Turkey: No change in central bank's policy approach

The Central Bank of Turkey kept its policy rate flat at the May meeting and concluded that the current rate is adequate to support the recovery from February's earthquakes. It did not offer any signals about a policy change or provide renewed forward guidance

The Central Bank of Turkey in Istanbul

At the first rate-setting meeting after the 14 May elections, the Turkish central bank kept its policy rate on hold at 8.50% in line with the market consensus and maintained its forward guidance that the current policy rate is adequate to support the recovery from the earthquakes earlier this year. Accordingly, the market's reaction to the decision was muted, as USD/TRY has been flat.

After the elections, the CBT took a tightening step and expanded the scope of the security maintenance requirements based on loan growth to include other commercial loans and consumer loans. But, a few days later, this was reversed ahead of the election run-off, though liraisation regulations and news reports of increased controls over banks' daily FX transactions have remained in place. In this environment, whether the CBT came up with any signal for a policy change or renewed forward guidance was quite important and closely watched by the market.

However, the CBT's assessment this month was almost a carbon copy of the note shared after the

April meeting:

- The bank has kept its assessment on the global economy completely unchanged, once again mentioning recession concerns due to a number of factors including "conditions threatening financial stability". Given this backdrop, financial markets are also shifting their expectations related to the end of tightening cycles in the near term.
- Regarding the domestic economic outlook, the CBT seems to be more positive with a faster-than-expected recovery in the earthquake region.
- It also kept the forward guidance unchanged while pointing out that "the effects of the earthquake in the first half of 2023 will be closely monitored". The bank also restated the need to keep financial conditions supportive in response to the earthquakes and repeated its emphasis on alternative policy instruments and alignment of all policy instruments with "Liraisation" targets.

The consensus view points to the need for normalisation in the conduct of monetary policy given the narrowing room for muddling through with continued pressure on reserves, which have declined by US$22.1bn on year-to-date basis, standing at US$105.1bn as of 12 May. In this regard, whether the new administration after the second round of the presidential elections is to change/revise the new economy model will be a key issue for watchers of the Turkish economy.

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