

## Turkey: To cut or not to cut?

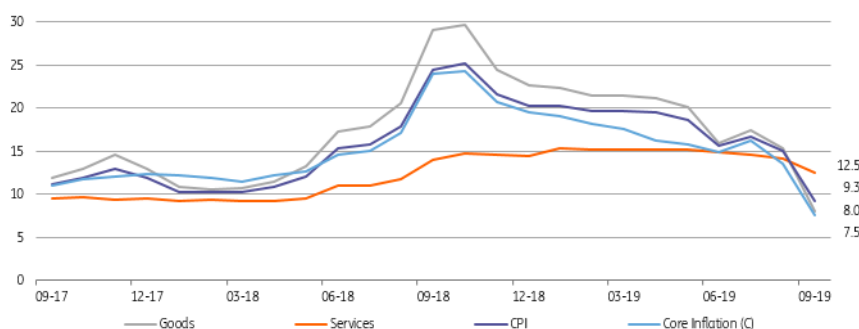
Given the easing geopolitical tensions and subsequent market rally, including that in the currency following an agreement between the US and Turkey on Northern Syria, the Turkish Central Bank will likely consider acting and cut the policy rate by 100bp to 15.5% in the rate-setting meeting on 24 October



The Turkish Central Bank in Ankara

Following large easing moves in 3Q with the increasingly more accommodative stance of global central banks and improving price pressures, the CBT had signalled a more cautious approach that would be conditional on the inflation path. Given the easing geopolitical tensions and subsequent market rally including an improvement in the currency, with an agreement between the US and Turkey on Northern Syria, the bank will likely consider cutting the policy rate by 100bp to 15.5% in the rate-setting meeting on Thursday, in our view.

## Inflation Trend (%)



Source: TurkStat, ING

In recent months, the surprisingly positive inflation releases pulled the annual figure to single-digit territory thanks to still weak domestic demand, moderating pass-through, easing cost-push factors and a favourable base along with further correction in unprocessed food prices despite some administrative price adjustments. Accordingly, the CBT felt more confident about the strength of the ongoing disinflation trend and came up with frontloaded moves in a deep easing cycle amounting to 750 bps in the last two MPC meeting; there was also the contribution of a supportive global backdrop. Regarding the latest interest rate announcement note in September, the CBT seemed confident about its moves as “the current monetary policy stance, to a large part, is considered to be consistent with the projected disinflation path”, also signalling more measured pace of easing in the remainder of 2019.

October witnessed significant volatility in local financial markets due to increasing geopolitical concerns. Accordingly, the swap curve in early October, pointing to a large, more than 300bp, easing until the year-end, shifted significantly towards pricing no move by the CBT in the remainder of this year given recent developments and the subsequent rise in the risk premium. However, the agreement between the US and Turkey last week has contributed to a significant drop in risk anticipation with a recovery in market sentiment and consequent strengthening in the exchange rate. This has supported market pricing, currently indicating around a 200bp rate cut in the last two MPC meetings of this year.

---

*The improving geopolitical backdrop should come as a relief to the CBT*

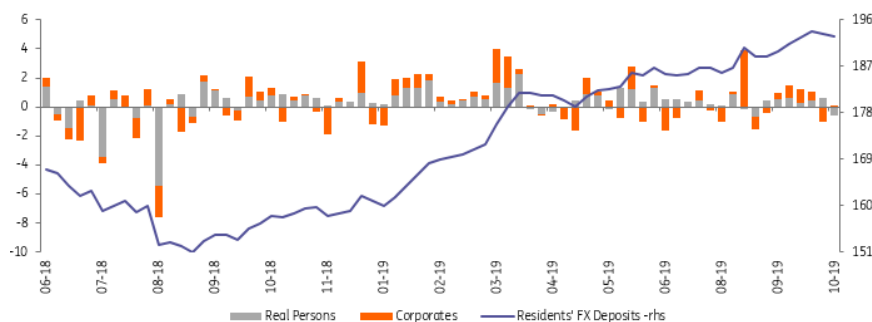
---

The improving geopolitical backdrop should come as a relief to the CBT and we expect it to continue the easing cycle with a 100bp cut this month. The inflation path should also provide room if we consider the official end-year projection at 12.0% showing the extent of the improvement in the outlook comparing the CBT’s 13.9% forecast in July inflation report. We think, it will likely remain in single digits in October and reverse thereafter because of unsupportive base effects, closing the year at 12.8%, though still supporting the case for further monetary easing in the October MPC.

It should also be noted that the risks are on the upside and the CBT may remain mute given:

1. still not well-anchored inflation expectations, high inertia especially in services inflation, and uncertainties surrounding the exchange rate path
2. economic policy uncertainty in the global environment with likely impact of trade tensions on growth prospects, despite the projected easing in global financial conditions
3. challenging macro backdrop with ongoing high dollarisation, subdued capital flow outlook, and close to all-time low consumer confidence levels.

## Residents' FX Deposits (US\$ billion)



Source: CBT, ING

Overall, we expect the CBT to maintain the easing bias on the back of still weak domestic demand and faster than expected disinflation and to come up with a slower easing pace in comparison to the previous moves. However, the recent acceleration in geopolitical newsflows and subsequent currency volatility weaken the case for further easing as the CBT may opt to be more cautious in an effort to strengthen credibility.

### Author

**Muhammet Mercan**

Chief Economist, Turkey

[muhammet.mercan@ingbank.com.tr](mailto: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 [www.ing.com](http://www.ing.com).