

Macro note – MPC Rate Decision

CBRT keeps policy rate steady at 46%, in line with expectations. While the corridor width is maintained asymmetrically, the CBRT adopts a cautious stance throughout the text.

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At its meeting this month, the Central Bank of the Republic of Turkey (CBRT) Monetary Policy Committee (MPC) kept the policy rate unchanged at 46%, in line with market expectations. The general market expectation was for a possible reduction in the lending rate, which is the upper band of the corridor. By keeping both the policy rate and the corridor width unchanged, the CBRT chose to send a cautious message to the market. Although some changes were made to the decision text, we see that the general tone remains consistent with the April decision. The main change relates to the slowdown in domestic demand in the second quarter. The decline in the output gap indicates that the cooling of the economy will become more pronounced. The second point concerns increasing protectionist measures, downward risks in global trade, and geopolitical developments. Negotiations on tariffs have yet to achieve the desired progress, and uncertainty continues. In addition, the current state of tension between Israel and Iran and the rhetoric of the parties escalating the tension could trigger a new wave of inflation, particularly in commodities. The CBRT has maintained its cautious stance, stating that it is closely monitoring all these processes and assessing their potential impact on inflation. Although market expectations for a rate cut were not met, it is understood that the disinflation process will continue with determination. The relatively tight monetary policy and relatively high real interest rates have significantly slowed down demand-pull inflation. The CBRT's decision to keep interest rates unchanged at this meeting is intended to test the persistence of external shocks and their impact on domestic macroeconomic indicators. Although the impact on financial markets is negative, we consider this to be an appropriate decision in the fight against inflation.

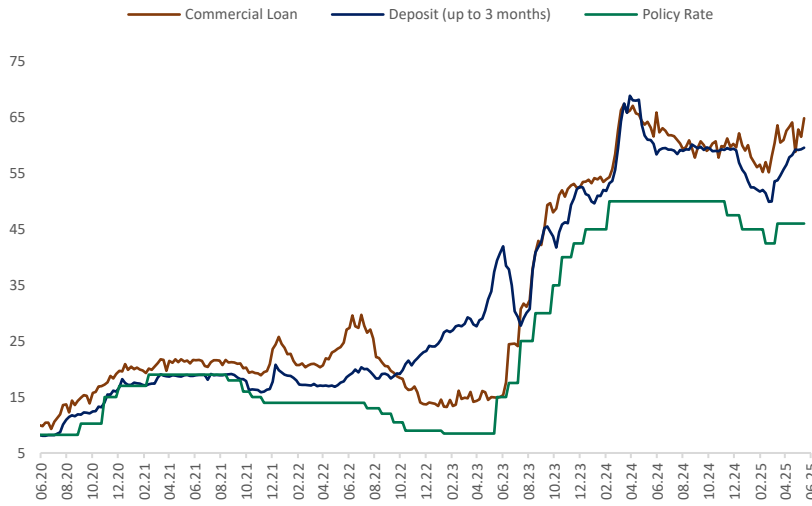
While the latest inflation report provided details on the year-end inflation forecast, there was a downward revision in energy prices. However, geopolitical tensions have increased the price of oil by approximately 20% (\$13) per barrel. In addition, the possibility of the Strait of Hormuz being closed in the event of escalating tensions keeps upward risk in oil prices alive. The addition of volatility in energy prices to global trade and tariff risks is emerging as a factor triggering inflation in all markets. These were also the points highlighted by the FED at yesterday's meeting when it kept interest rates unchanged. Policymakers, unwilling to risk the damage that an early and untimely interest rate cut could cause, opt instead to buy time until a new equilibrium is achieved. Taking all these developments into account, the CBRT wanted to gain time in the fight against inflation and see the contributions that the latest tightening has made/will make to disinflation. This is because the positive contributions of tightening may weaken due to local and global developments. The CBRT did not want to act without seeing this clear effect.

The details of the decision text include the reasons for the tight stance and current developments. According to this, "The main trend of inflation declined in May. Leading indicators point to a continuation of the decline in the main trend in June. Data for the second quarter show that domestic demand has slowed down. The potential effects on the disinflation process of geopolitical developments and increasing protectionism in global trade are being closely monitored. Inflation expectations and pricing behavior continue to pose a risk to the disinflation process. The determined stance of monetary policy is strengthening the disinflation process through balancing domestic demand, real appreciation of the Turkish lira, and improvement in inflation expectations. Increased coordination in fiscal policy will also contribute significantly to this process. A tight monetary policy stance will be maintained until a permanent decline in inflation and price stability are achieved. In this context, the policy

rate will be determined in a manner that ensures the tightness required by the anticipated disinflation process, taking into account inflation outcomes, the main trend, and expectations. The Committee will determine the steps to be taken regarding the policy interest rate with a cautious and meeting-based approach focused on the inflation outlook. In the event of a significant and persistent deterioration in inflation, all monetary policy tools will be used effectively. In the event of developments beyond expectations in the credit and deposit markets, the monetary transmission mechanism will be supported by additional macroprudential measures. Liquidity conditions will remain closely monitored, and liquidity management tools will be used effectively." The inflation trend is progressing in line with the CBRT's targets. The committee, which wants to see the tight stance reflected in all macro indicators, has once again emphasized the importance of fiscal policy, underscoring that monetary policy is sufficiently tight.

In summary, the Central Bank kept its policy rate unchanged at 46% in today's interest rate decision. The bank, which also maintained the corridor width asymmetrically, opted not to proceed with a reduction without seeing the effects of recent decisions and the impact of global developments on the domestic economy. A cautious stance prevails throughout the text. It was also reiterated that decisions would be made on a meeting-by-meeting basis and with a focus on inflation, implying that market volatility would not be tolerated. Uncertainty in global markets may disrupt the CBRT's disinflation targets for some time yet. We stress that improvements in this area may lead to interest rate cuts exceeding expectations. The CBRT, which effectively uses its primary policy tool and adjusts liquidity with complementary macroprudential measures, continues to maintain its determined stance in the fight against inflation. In this context, we anticipate that the rate cut process will begin in July, provided there are no additional shocks in local or global markets. We emphasize that in the event of new supply- or demand-side shocks, further adjustments to the policy rate stance may be necessary.

Graph 1: Policy, Loan, and Deposit Rates (%)



Source: CBRT, ŞEKER Invest

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