

# **DETERMINANTS OF DOMESTIC INVESTMENT**

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# **I. STRUCTURAL PROBLEM-1**

# Investment, savings and current account

	<b>Current account balance</b>	<b>Investment</b>	<b>Savings</b>
	<b>(%GDP)</b>	<b>(%GDP)</b>	<b>(%GDP)</b>
2008	-5.1	26.8	21.8
2009	-1.8	22.4	20.6
2010	-5.8	24.9	19.1
2011	-8.9	28.1	19.1
2012	-5.5	27.3	21.8
2013	-6.7	28.5	21.8
2014	-4.7	28.9	24.2
2015	-3.7	29.7	26.0
2016	-3.8	29.8	26.0
2008-16	-5.1	27.4	22.3

# EMEs and Turkey

	Investment (%GDP)	Savings (%GDP)
Country Group Name	2008-2016	2008-2016
Emerging market and developing economies	31.8	32.7
Commonwealth of Independent States	22.6	25.3
Emerging and developing Asia	41.3	43.4
Emerging and developing Europe	25.1	21.0
ASEAN-5 (Indon., Malays., Philip., Singo., Thai.)	28.3	30.2
Latin America and the Caribbean	21.7	19.4
Middle East, North Africa, Afghanistan, and Pakistan	27.5	33.3
Middle East and North Africa	28.6	34.8
Sub-Saharan Africa	20.6	18.2
Turkey (new GDP)	27.4	22.3

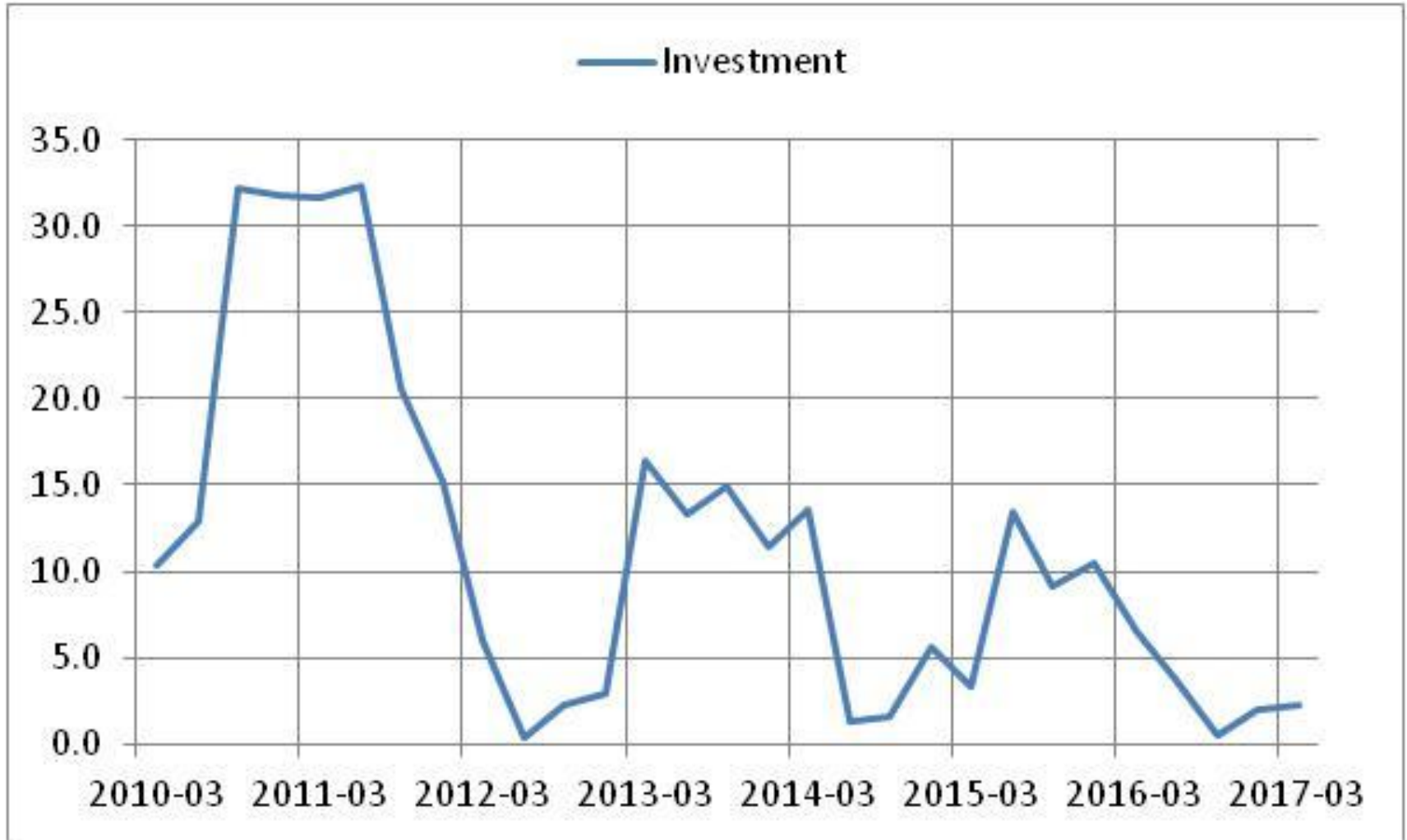
# Low savings rate is a constraint

- Low savings rate constraints investment growth
- To keep a mediocre investment performance intact Turkey has to borrow from abroad.
- This renders investment performance (and in general Turkish economy) vulnerable to change in risk appetite of foreign investors.

# Low savings rate is a constraint

- It also causes negative balance sheet effects.
- Real exchange rate fluctuations have a significant impact on the balance sheets of corporates.
- Balance sheets (with FX mismatch) deteriorate with sharp depreciations leading to a decline in investment desire.
- This also lowers credit supply.

# Rate of growth of investment expenditures (%)



# Low investment growth

- We do not know the private and government components of investment (new GDP).
- Investment growth is low in recent years. Why?
- Simple regression results for the determinants of investment:
  - Real credit growth
  - Confidence indicators
  - Real exchange rate
  - Demand factors
  - Inertia

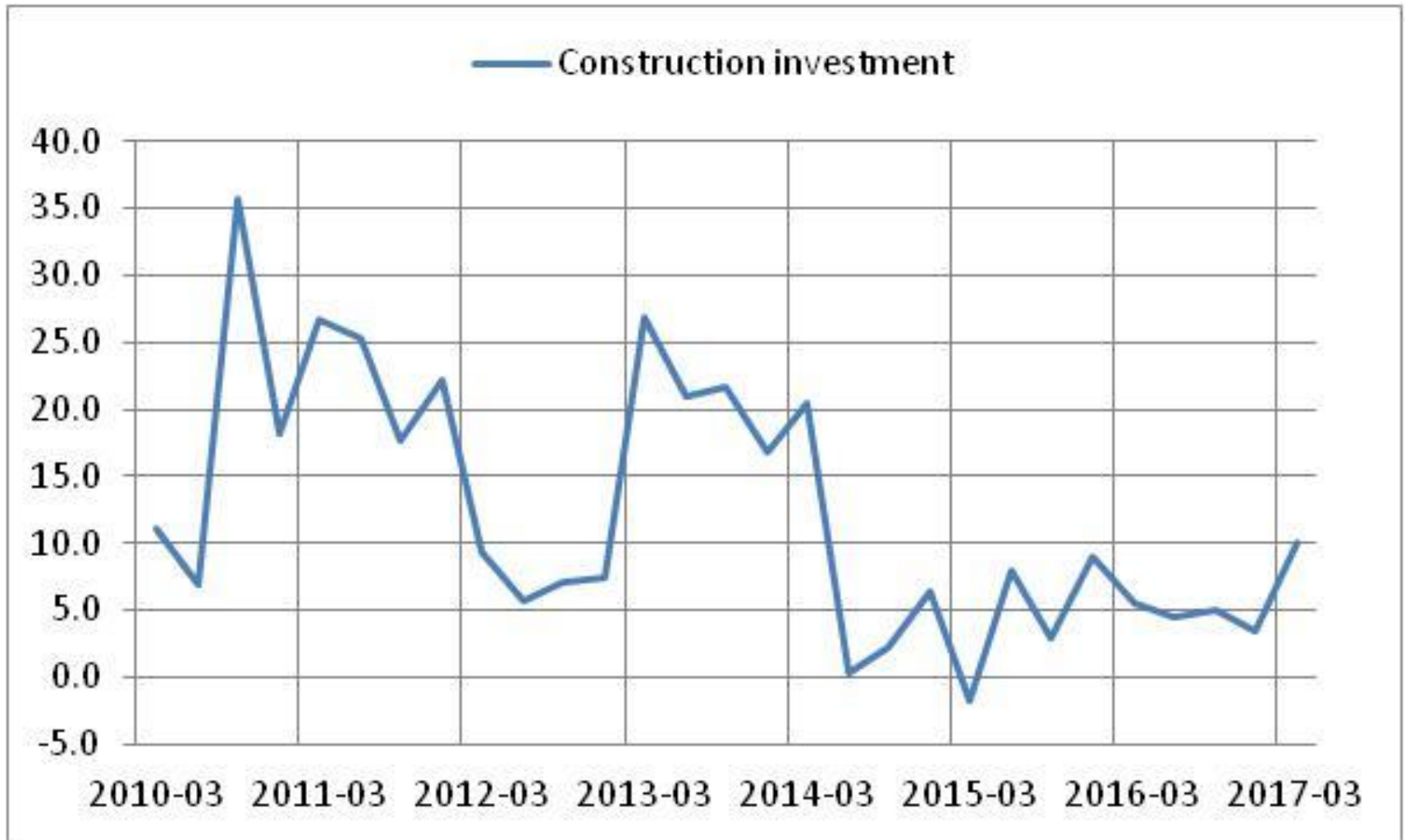


## **2. A SHORT TERM PERSPECTIVE**

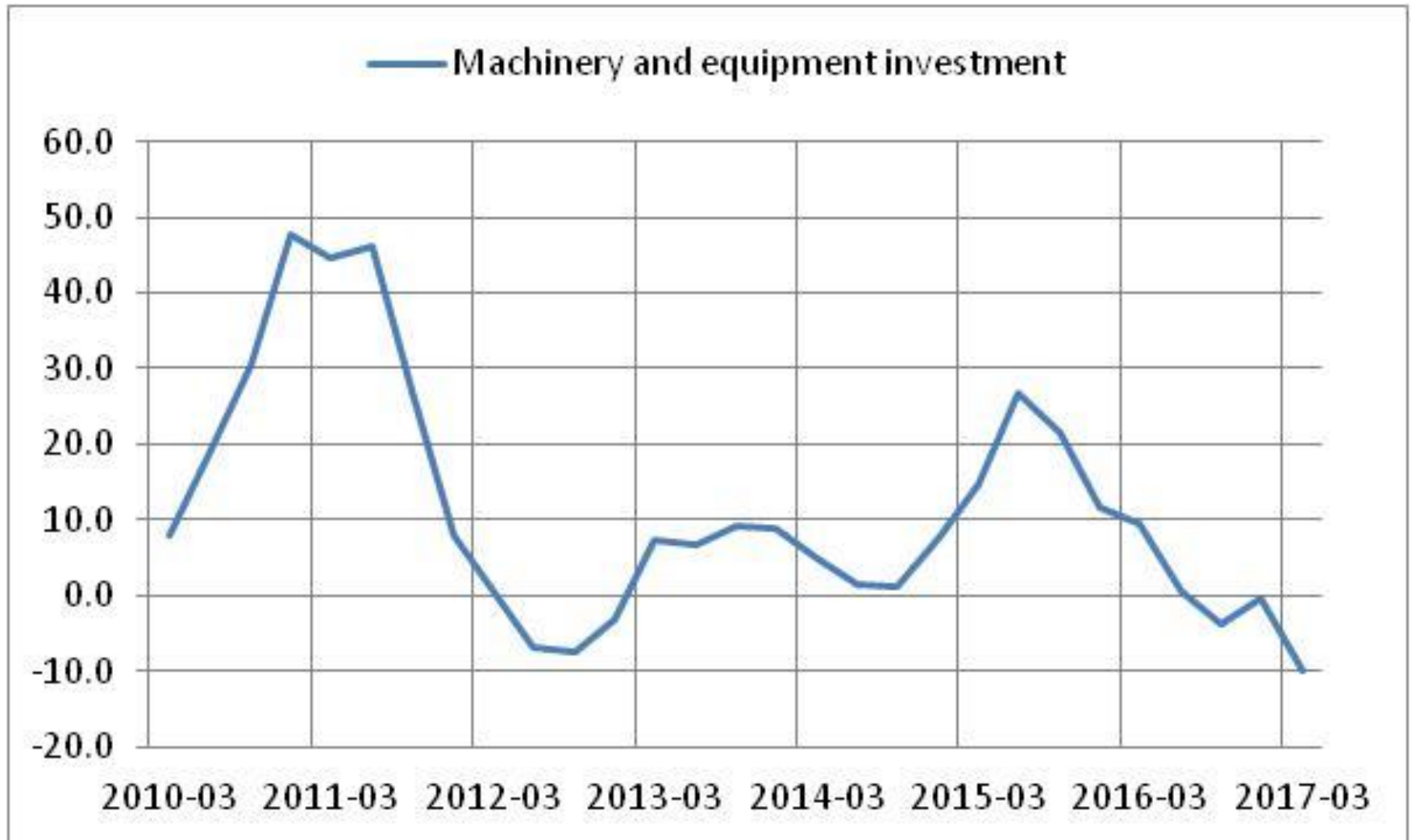
# Low investment growth

- Break down of investment expenditures (machinery versus construction) is important as well.
- In recent years the main problem is in machinery and equipment investment.
  - It has been following a downward trend since 2015Q2.
  - Moreover it has been declining for the last three quarters.

# Rate of growth of construction investment expenditures (%)



## Rate of growth of machinery and equipment investment expenditures (%)



# Low investment growth

- Factors stated above as the determinants of investment clearly played a role in this trend.
  - Foreign policy, terrorist activities, election after election: *Uncertainty, confidence...*
  - External shocks: *Fluctuations in capital flows -> sharp depreciations -> balance sheet effects...*
  - Macroprudential measures: *Constrained credit growth?*

### **3. A LINK BETWEEN SHORT-TERM AND STRUCTURAL PROBLEM-1**

# Credit, deposits and other sources

	Credit/ Deposits (%)	(Borrowing from banks + Securities)/Deposits (%)		Borrowing from banks/ Deposits (%)
2009	77.9	18.4		18.3
2010	81.1	17.8		17.5
2011	93.8	24.4		22.5
2012	101.7	27.7		23.6
2013	108.2	30.8		24.9
2014	114.8	34.6		27.2
2015	118.3	37.3		28.9
2016	119.4	36.0		28.2

# Looking ahead

- Additional potential constraint: Credit-to-deposit ratio > 120%.
- Deposit growth could constrain investment growth.
  - An external shock -> Lower borrowing from external world -> decrease in other funding sources -> credit/deposit ratio would decrease
  - Do not only consider this problem from financial stability perspective.



# Looking ahead

- Savings problem should be addressed.
- No easy solution.
- But we do know what no to do:
  - Do not try to keep real interest rates in the negative territory.
- How to address savings problem?
  - Public sector savings
  - Private sector savings

## **4. STRUCTURAL PROBLEM-2**

# Looking ahead

- Deeper problems:
  - Rule of law
  - Quality of institutions: Especially judiciary system
  - Thinking on construction growth
    - What are the underlying incentives?
    - Do some of these incentives increase growth of construction investments in the expense of machinery and equipment investments?