

Turkey's central bank opts to continue on at the same pace

At its October MPC meeting, the Central Bank of Turkey (CBT) raised the one-week repo rate from 30.0% to 35.0%, in line with both the consensus forecast and our own expectations



The building of Turkey's central bank in Ankara

By opting for another 500bp hike at its October rate-setting meeting, the Central Bank of Turkey (CBT) has pulled the policy rate to 35% and repeated its signal for further tightening steps in rates and macro-prudential instruments to achieve disinflation. According to the bank, the persistence of upward pressures and risks on the inflation outlook and the alignment of the disinflation course with the forecast path in 2024 were the major driving factors.

In a note explaining the rate decision, the bank reiterated that it will continue with monetary tightening steps in a "timely and gradual manner" until it achieves a significant improvement in the inflation outlook. In this regard, the CBT acknowledged that the pass-through from the post-election adjustment in FX, wages and taxes has been "largely completed". It pointed again to strong domestic demand, stickiness in services prices and a jump in inflation expectations as the key factors putting upward pressure on the inflation outlook, while also mentioning the upside risk to oil prices due to geopolitical developments.

The MPC statement once again noted a determination to set the monetary policy stance in a way

that achieves the projected disinflation path for 2024, which was set at 33% in the July inflation report (the next report will be released on 2 November) and the Medium-Term Plan. This stance is in line with Treasury and Finance Minister Mehmet Simsek's recent communication stating an aim to i) steer inflation expectations towards target levels and ii) move towards a positive ex-ante real policy rate. This is the case with the latest move, based on the CBT's forecast.

However, survey-based inflation expectations currently stand at 45.2% for the next 12 months, implying a higher trajectory in comparison to the central bank's target disinflation path. While the CBT expects underlying inflation trend "on course to decline", it also pledges that the policy rate will be determined in a way that will create the monetary and financial conditions necessary for ensuring a decline in the underlying trend of inflation. This guidance and current expectations both signal that the Turkish central bank's rate hike cycle is coming to the end, with the pace set decline in the months ahead.

The CBT stresses again the importance of FDI inflows, recovery in FX reserves, "stable" (changed from "improving" last month) external financing conditions, an improvement in the current account, as well as higher demand for TRY assets to contribute to price stability. Regarding domestic demand conditions, the CBT points to "rebalancing" this month, attributable to tightening financial conditions with a supportive impact on the inflation outlook.

Finally, to support the monetary policy stance, it pledged the continuation of quantitative and selective credit tightening moving at a gradual pace. Given the return of excess liquidity in the banking system prior to this decision, we should not rule out the possibility that the CBT may come up with a new quantitative tightening decision. Given the need for rebalancing to control inflation and reduce external imbalances, the central bank's move and its impact on deposit and loan rates will be key for tightening financial conditions and controlling domestic demand. Deposit rates (in up to three months and up to six months tenors) that moderated recently according to the latest data will be under close watch in order to prevent an early easing in financial conditions.

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.