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TURKEY

Turkish central bank holds rates, remaining cautious

The Turkish central bank left the policy rate unchanged at 37%, indicating satisfaction with the current stance but remaining alert to inflationary risks

People withdrawing money from an ATM in Istanbul, Turkey, where the central bank has held interest rates steady 37%

At its April rate-setting meeting, the Central Bank of Turkey (CBT) maintained its policy rate (1-week repo rate) at 37%, and the interest rate corridor stable at 450 basis points with the upper and lower bands remaining at 40% and 35.5%, respectively. Ahead of the meeting, expectations were divided between two alternative moves: 1) no 1-week repo hike, continued funding at the upper band, or 2) keeping the effective funding rate unchanged at 40% but hiking the policy rate to 40% from 37% and resuming funding via 1-week repo auctions.

The decision is likely attributable to two drivers, in our view. First is the recovery in reserves since early April, with the ceasefire between US-Israel and Iran. According to our calculations, the central bank has accumulated around US$20bn in April so far, partially reversing around US$50bn FX sales seen in March. As a result, we estimate that gross reserves increased to $175bn as of 20 April, from $161.6bn on 3 April, while net reserves (excl. swaps) stood at $38.6bn from $18.3bn in the same period. Second, concerns about growth moderation as the bank acknowledged that recent indicators point to a slowdown in economic activity. The decision implies that the bank likely prefers to preserve policy optionality, allowing for earlier easing of effective rates depending on geopolitical developments.

In its statement, the CBT acknowledged the decline in underlying inflation in March and pointed out a slight increase this month, while emphasising ongoing risks to the outlook on the back of geopolitical developments and energy prices that remain high and volatile. Accordingly, the bank has remained cautious and “highly attentive to upside risks” given that the war has driven an upward shift in inflation expectations as the current backdrop increases the risk of second-round effects. According to the latest market participants' survey, the expectations for 2026 and 2027 increased significantly to 27.5% and 20.1%, respectively. Expectations for the next 12 and 24 months, on the other hand, deteriorated to 23.4% and 18.0%.

Regarding the forward guidance, by emphasising a cautious stance against upside risks to inflation in its main policy message, the CBT signalled that the current monetary policy stance will be maintained in the near term. It also reiterated a prudent meeting-by-meeting approach and keeping the door open to further tightening if needed. In addition, it kept the messages regarding the macroprudential framework and liquidity management unchanged, indicating that a cautious approach in these areas would be preserved.

Overall, the central bank's rate decision implies an intention to move toward normalisation as the CBT does not see a need to introduce additional tightening, as referenced in the statement, or to gain additional flexibility by adjusting the upper band of the interest rate corridor. In the near term, the CBT will remain in a wait-and-see mode before deciding whether to reduce the effective cost of funding back towards the policy rate.

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