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Creating Opportunities

Economic Watch

Türkiye | The CBRT maintains a wait-and-see approach

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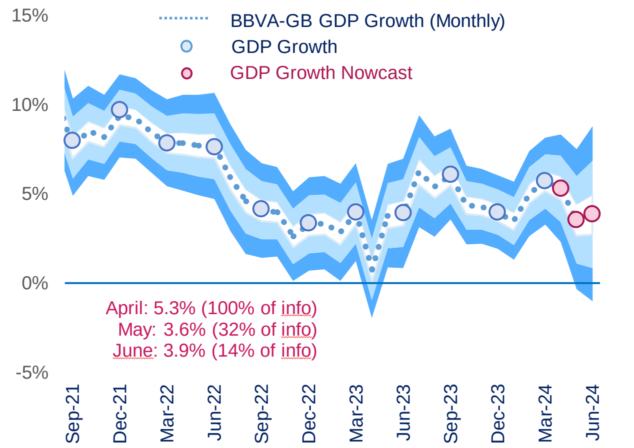
The Central Bank (CBRT) kept the policy rate at 50% in line with expectations without also adding new liquidity or credit measures. The CBRT maintains its cautious stance on inflation, given the risks from the inertia particularly in service inflation, high food prices, geopolitical risks and still inflationary but lately softening demand pressures. Most recently, the pace of reserves accumulation has lost momentum compared to early May mostly to due to weakening foreigner capital inflow, which reduces the need to sterilize TL liquidity in the market. Also, the likelihood of Treasury's higher domestic borrowing in the short term will also serve for additional sterilization. Therefore, they carefully monitor the liquidity and keep the door open for new sterilization tools in case of a need during the summer with current account surplus, ongoing de-dollarization of residents and likelihood of supportive capital inflows. We forecast that annual consumer inflation will come down to 45-50% by September on strong favorable base effects and finish the year at 43%. Yet, unanchored medium term inflation expectations would maintain upside risk on inflation outlook so there would be only a limited room to start monetary easing with very gradual steps in 4Q24.

The CBRT stated that inflationary pressures continue despite some softening in demand. According to our nowcasts, economic activity has slowed down more rapidly in 2Q24 (0-0.5% q/q GDP growth vs. 2.4% in 1Q24) but domestic demand, being still far from the expected level, has remained stronger than supply. High inflation expectations, wealth effects and retailers' spending availability on credit cards prevent a faster adjustment in private consumption. Despite some decline in deposit and loan rates in the recent period, we calculate that the broad policy stance still implies a level of around 5pp higher than the average CBRT cost of funding, given the monthly credit growth caps and different regulations. On one hand, since the adjustment of wages in 2H24 will be much more limited compared to 1H24, a more restrictive monetary stance on top of the easing in inflation trend will more clearly result in a deceleration of demand in the near future. On the other hand, a clearer fiscal consolidation will be needed to support monetary policy to fight against inflation. The draft tax bill may help to contain downside pressure on the budget deficit in the near term. Nonetheless, we still believe that additional fiscal savings on the expenditure side would be more effective to get a faster rebalancing in the economy and future income policies will be key to reduce the inertia impact gradually. According to our forecasts, monthly consumer inflation could retreat to nearly 2.2% in June, leading its annual inflation (72.6%) to get closer to the median of the forecast range of the CBRT, which shows an easing in inflation trend and confirms the MPC statement of a temporary pause in May inflation trend. We forecast that under the assumption of no minimum wage hike in 2H24, further rebalancing in the economy, steady depreciation of the currency and gradual household energy hikes, monthly consumer inflation trend may decline to around 2.5% in 3Q24 and 2% in 4Q24.

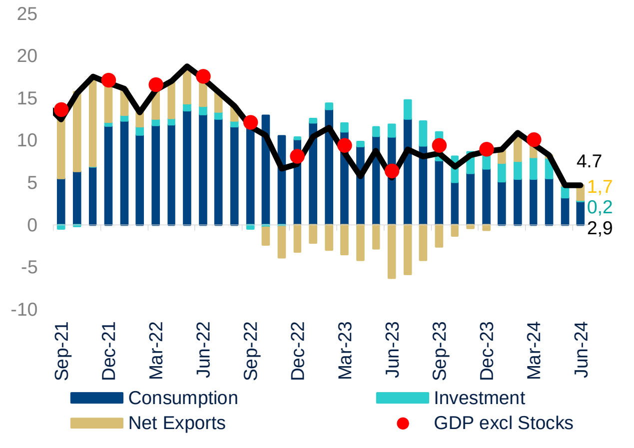
To sum up, monthly inflation trend will more clearly weaken in the coming months. However, upside risks on inflation outlook are still alive on strong inflation inertia, high inflation expectations and geopolitical risks. Inflation expectations remain far from the CBRT targets with 43.5% for 2024 end and 25.5% for 2025 end (vs. 38% and 14% targets of the CBRT respectively). Despite the CBRT's tighter steps on TL required reserves as of May, demand remains decisive on the TL lending rates, which results in a counter pressure on the TL deposit rates. Moreover, the lending composition continues to be in favor of retailer loans. Therefore, the CBRT also closely monitors credit and deposit developments and they commit to support the monetary transmission mechanism with additional macro-prudential policies in case of any undesirable developments. Since inflation expectations remain high, keeping a cautious and restrictive monetary stance against inflation as long as needed will be crucial. Given our expectations of an easing inflation trend more clearly towards the end of the year, we assess that the CBRT may start an easing cycle very gradually in 4Q24. However, before easing, we believe that loosening or removing some regulations, especially the commercial credit growth cap, may support the monetary transmission mechanism.

Chart 1. **Garanti BBVA Monthly GDP Indicator** (YoY, 3M moving average)



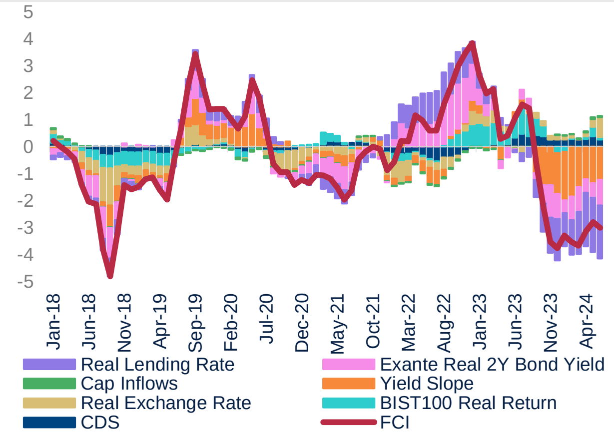
Source: Garanti BBVA Research, TURKSTAT

Chart 2. **Garanti BBVA Monthly GDP Contribution** (annual, pp, exc. Government Consumption)



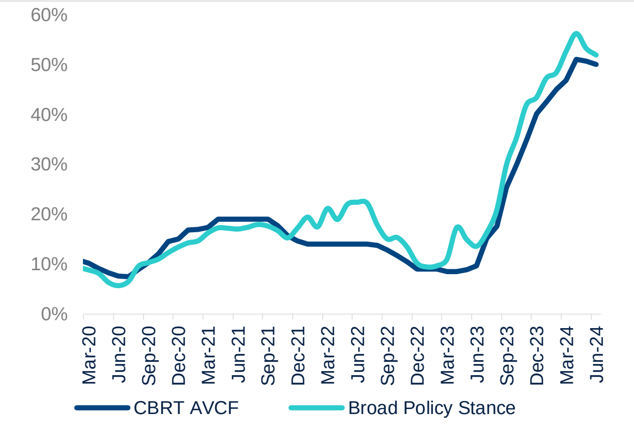
Source: Garanti BBVA Research, TURKSTAT

Chart 3. **Garanti BBVA Financial Conditions Index** (monthly, standardized, + easing, - tightening)



Source: Garanti BBVA Research, CBRT, Bloomberg

Chart 4. **Garanti BBVA Broad Monetary Stance Indicator** (monthly, %)

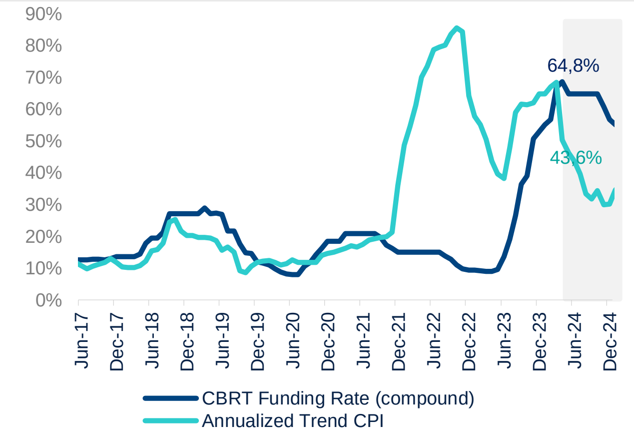


Source: Garanti BBVA Research, CBRT, Bloomberg

Chart 5. **CBRT Market Participants Survey Inflation Expectations** (%)

Source: Garanti BBVA Research, CBRT

Chart 6. **Garanti BBVA CBRT Funding Rate & CPI Forecasts** (%)



Source: Garanti BBVA Research, CBRT, TURKSTAT

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