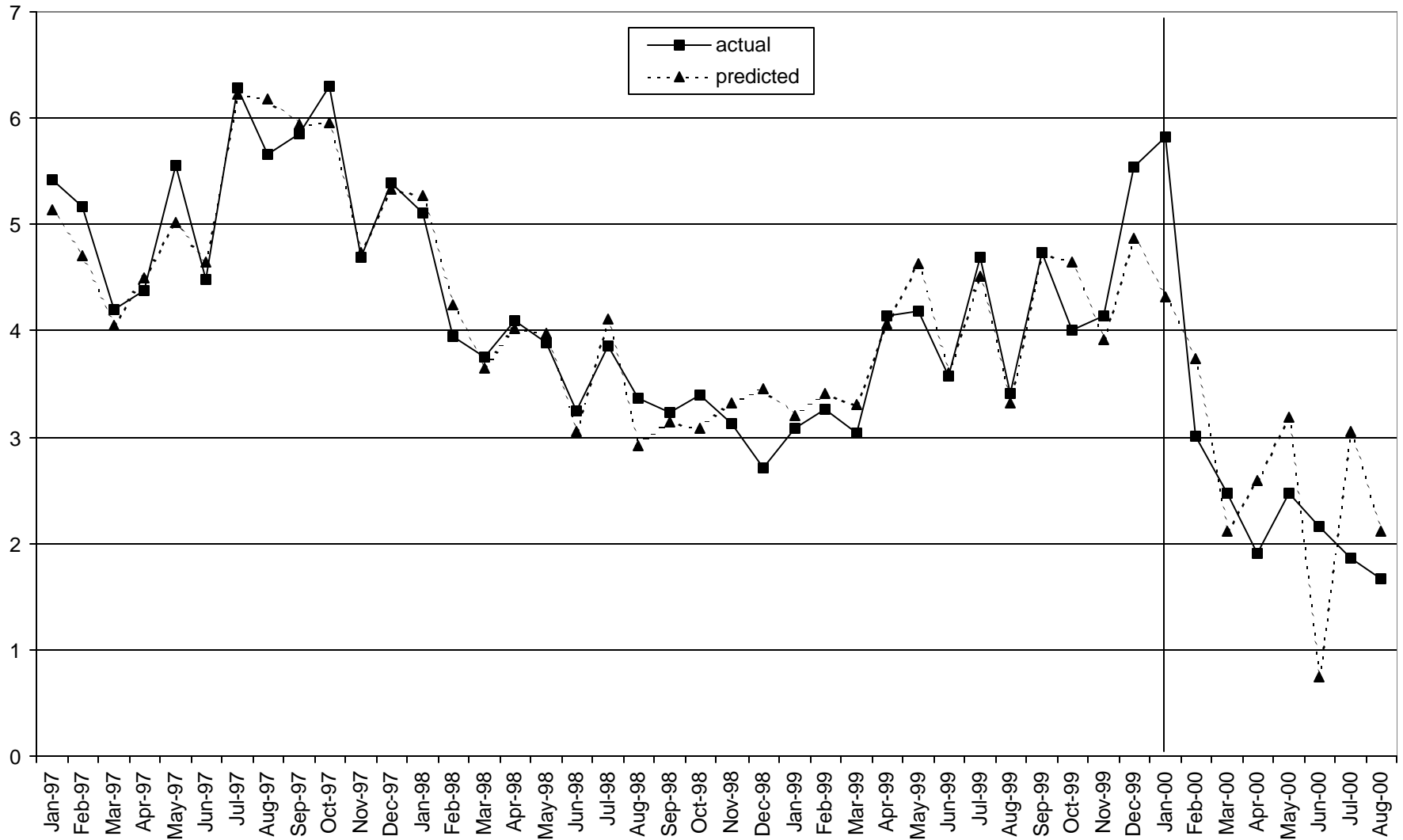
Inflation persistence coefficient over time
(with 95 percent confidence interval)



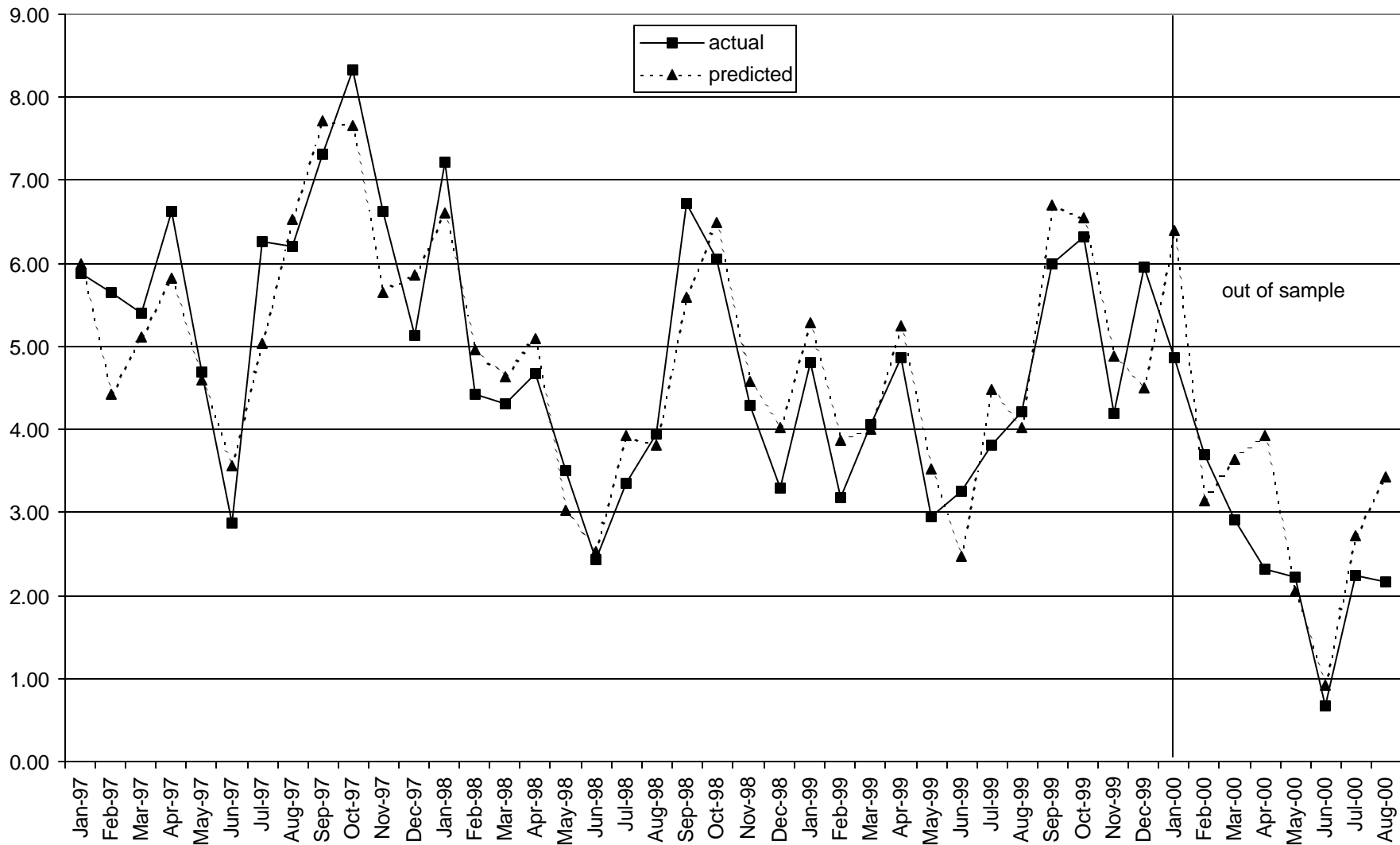
WPI
Predicted and actual inflation, January 1997-August 2000
(based on 1997:1-1999:12 sample)



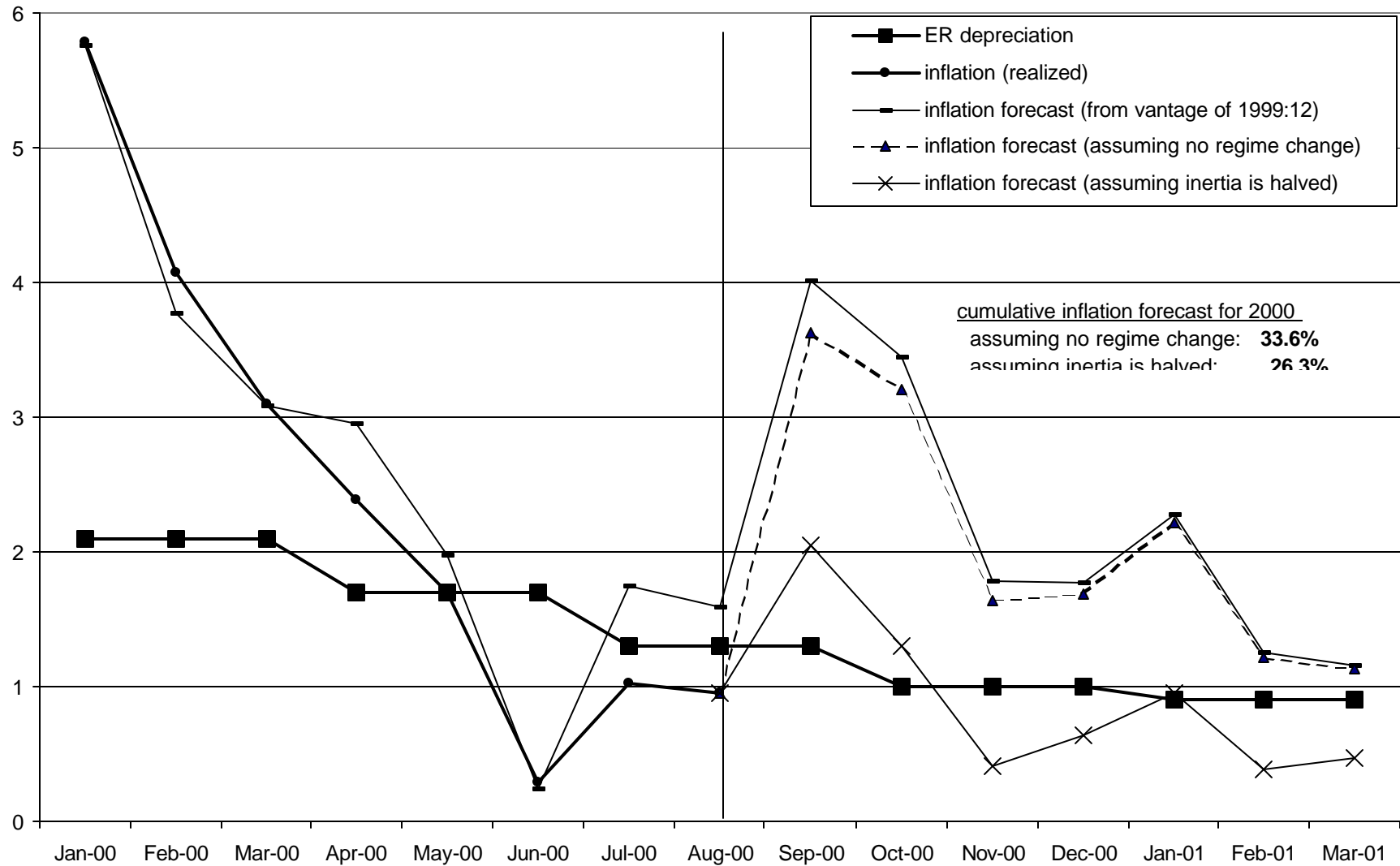
WPI - Private manufacturing
Predicted and actual inflation, January 1997- August 2000
 (based on 1997:1-1999:12 sample)



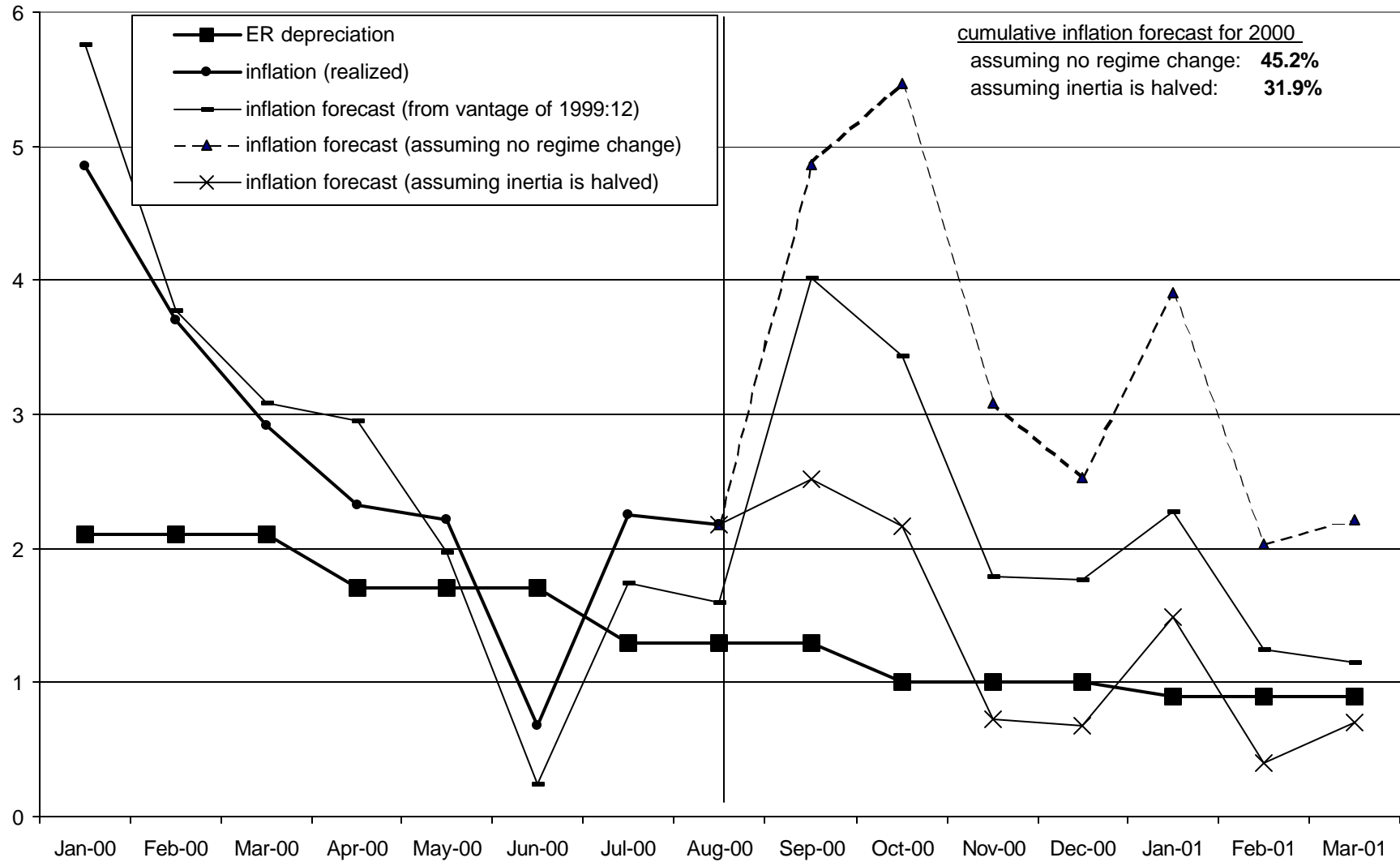
CPI
Predicted and actual inflation, January 1997- August 2000
(based on 1997:1-1999:12 sample)



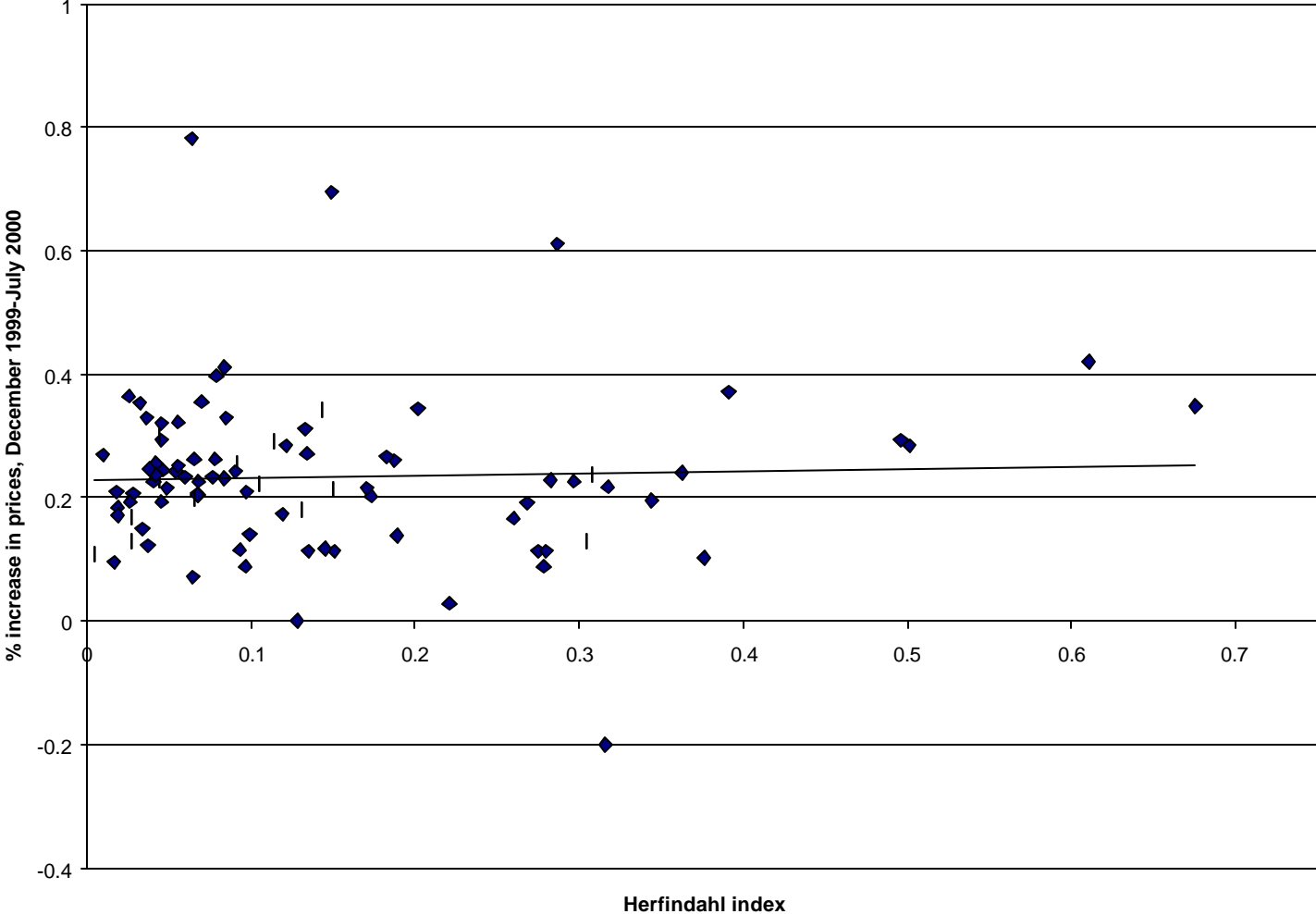
**WPI: Inflation forecast and exchange-rate path
(Jan-Aug 2000: realized inflation)**



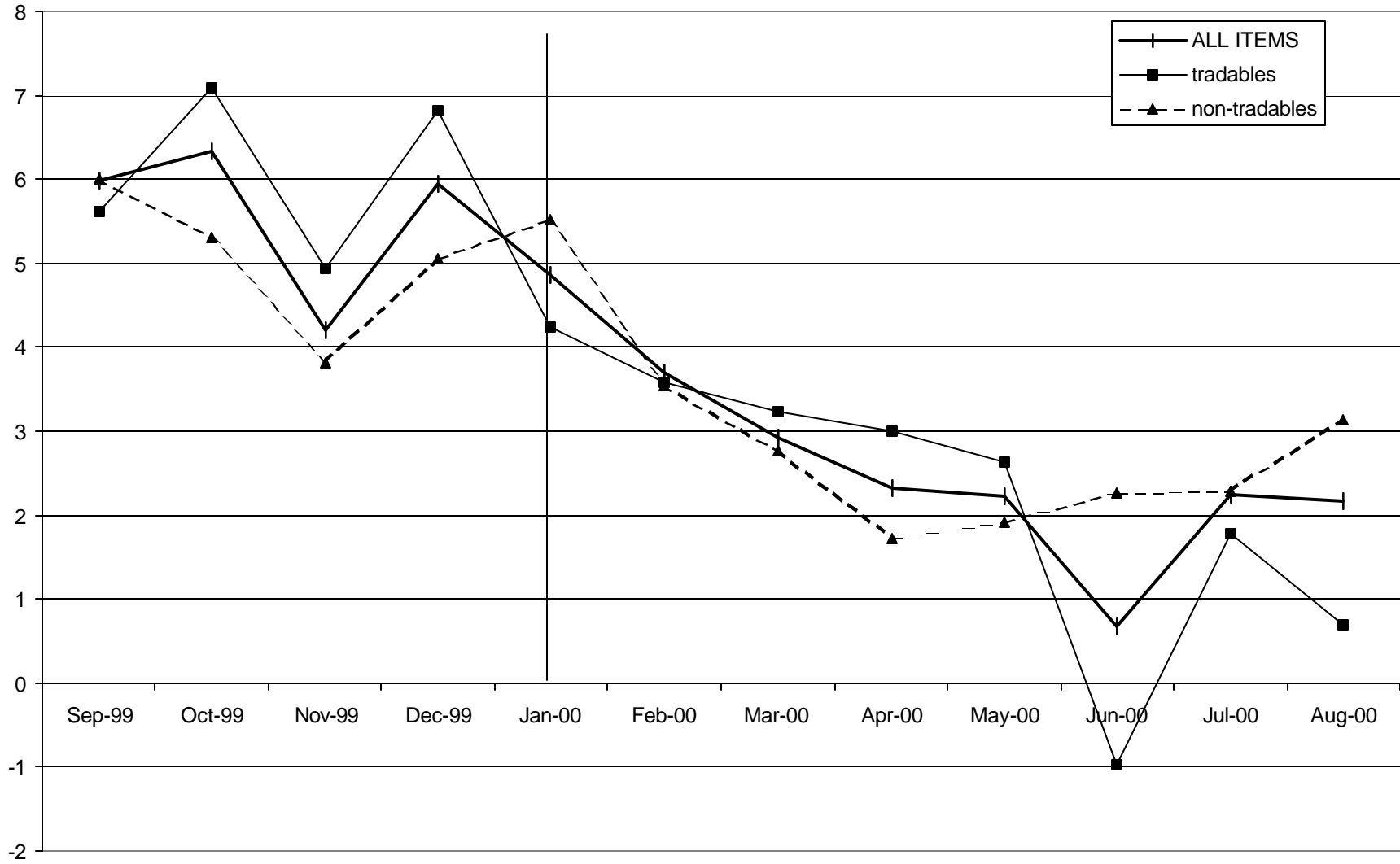
**CPI: Inflation forecast and exchange-rate path
(Jan-Aug 2000: realized inflation)**



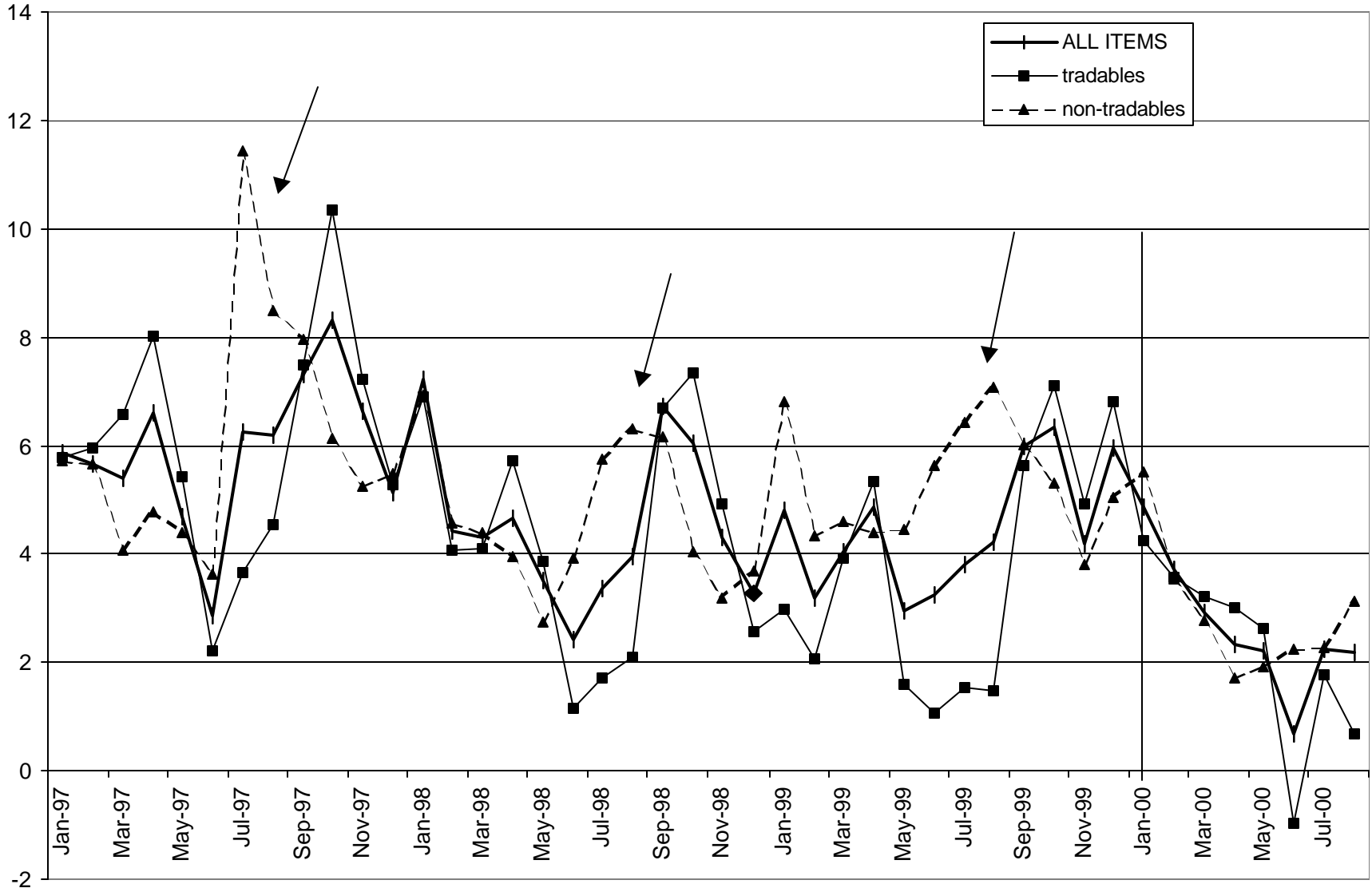
Relationship between firm concentration and price increases
(by 4-digit private manufacturing industries)



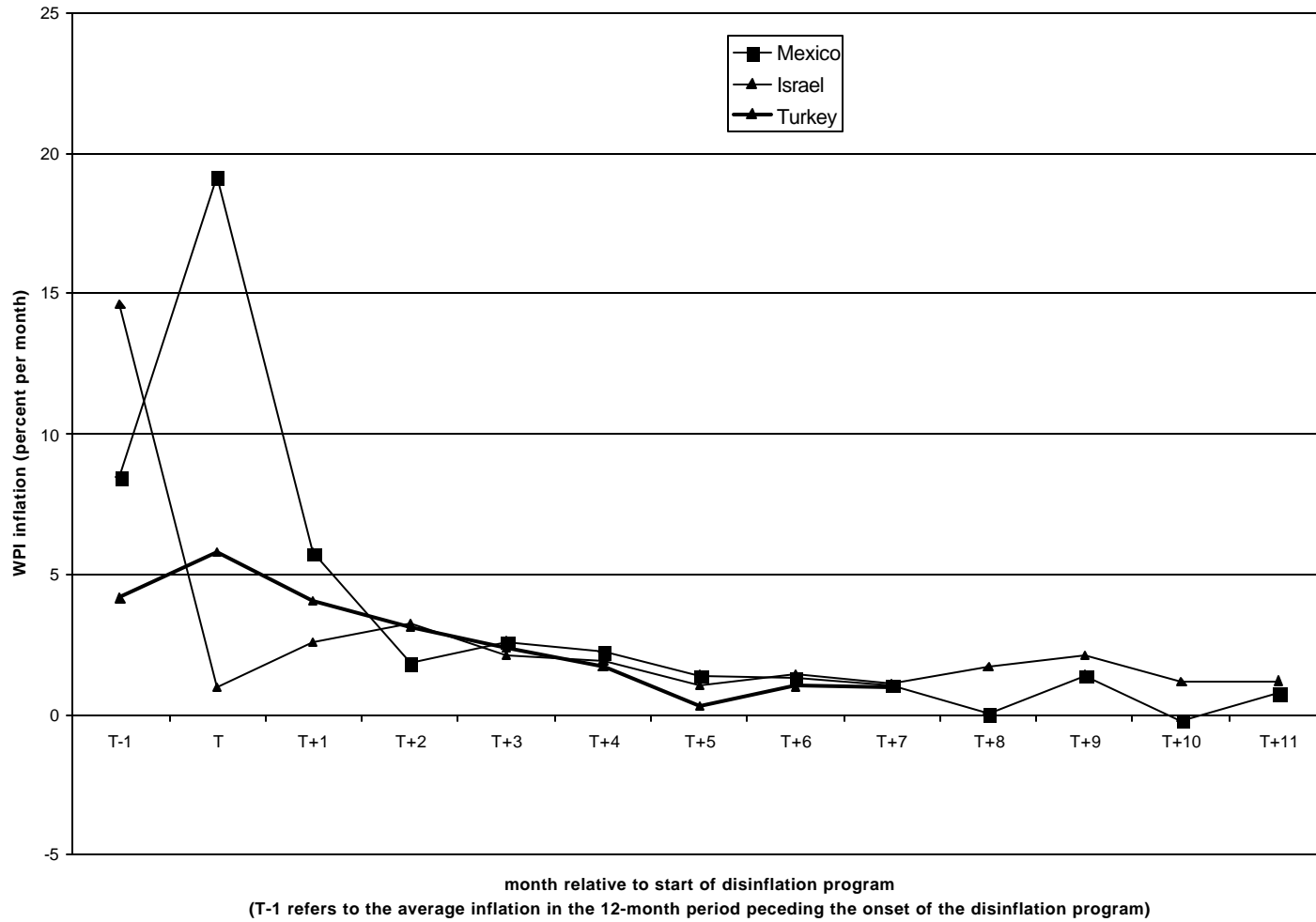
CPI by components



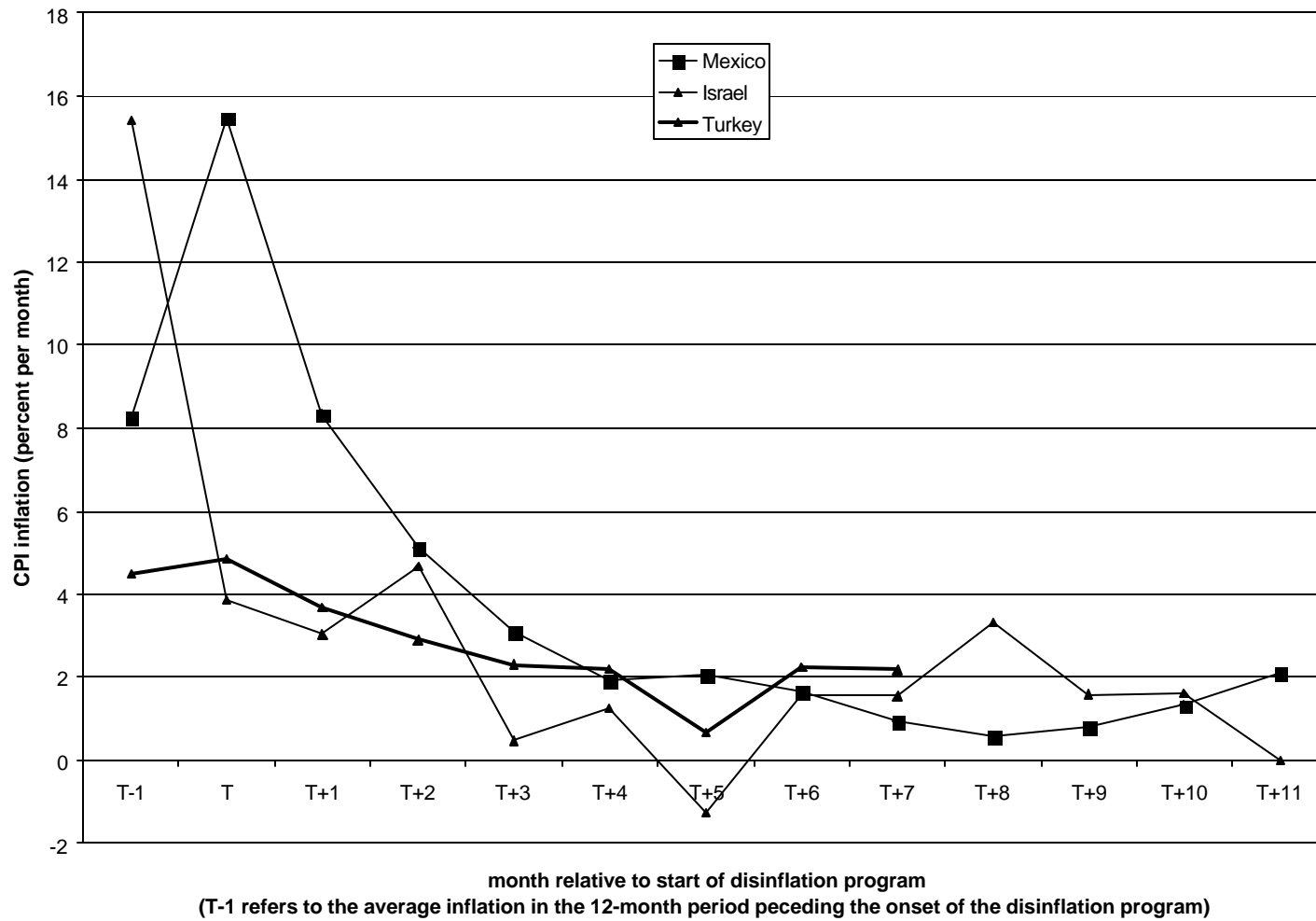
CPI by components



Comparative Disinflation Experience (WPI)



Comparative Disinflation Experience (CPI)



Bottom line on disinflation:

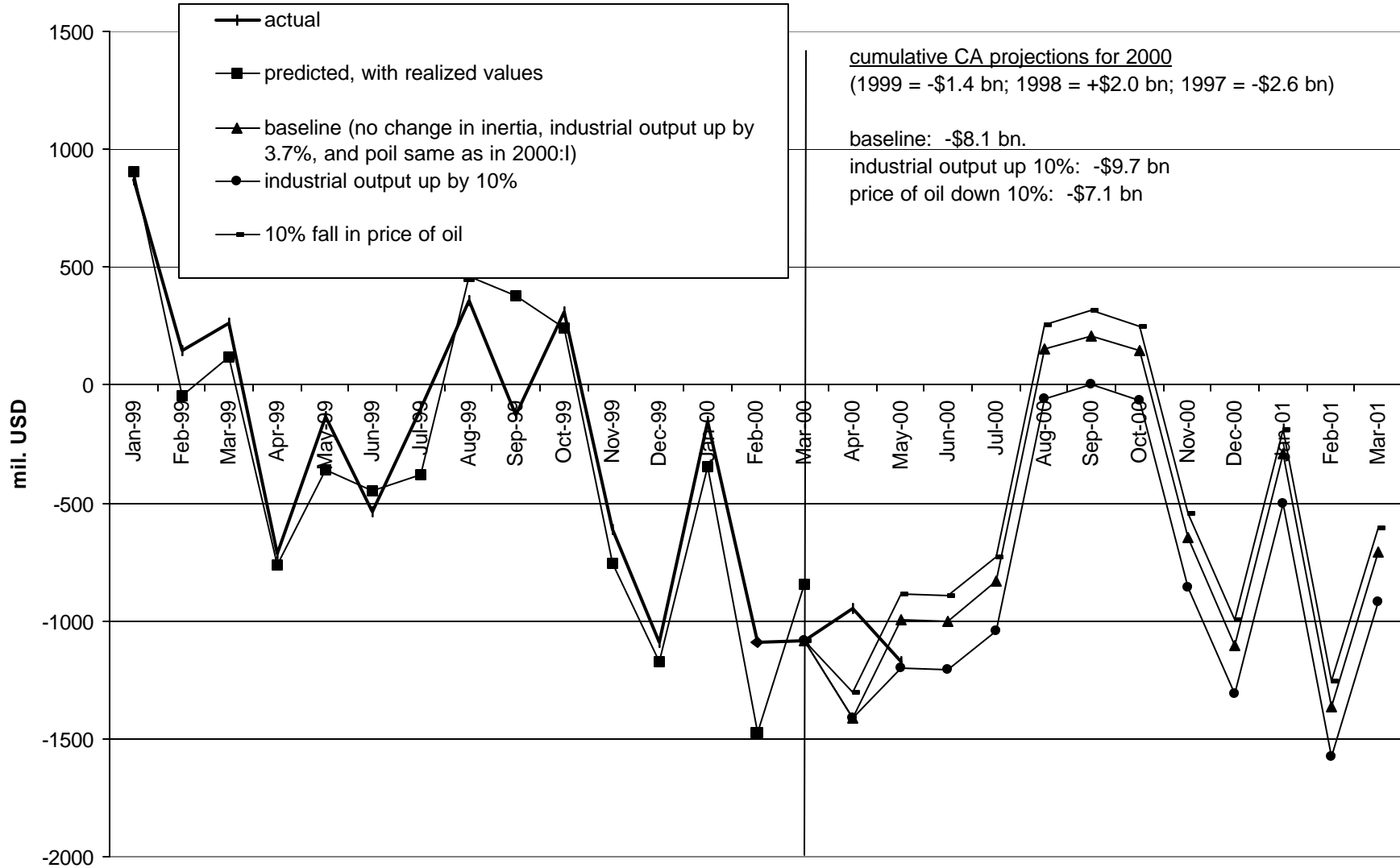
- Outcomes favorable, despite negative shocks (oil prices; \$ appreciation)
- Behavior of CPI or WPI-Pman not “unusual”
- Do not over-analyze each month’s outcomes
- Be patient and hold the line

Determinants of the trade and current account balances:

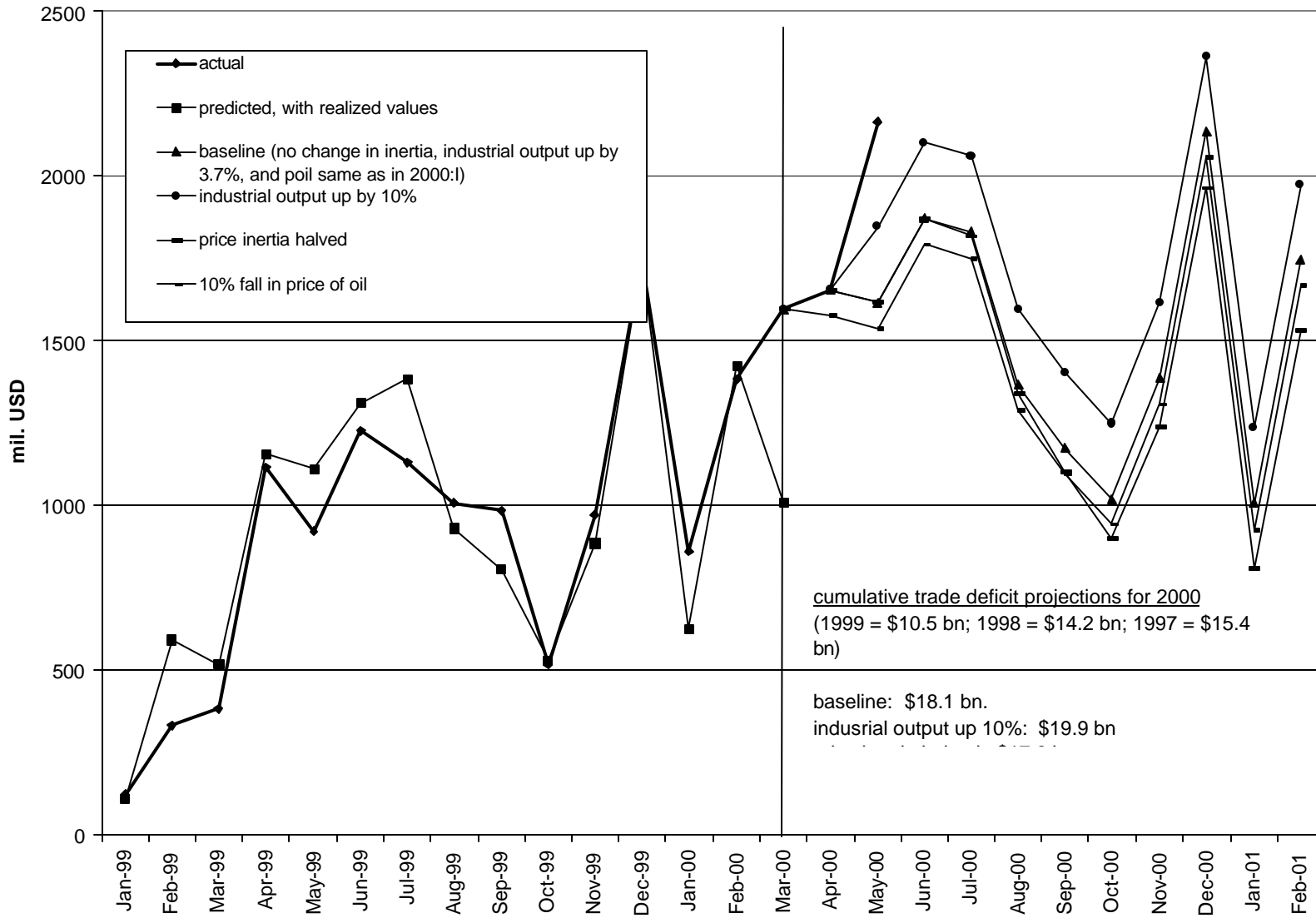
Trade balance = f (real exchange rate, econ. activity,
oil prices, seas. effects)

CA balance = g (real exchange rate, econ. activity,
oil prices, seas. effects)

CAB projections



Trade deficit projections



Why the consumption boom?

Interest-rate arbitrage

$$i = i^* + E\hat{e} + r$$

domestic interest rate = foreign interest rate + expected rate of currency depreciation + risk premium

CA deficit large, but possibly manageable on current trends until mid-2001

- Make more reasonable forecasts of the CA deficit
- Watch closely the financing of the CA deficit
- Do not promise a quick growth payoff
- Plan for preventive measures in the fall if CA deficit widens beyond forecast
 - raise consumption taxes on durables
 - discourage bank credit boom
 - tax short-term capital inflows

Wider incomes policies

- Their absence the weakest link in the program
- Incomes policies extending to private sector employers and employees, and negotiated under government leadership, may be a crucial confidence-boosting step to ensure the “exit strategy” works smoothly.