Turkey cuts rates again, but pace slows

The Central Bank of Turkey has cut its policy rate by 75bp to 11.25%, extending the easing cycle. The move is more measured this time, despite higher headline and core inflation at the end of 2019 pushing the ex-post real policy rate markedly down

Central Bank of Turkey governor, Murat Uysal

-75bp

CBT policy rate change

to 11.25%

The decision

In its first rate-setting meeting of the year, the Central Bank of Turkey (CBT) maintained the easing cycle at a slower pace and reduced the policy rate (1-week repo rate) by 75bp to 11.25%. Calls were split between no change and a 100bp reduction given the supportive global backdrop, continuing currency stability and still sub-par economic activity. We were expecting no move this month as the decline in the (ex-post) real policy rate with large rate cuts and a recent rise in inflation could risk TRY stability.

Key guidance

In its statement, the CBT kept key guidance sentences broadly unchanged, given that

1. it still sees after the move that "the current monetary policy stance remains consistent with the projected disinflation path", and
2. it will continue to determine monetary policy by considering "the indicators of the underlying inflation trend to ensure the continuation of the disinflation process".

Accordingly, the bank vows to maintain a cautious monetary stance. Despite the slower pace of easing compared with the deep cuts in the second half of 2019, no meaningful change in the statement and policy guidance over the last month indicates a lack of a clear signal for the near-term policy plan. This can also be an indicator that depending on the performance of the TRY, further (measured) easing cannot be ruled out.

Details of the statement

Regarding the inflation outlook, the CBT sees:

1. continuing improvement in the inflation outlook and sustained "widespread" decline in inflation expectations
2. a mild trend in core inflation driven by exchange rate developments, demand conditions and producer prices
3. the inflation path broadly in line with the year-end projection

There are risk factors for the CBT in reaching its year-end estimate, not least a likely reversion in unprocessed food inflation towards the long term average; benign food inflation significantly contributed to the disinflation process last year. It's also worth considering the inertia in services inflation along with still elevated forward-looking expectations despite some improvement in recent months.

As for economic activity, the CBT's assessment on growth remains unchanged, citing:

1. the contribution of net exports to growth to decline
2. growth to be supported by the ongoing disinflation and the easing in financial conditions
3. the improvement in the sectoral diffusion of the recovery and continuation of the weakness in investments.

Overall, given its ongoing growth priority along with a supportive global backdrop for EM risk and stability in the currency, the CBT extended its easing cycle further, though with a more measured move this time despite higher headline and core inflation at the end of 2019 pushing the ex-post real policy rate to negative. The bank will likely remain cautious in the near term on the back of likely stickier inflation readings with a less supportive base and a low real rate buffer. It wishes to maintain its easing bias and deliver if it should there be room to manoeuvre.

Author

Muhammet Mercan
Chief Economist, Turkey
muhammet.mercan@ingbank.com.tr