Turkey: No surprise from the CBT

The Central Bank of Turkey kept its policy rate unchanged as expected but remains concerned about medium term inflation, keeping the door open for more hikes, if needed

The Turkish Central Bank in Ankara

Despite prevailing inflationary forces and continued strength of economic activity, the CBT kept its policy rate unchanged at 17%, in line with the consensus, preferring to maintain a 'wait-and-see' stance, albeit with a hawkish tone. The decision can also be attributed to ongoing strength in the Turkish lira and an improvement in the risk premium.

Regarding the policy guidance, the February statement was updated with the bank's recent commitment in the January inflation report to maintain "the level between the actual / expected inflation rate path and the monetary policy interest rate path" until reaching the 5% inflation target (projected to be reached in 2023 according to its latest forecasts). This tighter for longer stance, with a signal to keep the real policy rate high enough to pursue "a strong, continuously sustained disinflationary balance" is encouraging as it shows the CBT's long-term perspective with reference to the inflation target.

The remaining part of the rate setting statement was a carbon copy of the previous one issued in January. Accordingly:

- The CBT remains vocal about the need to keep a tight stance for a longer period, given the risk of inflation expectations and pricing behaviour diverging from the medium-term target path and the bank has kept the door open for additional front-loaded tightening, if needed.

- On the inflation side, the CBT expects the impact of restrictive policy moves on credit and domestic demand to be more pronounced in the period ahead, ultimately leading to the start of disinflation. However, the bank is still concerned about the medium term outlook, given the increase in wages, supply constraints and the uptrend in commodity prices, leaving it cautious on the outlook.
- The bank sees that "economic activity is on a strong course". While the January manufacturing and sectoral PMIs point to a strong performance in 1Q of this year, construction and services related indicators i.e. turnover, signal some moderation lately, though they remain at relatively high levels, supporting the CBT's view.

All in all, the CBT has remained decisive on keeping a tight stance for longer, while also leaving an open door for more hikes. So the bank will continue to be cautious in the near term given not only inflationary pressures, but also concern about the level and composition of reserves, high dollarisation and the need to maintain capital flows and be ready to deliver, especially in case of further upside inflation surprises.

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