

Economic Watch

Turkey: The CBRT delivered 200 bps rate cut

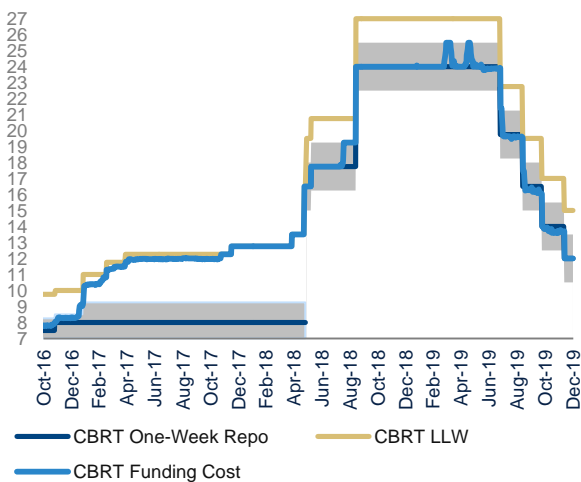
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The Central Bank of Turkey (CBRT) decreased the policy rate by 200 bps to 12% from 14%, slightly higher than market expectation of 150 bps. The market reaction was calm on the back of the global central banks dovishness and better inflation realization. The CBRT has confirmed its decision as stating that “...inflation is likely to materialize close to the lower bound of the October Inflation Report projections for the end of the year (11.2%), with risks around the disinflation path for 2020 being balanced”. Also, CBRT acknowledged that inflation expectations exhibited broad based improvement. Today’s action led real rate (actual rate minus expected inflation in a quarter ahead) close to zero, below the emerging market real average rate. We think that the CBRT has arrived the end of easing cycle at least for the first half of 2020 unless inflation continue to reduce in the short term. So far, the Global Central Banks Dovishness remain supportive but we think that complacency should be ruled out and the CBRT should be ready to act in any direction if the situation change.

Better disinflation path led another rate cut...

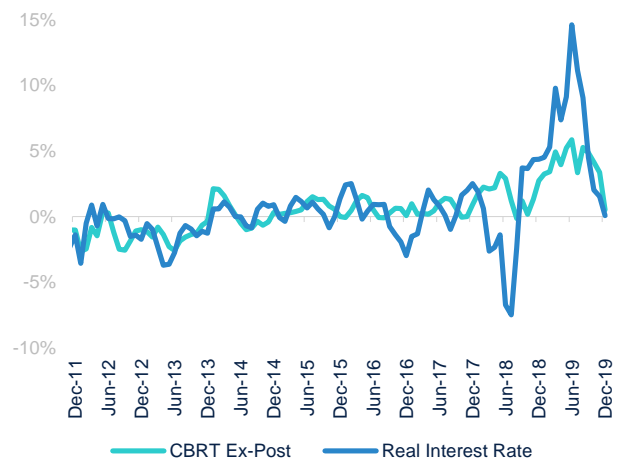
Annual inflation picked up to 10.6% in November on unfavorable base effect but could end the year around 11.5% , lower than the CBRT forecast of 12%. The Disinflation path have been supported by the normalization in food prices, the ease in core inflation on still negative output gap, stabilized currency and the weak cost-push factors. The 200 bps rate cut has based on the improvement in inflation expectations and the balanced risks on disinflation path in 2020. However, the inflation expectations in medium term are unanchored as one year and two year ahead inflation expectations remain in double digits. Secondly, inflation inertia is still alive as services prices continued to increase around 12% yoy. Finally, we expect that annual inflation could stay between 11-12% in the first half of 2020. Hence, we think that the risk factors on inflation and uncertainties stemmed from global and geopolitical factors should require CBRT to keep policy rate around this level in the short term.

Chart 1. **CBRT Official interest rates (%)**



Source: BBVA Research Turkey, CBRT Statements

Chart 2. **Real Interest Rates, (%)**



Source: BBVA Research & CBRT

.....taking real rates to low levels

Favorable base effect, weak demand and normalization in food prices have supported disinflation path so far but expected acceleration in economic activity, high inflation expectations, global and geopolitical uncertainties could pose upside risks on inflation outlook. We think that the CBRT should remain cautious and monitor closely inflation trends before continuing the easing cycle.

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