

Turkey maintains easing as geopolitical risks recede

The Central Bank of Turkey cuts its policy rate by a more than expected 250 basis points to 14%. The move comes as geopolitical tensions ease and stronger than expected disinflation in the country



Central Bank of Turkey Governor, Murat Uysal

-250bp

Higher than expected

CBT policy rate change

To 14.0%

The Central Bank of Turkey (CBT) has eased by more than expected at its October rate-setting meeting, cutting its policy rate (1-week repo rate) by 250bp to 14.0% vs the market consensus (and our call) of 100bp, while forward implied yields were pricing around 250-300bp. Given the CBT's objective of "a reasonable rate of real return", the ex-post real policy rate dropped to 470bp vs the average ex-post policy rate for major EM peers close to 300bp, while the ex-ante policy rate stands slightly higher than 280bp after the decision.

As far as the inflation outlook goes, the CBT sees year-end inflation to be "notably" below (revised from "slightly" in last month's statement) the July Inflation Report (at 13.9% vs 12% in the new economic programme). It cited the large base effects as the driver of September's significant fall along with domestic demand conditions and the level of monetary tightness.

So, given the bank's increasing confidence about ongoing disinflation, it utilised the room for policy manoeuvre and over-delivered again while maintaining its previous guidance that "the current monetary policy stance, to a large part, is considered to be consistent with the projected disinflation path"; that signals a more cautious policy stance. We think inflation will probably remain in single digits in October and reverse thereafter because of unsupportive base effects, closing the year at 12.8%. In our view, the case for further monetary easing in the last MPC meeting in December has significantly weakened after today's decision, while any move should take a more gradual pace.

Regarding economic activity, the CBT sees:

1. further improvement in economic activity spreading into more sectors
2. still weak investment demand
3. a moderate pace of growth in industrial production
4. further support of improved competitiveness in goods and services' exports, despite a weakening in the global economic outlook.

This, coupled with the disinflation trend and an improvement in financial conditions, leads the CBT to believe that the gradual recovery is likely to continue.

Overall, the CBT reiterated its commitment to a sustained disinflation process that will help reduce sovereign risk, lower long-term interest rates and support a stronger economic recovery. Given the earlier signals, this commitment also includes a positive ex-post real policy rate of around 1-2% in the medium-to-long term. So, in the future, the CBT will likely be even more cautious at this level given still not well-anchored inflation expectations and high inertia, especially as far as services inflation is concerned, along with high dollarisation and the subdued capital flow outlook.

Author

Muhammet Mercan

Chief Economist, Turkey

muhammet.mercan@ingbank.com.tr

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING

does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.