

Aggressive tightening from Turkey's central bank

The Turkish central bank made an aggressive 200bp adjustment to the policy rate on the back of deteriorating global risk appetite, an uptrend in commodity prices and a weakening lira, adding to elevated inflation risks



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200bp Policy rate change
(to 19%)

Higher than expected

The central bank of Turkey hiked the main policy rate by 200 basis points to 19% surpassing market consensus of 18%, as it reacts to increasing upside risks to the inflation outlook, which is already above the central bank's target and the backdrop of higher cost-push pressures and recent global economic developments that have weighed on the local currency,

The Bank acknowledged the recent shift in the global risk appetite, continuing strength of economic activity and rising pricing pressures, and cited those as the key developments that have contributed to “upside risks to inflation expectations, pricing behaviour and the medium-term inflation outlook” which required “a front-loaded and strong additional monetary tightening.”

- On the global front, the central bank mentioned rapid and across the board price increases in commodities on the back of growing inflation expectations with a loose monetary stance of global central banks coupled with large fiscal stimulus as one of the major developments and growing uncertainties about advanced-economy monetary policies along with volatility in global markets.
- For economic activity, the Bank saw a strong course and expected some pick up in certain sectors adversely impacted by the pandemic with the ease of pandemic restrictions. Signals of re-acceleration in lending momentum that lost pace in recent months with a more restrictive policy stance is another concern for the Bank regarding the domestic demand outlook.
- It also acknowledged rising pricing pressures that reflect strong cost-push factors, sticky services, inflation, and elevated inflation expectations. At the same time, upside risks continue given recovery expectations in pandemic-led weak demand conditions in certain groups with the normalisation process and the impact of rising international commodity prices.

The central bank hasn't changed the policy guidance, and:

- Maintained its tighter for longer stance
- Kept the door open for further hikes if required
- Reiterated the commitment to maintain “the level between the actual / expected inflation rate path and the monetary policy interest rate path”, suggesting a signal with a long-term perspective to keep real policy rate high enough to pursue a disinflationary balance.

The central bank made an aggressive adjustment to the policy rate on the back of deteriorating global risk appetite, the uptrend in commodity prices and a weakening lira, adding to the elevated inflation risk.

The Bank reiterated its pledge to maintain the tight stance longer justified by the need to accumulate FX reserves and restart the de-dollarization process.

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