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Snap

Turkey's central bank to announce additional measures in December

With its latest rate cut, the Central Bank of Turkey has now ended its easing cycle and has issued new policy guidance signalling further macro-prudential measures in December to support the effectiveness of the monetary transmission mechanism

The Central Bank of Turkey

In line with its latest forward guidance provided last month and President Erdogan's call for a single-digit policy rate, the Central Bank of Turkey cut its key rate by 150bp to 9% at the November MPC meeting. The CBT has cut rates by 500bp since August, bringing the rate into single digits for the first time since September 2020, at a time when headline inflation exceeds 85% and hence real interest rates were already deeply negative. The CBT cited growing downside risks to the growth outlook, and the latest cut is expected to be the last in this cycle.

The economy started to slow in the third quarter, mainly due to a weakening in external demand, and leading indicators for the fourth quarter suggest the slowdown in activity is likely to continue. In line with this backdrop, the CBT said that pressure on the manufacturing industry, and the "currently limited impact on domestic demand and supply capacity" from this pressure, has become more pronounced.

In this environment, the bank prioritises growth despite broad-based inflationary pressures (all 12 of the main CPI categories contributed positively to the increase in inflation in October). Given this backdrop, in the November rate-setting statement, the CBT reiterated the need for supportive financial conditions so as to preserve the growth momentum in industrial production and the positive trend in employment and added this month that this would be important “for the sustainability of structural gains in supply and investment capacity”.

So, despite high inflation and large external financing needs, the CBT seems to be determined to pursue accommodative measures, though it has also implemented a number of measures, including a selective credit policy and “liraisation” strategy, in an environment of deeply negative real rates. Given this backdrop, in the latest note released with the interest rate decision, the CBT came up with further policy guidance which signalled more macro-prudential measures to support the effectiveness of the monetary transmission mechanism in the “2023 Monetary and Exchange Rate” document that will be released in December.

There are expectations of some easing in the current banking sector regulations along with targeted credit stimulus measures in the pipeline such as Credit Guarantee Fund (CGF) loans. The ongoing expansionary stance on the fiscal side has also become more pronounced lately. We expect the CBT to keep its policy rate unchanged at 9% ahead of the elections. The CBT’s macro-prudential framework may be strengthened further in December, which would be key for the macro and financial outlook in the near term.

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