Reel Effective Exchange Rate Volatilities Impact On Tourism Sector In Turkey: An Empirical Analysis Of 2003-2014

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Abstract

There have been positive changes in the macro indicators of the economy in Turkey over the last decade. The foreign trade volume increased remarkably whereas serious progress has also been observed in many sectors. The volatility in the Turkish currency was relatively reduced in the aftermath to the regulations in the finance sector. Tourism is one of the sectors in Turkey that is open to international markets and attracts foreign currency. The contribution and added value of the tourism sector to the national economy has been growing in recent years. The stability in the domestic currency also positively affected tourism sector. To this end, the revenues in this sector have also increased. This study analyses the dynamics of the macro performance in Turkish economy over the last decade and empirically reviews the developments in tourism sector as well as the reflections in the monetary policies and the real effective exchange rate (REER) volatility. Additionally, empirically tests the relationship between the tourism sector revenues and the REER in the period between 2002 and 2014.

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1. Introduction

Turkish economy has been experiencing a process of structural transformation in order to become more competitive in the global markets and increase domestic welfare in recent years. While agricultural and relevant sectors constituted the backbone of the economy up to 1970s, textile sector has become more important in the aftermath of the 1980s. Automotive sector became the locomotive in the exports in 2000s. On the other side for the service industry, Tourism is a leading sector in terms of its contribution to the foreign trade volume.

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According to the world tourism organization, tourism sector gains importance thanks to its contribution to the development (Akan & İşık, 2009). The spending by the foreign tourists revives the economy and makes huge contributions to the domestic sub-sectors in different ways. When people become wealthier and the price differences between the nations in a rapidly globalized are reduced, the tourism revenues increase (Khan & Lin, 2001). Generating financial resources the developing nations need in their economic development is less costly than the exports (Sinclair, 1998). The sector has been positively affected by the recent developments in Turkish economy; currency policy is one of the most important factors in foreign trade. REER may affect many sectors in countries adopting an open economy. For this reason, the central banks take measures to ensure that volatility remains minimum in the currencies. The central banks in developing countries have to take proper measures vis-à-vis the volatility problem because the destruction to be caused by instability in currency rates to the economy is huge. One of the most important data used in a number of accounts focusing on exports and imports in economics literature is REER. Recent theoretical models take tourism as an export item. Rapid development in tourism leads to direct increase in household and public incomes whereas it also has an indirect impact upon improvement the balance of payments (Polat & Günsel, 2012).

Additionally tourism is one of the sectors in Turkey that is open to international markets and attracts foreign currency. The contribution and added value of the tourism sector to the national economy has been growing in recent years. Attention to the tourism policies goes back to the 1980s. The bill on incentives for tourism introduced in 1982 contributed to the development of the sector and the tourism actors involved in tourism activities. For instance, since the introduction of this law in 1982, number of visitors to Turkey has increased by 22 times whereas the tourism revenues have grown by 62 times. In these figures, the incentives and supports supplied to the tourism enterprises played a determinative role. The first part of this study answers the question as to why REER is important in terms of the foreign trade transactions and offers a theoretical framework on REER. The following part seeks to empirically analyze the relationship between REER and the income, expenditure and number of foreign tourists in the tourism sector.

2. Literature Review And Hypotheses

2.1 Real Effective Exchange Rate and International Trade Theory

Currency rate generally refers to the nominal currency rate between two national currencies. Nominal currencies have to be adjusted in accordance with the external and domestic inflation rates. To ensure stability between currency rates, some measures are taken in consideration of the domestic and external inflation rates; these measures vary depending on the regime preferred in a given country. The relationship between the domestic goods and services and the prices of these goods and services in external markets is called REER (Copeland, 2005; Seyidoğlu, 2009).

Dornbusch (1997) holds that REER refers to an important indicator used in the measurement of the competitive power of a national economy in form of the prices of the goods relative to the prices of the same goods in domestic markets. In other words, when the same currencies of both countries are expressed in form of relative prices, this could be seen as the measurement of the international competitiveness (Özkan, 2003). Due to the impact of the decisions of the makers of the economic policies upon production, consumption and expenditures in the local economy, REER is determinative in the current balances (Braur, 2003). Because the sectors are classified as sectors open and not open to foreign trade in REER measurements, the relative prices of the goods subjected and not subjected to foreign trade are considered in theoretical accounts (Edwards, 1988). The changes in the currency rates lead to changes in the prices of the goods and services subject to international trade. At the same time, the increase and decrease in REER provides insights on the balance sheet of the national foreign trade. In general, decline in the REER refers to negative developments in the trade balance (Seyidoğlu, 2009). The increase in the REER refers to the increase of competitiveness in the goods produced under c.p. assumption in the global markets; and a decline refers to the decline in the competitiveness in these goods. These theoretical approaches explain the situations where goods and service transfer is performed from one country to another. In tourism sector, the spending by the foreign tourists in local markets is taken into account. Goods and services are sold in domestic market; for this reason, it
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