Makale / Article

Is the Liraization Strategy of the Central Bank of Republic of Türkiye Successful?

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Abstract

This study aims to analyze the success of the "Liraization Strategy" introduced by the Central Bank of Republic of Türkiye. Liraization, the main component of unusual monetary policy, officially implemented from the beginning of 2022 to the second half of 2023. Using the policy texts of the Central Bank and literature review; regulations, tools and targets of the liraization strategy has been figured out. To evaluate the success of liraization, realization of the goals has been examined employing real data and graphical analysis. The outcomes indicate that the strategy has failed in price stability and financial stability. In addition, the current account balance has worsened. On the other hand, rising the share of TL in balance sheets of companies and bank via intensive regulations has caused to high cost on budget and the Central Bank. Also, market interventions to support TL have disrupted the market mechanism and relative prices; and have increased the inequality in income distribution.

Keywords: Unusual Monetary Policy, Liraization Strategy, FX Protected Deposits, Market Intervention.

JEL Codes: E52, E58, E61, E62

Türkiye Cumhuriyeti Merkez Bankası'nın Liralaşma Stratejisi Başarılı mı?

Öz

Bu çalışma, Türkiye Cumhuriyet Merkez Bankası tarafından uygulamaya konulan Liralaşma Stratejisinin başarısını analiz etmeyi amaçlamaktadır. Liralaşma, geleneksel olmayan para politikasının temel bileşeni olup, 2022 yılı başından 2023 yılı ikinci yarısına kadar resmi olarak uygulanmıştır. Çalışmada, Merkez Bankası'nın politika metinleri ve literatür taraması kullanılarak liralaşma stratejisinin araçları ve hedefleri ortaya çıkarılmıştır. Liralaşmanın hedeflerine ulaşma başarısını değerlendirmek için gerçek veriler ve grafiksel analiz kullanılmıştır. Sonuçlar, stratejinin fiyat istikrarı ve finansal istikrarın sağlanmasında başarısız olduğunu göstermektedir. Ayrıca cari işlemler dengesi kötüleşmiştir. Diğer taraftan, yoğun düzenlemeler yoluyla şirket ve banka bilançolarında TL'nin payının artırılması, bütçe ve Merkez Bankası için yüksek maliyetlere neden olmuştur. Bunların yanında, TL'yi desteklemek için yapılan piyasa müdahaleleri, piyasa mekanizmasını ve göreli fiyatları bozmuş ve gelir dağılımındaki eşitsizliği artırmıştır.

Anahtar Kelimeler: Alışılmadık Para Politikası, Liralaşma Stratejisi, Kur Korumalı Mevduat, Piyasa Müdahalesi.

JEL Kod: E52, E58, E61, E62

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ORCID: 0000-0001-6993-7617 | DOI: 10.36484/liberal.1540390
Liberal Düşünce, Year: 29, Issue: 115, Summer 2024, pp. 105-142.
Date of Submission: 29 Aug 2024 | Date of Acceptance: 23 Sep 2024

Introduction

The Central Bank of Republic of Türkiye (CBRT) introduced unusual monetary policy in the last quarter of 2021. CBRT employed inflation targeting regime and used policy interest rate to control the inflation up to 2021: Q4. Then CBRT claimed that orthodox policies cannot provide the price stability in Türkiye and designed a new policy mix. Accordingly, policy interest rate decreased gradually to support investment and production despite having high inflation. In addition to lower interest rate, it was believed that depreciation of national currency would lead to high international competitiveness and high export volume. As a main component of new monetary policy, liraization strategy was introduced at the beginning of the year 2022 in the inflation report. In this strategy, it is aimed to ensure financial and price stability by increasing the share of TL-denominated instruments using intensive regulations and market interventions, and at the same time to solve the structural problems of the economy.

The liraization strategy has been employed officially from the beginning of 2022 to second half of 2023. Within the framework of liraization, TL-denominated instruments that protect against exchange rate risk, selective credit policy and liquidity management accompanied the negative real interest rate policy. The aim this study is to evaluate success of the liraization strategy by analyzing the targets and outcomes. This work contributes to literature examining this strategy for the first time by using real data and policy reports of CBRT.

In the first part of the study, the financial and economic environment in Turkish economy will be discussed briefly before the liraization strategy. Then, unusual monetary policy, mainly content of the liraization and its targets will be handled using inflation reports, financial stability reports and regulations of CBRT in the second part. The regulations of this strategy will be explained in the third part. In the fourth part, results of the liraization strategy will be discussed by graphical analysis. Finally, the study will be finished with suggestion for future monetary policy applications.

Turkish Economy Before the Liraization Strategy

Türkiye has ensured the financial and price stability employing IMF supported economy program after the 2001 crisis. Inflation was reduced to single digits in a short time by the help of the regulations to verify the independence of the Central Bank, the implementation of the inflation targeting regime, ensuring budget discipline, the stability of the exchange rate and the improvement of expectations. Significant capital inflow was experienced owing to improving macro-economic indicators, implementation of the IMF program and ample global liquidity. While the exchange rate started to appreciate, central bank reserves started to be strengthened. Restructuring the banking system and increasing monitoring and supervision have made a significant contribution to the development of financial markets. There have been significant increases in individual and commercial loans with the well-functioning credit market.

Despite macroeconomic stability, Türkiye has not started to micro reforms and the country has not solved the structural problems such as the current account deficit and dependence on external financing. In this environment, Türkiye experienced the 2008 global financial crisis. The country quickly overcame the effects of the global crisis as a result of the renewed abundance of global liquidity and domestic expansionary policies. High growth rates have led to the postponement of structural reforms and the accumulation of problems. Domestic production has been not developed to reduce imports of intermediate goods, capital goods and energy. The production and export of high-tech products that has high value-added have stayed at low levels. The country has not matured its industry, and the share of construction and many inefficient service sectors has increased. In addition, justice in income distribution could not be achieved, tax reform could not be carried out, and the high informal economy could not be controlled.

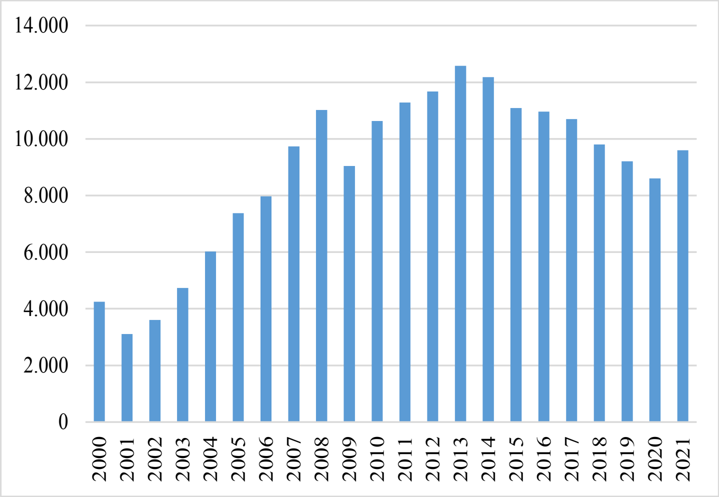
The economy, which lost momentum after 2013, GDP per capita started to decline (Graph 1). Türkiye tried to grow with loans, demand shocks and short-term solutions (Graph 3). As a result of these policies, price stability began to deteriorate with double-digit inflation since 2017 (Graph 2). Publicly supported expansionary policies also increased budget deficits. As global liquidity decreased and domestic expansionary policies became unsustainable, the fragility of the economy and growth volatility increased.

As a result of the accumulated problems in the economy and the tension with the USA, a significant exchange rate shock occurred in 2018, and financial and price stability were negatively affected. Türkiye started to use public resources intensively again to quickly recover from the impact of the 2018 exchange rate shock. Macroeconomic indicators were tried to be improved by using the CBRT's reserves and funds, the resources of the unemployment fund and the resources of public banks. However, Türkiye, which rapidly consumed the resources it had accumulated for bad times, entered the global pandemic in 2020 with a fragile economy. To quickly overcome the effects of the pandemic, an uncontrolled credit growth was carried out and it caused to rapid increase in asset prices and inflation (Graph 2 and Graph 3). In addition, the fact that the Central Bank's net reserves, excluding swaps, were in negative led to a rapid increase in the exchange rate (Graph 5). Frequent changes of the central bank president have led to the questioning of the bank's independence and increased concerns about price stability and financial stability.

In September 2021, while inflation accelerated upwards from 20%, the CBRT started to reduce the policy interest rate. The unusual monetary policy signals initiated an unprecedented upward movement in the exchange rate and inflation. Despite these developments, continuing interest rate cuts distorted the relative prices in the market and led to a negative real return on TL-denominated assets. Under these conditions, CBRT carried on new monetary policy and introduced liraization strategy.

Main Macroeconomics Indicators

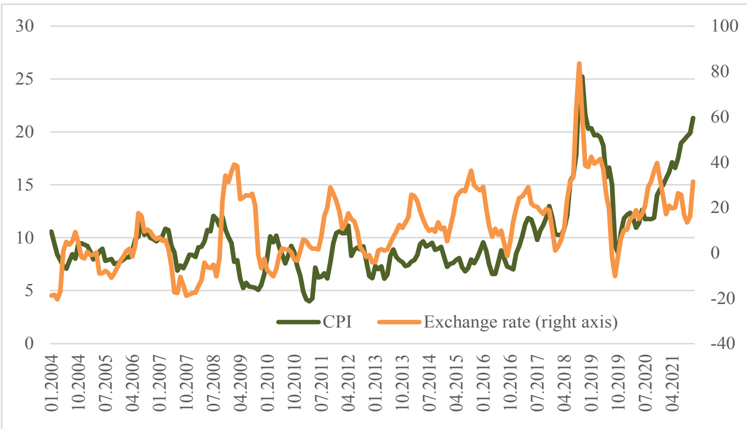
In Türkiye, per capita income, which had been on the rise after the 2001 crisis, peaked in 2013 and then began to decline (Graph 1). This situation is mainly due to the increased volatility in growth, the postponement of structural reforms, the decrease in productivity and the depreciation of the national currency, and Türkiye missed the chance to rise to the league of high-income countries.



Graph 1. GDP per capita (US dollar)

Source: TSI

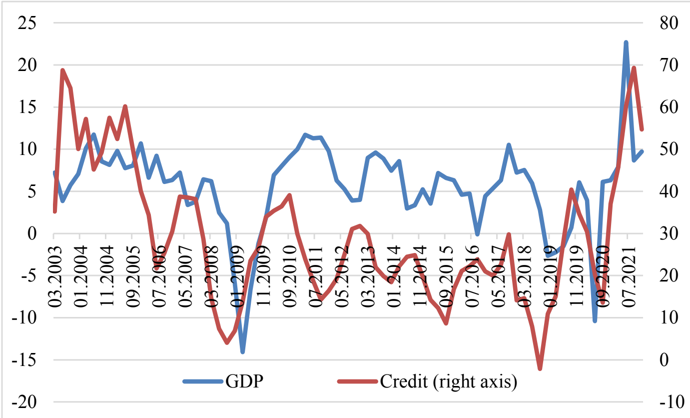
Inflation, which remained in single digits for a long time after 2004, has reached double digits since 2017 (Graph 2). The exchange rate shock in 2018 and the global pandemic in 2020 accelerated the deterioration in the inflation outlook. The significant deterioration in inflation expectations since 2021 has triggered the upward movement. While the exchange rate followed a stable path until the 2008 global crisis, a gradual depreciation in the national currency began after this date. With the 2018 shock, the exchange rate became more unstable, and an increase in the pass-through from the exchange rate to inflation was also observed.



Graph 2. Change of CPI and exchange rate (%)

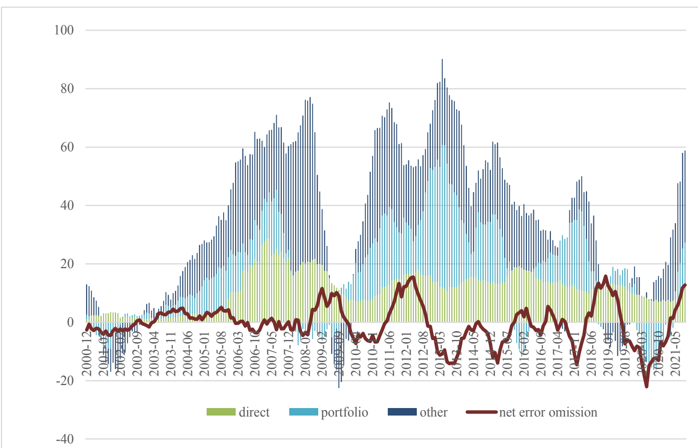
Source: CBRT

When the relationship between credit growth and GDP growth is examined, it is seen that the dependence of economic growth on credit is increasing (Graph 3). Especially after 2008, growth is triggered by credit growth cycles and demand shocks. In addition, after the 2020 pandemic period, it is seen that growth was increased only by massive credit growth. This situation also implies that credits are used for unintended purposes such as debt rollover, foreign exchange demand, and imports of luxury consumer goods.



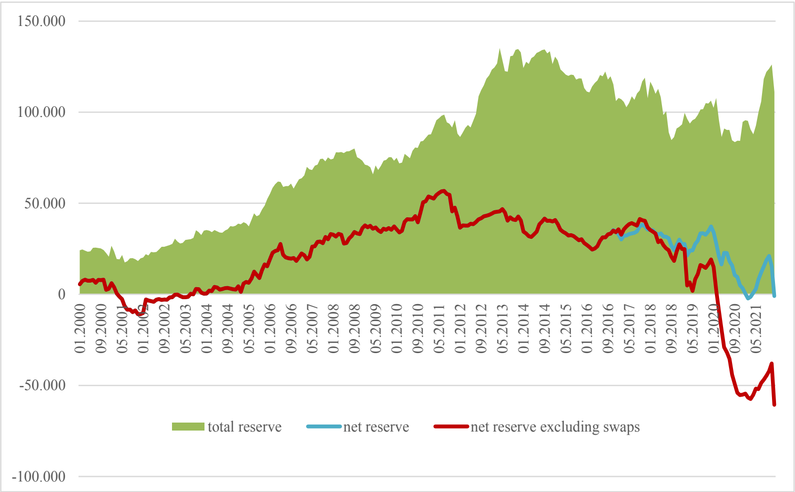
Graph 3. Growth rate of GDP and credit (%)
Source: CBRT, TSI

Since the beginning of the 2000s, the global conjuncture has also supported Türkiye for a long time, and external financing opportunities have become easier (Graph 4). In the period before the 2008 global crisis, external financing was largely provided through direct investments and other investments. After this date, the weight of portfolio investments began to increase, and significant fluctuations began to be seen in the net errors and omissions item. Türkiye benefited significantly from the abundance of global liquidity until 2017. In the period after 2018, direct investments began to decrease, and there were sharp declines and significant fluctuations in portfolio investments and other investments. In addition, the net errors and omissions item, which shows money of unknown source, has become more volatile. This table shows that external financing opportunities have become more difficult after 2018.



Graph 4. Net capital inflows (billion US dollar)
Source: CBRT

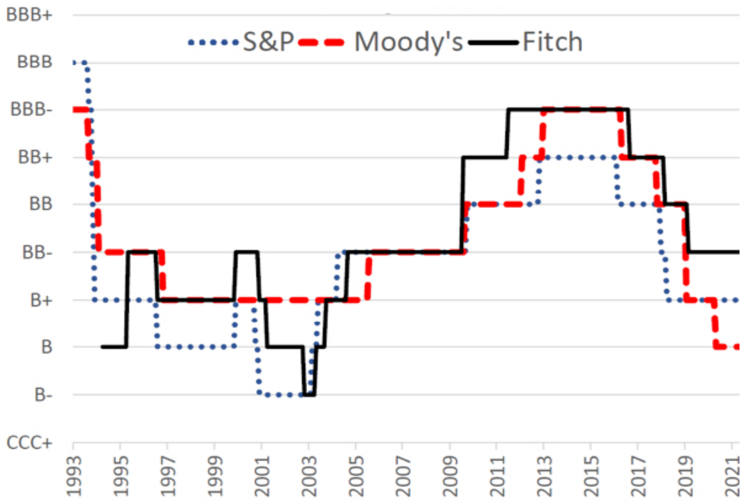
While the central bank's gross international reserves have been on a downward trend since 2013, the downward trend in net reserves has accelerated since the beginning of 2018 (Graph 5). The volume of foreign exchange reserves provided through swap transactions has started to have a significant weight since 2017. In addition, since 2020, the dependence of the CBRT reserves on the swap channel has increased, and the temporary foreign exchange volume provided through these transactions has exceeded 60 billion dollars. While gross reserves were at 110 billion dollars at the end of 2021, the fact that net reserves were close to zero and net reserves excluding swaps were at -60 billion dollars indicates that Türkiye is experiencing a significant external financing problem and the country's fragility is rising.



Graph 5. International reserves (million US dollar)

Source: CBRT

The CSD premium used to measure countries' credit risk has reached high levels in Türkiye since 2018. A rise in this indicator suggests that the country may have difficulty paying its external debt. As of the end of 2021, Türkiye's 5-year CSD premium has exceeded 500 points, implying that the country is risky for foreign investors. In addition, the scores of international credit rating agencies indicate that the investment environment in the country has started to deteriorate since 2017 (Graph 6). Before the implementation of the unusual monetary policy, it is seen that the credit rating of Türkiye has fallen to the levels of the early 2000s in the last quarter of 2021, and the country's chance of being preferred by foreign investors has decreased.



Graph 6. Türkiye credit rating

Source: World Government Bonds

Note: Moody's rating scale has been adapted to others.

Conventional and Unconventional Monetary Policy

Many developed and developing country central banks adopted a monetary policy framework focused on achieving price stability until the global financial crisis in 2008. In this approach, called traditional monetary policy, the policy rate is the main tool of central bank, while open market operations and reserve requirements are also used to support interest rate policy (Bindseil, 2014). Central banks have decided interest rate level considering the reaction functions in inflation targeting regime. Many central banks have determined the reaction function according to different versions of the Taylor rule (Asso et al., 2007). Taylor (1993) defined the interest rate reaction function using the relationship between interest rate, output and inflation as follows:

$$R= a + b_1(P - P^*) + b_2(y-y^*) \quad \text{(Function 1)}$$

In the function 1, (R) represents the short-term interest rate, (P-P*) the deviation of inflation from the target, and (y-y*) the deviation of production from the potential level, in other words, the out gap. When inflation and production deviate from their potential levels, central banks can direct these variables closer to the long-term values by using the short-term policy interest rate (Paranavithana et al., 2020).

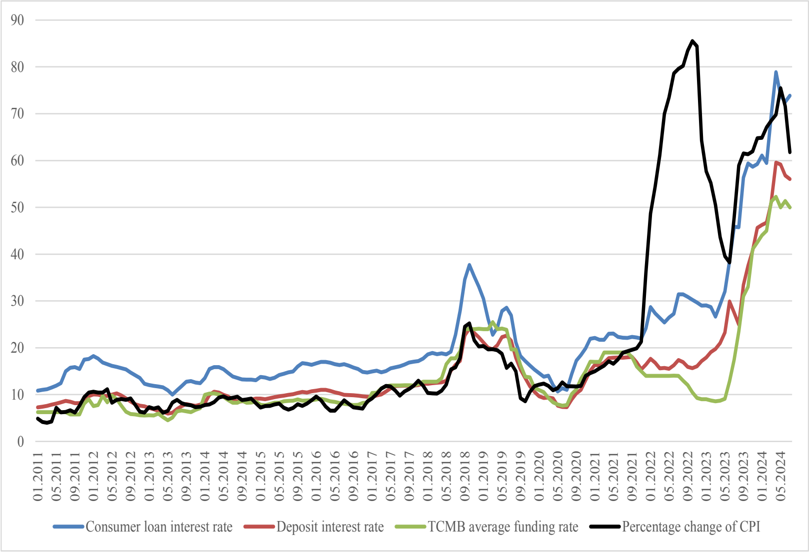
The global crisis in 2008 has shown that the focus of central banks on price stability is not enough to prevent crises (CIEPR, 2011; Canuto and Cavallari, 2013). Increasing concerns about financial stability have led central banks to apply unconventional monetary policies. Preventing asset bubbles, restricting excessive debt of the financial sector and companies, managing liquidity risk, limiting exchange rate and capital flow volatility have been on the agenda of central banks (Costa et al., 2011). In the new policy approach, some instruments of traditional monetary policy have been developed and implemented, while some tools have been used for the first time.

Quantitative monetary easing, interest rate corridor, credit policy, international reserve policy, required reserve policy, zero or negative interest rate policy, forward guidance, macro and micro prudential measures have been implemented within the framework of unconventional monetary policy (IMF, 2013; Sheedy, 2017). Central banks have preferred monetary policy tools which are simple and easy to communicate. In addition, the new tools implemented have been complementary to interest rate policy, not a substitute (Krishnamurti and Lee, 2014). On the other hand, when concerns about price stability began to rise, central banks returned to traditional monetary policy practices.

To ensure financial stability, the CBRT has also applied to unconventional monetary policy in the post-global crisis period. The reserve option mechanism, interest rate corridor, required reserve policy, and liquidity management have been the main tools (Başçı and Kara, 2011). When international and domestic conditions normalized, the CBRT returned to conventional policies in line with the global trend. However, in the last quarter of 2021, in an environment where price stability was disrupted and the financial structure was fragile, the CBRT changed its monetary policy again. Some unconventional monetary policy tools and some new instruments have been used as a substitute for interest rate policy, and CBRT targeted price stability and financial stability through intensive regulations. The functioning of the market mechanism and relative prices has been disrupted owing to intensive market intervention. Therefore, the CBRT's new monetary policy can be called an unusual monetary policy, as it also differs from unconventional monetary policy.

Unusual Monetary Policy of CBRT

There has been no significant change in monetary policy in Türkiye since the period following the 2008-2009 global crisis until 2017. While inflation was kept at single-digit levels with minor fluctuations, the CBRT average funding rate generally remained above inflation. In addition, it is seen that the policy rate has a high power to direct market interest rates (Graph 7). While the exchange rate shock in 2018 led to an increase in inflation and interest rates, the impact of the shock was quickly overcome by intensive use of public resources. Then, inflation and interest rates began to approach single digits again. However, the global pandemic in 2020 led to a divergence between policy rates and inflation. On the other hand, in the last quarter of 2020, the CBRT focused on combating inflation again, but the dismissal of the CBRT governor at the beginning of 2021 and uncertainties regarding monetary policy led to a widening gap between the CBRT rate, market rate, and inflation. In this environment, the CBRT's unusual monetary policy implementation and insistence on low-interest rate policy since the last quarter of 2021 caused to an unprecedented increase in inflation in a short time. In addition, CBRT's power to direct market interest rates decreased and the transmission mechanism of monetary policy was damaged. The liraization strategy was implemented as the main element of the new monetary policy. It was aimed to increase production and exports with low interest rates and competitive exchange rates via new policy combinations. As a result of the failure to achieve the desired targets with the new policies, the CBRT started to return to its traditional monetary policy as of the second half of 2023.



Graph 7. Change of interest rate and CPI

Source: CBRT

Liraization Strategy and Goals

Liraization can basically be named as the application of reverse currency substitution or reverse dollarization specific to Türkiye. Currency substitution or dollarization can be defined as the substitution of foreign currency for national currency. It is valid when a foreign currency can fulfill any or all of the functions that a domestic currency is expected to have; unit of account, medium of exchange, and store of value. (Öztürk, 2022: 1). In other words, it is the phenomenon of preferring a foreign currency that is seen as more stable. The ensuring of macro and financial stability in the country, the cessation of the depreciation of the national currency and the return to the national currency are defined as reverse currency substitution or reverse dollarization (Eğilmez, 2009: 289).

In order to have a successful reverse currency substitution, domestic financial markets must be deepened, alternative savings and investment instruments in national currency must be developed, and structural problems must be solved (Akıncı et al., 2005: 14; Bocola and Lorenzoni, 2020; Yeyati, 2021). The reverse dollarization process is a difficult and long process, and one of the necessary elements for its success is to ensure price stability as well as financial stability and to manage expectations with reliable policies (Serdengeçti, 2005). It is also suggested that a flexible exchange rate regime that can move freely in two directions will be complementary for a permanent reverse currency substitution (Kokenyne et al., 2010: 8). In addition, there are studies indicating that strengthening the institutional structure of the central bank and focusing monetary policy on providing stability in the value of the national currency will also be beneficial for reverse dollarization (Alvarez-Plata and García-Herrero, 2008: 23). Countries that have experienced high dollarization also show that measures such as taxing foreign exchange transactions and increasing foreign exchange storage costs contribute to reverse currency substitution (Vidal et al., 2020: 32). Finally, Fischer (2006) suggests that regulations aimed at providing reverse currency substitution should be initiated when macro and financial stability are achieved as a prerequisite.

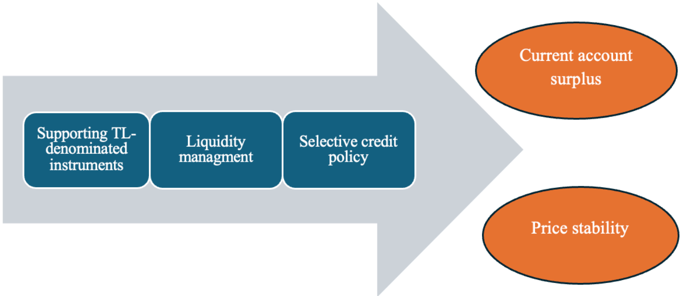
The reverse currency substitution steps that emerged in Türkiye at the end of 2021 were later announced to the public in policy texts under the name of liraization. The liraization strategy aims to provide that the Turkish lira is highly preferred as a store value, to increase the weight of the national currency significantly in corporate and bank balance sheets, to make the collateral of banks for borrowing from the CBRT fixed-return Turkish lira assets, and to support Turkish lira used as the sole medium of exchange in commercial transactions within the country. In this context, the CBRT is responsible for managing the macro process of the policy mix with other institutions such as the Ministry of Treasury and Finance (MTF) and the Banking Regulation and Supervision Agency (BRSA) (CBRT, 2022a).

According to the findings of the CBRT, there are two main reasons for the failure to achieve permanent price stability: high currency substitution by households, companies and banks and chronic current account deficit. Low level of national currency preference of domestic market and the high current account deficit interact with each other and disrupts the functioning of the monetary policy transmission mechanism. In addition, this situation increases the economy's dependence on external financing, making the country vulnerable to shocks and leading to a high trade-off between growth and price stability (Kavcıoğlu, 2022). Arguing that traditional monetary policy cannot work effectively in an environment where the current account deficit and dollarization are high, CBRT presented the liraization strategy within the scope of the new monetary policy.

The first signals regarding the liraization were given in the monetary policy decision in December 2021. The CBRT stated that the monetary policy framework would be reviewed, arguing that current policies were not sufficient to ensure price stability. Accordingly, the liraization strategy was presented to the market as a component of the new policy approach in the Inflation Reports for January, April, July and October 2022. In addition, the steps taken within the framework of liraization were collectively shared in the Financial Stability Reports (FSR) published in May and November 2022.

In the January 2022 Inflation Report, the liraization strategy was discussed explicitly for the first time. In the April 2022 Inflation Report, it is stated that the aim of liraization is to control the sensitivity of inflation to the exchange rate and to solve structural problems in the current account balance by increasing production and export capacity. In addition, it is stated that the liraization strategy will support the fight against inflation through three channels (Figure 1). The first is to encourage instruments that provide savings in national currency and to support alternative instruments such as FX Protected Deposits (FXPD) to make their returns competitive. The second channel is to gradually increase the weight of Turkish lira instruments in liquidity management and reserve requirement (RR) practices. In this direction, it is aimed to significantly increase the share of Turkish lira collateral in Turkish lira borrowings and to reduce the weight of currency swap transactions between national currency and foreign currency. The last channel is to provide financial support to sectors that earn foreign currency through selective credit policy. It is targeted to increase production capacities and improve the current account balance by providing Turkish lira financing at appropriate maturities to sectors have foreign exchange revenue (CBRT, 2022b).

Figure 1. Liraization strategy transmission mechanism



The monetary policy text for the upcoming year, published by the CBRT at the end of December each year, has been shared with the public as the Monetary Policy and Liraization Strategy for 2023. The policies to be implemented within the scope of the liraization strategy are included in the text. It has been stated that adjustments will be made within the scope of the liraization targets in the funding, credit and collateral channels (CBRT, 2022c). In the inflation reports published in the first half of 2023 and in the FSR, the liraization strategy has been frequently emphasized and its results have been discussed.

As a result of return to traditional monetary policies as of the second half of 2023, the liraization strategy has not been included in the inflation reports, FIR and policy texts of the CBRT. In addition, the regulations made within the scope of liraization have begun to be gradually removed. This situation shows that the life of the liraization strategy officially lasts from the beginning of 2022 to June 2023.

Regulations of Liraization Strategy

Accompanying the unusual monetary policy and low-interest rate policy, the liraization strategy, although not openly declared, actually started in the last quarter of 2021, and its official inclusion in the CBRT policy text was with the Inflation Report at the beginning of 2022. Within the scope of the Liraization Strategy, many regulations that can be called macroprudential measures have been implemented. The steps taken within the framework of liraization are discussed below under 5 subtitles.

Regulations Regarding Deposit and Participation Funds

The most striking financial instruments within the scope of liraization are the FX Protected Deposit and Participation Funds accounts in terms of TL (TLFXPD) and the Deposit and Participation Funds Converted from FX to TL (CFXPD) accounts. Of these newly developed financial instruments, TLFXPD was introduced to the market by the Ministry of Treasury and Finance, while CFXPD was introduced to the market by the CBRT. These financial products were developed and put into practice as of the end of December 2021.

The TLFXPD product is designed to protect savers against exchange rate risk. It is a newly opened TL deposit account, offering savers TL-denominated returns. This product based on the principle that the alternative return that will be lost due to the increase in the exchange rate will be compensated by the public. In other words, TL savings are encouraged without depriving them of potential foreign exchange returns. TLFXPD accounts can be renewed again at the end of the term as long as the application carries out (CBRT, 2022a).

CBRT-supported CFXPD accounts, which have a structure similar to TLFXPD, are designed to enable the conversion of foreign exchange and gold accounts into TL deposit accounts. Depositors can benefit from this account only once. However, savers who transfer from CBRT-supported foreign exchange and gold accounts to TL deposit accounts can continue to be protected from exchange rate risk by transferring to TLFXPD accounts at the end of the term (CBRT, 2022a). In short, savers have a TL account indexed to foreign exchange with these new products and only earn bank returns if the exchange rate falls and receive additional public support if the exchange rate rises.

The TLFXPD and CFXPD products aims to increase the share of TL-denominated instruments in the total deposit/participation fund, extend the maturity of deposits, use foreign exchange assets in the country more efficiently, improve bank balance sheets by reducing exchange rate risk, and reduce the pressure on CBRT reserves. In addition, when switching from foreign exchange accounts to CFXPD accounts, the sale of foreign exchange to central bank protects CBRT against exchange rate risk. As the share of TL products increases, it is expected that the upward pressure on the exchange rate will be eliminated and TLFXPD ‘s burden on the budget will decrease (CBRT, 2022d). The execution and financing of TLFXPD accounts were transferred to CBRT in July 2023.

TLFXPD can be opened with 3, 6, 9 months and 1-year terms, while CFXPD can be opened with 3, 6 months and 1-year terms for individuals and 6 months and 1-year terms for companies. In both accounts, the CBRT one-week repo auction interest rate has been determined as the minimum return rate. While the maximum return for TLFXPD was set as the CBRT one-week repo auction interest rate + 300 basis points, no upper limit was initially set for CFXPD, but the same application was later adopted with TLFXPD. (CBRT, 2022a). To encourage these products interest rate upper limit was removed for CFXPD in January 2023 and for TLFXPD in March 2023.

Like TLFXPD and CFXPD accounts, a new product has been developed to get the support of Turkish citizens living abroad to lira. To finance the growth and the current account deficit, the Deposit and Participation System for Citizens Living Abroad (YUVAM) account was launched by the Central Bank in February 2022. This product is an account in terms of TL that enables non-residents and their companies abroad to move their savings to Türkiye. CBRT offers a guarantee to protect against change in FX rate and assures of additional return. In addition, in March 2022, foreign households and companies have been allowed to enter the YUVAM application. YUVAM accounts can be opened with terms of 3, 6, 12 and 24 months. While there is no time or limit restriction for opening a YUVAM account, there is no obstacle to converting the account back into foreign currency at the end of the maturity (CBRT, 2022d).

To make TLFXPD, CFXPD and YUVAM products attractive, corporate tax exemption was introduced for the income obtained from these instruments, the withholding tax rate was determined as zero and no tax was collected from the interest and dividends. Banking and Insurance Transactions Tax (BSMV) was also reduced to zero for foreign exchange sales at the end of the term. Within the scope of the RR policy, deposits converted to FXPD were exempted from required reserves, and remuneration and commissions of RR arranged to encourage these products (CBRT, 2022d).

CBRT has signaled for exiting FXPD as of the second half of 2023, and regulations have been made in the RR policy in this direction. While tax exemptions have been gradually eliminated, opening new accounts and renewal of existing accounts have been restricted. At the end of September 2023, minimum interest rate rule has been removed, and FXPD has been made less attractive. As of the beginning of 2024, the opening of TLFXPD accounts has been terminated and it has been regulated that expired accounts will not be renewed. CFXPD continues to be applied for individuals.

Regulations Regarding Required Reserves and Securities Maintenance Practice

The required reserves policies used by the CBRT in the post-2008 global crisis period for many purposes, such as liquidity management, extension of the maturity of liabilities, control of foreign borrowing and limitation of credit expansion, have been also used intensively within the scope of the liraization strategy. In addition to these policies, the maintenance of securities was also revived as an additional tool within the scope of the liquidity application that was repealed in the early 2000s.

Within the scope of liraization, the Reserve Option Mechanism (ROM) in the required reserve system, which has been actively used in the CBRT toolkit for a long time, has been gradually terminated. It is claimed that the ROM application, which allows banks to keep a certain percentage of their TL required reserves in FX and gold at the Central Bank, encourages banks to borrow foreign currency and disrupts the transmission mechanism of monetary policy by reducing banks' TL borrowing needs. For this reason, the ROM FX facility was completely abolished in the last quarter of 2021, and the ROM gold facility was completely abolished in June 2023.

The average TL RR rates have not been changed for a long time since the end of 2021 but have been used to control loans. On the other hand, to encourage the conversion to TL in the financial system, FX RR rates have been significantly increased since the end of 2021, and the weighted average FX rate has reached 23% in 2023. In addition, deposit/participation accounts converted from foreign exchange and gold accounts to TL at the beginning of 2022 were exempted from the RR application, and RR interest and commission rates were used to increase the share of the TL deposit/participation fund.

The measures have been taken regarding RR policy and security maintenance practice are listed on Table 1.

Table 1. Regulations regarding RR and security maintenance practices

Date	Regulations
April 2022	Required reserves (RR) have also started to be applied to the asset side of balance sheets, and commercial loans other than special purpose loans determined by the CBRT have been subject to RR.
April 2022	While RR rates are differentiated according to loan growth rates, financing companies that previously had zero RR rates have been subject to the same application as banks, and their liabilities to domestic banks have been included in the RR application.

April 2022	RR rates for foreign currency deposits/participation funds have been differentiated based on the conversion rate of individuals to TL, and an additional RR has been imposed for banks with a conversion rate of less than 10%.
April 2022	To charge a commission on amounts hold in FX RR, the reference TL conversion rate has been changed to 10%, and commission rates have been updated.
June 2022	The RR rate, which was 10% for TL commercial loans, has been increased to 20%.
July 2022	The securities maintenance application, which was repealed in the early 2000s, has been re-implemented. Banks have started to hold long-term and fixed-interest securities in TL for the periods determined by the Central Bank in addition to the FX required reserves for deposits/participation funds. The securities maintenance rate has been differentiated according to the TL conversion performance.
August 2022	Banks have been required to hold securities according to the loan interest rates exceeding the reference interest and loan growth rates
September 2022	The additional FX RR holding practice according to the TL conversion rate have also included the companies and the reference values have been increased.
December 2022	The commission rates determined for RR have been changed to encourage the share of TL deposits.
December 2022	In addition to banks, factoring companies have also been imposed a security maintenance practice according to the interest rate they apply to their factoring receivables in Turkish lira.
January 2023	To encourage the extension of the maturity in TL deposits, RR exemption has been introduced until the end of 2023 for TL deposits longer than 3 months and foreign currency debts directly provided from abroad longer than 6 months.
January 2023	The security maintenance rate has been associated with the share of TL deposits instead of the TL conversion rate.
February 2023	As a result of the renewal of the liraization targets, the security maintenance rate has been increased from 5% to 10%. Banks that achieve the 60% target in TL deposit share have been given a discount in the security maintenance.

April 2023	While new obligations have been determined within the scope of the security maintenance for banks that remain below the 60% threshold in TL deposits, discounts have also been made for banks that exceed 70%. The FX conversion rate has been associated with the security maintenance again to ensure a decrease in foreign exchange deposits.
April 2023	In order to strengthen the functioning of the monetary transmission mechanism, the security maintenance application, which previously covered commercial loans, has been updated to include consumer loans.
April 2023	The security maintenance obligation has been increased from 90% to 150% for institutions having an interest/profit share ratio higher than 2 times the reference interest rate announced by the CBRT in consumer loans and having a ratio higher than 1.8 times in commercial loans.

Source: CBRT

As of the second half of 2023, the securities maintenance practice has been simplified and gradually abolished. As of July 2023, FXPD accounts have been made subject to reserve requirement and steps have been taken to exit. Within the scope of the simplification process, the conversion target application from FX deposits to FXPD and RR application according to TL share have been terminated. The regulations aim to reduce share of the FX protected deposits. (CBRT, 2023d). RR rates, remuneration and commissions of RR have been used to increase the share of Turkish lira deposits and to support the conversion from FXPD to Turkish lira deposits.

Regulations Regarding Liquidity Management and Collateral

At the end of 2021, a regulation was made regarding the collateral used in banks' borrowing from the CBRT. To reduce the share of collateral in FX, the weight of collateral in national currency, such as Government Domestic Debt Securities (DIBS) and/or lease certificates issued domestically by the Undersecretariat of Treasury Asset Leasing Joint Stock Company (HMVKŞ), was increased in the Interbank Money Market borrowings. In addition, it was determined that the collateral used in swap transactions should consist of at least 30% national currency assets (CBRT, 2022d). In May 2022, the weights of TL assets in the collateral system were updated again in line with the liraization, and the discount on indexed securities and foreign exchange/gold collateral assets was increased from 5% to 15%. With the regulations made in June, July and August 2022, the discount rate of CPI-indexed securities and foreign exchange and gold collateral was increased from 15% to 60%. With the regulations in July and August 2022, the share of TL securities was increased again. The minimum DİBS holding rate in CBRT-sided swap transactions and Interbank Money Market transactions was increased to 50% (CBRT, 2022f; CBRT, 2022g). Finally, with the changes made in January and April 2023, the discount rates of CPI-indexed securities and foreign exchange/gold type collateral were increased to 80% (CBRT, 2023a; CBRT, 2023b).

Regulations Regarding Selective Credit Policy

CBRT determined the policy rate low in a high inflation environment and made regulations to direct the interest rates of bank loans in the same way. It led to a significant increase in loans, especially commercial loans. The new economic policies targeted to increase investments and production by credit growth. However, having financing cost remained well below the expected inflation led to the use of loans for unintended purposes. As a result of this credit growth, the demand for foreign exchange, fixed assets and the luxury consumer goods increased. The rapid growth of loans worsened inflation and the current balance, and use of credit for unintended purposes put pressure on the exchange rate. Then, credit growth was limited, and credit composition was controlled by excluding special purpose loans such as agricultural loans, small and medium enterprises loans, export and investment loans and state economic enterprise loans.

In addition to the policies of RR and securities maintenance explained in the previous section, the following measures have been taken regarding loans (Table 2).

Table 2. Regulations Regarding Loans

Date	Regulations
September 2021	It is allowed to use export rediscount credits in TL. To prevent unintended use and foreign exchange demand originating from this funding, TL-denominated spending areas have been determined.
January 2022	It has been made mandatory to sell at least 25% of the income obtained from exports and foreign exchange earning services to the CBRT, and this rate has been increased to 40% in April 2022. In addition, it has been determined that companies that want to use TL-denominated rediscount financing can use credit by committing to sell 30% of their export income to domestic commercial banks.
February 2022	The limits of rediscount credits provided for export and foreign exchange earning services converted to TL.

February 2022	The maturity restrictions and credit value ratios in vehicle loans and financial leasing transactions of consumers have been rearranged.
March 2022	The investment commitment advance credit has been rearranged, and the condition of being an exporter or making import-substituting production has been introduced for long-term TL credit support. Companies benefiting from this financing are required to use TL in domestic commercial transactions related to their investments and in domestic sales of the outputs.
May 2022	The risk weights of the loans in the capital adequacy ratio are rearranged, and the risk weights of cash commercial loans were increased; agricultural loans, SME loans, export and investment loans, SEE loans, corporate credit cards and loans given to banks or financial institutions were excluded from the regulations.
June 2022	To prevent the expansion in loans caused by the low interest policy, the maturity in consumer loans was reduced and the BSMV rate was increased, and the minimum payment rate was increased in high-limit credit cards.
June 2022	The loan/value ratio in housing loans was differentiated and the use of loans for those with a value over 10 million TL was terminated.
June 2022	Restrictions have been imposed on the use of TL commercial loans The provision of TL commercial loans to companies that are subject to independent audit, have more than 15 million TL in FX cash assets, and whose FX cash assets exceed 10% of their total assets/net sales revenue for the last 1 year has been terminated. In November 2022, the threshold values were reduced to 10 million TL and 5%.

Source: CBRT

Other Regulations

Other prominent regulations implemented in 2022 within the scope of the liraization strategy are listed below:

a. In January 2022, to encourage the use of TL in domestic transactions, it was regulated that housing sales to foreigners would be made in foreign currency, the obtained foreign currency would be converted into TL through the CBRT.

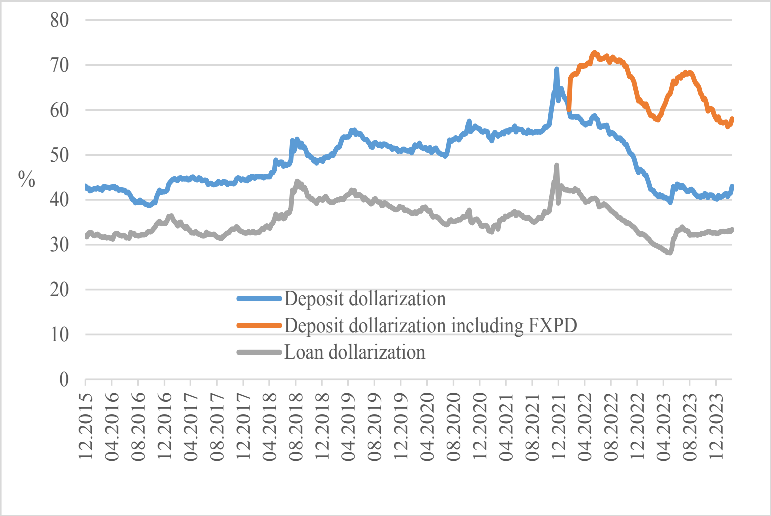
b. In January 2022, the state contribution in the individual retirement system was increased from 25% to 30%, and individuals were given the opportunity to make partial payments up to half of their own savings.

c. In March 2022, it was encouraged to convert the physical gold deposited in banks into TL deposit/participation accounts to include the physical gold of domestic residents in the financial system.

d. In April 2022, it was determined that payments of securities sales contracts should be made in TL, while the amounts in the contract were allowed to be determined in foreign currency or indexed to foreign currency (CBRT, 2022d).

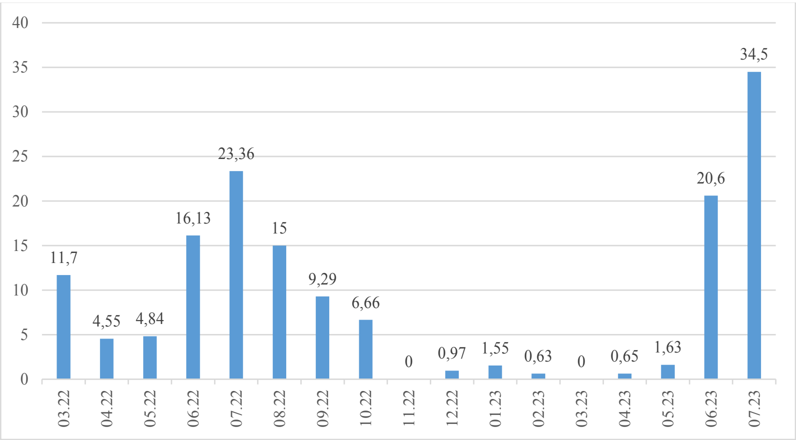
Assessment of Liraization Strategy

Thanks to the intensive regulations of the liraization strategy, the share of TL in the asset and liability of companies has increased, and improvements have been also observed in their FX positions. In addition, the share of the Turkish lira in households' investment and savings preferences has increased. While the attractiveness of FXPD accounts was effective in the deposit composition, the regulations made by the BRSA were effective on foreign loans. The credit and deposit dollarization rate in bank balance sheets has illustrated a significant decline as of the end of 2021 (Graph 8). Then, dollarization has been flat as of the second half of 2023. On the other hand, when FXPD accounts that have exchange rate risk are also included in foreign exchange accounts, the decline in deposit dollarization remains limited. As a result of return to traditional policies after the second half of 2023, an important outflow from FXPD has been observed but it has not led to increase in deposit dollarization.



Graph 8. Deposit and loan dollarization (%)
Source: BRSA

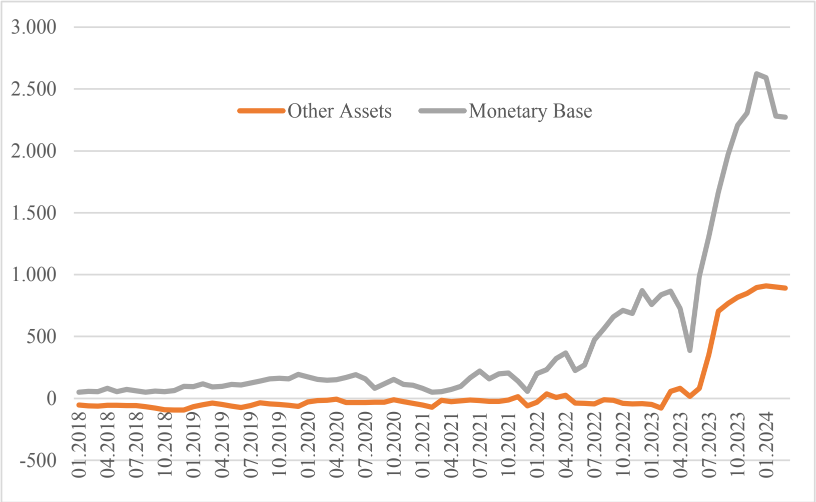
The heavy market interventions and regulations enabled a significant increase in the share of TL-denominated products, but this situation has been quite costly for the public. TLFXPD's burden on the budget due to the exchange rate fluctuations was 152 billion TL from the beginning of 2022 until the end of July 2023 (Graph 9). It is estimated that the foregone tax revenues were around 100 billion TL. The total cost for the budget in 1.5 years was around 250 billion TL. Moreover, approximately 73 billion TL support was provided by the CBRT in 2022 due to the exchange rate volatility in CFXPD accounts. In addition to CFXPD, the transfer of burden of TLFXPD accounts to the CBRT caused to loss of 833.4 billion TL in 2023. This huge loss has prevented the transfer of profits to the Treasury, while indicating that a tremendous income transfer has been made to a small number of depositors (Özatay, 2023).



Graph 9. Cost of TLFXPD on budget (Billion TL)

Source: MTF

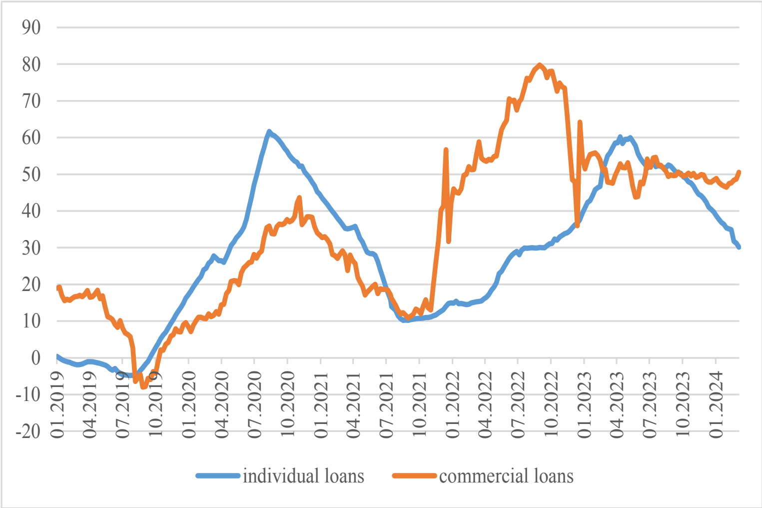
On the other hand, with the exchange rate cost for CFXPD accounts covered by the CBRT as of the beginning of 2022 and the transfer of TLFXPD to the CBRT as of July 2023, there has been a significant increase in monetary aggregates. An unprecedented increase has been recorded in the other assets item and the monetary base, which show the effect of these products on the CBRT balance sheet (Graph 10). It means that FXPD products have been a significant obstacle to fight inflation by increasing the money supply.



Graph 10. Effects of FXPD on CBRT balance sheet (Billion TL)

Source: CBRT

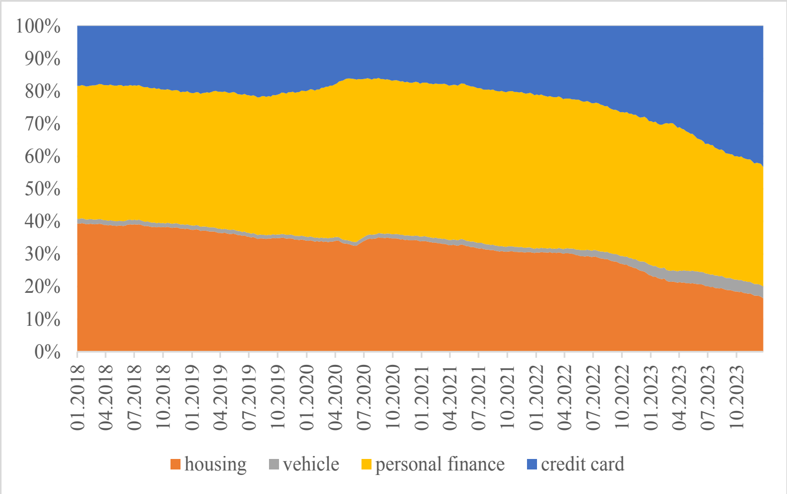
Selective credit policy is one the tools of the liraization strategy to support production, to improve current account and to have price stability. When the composition of the loans is examined, the share of commercial loans has increased since the end of 2021 with the incentives. In a high inflation environment, commercial loan growth has exceeded consumer loan growth as a result of policies providing commercial loans with low interest rates (Graph 11). There has also been an increase in loans supporting special-purpose investment and production within commercial loans. In addition, net exporter companies and SMEs have started to receive a larger share of total loans. Despite increasing commercial loans, the desired acceleration in domestic production could not be achieved. Rapid credit expansion boosted the concerns about financial stability and commercial loans have been restricted since the last quarter of 2022. On the other hand, the increase in individual loans continued until the second half of 2023 then a rapid slowdown was observed in all loans owing to the return to traditional policies and the increase in market interest rates.



Graph 11. Loan growth rate (%)

Source: BRSA

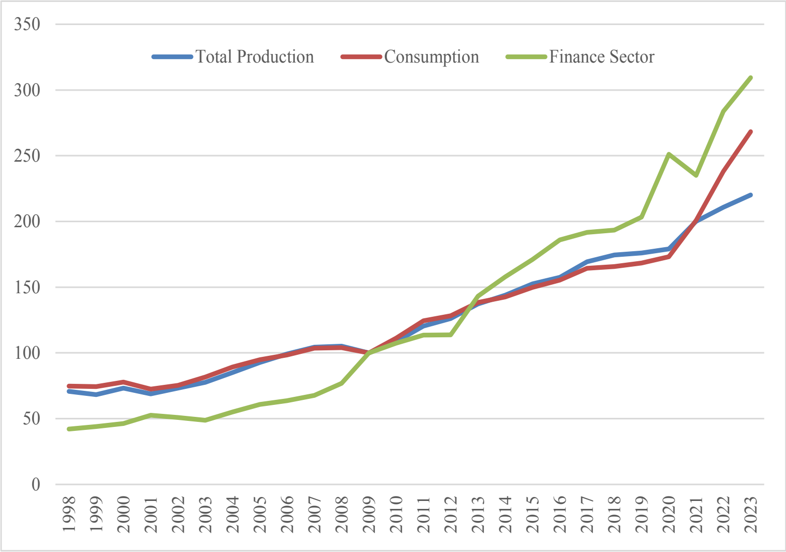
When the composition of individual loans is examined, as a result of increased spending due to high inflation, rise in demand and low interest rates, there has been a boom in credit card spending since 2022 (Graph 12). As the inflationary environment increased demand for fixed assets, a significant increase was also seen in the share of vehicle loans. Owing to banks not wanting to provide long-term loans and limited financing facilities for housing purchases, there has been a significant decline in housing loans since early 2022.



Graph 12. Composition of individual loans (%)

Source: BRSA

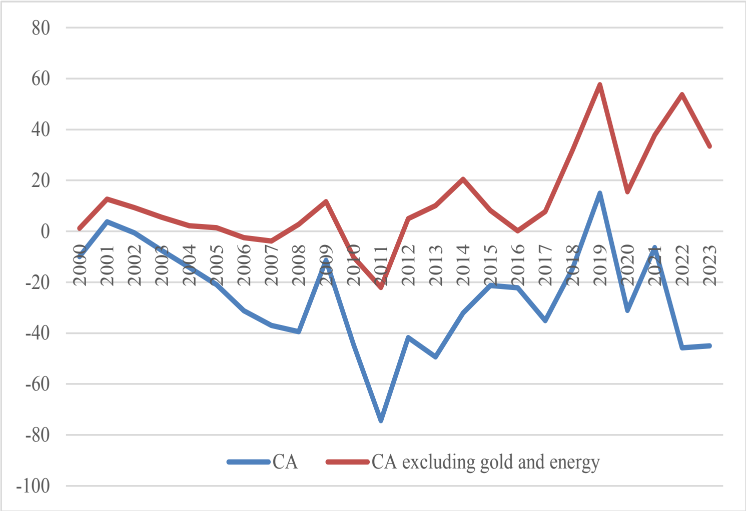
Having the financing cost well below the expected inflation has led to commercial and consumer loans used for unintended purposes by increasing the demand for foreign exchange, fixed assets and luxury consumer goods. Starting in 2022, consumption expenditures have started to boost much faster than production (Graph 13). At the same time, the rapid growth in the financial sector implies that Türkiye has started to grow by borrowing and consuming rather than producing.



Graph 13. Development of consumption, production and finance sector (2008=100)

Source: TSI

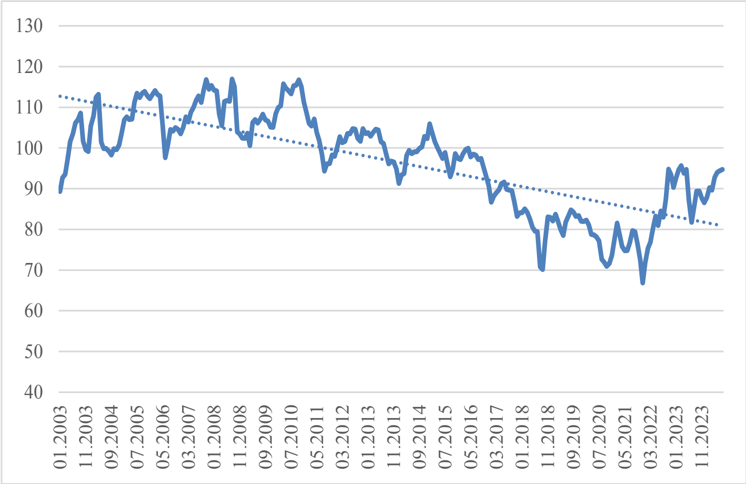
Due to the uncontrolled growth of loans, especially the quick increase in credit card spending and vehicle loans, a rapid deterioration in the current balance has been observed since 2022 (Graph 14). While the unit value of exports has decreased, the unit value of imports has increased. The cheap financing channel has increased domestic consumption and import spending. Despite the depreciation of the national currency, the rapid rise in domestic prices and the dependence of exports on imported goods have prevented the desired increase in exports. Owing to these effects, a significant deterioration has occurred in the total current balance and the current balance excluding energy and gold. These developments indicate that the goal of the liraization strategy has failed in current account balance.



Graph 14. Current account (Billion dollar)

Source: CBRT

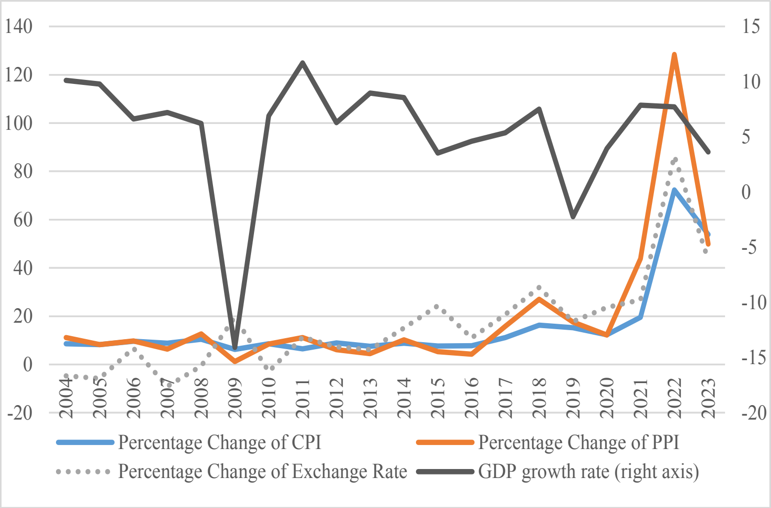
The real exchange rate index, calculated considering the producer price index, also shows that despite the increase in the nominal exchange rate, the index started to rise as of the beginning of 2022 due to the rapid increase in domestic prices (Graph 15). This change has affected competitiveness in foreign trade negatively. Real exchange rate implies that it will not be possible to improve the current balance with a competitive nominal exchange rate alone without ensuring price stability and final stability.



Graph 15. Real Exchange rate index (2003=100)

Source: CBRT

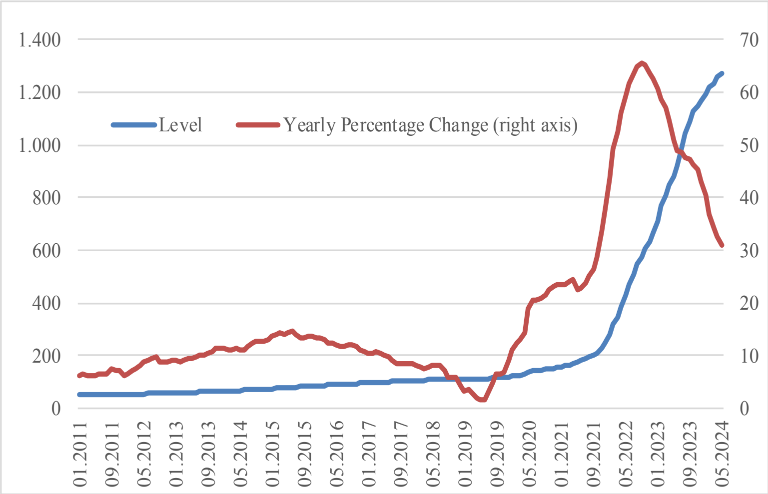
The negative real interest rate policy, the deterioration of inflation expectations and the uncontrolled growth of loans have rapidly reduced the internal and external value of the national currency. Since 2021, an unprecedented increase has been recorded in the exchange rate and consumer and producer price indices (Graph 16). The two-sided interaction between the exchange rate and inflation has strengthened, and the change in the producer price index has been greater than the change in the exchange rate. This picture implies that the exchange rate pass-through has increased considerably. The target of liraization strategy ensuring price stability has failed. In addition, Türkiye has lost its past gains in price stability and has had to sacrifice many years to bring inflation back under control. On the other hand, new policies cannot provide sustainable and high economic growth despite the heavy incentives to market actors.



Graph 16. Change of CPI, PPI, exchange rate and GDP (%)

Source: CBRT

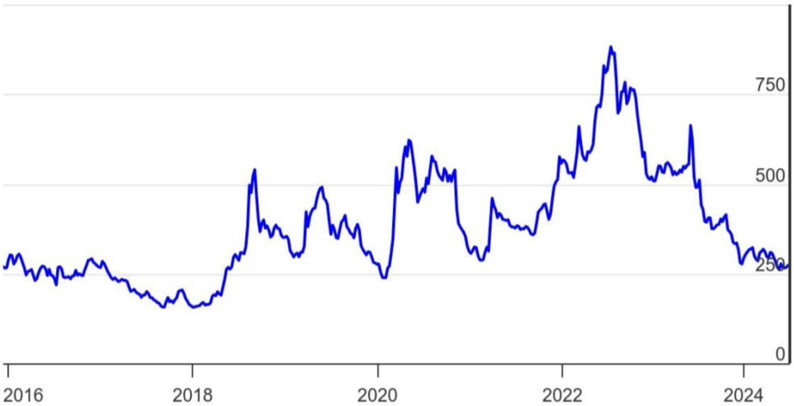
The high inflation issue has boosted the demand for housing, which is seen as an important investment tool to protect against inflation, despite the slowdown in housing loans. In addition, a rapid increase has been recorded in construction costs, which are highly sensitive to imported inputs and exchange rate. Owing to these effects, an unprecedented jump in housing prices has emerged since the last quarter of 2021, as a result of deterioration in inflation expectations (Graph 17). Thanks to the significant blockage of the credit channel, the rate of increase in housing prices has started to slow down as of 2023.



Graph 17. Development of housing price index (2003=100)

Source: CBRT

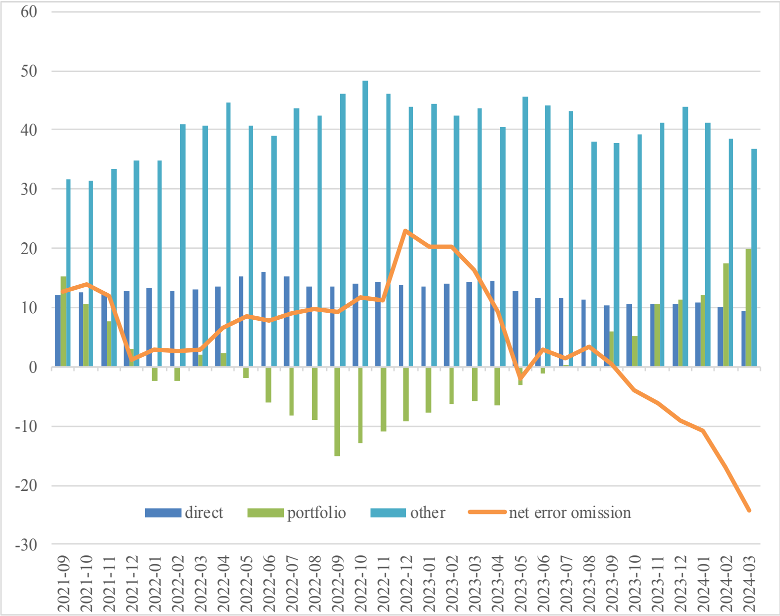
The CDS premium, which reflects the risk of the country not being able to pay its external debt, has reached record levels since the end of 2021 owing to unusual monetary policy practices (Graph 18). Change of CDS indicates that the economy is in a very fragile structure. In addition, high CDS makes external financing opportunities more difficult. High inflation, exchange rate volatility and unusual policy experiments in Türkiye are key facors in the increase of CDS. As of the second half of 2023, CDS has decreased to reasonable levels as Türkiye's credit risk has decreased.



Graph 18. CDS premium

Source: investing.com

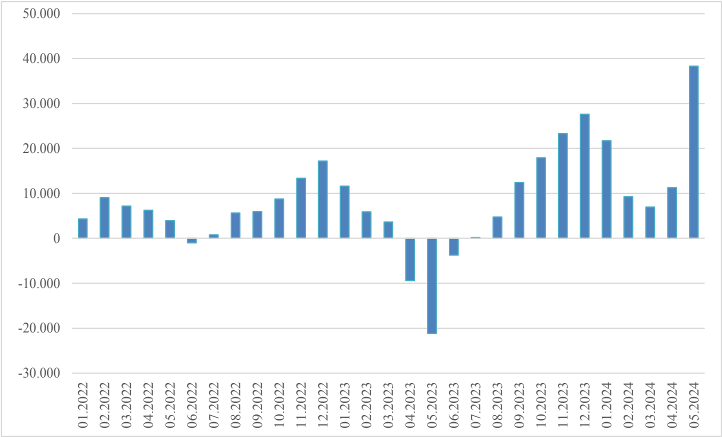
The increasing uncertainty in economic policies and intensive market interventions have also affected the volume and composition of capital flows. Since the beginning of 2022, significant outflows have been observed in portfolio investments consisting of bond and stock investments (Graph 19). During the same period, there has been a slight decline in direct investments indicating long-term and stable investments. Also, there has been a slight increase in other investments indicating borrowings of banks and the real sector from abroad. However, there has been a significant rise in the net error and omission account indicating capital inflows of unknown source from the beginning of 2022 to the first half of 2023. After returning conventional policies, this item turns negative, implying that capital inflows of unknown source have left the country.



Graph 19. Capital inflows (Billion dollar)

Source: CBRT

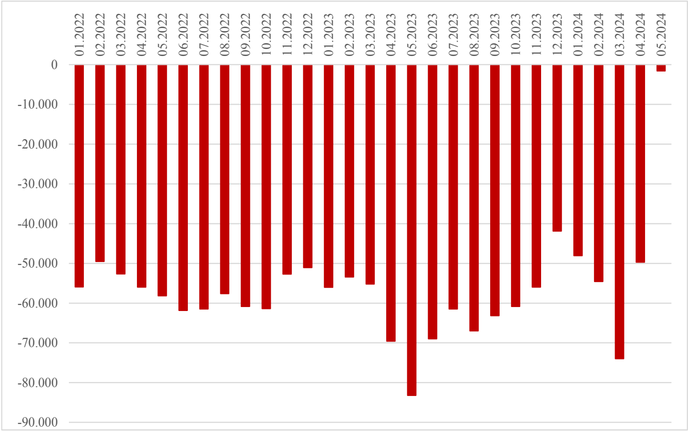
The boost in capital outflows from the country and the rising domestic demand for foreign exchange have created significant pressure on the CBRT reserves. Despite the mandatory sale of a portion of export revenues to the central bank and interventions to discourage foreign exchange demand, the erosion in net reserves could not be stopped. The decline in the CBRT net reserves to minus 22 billion in May 2023 has shown that unusual policies are unsustainable (Graph 20). On the other hand, as of the second half of 2023 the increase in capital inflows along with the policy change has provided a significant improvement in net reserves, and in a short time, the levels of the 2010s have been reached.



Graph 20. CBRT gross international reserves (Billion dollar)

Source: CBRT

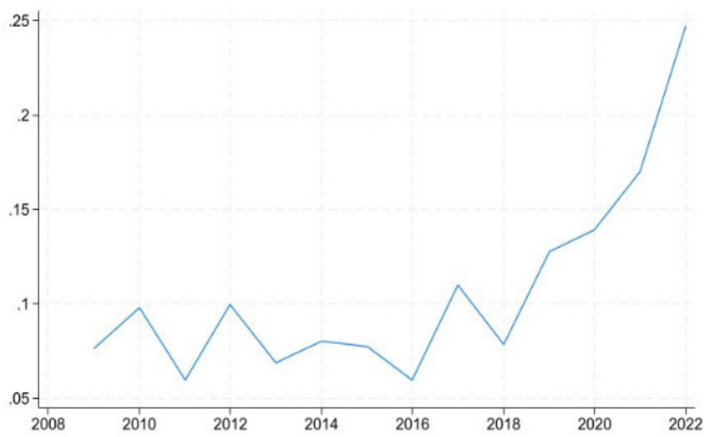
The CBRT's dependence on foreign exchange reserves provided through swap channels has increased considerably in the new policy period (Graph 21). The temporary nature of the foreign exchange provided through swaps and concerns about the sustainability of this resource have further increased the country's fragility. Starting from the second half of 2023, the weight of the swap channel in reserves began to be reduced to decrease the country's fragility, and starting from the second half of 2024, net reserves excluding swaps has returned to positive region.



Graph 21. CBRT net international reserves excluding swaps (Billion dollar)

Source: CBRT

In a negative real interest rate environment, uncontrolled growth in loans led to a demand explosion, while companies exhibited high pricing behavior due to irrational demand. Opportunism and moral corruption in pricing led to an excessive increase in company profits, in the uncertainty environment created by the high inflation. When the development of companies' equity return ratio and average profitability is examined, a serious upward trend is seen since 2020, and it is revealed that profitability rates have gained greater momentum since the end of 2021 (Graph 22 and Graph 23). Similarly, although the share of companies in total income has increased after 2020, the share of the wage earner has decreased. While the role of wage increases in inflation is discussed heavily, the contribution of the large increase in companies' profitability to inflation is not discussed enough. Wage adjustments are made as a correction to protect employees' income against inflation, and in turn, they have a limited effect on inflation. On the other hand, the rapid increase in company profitability directly leads to high pricing and inflation.



Graph 22. Return on equity

Source: Yılmaz and Bulut, 2024

Graph 23. Average company profit

Source: Yılmaz and Bulut, 2024

To follow the developments in income distribution, income earners can be divided into 5 percentage groups and the situation of each quintile can be analyzed over the years. While the lowest income group of the society obtained a similar share with minor changes from 2010 to 2021, the share of this group started to decrease from 2022 and reached its lowest level in 2023 (Table 3). The share of the middle-income group decreased more significantly after 2014, and this trend accelerated from 2022 onwards. On the other hand, the last 20% group having highest income rapidly increased its share in the same period and reached its highest level in the 2022-2023 period. Hence, it can be argued that especially the middle-income group has been greatly suffered by the economic policies in Türkiye. In addition, in the recent years owing to unusual monetary policy, the lowest income group has joined this group and the injustice in income distribution has increased. Practices such as FXPD and giving commercial loans with negative interest rate contributed to this result. Also, tightening policies to control the inflation since the second half of the 2023 have worsened the situation of the wage earners, especially minimum wage workers and retirees.

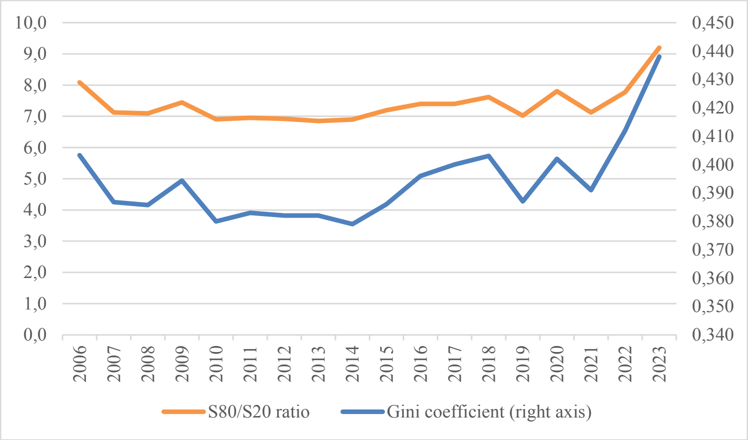
Table 3. Income distribution in Türkiye by quintiles

Year	First quintile	Second quintile	Third quintile	Fourth quintile	Last quintile
2006	5,75	10,47	15,17	22,12	46,48
2007	6,38	10,93	15,44	21,79	45,46

2008	6,39	10,87	15,4	22	45,34
2009	6,18	10,72	15,26	21,85	46
2010	6,5	11,09	15,62	21,91	44,87
2011	6,5	11	15,5	21,9	45,2
2012	6,5	11	15,6	22	45
2013	6,6	10,9	15,4	21,8	45,2
2014	6,5	11	15,6	22,2	44,7
2015	6,29	10,85	15,54	22,02	45,3
2016	6,26	10,63	15,19	21,62	46,29
2017	6,3	10,58	15,08	21,38	46,65
2018	6,14	10,53	15,08	21,49	46,76
2019	6,47	10,97	15,49	21,65	45,42
2020	5,96	10,69	15,21	21,63	46,51
2021	6,44	10,88	15,25	21,53	45,9
2022	6,13	10,37	14,77	21,1	47,63
2023	5,41	9,73	14,35	20,79	49,72

Source: TSI

Also, the development of the GINI coefficient can be used to examine inequality in income distribution. A rise in the coefficient means that inequality in income distribution has increased. The GINI coefficient decreased slightly after 2006, remained flat between 2007 and 2014, and then began to increase (Graph 24). There has been a sharp rise in the coefficient especially after 2021. This situation shows that inequality in income distribution in Türkiye has increased in recent years. The P80/P20 ratio, which expresses the ratio of the last 20% of the highest income earners in society to the first 20% of the income earners, indicates a similar result and increases rapidly after 2021 and reaches its highest level.



Graph 24. GINI coefficient and S80/S20 ratio

Source: TSI

In addition to the unusual policies implementation in Türkiye, the enormous earthquake disaster in February 2023 also contributed to the deterioration of income distribution. However, the income distribution statistics for 2023 were calculated based on the 2022 calendar year. Despite the return to realistic policies aimed at reducing inflation, high inflation is expected to go on for following 1-2 years. It is estimated that the worsening in income distribution will continue. Inflation is a problem that increases the deterioration in income distribution, but the policy tools preferred in combating inflation can also deepen this problem. Contractionary monetary and fiscal policies negatively affect the middle- and lower-income groups through increasing indirect taxes, reducing transfer expenditures from the budget, and suppressing wages (Yenice, 2024: 34). To prevent the cost of inflation is borne only by these groups, a comprehensive tax reform is needed that will reduce the informal economy. Also, additional measures are needed to protect the purchasing power of the middle- and lower-income groups, to increase direct taxes, and to ensure that more taxes are collected from high income earners.

Conclusion and Suggestions

When the Turkish economy was in a fragile structure, the CBRT's unusual monetary policy and its basic component, the liraization strategy, have been implemented. The liraization strategy targeted to increase the weight of TL-denominated tools, to carry out liquidity management mainly with TL-denominated instruments and to be selective in supplying loans. By these channels, it is aimed to achieve a current account surplus with the support of a competitive exchange rate and to ensure permanent price stability. However, in an environment where market interest rates were well below inflation, rising the TL preference of economic actors was only possible with intensive regulations and market interventions. The market interventions constantly necessitated new interventions, and relative prices and market mechanism were disrupted.

In order to analyze the success of the liraization strategy, it is necessary to examine the realization of the targets. The negative interest rate policy accelerated the depreciation of the national currency through domestic demand and capital outflows. Due to the unusual policies, expectations were distorted and an unprecedented increase in inflation occurred in a short time. Thanks to uncontrolled growth in credit and high domestic demand, imports exploded, and the current account balance deteriorated. As a result, not only the current account surplus and price stability targets failed, but also past gains of price stability were lost. The expected acceleration in production could not be achieved, and an economy could grow by borrowing and consuming. The increase in the country's CDS premium, the significant decline in capital inflows, the boost in dependence on the swap channel, having negative net reserves, and high cost of FXPD to the public have shown that unusual policies cannot be sustained.

In addition to the deterioration of price stability and financial stability, the unusual monetary policy and the liraization strategy have further increased inequality in income distribution. While high-volume loans given at low interest rates and practices such as FXPD have increased the share of the upper income group, the lower- and middle-income groups became poorer. The depletion of public resources and CBRT reserves resulted in the benefit of only a small group.

Despite the intensive regulations within the scope of liraization steps, there has been a slight increase in the weight of TL in bank and company balance sheets. The gains have been very small compared to the costs incurred. While FXPD products created a huge burden for the budget and the CBRT via exchange rate fluctuations and tax exemptions, they also made the fight against inflation difficult. Owing to selective credit policy, which is one of the tools of the liraization strategy, there has been an increase in the amount of special purpose loans that support investment and exports, but due to the negative interest policy, a rapid growth has occurred in total loans. It led to the use of loans for unintended purposes; rise in the demand for foreign currency, imports of luxury consumer goods and fixed asset prices. The low-interest loan policy was mainly supported by public banks, and there was a significant decline in the profits of these banks.

As of the second half of 2023, the monetary policy approach has been changed and the liraization strategy has been removed from the CBRT reports and policy texts, and the regulations of this strategy have been gradually removed.

There are lessons to be learned from the liraization strategy. First of all, it has been experienced again that it will not be possible to realize reverse currency substitution without ensuring price stability and financial stability. It has also been understood that production and exports could not be increased only via competitive exchange rates and low interest rates. To achieve these goals, a long-term comprehensive program is needed that includes investment incentives in selected sectors, solving structural problems, applying micro reforms and increasing productivity. Additionally, monetary policy should be simple and easy to communicate. Policy tools having too many tasks such as RR and securities maintenance seem to have little chance of success. Moreover, institutional quality and management of expectations are key factors for success. Finally, it would be appropriate to avoid regulations that would disrupt the market mechanism and relative prices. The balance between interest rate, inflation and exchange rate should be protected.

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