Economic Watch

Türkiye | The CBRT seems to be ready for easing

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The Central Bank (CBRT) kept the policy rate at 50% in line with the expectations, yet with important changes in their communication, signaling an easing cycle potentially as early as December MPC meeting. First, their assessment on the inflation outlook turned out to be more positive. Second, they stressed the fiscal policy for the first time with an increased coordination, most likely as a reference on the minimum wage hike and public administrative price hikes in line with the interim inflation targets. Last but not the least, their new communication on the future level of the policy rate to be determined in a way to ensure the tightness required by the projected disinflation path, taking into account both realized and expected inflation, seems to be a preparation for a forward guidance on a rule based approach. Overall, high likelihood of monthly inflation realizations below 2% in November and December and the potential commitment that the CBRT has received on price adjustments at the start of the year seem to help the CBRT be ready for an easing cycle as of December. Nevertheless, as we also highlighted in our baseline, the CBRT will be required to start easing with very cautious steps. This is why after the upward inflation surprise in October we had kept our first rate cut expectation as December but reduced the pace of cut as 100bps, lower than the current market pricing of 200bps.

On inflation outlook, the CBRT now evaluates domestic demand conditions at disinflationary levels rather than signaling a convergence, most likely referring to the most recent output gap getting closer to negative levels. It seems the CBRT is now more comfortable on the signs for an improvement in services inflation with their assessment on core goods inflation continuing to be low. Furthermore, they refer to inflation expectations and pricing behavior tending to improve, this time stressing the declining trend in addition to their previous assessment as being risk factors on the disinflation process. Finally, the underlying trend of inflation declined in October and they signal that November inflation could also be similar with unprocessed food inflation remaining elevated due to temporary supply conditions.

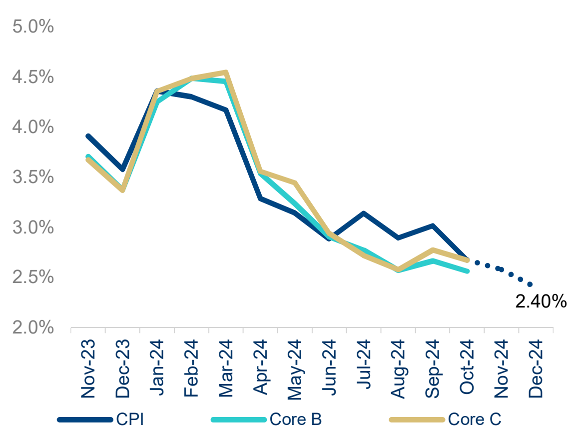
Secondly, the CBRT stresses an increased coordination with the fiscal policy, which will contribute significantly to the disinflation process. After the President Erdogan’s comments yesterday, a minimum wage hike in a range of 25-30% in line with the CBRT projections might be more likely. Also, the Minister of Finance Simsek had mentioned the will to adjust the public prices according to the expected inflation next year. Therefore, the CBRT might have been given the commitment on price adjustments at the start of the year, which will help contain the uptick in the monthly inflation trend in the first quarter of the year and provide room for the CBRT to start easing steps. Other than these factors, we still need to monitor how the non-primary fiscal cash spending will evolve in the next months, particularly in 2025.

The CBRT also adds a new communication on the future level of the policy rate to be determined in a way to ensure the required tightness by the projected disinflation path, taking into account both realized and expected inflation, which we perceive as a preparation for a forward guidance on a rule based approach. Yet, inflation expectations are divergent and we suspect the CBRT pays particular attention on the companies’ inflation expectations as being price setters. In this respect, 2024 and 2025 year-end inflation expectations of professional forecasters were revised slightly upward to 44.8% and 26.2% in November (vs. 44.1% and 25.6%, previously); and therefore 2025 year-end expectation still stayed above the most recently revised upper bound of the CBRT targeted inflation range (26%). Besides, 12-month ahead inflation expectations of corporates and households, stood at 49.5% and 67.2%, respectively, with only limited improvement so far.

On liquidity, the CBRT again repeated their commitment to effectively implement sterilization tools. We expect the CBRT to carefully monitor the TL deposit rates and maintain certain deposit rules accordingly. Because of the non-manageable excess TL liquidity since September, O/N TL repo rate hovers around 49%. In this regard, the first rate cut of the CBRT could be a technical adjustment, which will bring the CBRT funding rate closer to the current ON TL repo rate.

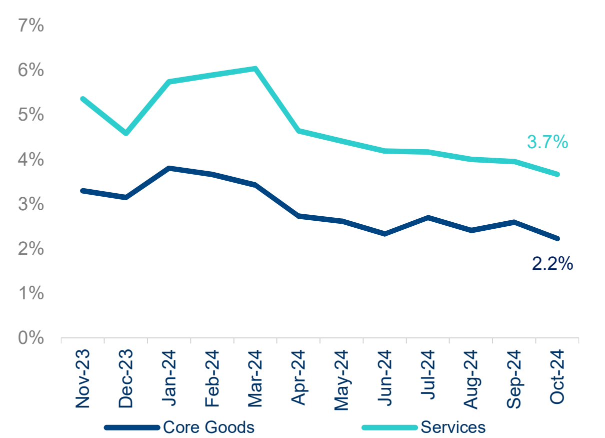
Overall, lagged effects of the monetary tightening have started to be seen with output gap narrowing more clearly as of 3Q24. Accordingly, the CBRT seems to get ready for an easing cycle with comfort from an increasing coordination with the fiscal policy. As we highlighted in our baseline, the CBRT will be required to start easing with cautious steps since domestic demand has slowed down only limitedly so far compared to much weaker aggregate supply and financial conditions albeit tight have started to weaken since summer, keeping inflation expectations high.

Chart 1. **CBRT Underlying Monthly Inflation Trend** (sa, m/m, 3m average)



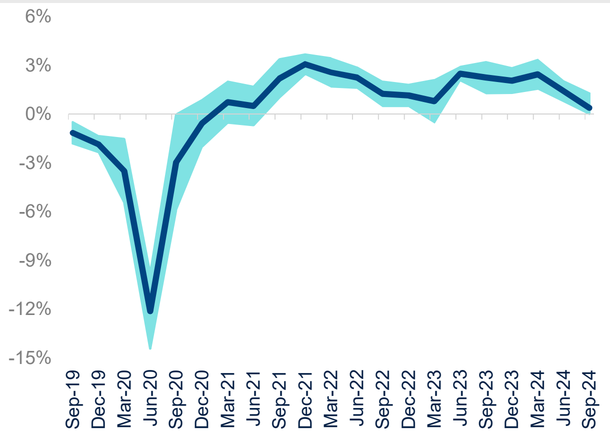
Source: CBRT, TURKSTAT

Chart 2. **CBRT Underlying Monthly Inflation Trend** (sa, m/m, 3m average)



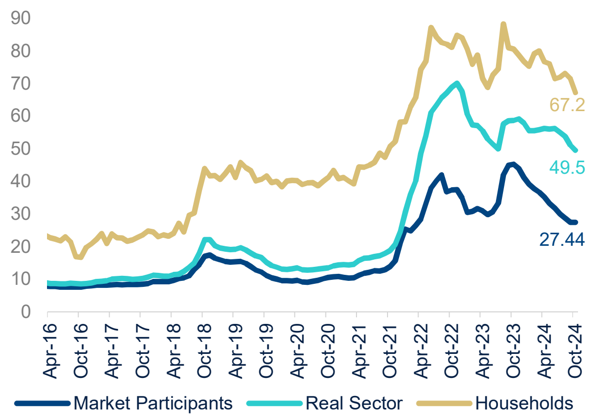
Source: CBRT, TURKSTAT

Chart 3. **Garanti BBVA Output Gap Estimate** (%, deviation from potential GDP)



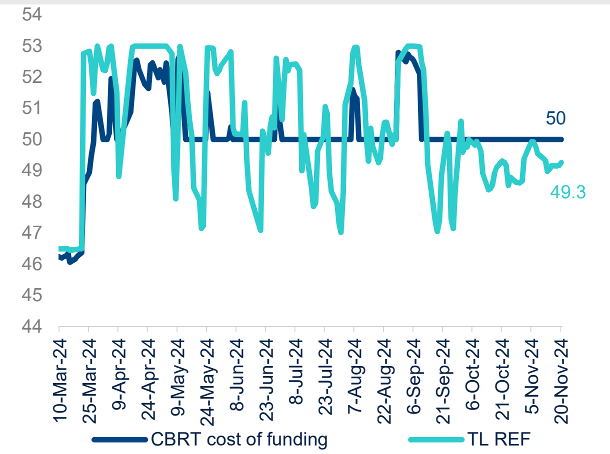
Source: TURKSTAT, CBRT and Garanti BBVA Research

Chart 4. **Sectorial Inflation Expectations** (one year-ahead, %)



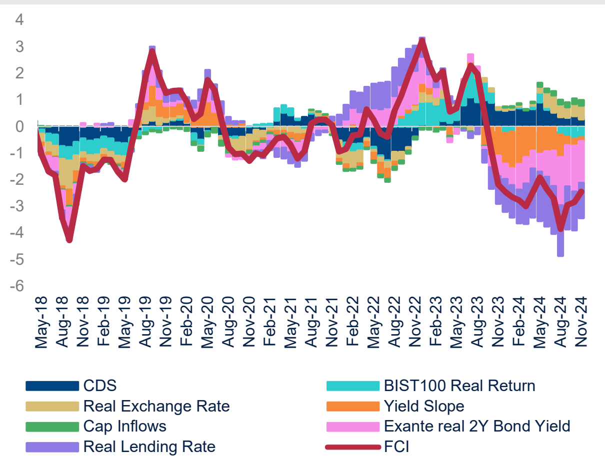
Source: CBRT and Garanti BBVA Research

Chart 5. **CBRT Funding & O/N BIST TL REF Rate** (%)



Source: CBRT and Garanti BBVA Research

Chart 6. **Garanti BBVA Financial Conditions Index** (standardized, + easing, - tightening)



Source: CBRT, Bloomberg and Garanti BBVA Research

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