



NORTH-HOLLAND

Journal of Policy Modeling
26 (2004) 1003–1013

Journal of
Policy
Modeling

Inflation dynamics and monetary policy strategy: some prospects for the Turkish economy

Vuslat Us*

Central Bank of The Republic of Turkey, Research Department, Ankara, Turkey

Received 1 March 2003; received in revised form 1 January 2004; accepted 1 July 2004
Available online 11 September 2004

Abstract

This paper analyzes the dynamics of inflation in the Turkish economy, which has experienced increasingly high levels of inflation over the last 30 years. By conducting a Vector Autoregression (VAR) analysis, the variance decomposition (VDC) and the impulse response functions (IRF) show that the relatively high and inertial nature of inflation mainly stems from the increases in public sector prices and the depreciation of the Turkish lira. On the other hand, the Granger causality tests as well as the VDC and IRF demonstrate that high prices have not been as a result of an expansionary monetary policy. These results together with the previous results show that inertial inflation is not a monetary phenomenon in Turkey, but rather an outcome of a political misconduct, which therefore shows the fiscal dominance. © 2004 Society for Policy Modeling. Published by Elsevier Inc. All rights reserved.

JEL classification: E310; E500; E690

Keywords: Persistent inflation; Inflation inertia; Vector Autoregression; Impulse response function; Fiscal dominance; Credibility; News effect

1. Introduction

During the last 30 years, Turkish economy has experienced relatively high levels of inflation. Large budget deficits in addition to high and rising real interest rates

* Tel.: +90 312 311 3921; fax: +90 312 324 2303.

E-mail address: vuslat.us@tcmb.gov.tr.

fed into high inflation, and in turn, are fed by high inflation and the associated risks. Yet, chronic and high inflation has not degenerated into hyperinflation as it did in most other countries. However, the average of about 20% inflation rate in the 1970s, and 60% in the late 1980s and early 1990s, and finally, 80% in the late 1990s clearly show the persistence and the upward trend in inflation.

It is commonly argued that high and persistent inflation in Turkey has been fed by:¹

- a. High public sector budget deficits,
- b. Monetization of public sector budget deficits,
- c. Immense infrastructure investments such as Southeastern Anatolian Project,
- d. High military expenditures including the fight against terrorism attacks,
- e. Political instability and populist election economy policies,
- f. High real interest rates and risk premium due to high public sector borrowing requirement,
- g. Increasing regulated prices for the public sector products such as gasoline, utilities,
- h. Devaluations that feed into inflation by exchange rate pass-through, mechanism,
- i. External shocks such as oil price increases, Persian Gulf crisis, Russian crisis, 2 devastating earthquakes,
- j. Persistent inflationary expectations.

The aim of this paper is to provide an analysis on the sources of inflation. In doing so, the dynamics of inflation is studied by conducting a Vector Autoregression (VAR) analysis. The results of the variance decomposition (VDC) analysis and the impulse response functions (IRF) show that inflation has been mainly fed from two sources: the public sector prices and the pass through from exchange rate to domestic prices. The paper proceeds as follows: The following section gives an overview of the previous studies on the dynamics of persistent inflation. The following section presents the empirical evidence on the inertial nature of the inflation in Turkey. Finally, the last section concludes this paper.

2. A quick review of the dynamics of persistent inflation

In models that study inflation persistence vis-à-vis expectations, a common practice is to assume sticky prices. One of the most crucial aspects of these New Keynesian sticky price models is money matters- monetary policy can affect real variables such as output. In these sticky price models of staggered adjustment, wages or prices are set by multi-period contracts. In each period, the contracts

¹ Kibrıçcioğlu (2002), Diboğlu and Kibrıçcioğlu (2001) provide an extensive discussion on the sources of inflation in Turkey over the last 25 years.

متن کامل مقاله

دریافت فوری ←

ISIArticles

مرجع مقالات تخصصی ایران

- ✓ امکان دانلود نسخه تمام متن مقالات انگلیسی
- ✓ امکان دانلود نسخه ترجمه شده مقالات
- ✓ پذیرش سفارش ترجمه تخصصی
- ✓ امکان جستجو در آرشیو جامعی از صدها موضوع و هزاران مقاله
- ✓ امکان دانلود رایگان ۲ صفحه اول هر مقاله
- ✓ امکان پرداخت اینترنتی با کلیه کارت های عضو شتاب
- ✓ دانلود فوری مقاله پس از پرداخت آنلاین
- ✓ پشتیبانی کامل خرید با بهره مندی از سیستم هوشمند رهگیری سفارشات