

# Accepted Manuscript

Credit Market Imperfections and Business Cycle Asymmetries in Turkey

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PII: S0927-5398(15)00092-4  
DOI: doi: [10.1016/j.jempfn.2015.08.008](https://doi.org/10.1016/j.jempfn.2015.08.008)  
Reference: EMPFIN 830

To appear in: *Journal of Empirical Finance*

Received date: 25 July 2013  
Revised date: 27 March 2015  
Accepted date: 27 August 2015



Please cite this article as: Günay, Hüseyin, Kiliç, Mustafa, Credit Market Imperfections and Business Cycle Asymmetries in Turkey, *Journal of Empirical Finance* (2015), doi: [10.1016/j.jempfn.2015.08.008](https://doi.org/10.1016/j.jempfn.2015.08.008)

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Credit Market Imperfections and Business Cycle Asymmetries in Turkey<sup>1</sup>

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May 2011

The credit market imperfections have important consequences for aggregate cycles, especially for developing countries. The research on the relationship between imperfections and output dynamics at the macro level are ample, but the lack of wide coverage micro data sets for developing countries limit the study of aggregate implications of the micro level capital market imperfections. This paper presents micro evidence on the credit market imperfections in Turkey and connects these imperfections to macro movements. First part of the paper documents the aggregate boom-bust cycles in Turkey and shows that non-tradable sector is more volatile over the business cycle than tradable sector. Additionally, this sector based asymmetry is found to be strongly correlated with aggregate credit movements. To establish the connection between the sector based asymmetries and the credit markets further, second part of the paper constructs two micro data sets. Using structural estimation, we find that non-tradable sector is financially more constrained than tradable sector. With non-tradable sector being more constrained, credit movements become an important determinant of boom-bust cycles. Therefore, we can establish that the asymmetry in the financial constraints of the different sectors at the micro level can generate the observed asymmetrical aggregate response of sectors over the business cycle.

JEL Classification: D92; E44; G31

Key Words: Credit constraints; business cycle asymmetries; cash-flow regressions.

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