# Turkey's central bank remains on hold

At the December MPC meeting, the CBT kept the policy rate flat at 24%, while pointing out the upside risks to the inflation outlook

Source: Flickr

24% 1-week repo rate

(Unchanged)

As expected

## Turkey on hold

At the December rate-setting meeting, the central bank of Turkey kept the policy rate (1-week repo rate) unchanged at 24%, in line with the Bloomberg median consensus and our call, despite the short-term favourable trend in inflation, the sharp lira recovery since September and the significant momentum loss in the economic activity given the financial shock in the summer months and consequent tightening of financial conditions that have weighed on domestic demand.

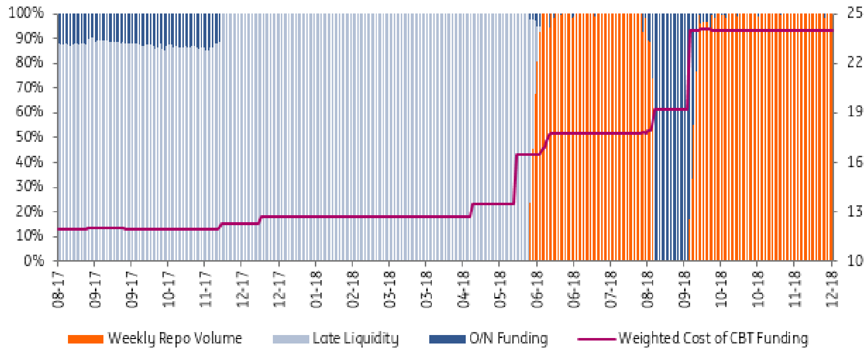
USD/TRY has remained in a wide 5.30-5.40 range before and after the CBT decision.

## Currency still fragile

The recent recovery of the currency has caused an optimism on the inflation front, while market pricing based on the short-end of the lira swap curve shows a significant downward adjustment priced in over the current effective funding.

However, the still-fragile lira, as observed in recent days with rapid a move to close to 5.40 against USD from slightly above 5.10, likely attributable to some recovery in oil prices, concerns about change in the CBT's tight stance ahead of the December MPC meeting and end of the temporary cut in withholding tax collected from TRY deposits should be a signal for policy makers to be cautious on a premature easing.

## Funding Comp. & Cost of Funding (5d-MA, %)




Source: CBT, ING Bank

Accordingly, the CBT maintained the main policy guidance that while highlighting the determination to tighten further, if needed, it would continue to monitor lagged impact of monetary policy decisions, the contribution of fiscal policy to rebalancing process in addition to inflation expectations, pricing behaviour and other factors affecting inflation.

However, we see a slight change in its communication that "the committee has decided to maintain the tight monetary policy stance until inflation outlook displays a significant improvement" in the latest statement vs "tight stance in monetary policy will be maintained decisively until inflation outlook displays a significant improvement" in October.

The CBT has also remained vocal about inflation risks by reiterating that "risks on price stability continue to prevail price increases" despite "developments in import prices and domestic demand conditions have led to some improvement in the inflation outlook".

In fact, with the lowest monthly figure since the inception of the current inflation series in 2003 at -1.44% in November, yearly inflation posted its sharpest monthly decline in more than ten years. The impact was clear on goods' inflation as it plunged markedly with significant contributions from energy, unprocessed food and core goods. However, sticky services inflation remained broadly unchanged despite price drops in transportation services.

It should be noted that we'll likely see some further inflationary pressures in early 2019 before falling more rapidly in the second half given the impact of a reversal in temporary tax cuts and unfavourable base effects.

> The central bank remained on hold this month and maintained its tightening bias, with a promise to deliver further monetary tightening, if needed, on the back of continuing challenges on the inflation front, risk of the lira coming under pressure again and currently fragile capital flows, as evidenced by the latest balance of payments data.

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