Economic Watch

Turkey: No change in the CBRT monetary stance

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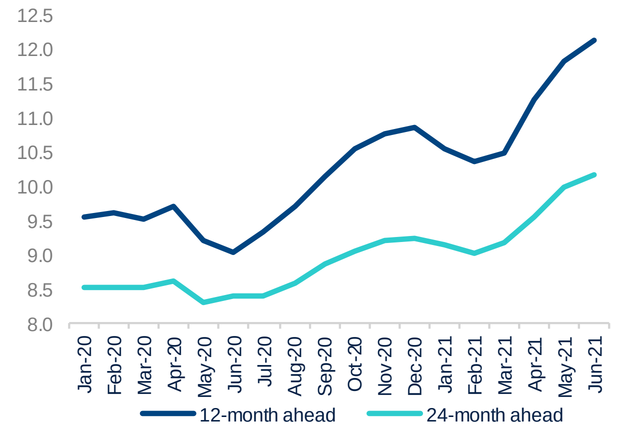
The Central Bank of Turkey (CBRT) maintained the policy rate (one-week repo) at 19% in line with the expectations. Given the high levels of inflation and inflation expectations, the CBRT repeated the need to decisively keep the current "tight" monetary policy stance (this time adding "decisively tight" to the sentence) until a significant fall in the April Inflation Report's forecast path is achieved. In its April projections, the CBRT forecasted a clearer decline in inflation only starting from late 3Q. Therefore, the CBRT once again tried to eliminate early rate cut expectations. Though, inflation expectations have continuously increased since March with 14.5% for the end of the year (vs. 12.2% projection of the CBRT). The CBRT still relies on the decelerating impact of the monetary tightening on credit and domestic demand but economic activity remains strong, as the Bank also confirms. Led by strengthening cost push factors, supply side effects, still not clearly decelerating domestic demand and continuing exchange rate pass-thru impact, we expect consumer inflation to hover near 17% till November before declining to 15% at the end of the year. Last but not least, the recent hawkish messages of the FED, rising global inflation and inflation expectations and their potential effects on the markets will be important for especially the EMs. So, we expect the CBRT to start an easing cycle only very gradually in late 3Q and end the year with 16% policy rate.

Not a clear deceleration in domestic demand, inflation expectations worsen further

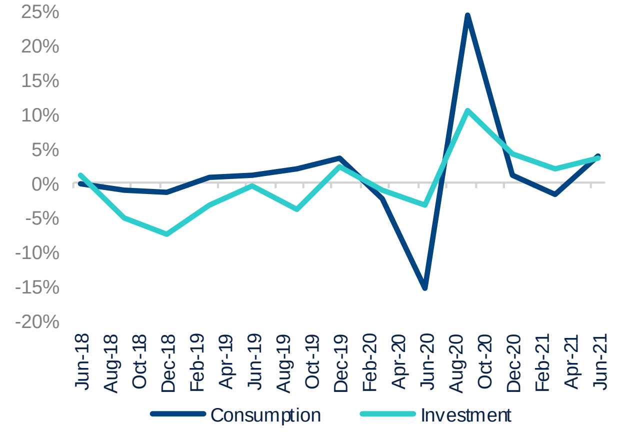
One of the important changes in the decision is about the assessment on credits. This time, the CBRT seemed more careful about the credit growth on top of the course and composition of loans for macroeconomic stability. This might be linked to the last weeks' acceleration in credits in both consumer and commercial segments following the re-opening in the economy. Second, the acceleration of domestic vaccination might eliminate negative risks on certain sectors but reinforces uncertainty over the inflation in a period of both deepening cost-push factors and continuing domestic demand. Also, inflation expectations deteriorated further as year-end expectation increased to 14.5%, while the 12-month and 24-month ahead expectations also rose to 12.1% and 10.2%, respectively (Chart 1). All in all, if the potential impact of the reopening in the economy is considered as we confirm with our Big Data demand indicators (Chart 2), the uncertainty increased further on inflation, given the delayed demand and supply-side factors. Therefore, worsening inflation outlook and potentially increasing global yields following the hawkish messages of the FED will require the CBRT to be more cautious, which the CBRT tries to manage right now by trying to eliminate any early rate cut expectations.

Chart 1. **12-Month and 24-Month Ahead Inflation Expectations** (%, yoy)



Source: Garanti BBVA Research, CBRT

Chart 2. **Garanti BBVA Domestic Demand Big Data Indicators** (sa real, QoQ)



Source: Garanti BBVA Research

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