

## Turkey's central bank does not rule out tightening

The CBT keeps inflation forecasts unchanged for this year and next, while not ruling out the possibility of additional tightening with further risks of inflation and downward pressures on the currency



Murat Cetinkaya,  
Governor of the Central  
Bank of Turkey

### Major areas to consider

There are three things to consider in the inflation report, released by the CBT Governor, Murat Cetinkaya:

- 1) New inflation forecasts and revisions in key assumptions
- 2) Further explanation on the changing MPC statement
- 3) Comments on reserves.

### The inflation report picture

According to the report, the CBT expects 14.6% CPI inflation this year, remaining flat in comparison to the January inflation report given that

1. higher food inflation assumption at 16% vs 13% previously (creating +0.7ppt impact)
2. changing assumptions for TL-denominated import prices (+0.3ppt impact on the headline forecast) were balanced out by
  - improvement in the underlying trend (with -0.3ppt impact)
  - revised assumptions for taxes and administered prices (impacted the 2019 inflation estimate by -0.6ppt) and
  - downward adjustment in output gap estimate as the bank expects it to remain negative territory beyond 2021, (pulling the headline forecast down by -0.1ppt).

For 2020, the CBT sees 8.2% inflation, unchanged in comparison to the January report as revised food inflation assumption was offset by improvements in the underlying trend. So, the CBT portrays the same inflation outlook as in the previous report, seeing the inflation to converge to the target in 2021.

## Looking to the future

In the meeting, the Governor clarified the CBT position following the unexpected revision in its policy guidance by dropping tightening bias in the April MPC meeting. This caused an interpretation that the move would lead to premature monetary easing. With the removal of the tightening bias the CBT sounds less hawkish in a backdrop of macro uncertainties and currency volatility with heightened risks of inflation.

However, Governor Cetinkaya has not ruled out the possibility of additional tightening with further risks of inflation and downward pressures on the currency. That is the major reason for the CBT leaving inflation forecasts unchanged in the April report, as implied by the governor. So, given still fragile currency, continued dependence on external financing and ongoing inflationary risks, the bank would likely remain tight for a long while.

## News on reserves

Regarding the reserves, the message from the Governor is that:

1. Fluctuations are not exceptional but an outcome of usage of several CBT flexibilities by banks in the system
2. Focus should be on general reserve trend rather than the short-term fluctuations
3. No meaningful deterioration in reserve adequacy indicators
4. Swap transactions are recognized in accordance with international accounting standards.

As an additional note, the CBT expects an approximately US\$14.1 billion contribution to the reserves in the remainder of 2019 from the export rediscount credits on top of the US\$5.04 billion impact in the first quarter.

## Policy stance clarification

Overall, the CBT Governor clarified the policy stance after the drop of a reference to its determination to deliver further monetary tightening and given continuing challenges on the inflation front, the risk of the TRY coming under pressure again and currently fragile capital flows, he did not rule out the possibility of additional tightening. The language that the bank would implement additional tightening to keep inflation in line with the targeted path, has provided a relief, as markets have been cautious over the possibility of earlier rate

cut(s) after the April MPC statement.

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