

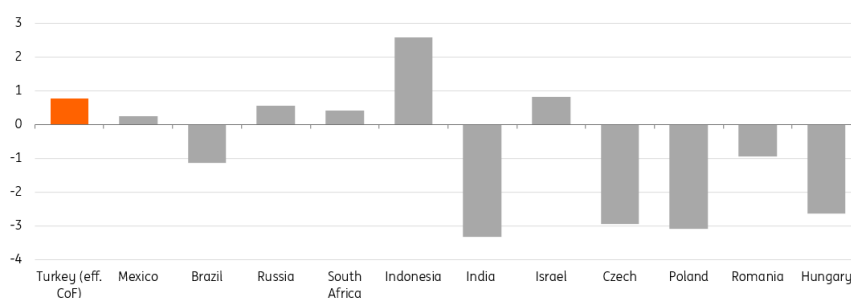
Turkey: Flat policy rate, but change in the rate corridor

In the October rate setting meeting, the central bank did not see the need to make an adjustment in the policy rate, however, it signalled that it will continue with liquidity management tools given ongoing financial and price stability concerns



Ex-post Real Policy Rate (%)

(Ex-post real effective cost of funding for Turkey)



Source: Thomson Reuters, ING

Contrary to rate hike expectations ranging from 100bp-to-300bp, the Central Bank of Turkey kept the policy rate (1-week repo rate) unchanged at 10.25%. However, the bank has lifted the late liquidity window (LLW) rate to 14.75% with a 150bp hike, widening the corridor so as to gain room to manoeuvre in the liquidity tightening process and signalled it will continue on this path in the near term.

In the current setup, the CBT has been using 1-month repo auctions (interest rate being determined by the liquidity conditions) along with the upper band of the rate corridor (remaining unchanged at 11.75%) and late liquidity window in providing liquidity to the banking system. The latest move will provide additional flexibility to the CBT. Given that the ex-post effective cost of funding is already positive at around 0.8% and broadly aligned with or above of real policy rates of other key EMs (with the exception of Indonesia above 2.5%), any additional tightening via changing the liquidity composition and pulling the effective cost of funding towards the LLW should add to already positive real rates.

The statement seems to be shortened compared with that of September. The CBT reiterated that inflation has remained elevated on the back of rapidly improving economic activity with large credit stimulus and exchange rate developments. This backdrop has required reorientation of monetary policy and liquidity management since early August, leading to significant tightening in financial conditions. The bank still sees the need for a continuation of liquidity measures and makes an adjustment in the corridor structure “to enhance flexibility”.

There are also some other modifications in the MPC statement:

- i) the CBT acknowledges the continuation of the recovery in economic activity
- ii) for the credit stimulus, the bank now sees momentum loss not in corporate loans, but also in consumer loans. The normalisation trend has turned more evident lately in both categories thanks to the policy moves by the Banking Regulation and Supervision Agency and the CBT as evidenced by broadly unchanged FX adjusted lending volume since early September.
- iii) Regarding external balances, the CBT points out the rebalancing in imports and likely improvement in the current account deficit with a strong recovery in exports, supportive commodity prices and competitive currency.

Overall, in the October rate setting meeting, the CBT did not see a need to make an adjustment in the policy rate given signs of momentum loss in activity with a normalisation in credit and rebalancing signals in external balances. However, given continuing financial and price stability concerns, the bank signalled it will continue with liquidity management tools that should provide additional support to the TRY. Exchange rate developments are likely to remain as one of the key determinants of CBT policy in the period ahead given ongoing geopolitical issues and US elections-related sensitivities.

Author

Muhammet Mercan

Chief Economist, Turkey

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.