

## Turkey: Tighter for (even) longer...

The Central Bank of Turkey kept its 2021 inflation forecast unchanged despite growing pricing pressures and signalled a commitment to reduce inflation with further tightening if needed. The bank also strengthened its forward guidance and suggested it would keep policy tighter for longer



The Turkish Central Bank in Ankara

CBT Governor Naci Ağbal introduced the first inflation report of the year and provided detailed comments about the latest developments and their impact on the current monetary policy stance, with clear forward guidance.

The CBT kept its 2021 and 2022 inflation projections unchanged at 9.4% and 7.0%, respectively, with the Bank expecting a convergence to its 5% inflation target in 2023. The Bank cited the following variables as major determinants in its forecast trajectory for this year:

- Food inflation (+0.2ppt), due to an upward revision in the annual figure to 11.5% from 10.5%, with ongoing pressure in global food prices and the impact from an expected improvement in the tourism sector.
- An increase in real unit labor costs (+1.0ppt).
- TL-denominated import prices (-0.4ppt), likely due to a different exchange rate path projection despite a hike in oil price forecasts to US\$54.4 per barrel from US\$43.8 per barrel.

- Falling inflation expectations in the CBT's policy framework (-0.5ppt). For the next year, the bank sees support from a tight monetary stance and an improvement in expectations.

In December, annual inflation was again higher than expected, reaching 14.6%, due to food and transportation prices. This was a reflection of continuing cost-push factors, still strong domestic demand and elevated services inflation being highly sticky at current levels.

The outlook has also deteriorated due to a recent significant hike in the minimum wage, by 21%, as well as a rise in oil and commodity prices and the continuing uptrend in food inflation. Given that the CBT's forecasts in the inflation report are actually targets now, and the CBT has not made a change to the 2021 inflation forecast despite growing pricing pressures, it remains committed to its previous target/forecast for this year.

In this regard, the bank has again been vocal on keeping a tight policy stance for a longer period and kept the door open for more hikes if needed. Accordingly, the governor reiterated a continuation of policy tightness "for an extended period" until "strong indicators point to price stability."

The CBT also committed this time to maintain "the level between the actual / expected inflation rate path and the monetary policy interest rate path" until reaching the 5% inflation target, which is projected to be reached in 2023, according to its latest forecasts. This implies that it will continue to keep the real policy rate high enough to pursue "a strong disinflationary balance" and "this balance will be sustained continuously". So, even if we see some downward adjustment in the policy rate depending on an improvement in the inflation outlook, the CBT will allow a higher interest rate level to continue in order to maintain disinflation. This should also be helpful for the reserve accumulation objective by contributing to capital flows and de-dollarisation over time.

The CBT's new target forecast is unchanged compared to its previous report despite growing pricing pressures. It's shown a commitment to reduce inflation by continuing its prudent policy stance, and the bank has provided a clear commitment to remain cautious in the conduct of monetary policy to sustain the disinflationary balance in the medium term.

## Author

### Muhammet Mercan

Chief Economist, Turkey

[muhammet.mercan@ingbank.com.tr](mailto: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 <http://www.ing.com>.