Article | 8 December 2025 TURKEY

Monitoring Turkey: Continuing upside risks to the inflation outlook

November CPI once again came in below expectations, while annual inflation continues its downward trend. But upside risks remain, driven by stronger-than-anticipated domestic demand and the elevated inflation trajectory seen so far in 2025, which has weighed on expectations

Turkey's economy at a glance

- Inflation remained on a declining path in November, and we anticipate that the annual inflation rate could be around 31% by the end of 2025. For next year, we expect inflation to decelerate to around 22% (vs the Central Bank of Turkey's interim target of 16%) with the balance of risks tilted to the upside.
- The outcome of the minimum wage negotiations for 2026 will be crucial for the inflation outlook. The current level of the minimum wage-to-hunger index ratio, which is close to the minimum of the 2016-22 range, implies the possibility of a larger-than-expected adjustment, which will be announced towards the end of this month.
- Survey of market participants released by the CBT shows further deterioration in inflation expectations in November. The 12-month-ahead inflation expectations

increased to 23.5%, while the 24-month-ahead CPI expectations rose to 17.7%. In the survey, year-end inflation expectations for 2025 and 2026 stood at 32.2% and 23.2%, respectively, recording a deterioration in comparison to a month ago. While we will likely see an improvement in December with the favourable November inflation surprise, the survey implies that the market sees the disinflation process likely to proceed more slowly than implied by the CBT's interim targets.

- While year-on-year GDP fell more than expected in the third quarter, the seasonally adjusted quarterly pace has remained strong, defying previous expectations of a significant slowdown in momentum. This suggests upside risks to the growth outlook. Leading indicators, including PMI, capacity utilisation, consumer and real sector confidence indices that point to an acceleration in GDP growth in the last quarter also support this view. Accordingly, we have raised our full-year GDP growth forecast for 2025 to 3.8%, up from the previous estimate of 3.4%.
- While the November inflation data should encourage the central bank to remain on its easing path, the latest 3Q GDP data and early indicators for the last quarter imply less supportive demand conditions for the disinflation process, increasing upside risks to the inflation outlook with the ongoing rate cut cycle and easing financial conditions. Accordingly, the central bank will likely remain cautious with a measured 100bp cut in the December MPC, in our view, though we should not rule out the possibility of a larger hike.
- The current account surplus in September aligned with expectations, while the capital account once again played a crucial role due to significant outflows. Preliminary customs data from the Ministry of Trade suggest further deterioration in the October current account, as the foreign trade deficit appears to have widened in comparison to last year. Looking forward, a combination of external risks – including developments in global trade and geopolitical tensions – as well as ongoing weakness in domestic demand, is expected to shape the path of the current account balance.

Quarterly forecasts

	3Q25	4Q25F	1Q26F	2Q26F	3Q26F	4Q26F	1Q27F	2Q27F
Real GDP (%YoY)	3.7	4.0	3.5	3.7	3.9	4.5	5.2	4.6
CPI (eop, %YoY)	33.3	31.0	27.4	24.6	22.5	22.0	20.6	19.4
Central bank key rate (eop, %)	40.50	38.50	35.50	32.50	29.50	27.00	25.50	24.00
3m interest rate (eop, %)	42.58	38.89	35.31	32.43	29.37	27.75	26.33	24.69
10yr yield (eop, %)	31.54	30.74	28.05	26.12	24.60	23.34	21.43	20.65
USD/TRY exchange rate (eop)	41.57	43.00	45.19	47.24	49.18	51.00	53.09	55.12
EUR/TRY exchange rate (eop)	48.80	50.74	53.77	56.69	59.51	62.22	64.77	67.25

Source: Various sources, ING

FX and rates outlook

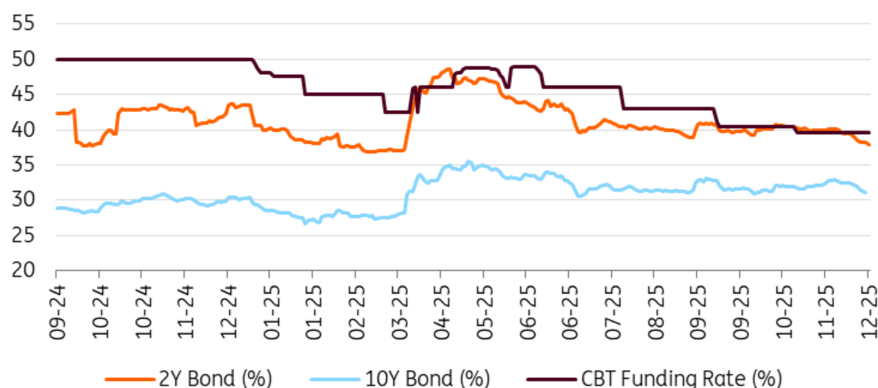
The market is considering further disinflation and the pace of rate cuts. November inflation was enough for the front of the curve to fall below the lower end of the current range after several months, where we were for the entire second half of the year, despite the economy showing greater resilience than we had previously expected.

Although the rates market is enjoying a decent rally, the FX market has not changed much, and we cannot expect much change here in the coming months. Given the hawkish and cautious approach of the central bank, it can be assumed that potential changes in the FX regime will come earlier rather than later. At the same time, the market has become fully accustomed to political noise. Therefore, we believe that TRY will remain a popular carry trade next year as well, despite the ongoing cutting cycle. For the middle of the year, we expect USD/TRY to be at 48.40 and 51.00 at the end of the year.

In the rates space, the front of the OIS curve has seen new lows in recent days, with 2y for the first time below the levels before the March sell-off. At the same time, the long end of the curve and TurkGBs have seen a decent rally since late November, suggesting some renewed confidence in the disinflationary outlook. But the curve retains the expected steepening bias, which we expect to continue.

In the short term, we believe the market has gone too dovish and the CBT meeting this week is a hawkish risk to current market pricing unless the central bank cuts by more than 150bp (100bp is our baseline). In the medium term, however, we believe the market should price in more rate cuts, more in line with our forecast once we see further weaker inflation prints.

Local bond yields vs CBT funding rate



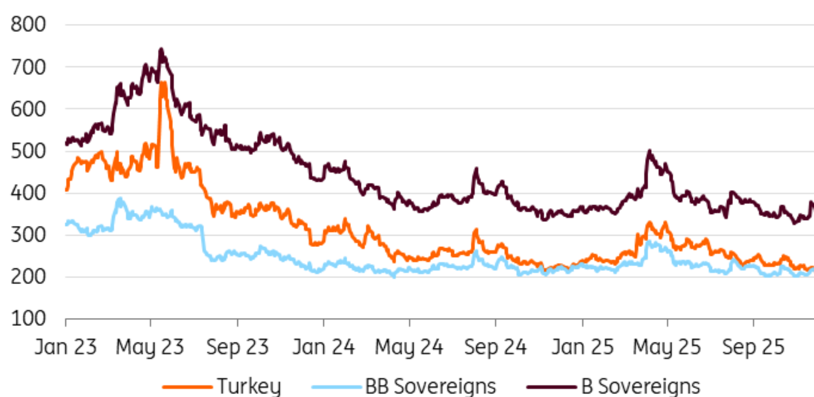
Source: CBT, Bloomberg, ING

Sovereign credit views

With political headline noise dying down, or markets at least becoming more accustomed to it, performance has been relatively strong for Turkey's dollar bonds recently. Spread levels have squeezed tighter than the BB sovereign average, their tightest relative level since 2016. That being said, fundamentals remain solid, with the disinflation process continuing and the current account deficit under control, so we expect the strong sentiment to continue.

Issuance of $13bn is planned in external markets for next year, the same as this year's above-target execution, so early activity in January is possible if general market sentiment remains robust. This could offer a more attractive entry point relative to the relatively stretched valuations seen across the dollar curve for Turkey at the moment.

US$ Bond Sub-Index Spreads vs USTs



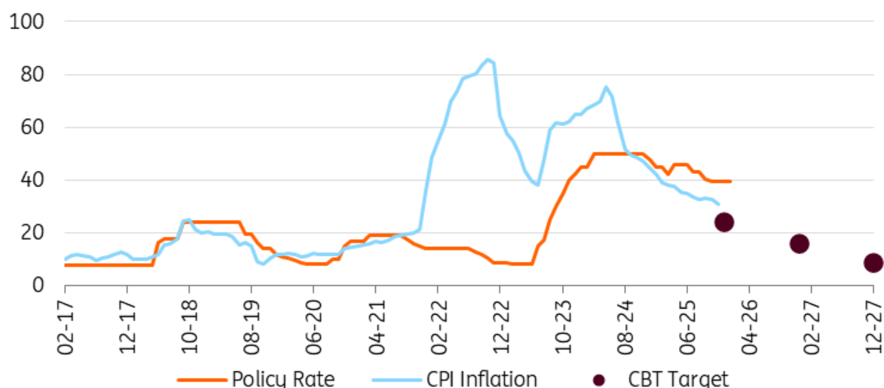
Source: Refinitiv, ING

Favourable surprise in November inflation

November CPI inflation was 0.87% month-on-month, coming in lower than the consensus estimate. This was mainly due to unprocessed food and some non-food groups. As a result, annual inflation has maintained its downtrend with a further decline from 32.9% to 31.1%. While inflation rose by 2.2% in November 2024, the five-year average for November in the 2003-based index was just 2.8%. This suggests a strong base effect, reinforcing the continued decline in annual inflation.

In November, the PPI increased by 0.84% MoM, while a significant portion of the monthly change is attributable to coke and refined petroleum products, as well as basic metals. Annual producer inflation inched up to 27.2% YoY, remaining on a gradual uptrend since April. However, the current level of PPI inflation indicates that cost pressures remain moderate as the FX basket showed only a very limited average increase of 0.7% MoM in November and its cumulative increase over the last 12 months remained at around 28.0%.

Inflation outlook (YoY%)



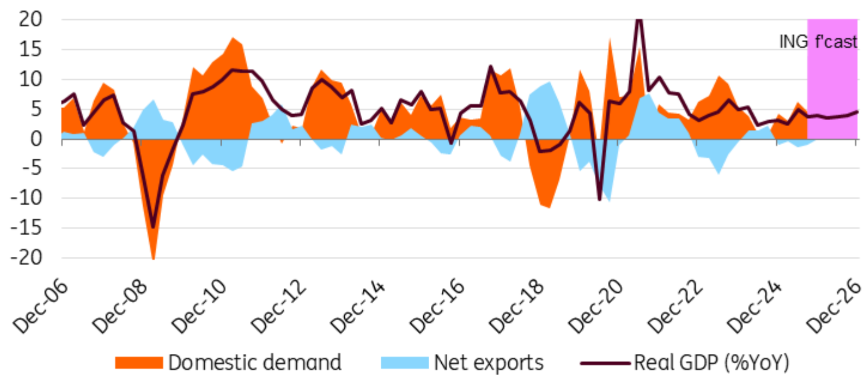
Source: TurkStat, CBT, ING

Below consensus third-quarter GDP, but sequential growth is strong

In the third quarter of 2025, GDP grew by 3.7% year-on-year, below the market consensus. This marks a deceleration compared to the previous quarter, which recorded 4.9% YoY after a revision by TurkStat. The growth was primarily driven by private consumption and investment activity, while external demand and stock depletion reduced the headline. As a result, GDP growth for the first nine months of the year stood at 3.7%.

After seasonal adjustments, 3Q25 GDP corresponds to a quarter-on-quarter growth rate of 1.1%, representing a slowdown in comparison to the previous quarter of 1.6% – the highest quarterly increase in the past two years. However, the pace of slowdown is not as strong as expected, implying persistently strong quarter-to-quarter momentum. The sequential performance is attributed to a shift in the contribution of private consumption to positive territory, further strengthening in investments, and a positive contribution from net exports, while stock depletion partially reduced the growth.

Real GDP (%YoY) and contributions (ppt)



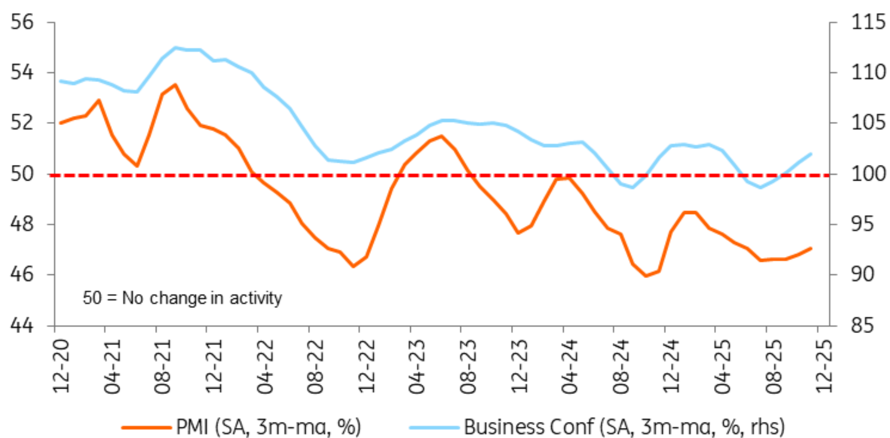
Source: TurkStat, ING

PMI at the highest since February

The manufacturing sector (seasonally adjusted basis) PMI, which has been below the 50 threshold since the first quarter of 2024, experienced a recovery to 48 in November, the highest reading since February, from 46.5 in October. While the figure is still in contractionary territory, it signals an easing of business conditions. The October-November average of 47.25 indicates a slight increase from 46.6 in the third quarter, supporting this view. In the breakdown, the data shows less pronounced moderations across key variables such as output, new orders and employment, in addition to a modest rise in output prices.

Findings in the sectoral PMIs, on the other hand, released by the Istanbul Chamber of Industry, are in line with what the manufacturing PMI data suggests in November, as all seven out of 10 sectors recorded an increase in their PMIs, while three of them exceeded the 50 level.

PMI & Business Confidence



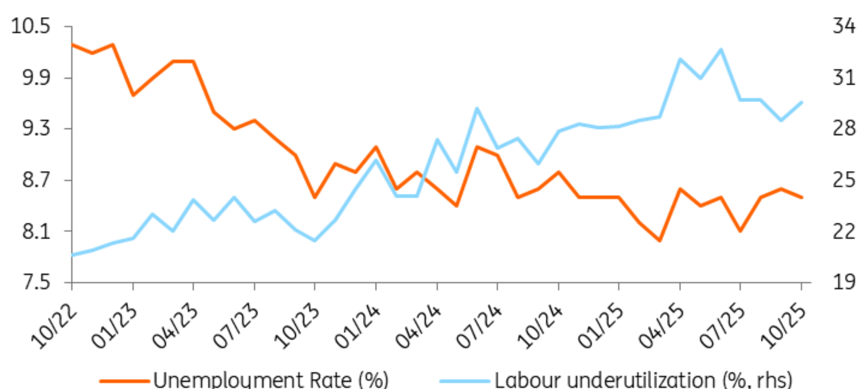
Source: ICI, CBT, ING

Unemployment rate drops to 8.5% in October

The unemployment rate declined by 0.1ppt in October, settling at 8.5%, while the number of employed persons increased by 185K compared to the previous month, pushing the employment rate up to 49.2%. Additionally, the labour force grew by 157K, bringing the labour force participation rate to 53.8%. Among broadly defined unemployment indicators, the underutilisation rate – which combines time-related underemployment, potential labour force, and the unemployed – rose by 1.1 ppt month-on-month to 29.6%. This indicator, which has shown a volatile trend recently and reached a historic peak of 32.7% in June, has remained above 28% since the beginning of this year.

In summary, the Household Labour Force Survey revealed that the headline unemployment rate declined in October due to employment growth outpacing the increase in labour force participation. However, broadly defined unemployment indicators presented a more negative outlook compared to the previous month.

Labour market outlook



Source: TurkStat, ING

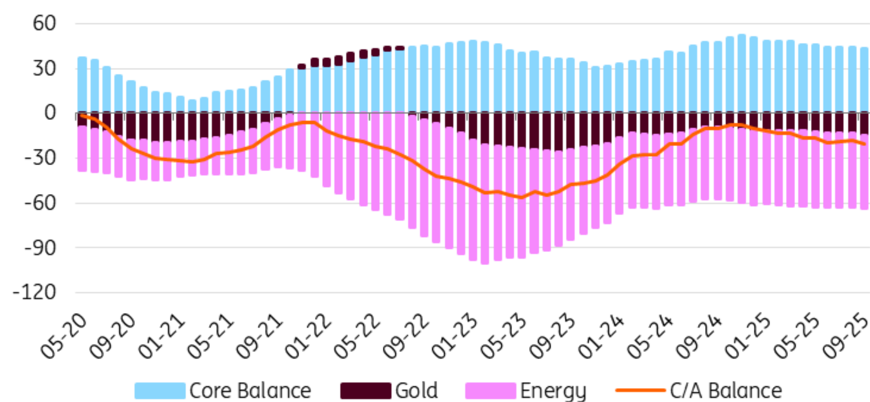
September current account in surplus

The September current account posted a surplus of US$1.1bn, broadly in line with the market forecast. A closer look at the monthly figures shows that the surplus narrowed compared to the same month last year, primarily due to a higher trade gap, which deteriorated from $-3.1bn to $-5.4 bn. This deterioration was mostly driven by a lower core trade surplus and a worsening balance in net gold trade.

However, a further increase in the services income, driven by growing transportation and tourism revenue, limited the decline in the current account surplus. As a result, the 12-month rolling current account deficit, which began rising in November of the previous year, maintained the uptrend and reached $20.1bn, or approximately 1.5% of GDP, from $18.4bn a month ago.

On the capital account side, we saw outflows following the political news flow in September at $6.0bn. With net outflows from errors and omissions of $3.8bn, and considering the current account surplus, official reserves contracted by $8.7bn.

Current account (12M rolling, US$bn)



Source: CBT, TurkStat, ING

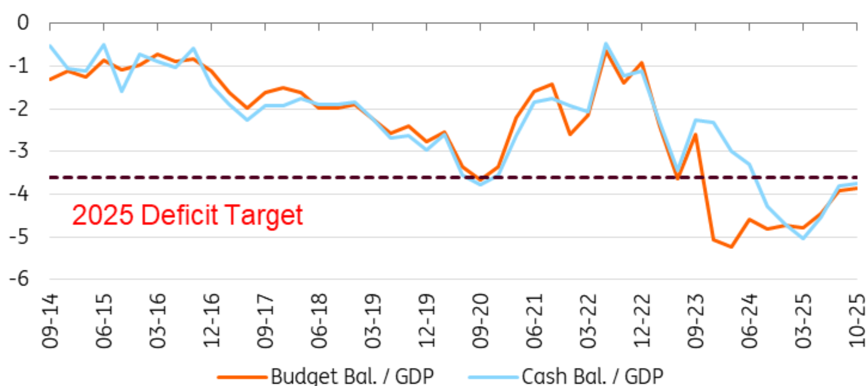
Budget deficit expanded in October

In October, the total budget deficit reached TRY223.2 bn, surpassing the TRY186.3 bn recorded in the same month last year. Tax revenues accelerated with an annual increase of 51.6%, driven primarily by a sharp 90% rise in income tax collections. Meanwhile, corporate tax revenues continued to contract on a yearly basis.

Among indirect taxes, the annual growth in VAT and SCT collections also showed signs of slowing. On the expenditure side, non-interest spending was pushed higher by faster growth in goods and services procurement (59% YoY) and current transfers (48.4% YoY). Accordingly, excluding interest payments, expenditures rose by 48.0% YoY.

As a result of these developments, the ratio of the budget deficit over the past 12 months to GDP climbed to 3.9%, while the primary balance posted a deficit of 0.4%. Additionally, excluding one-off revenues, the 12-month budget deficit stood at 4.5% of GDP.

Budget performance



Source: Ministry of Treasury and Finance, ING

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