

Economic Outlook

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Coincident Economic and Financial Conditions Indexes Current Estimates

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This report publishes the current estimates of the coincident economic (CEI) and financial conditions indexes (FCI) we have designed for the Turkish economy using advanced econometric methods. We used a rich dataset including many macroeconomic and financial indicators with different timing and frequencies.

As financial stability is one of the main conditions for economic growth, FCI is considered a primary leading indicator for CEI. Therefore, based on the joint behavior of these two indexes, we computed the probability of entering an economic recession within the same model framework. This report also publishes these probabilities' current estimates as a numerical reflection of our expectations of the economy's direction in addition to the current estimates of these indices.

The model we use in this report has been published in one of the internationally respected journals in the field. For details, our article can be found at <https://onlinelibrary.wiley.com/doi/full/10.1111/obes.12413>.

Coincident Economic Index (CEI)

According to the most recent model estimates, EDE increased by 1.6% compared to the previous month in August.¹ The changes in July and June were 1.5% and 0.2%, respectively.

Elaborating the changes in EDE's components on the production side, according to the latest industrial production index data, there was a 1.5% increase in June compared to the previous month. After the correction in March following the February earthquake, it had remained low. This relatively strong rise in May and also in June after the decline in April indicates a strong correction. PMI, which is published timelier, fell below the critical threshold of 50 with a value of 49 in July. The PMI data has been above 50 for the past four months. On the other hand, we observe a stark increase in both export and import quantity indices.

Looking at the labor market, total employment increased by 1.2% in June. Considering all these components, we see that EDE has been quite volatile throughout the year.

Financial Conditions Index (FCI)

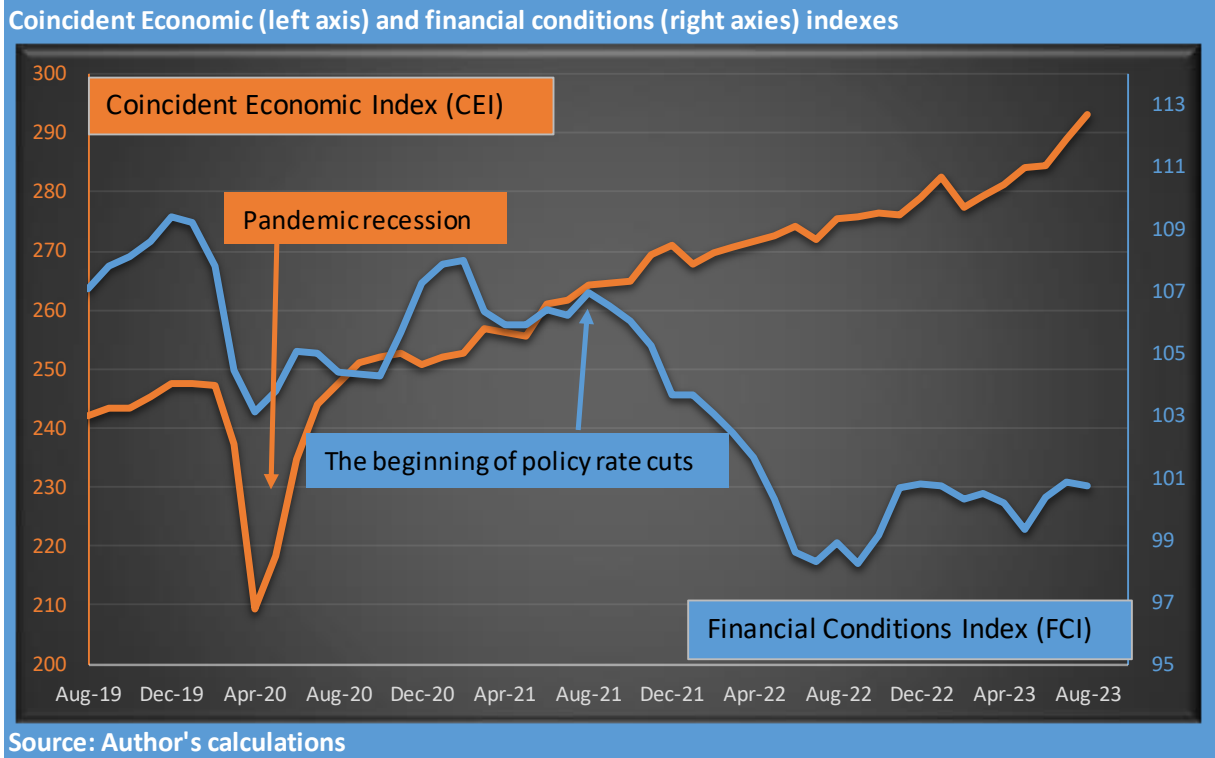
According to the most recent model estimates, FDE decreased by -0.1% in August compared to the previous month. The changes in July and June were 0.5% and 1.0%, respectively. The index's volatility has increased significantly in recent months due to the uncertainties surrounding the elections in May. Despite the efforts to recover in financial conditions, there is currently no clear trend of improvement or deterioration.

Focusing on the sub-components of FDE, there was a strong surge in gross reserves in June. Turkey's 5-year Credit Default Swap (CDS) premium decreased to 380 basis points and thereby below 400 basis points after several months. There has been a decline in credit momentum, leading to a sharp decrease of 8.2% in real credit volume. Despite contractions in real credit volume and many similar indicators, the improvement in Turkey's risk perception compared to previous months led to divergent movements of the sub-components of the index. Consequently, a clear trend has not yet formed in financial conditions.

Figure 1 shows the evolution of FCI and CEI starting from 2019. In the first half of 2020, the sharp economic contraction caused by the Covid-19 pandemic and the subsequent rapid rebound is observed in CEI's evolution. Similar drops and rapid rises can be detected for FCI, especially during the term of former Central Bank Governor Naci Ağbal.

¹ As a result of the standardization of the data we imposed for the sake of interpretation of the outcomes, the rate of change in both economic and financial condition indices is expected to be between 2% and +2%. Values less than -2% or higher than +2% can be interpreted as low probability extreme values. For example, in the past, these values were observed as -2.08% in November 2008, the trough of the 2008 recession, and -2.17% in July 2016. Therefore, the proximity of these values to 2% will also inform us about the severity of the contraction.

Figure 1. Coincident Economic and Financial Conditions Indexes Estimates as of August, 2023

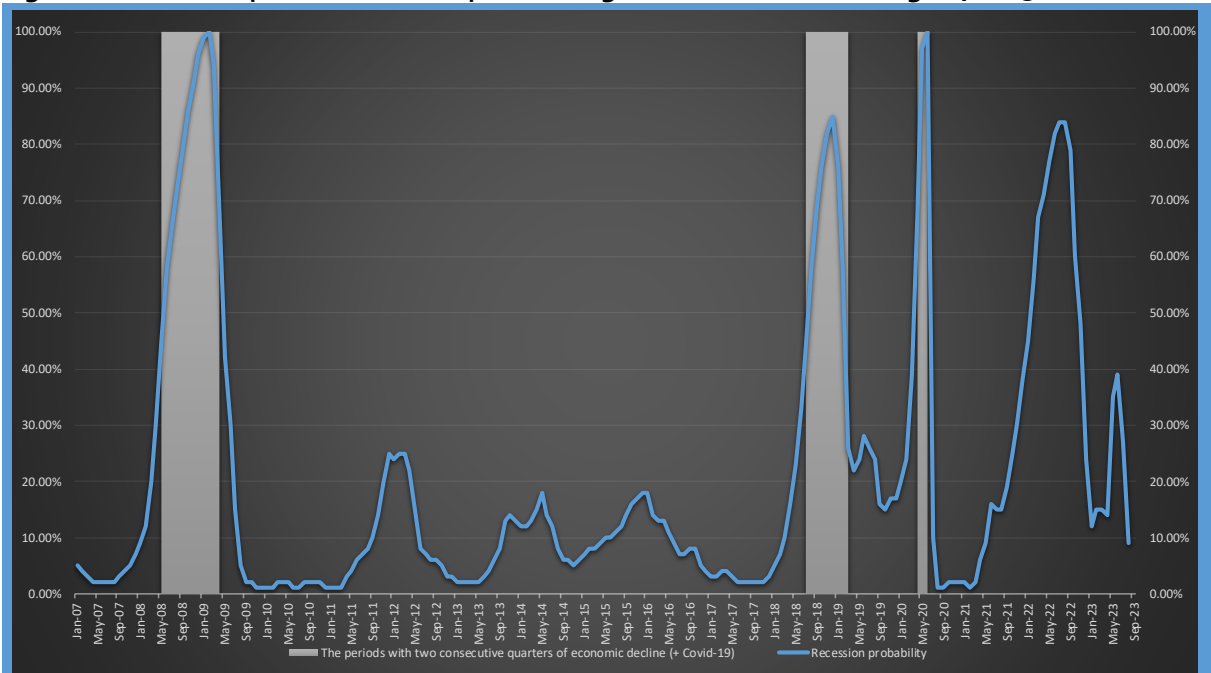


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Probability of Economic Recession

We compute the probability of the economy entering a recession in the short term based on the joint behavior of CEI and FCI. Figure 2 illustrates these probabilities' evolution from 2007 to the present. In June, we had calculated this probability to be 39%. However, this month, due to the increase in industrial production in May and the relatively improved risk perception of Turkey, this probability has decreased to 9%.

Figure 2. Recession probabilities computed using available data as of August, 2023



Source: Author's calculations