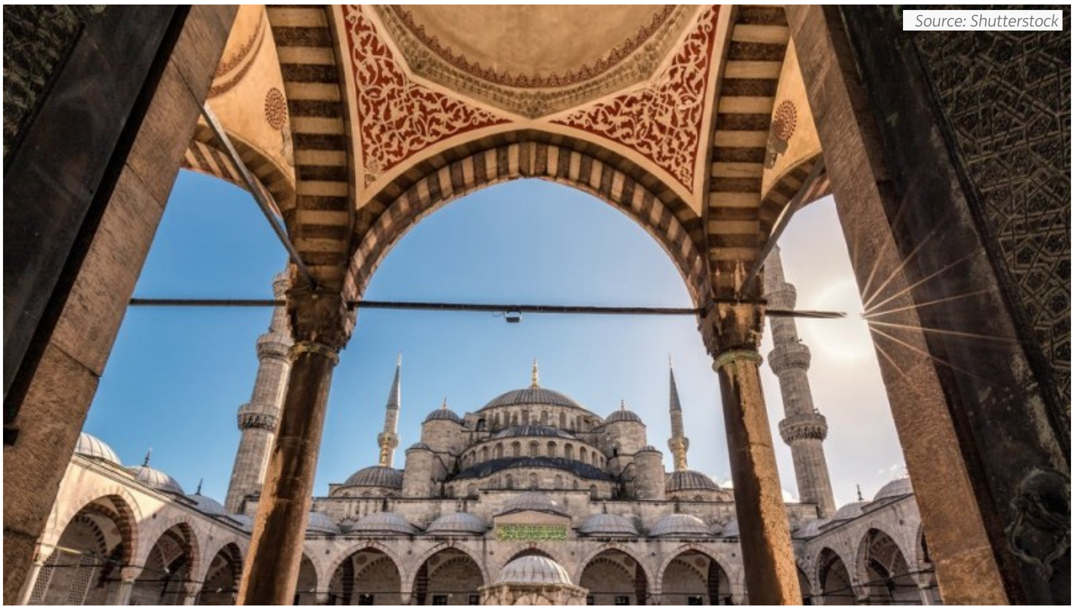
21 May 2020
Snap

Turkey cuts rates again!

Turkey's central bank has cut rates by 50bp taking the policy rate to 8.25% but it hasn't signalled that this is the end of the rate-cutting cycle

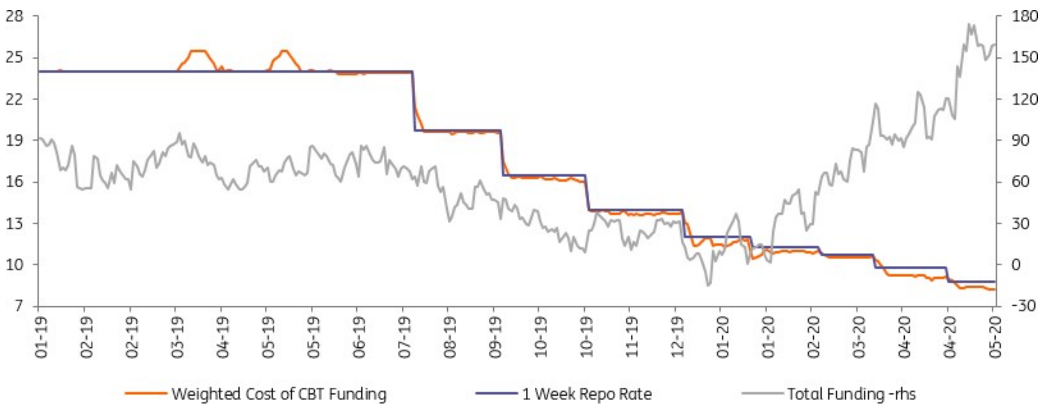

Source: Shutterstock

The central bank of Turkey cut policy rates again today by 50 basis points taking the policy rate to 8.25% from 8.75%. This was in line with market consensus versus our call of 8%.

The decision is likely attributable to the ongoing stance of providing additional support on the fiscal and credit side and negative output gap weighing on inflation, while the shift in global policies has also been encouraging. Before the decision, the effective cost of funding for the banking sector was at 8.24%, already significantly below the policy rate on the back of newly introduced channels, allowing the central bank to fund banks at relatively lower rates.

The decision will probably take the cost of funding further down to below 8%.

Central bank funding (in % and TRYbn)



Source: CBT, ING

Inflation outlook

On the inflation outlook, the central bank reiterated the outlook portrayed in the latest inflation report released a few weeks ago.

Accordingly, following the temporary elevated course in the near term because of “seasonal and pandemic-related effects on food prices”, the bank sees “demand-driven” disinflation trend to be more evident in the second half of the year, reaching 7.4% by the end of 2020. The central bank continues to focus on the ex-ante real rate to guide its policy decisions and relies on its year-end inflation forecast in real interest rate calculations and the current outlook “in line with the year-end inflation projection” likely supports the case for further monetary easing.

The central bank kept an entire paragraph including key guidance sentences unchanged. It reiterated that “a cautious monetary stance” is required so as to keep “the disinflation process in track with the targeted path” and that it would continue to determine monetary policy by considering “the indicators of the underlying inflation trend to ensure the continuation of the disinflation process”.

In the remainder of the statement, the CBT also shared views about:

1) *current global outlook:* emphasizing high uncertainties on global economic recovery this month along with a focus on normalization steps of other countries
2) *economic activity:* pointing to a more pronounced weakness in April, though bottoming out signals from the high-frequency indicators for early May
3) *external rebalancing:* reiterating expectation of a moderate course in the period ahead with lower imports driven plunge in oil prices and sluggish domestic demand despite the fall in goods and services exports.

After easing with more than expected cuts, the market was seeing a downside risk to the consensus. The rate cut was followed by slight appreciation by the lira.

With the decision, the central bank maintained the easing bias but it did not signal that this is the end.

We think, in the period ahead, currency developments that can risk price and financial stability will be closely monitored.

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