

## Chapter 2

# Financial Marketing–Based Role of Exchange Rate to Increase Foreign Trade in Turkey

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### **ABSTRACT**

*This chapter tries to determine whether there is a causal relationship between exchange rate and foreign trade. The study includes monthly data between February 2003 and December 2018 including dollar foreign exchange selling rate and inflation related real exchange rate for exchange rate, and export amount, import amount, export increase/decrease rate, and import increase. Increase/decrease rate is used for foreign trade among other variables, for a total of 6 variables. According to the obtained results of Engle-Granger cointegration analysis, there is a cointegration between variables in the long run. However, according to the results of the Toda-Yamamoto causality analysis, it was understood that there is no causality relationship between exchange rate and foreign trade.*

### **INTRODUCTION**

In a narrow sense, foreign exchange is the name given to foreign currency. In the broadest sense, foreign exchange is the means of payment used by countries to pay for goods or services. The means referred to herein as payment means may be money, as well as valuable documents such as checks, bills and policies. If a currency can buy more foreign currency, we can call it an increase in the exchange rate, and if a currency can buy less foreign currency, we can call it a depreciation in the exchange rate. As a result of the depreciation of the exchange rate, the country's exports to another country fall while im-

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ports increase. As a result of the increase in the exchange rate, the country's exports to another country increased while imports decreased (Ison & Wall, 2007).

The foreign exchange market is the market where foreign demand and supply come together. Unlike other markets, the foreign exchange market is a global market that is open 24 hours a day. Taking into account the time difference between countries, the closing foreign exchange market in other countries may be open in other countries. Therefore, there is constant activity in the foreign exchange market (Dinçer & Yüksel, 2018). While the foreigners provide foreign exchange inflow to the country as a result of export, those who demand foreign exchange provide foreign exchange out of the country as a result of imports. In other words, while the most important economic activity that increases the foreign exchange supply is exports, it leads to the increase in foreign exchange demand from the country by importing the goods and entering the goods (Dinçer et al., 2018a,b,c).

With the collapse of the Bretton-Woods system, which accepts the US dollar as a reserve index indexed under gold, many changes have occurred between countries and markets. The disappearance of the economic boundaries between countries, especially with the globalization, has led to increased mutual trade and the world becoming a single market. In this regard, the increase in uncertainties in exchange rates as a result of the countries' transition from fixed exchange rate system to floating rate system affected the return of investors and foreign trade balance. Until today, in past years, different exchange rate policies were applied in different periods in Turkey. Applying the fixed exchange rate system in the 1980s, Turkey has moved to a floating exchange rate system in February 2001 after the crisis. Especially after 1980, with the adoption of export-based growth hypothesis, the effect of changes in exchange rates on foreign trade attracted the attention of many researchers (Karaçor & Gerçeker, 2012). In other words, exchange rate and foreign trade have become a detailed research topic for economists.

When the studies dealing with the relationship between exchange rate and foreign trade were examined, it was found that independence results were obtained from each other. In this context, some researchers have stated that this relationship is one-way or two-way, while some researchers argue that there is no relationship. In other words, the researchers could not agree on the subject. Therefore, the issue should be handled empirically in different ways. Considering the mentioned considerations, the aim of this study referred to in Turkey to determine whether the relationship between the variables. If the relationship is determined, it is to understand the direction of the relationship. In this context, monthly data for the period of 2003: 02-2018: 12 were tested by Engle-Granger Cointegration and Toda-Yamamoto Causality analysis.

The study consists of 3 chapters. In the first part of the study, general information about exchange rate and its types will be given. Then, the exchange rate system and approaches for determining the exchange rate will be discussed in detail. In the second part of the study, foreign trade concepts and policies applied in foreign trade will be mentioned. Immediately after these topics, classical and new foreign trade theories will be discussed in different topics. In the third and last part of the study, after considering the studies done in the literature, Engle-Granger Cointegration and Toda Yamamoto causality analyzes which we will use in the analysis of the data will be mentioned theoretically and then the estimation results and findings will be shared. In the conclusion part of the study, the results obtained in the study will be evaluated.

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