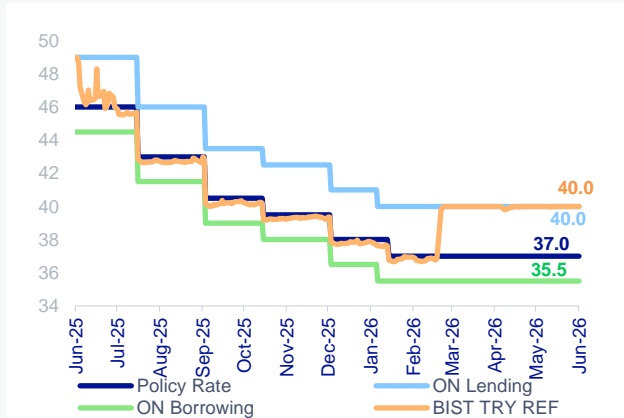


Türkiye | Holding the Line, Eyeing Easing

Adem Ileri / Seda Guler Mert

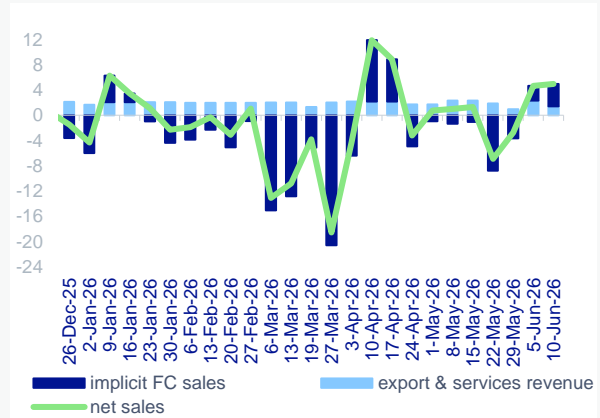
- The Central Bank (CBRT) again kept the policy rate unchanged at 37%, in line with market expectations, while maintaining the cost of funding at 40% through the overnight lending rate. This marks the fourth consecutive month in which funding through the policy rate has been suspended, which the CBRT Governor also criticized in the last inflation report presentation, stating that the extraordinary funding conditions would not be extended too long. However, given the reduced pressure on the CBRT reserves and the signals on a weakening growth outlook, the CBRT appears comfortable with the current policy mix reinforced by tougher macroprudential measures, while placing greater emphasis on financial stability.
- Regarding inflation, the CBRT noted a slight moderation in the underlying inflation trend in May following the upside surprise in April amid the energy price shock. Indeed, May inflation did not point to a further deterioration and suggested limited second-round effects from the unexpected price adjustments seen in April. However, short-term inflation expectations have continued to deteriorate, with year-end inflation expectations rising further to 28.9% and end-2027 expectations to 21.1%, according to the CBRT's May Market Participants Survey, remaining well above the CBRT's targets of 24% and 15%, respectively. We nowcast June monthly CPI inflation at 1.0–1.5%, with risks tilted to the downside due to favorable seasonal factors. However, the underlying trend will likely remain near 2%, while domestic and external uncertainties continue to pose challenges to the disinflation process.
- On growth, we nowcast an annual GDP growth of around 2% y/y as of May, which could recover a little bit in June, driven by higher number of working days (implying still a weak positive q/q growth). We observe further moderation in domestic demand conditions; however, we still believe authorities' tendency to maintain growth at around 3% is largely being preserved, given the latest efforts of selective easing with new credit packages and fiscal support for foreign currency income generator sectors. In our view, there is limited room for positive surprises that could support a sustained improvement in the inflation outlook in the short term.
- Despite rising risks, today's decision once again confirms the CBRT's pro-growth bias, and the Bank may begin easing preemptively once conditions allow. We expect the funding rate to gradually normalize in September and converge to the policy rate in October. Given the prospect of higher energy prices for longer and potential second-round effects amid a pro-growth policy stance and unanchored inflation expectations, we maintain our year-end inflation forecast at 30%, while expecting the policy rate to remain at 37% by year-end, based on assumptions of USDTRY at 52 by end-2026, an average Brent oil price of USD 90/bbl, GDP growth of 3% in 2026, and a fiscal deficit of 3.8% of GDP. Depending on evolving conditions, the CBRT may pursue further rate cuts while increasingly relying on macroprudential measures, which, in our view, would further complicate the balance of risks given rising external financing requirements.

Figure 1. CBRT Interest Rate Corridor & BIST TRY ON Ref Rate (%)



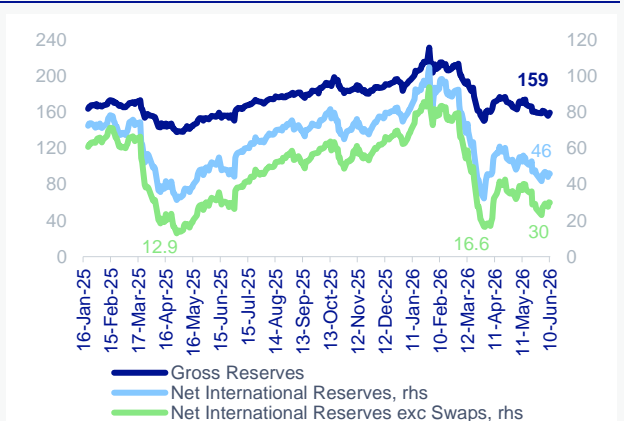
Source: Garanti BBVA Research, CBRT

Figure 2. Flow of CBRT Reserves* (weekly, \$USbn)



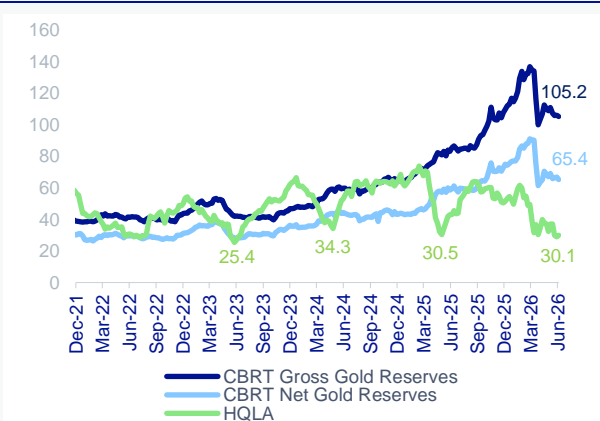
Source: Garanti BBVA Research, CBRT, * The week ending by June 10th refers to the first three days of the week

Figure 3. CBRT International Reserves (\$USbn)



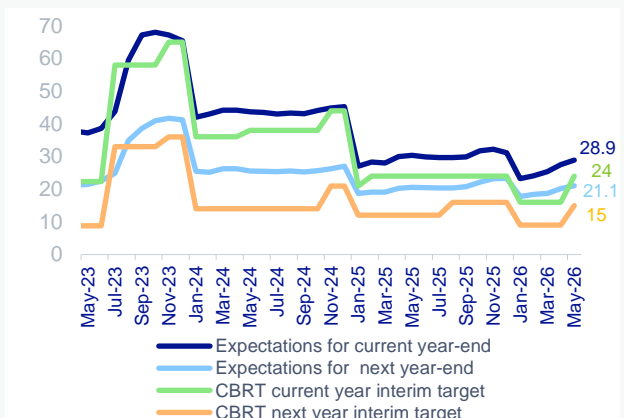
Source: Garanti BBVA Research, CBRT

Figure 4. CBRT Gold Reserves & High Quality Liquid Foreign Assets (HQLA) (\$USbn)



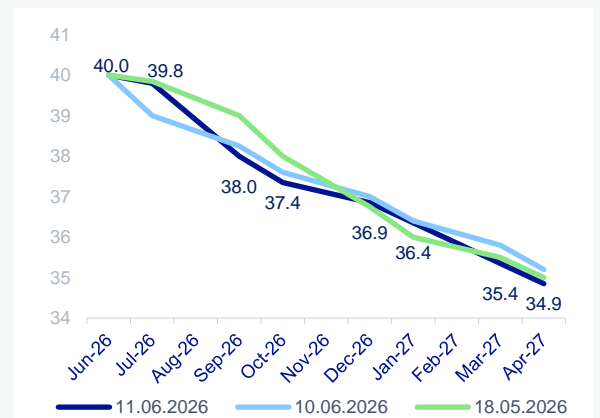
Source: CBRT

Figure 5. Inflation Expectations of Market Participants (%)



Source: Garanti BBVA Research, CBRT

Figure 6. CBRT Funding Rate Pricing Implied by OIS Curve (%)



Source: Bloomberg

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