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Turkey Economics | Europe

CBT Review: Setting the Stage

A softer tone and implicit real rates guidance signal that the CBT is getting ready to start gradual rate cuts in line with a decline in realised and expected inflation. We bring forward our expectation for the first cut to December from January, but still see a tight monetary stance prevailing.

Unchanged rates but a shift in forward guidance: The CBT kept its policy rate unchanged (at 50%) for an eighth month as widely expected. The MPC adopted a softer tone on the inflation outlook compared to last month, while it shifted to **implicit guidance on real rates**, in our view, by adding this new sentence: "...the level of the policy rate will be determined in a way to ensure the tightness required by the projected disinflation path, taking into account both realised and expected inflation". This echoes the governor's remarks during the last [Inflation Report press conference](#) where he said that maintaining the current level of the policy rate implies an effectively tighter monetary policy stance as inflation and inflation expectations decline. While opening the door for gradual rate cuts to start soon, the CBT intends to keep the monetary stance tight in view of the projected disinflation path, and "remains highly attentive to inflation risks".

A softer tone, pointing to an improvement in inflation and inflation expectations: The MPC noted a decline in the underlying trend of inflation in October, a continued slowdown in domestic demand (reaching disinflationary levels) and signs of improvement in services inflation. Moreover, the previous mention of increased uncertainty regarding the pace of improvement in inflation was removed from the statement. On the side of caution, the MPC mentioned elevated levels of unprocessed food inflation due to temporary supply conditions, and risks regarding inflation expectations and pricing behaviour. Another notable change was the newly added sentence that factors in increased coordination with fiscal policy as contributing significantly to disinflation. Accordingly, we think that the CBT's base case scenario assumes new year wage and price hikes to be compatible with its disinflation path. We think that a minimum wage hike of around 30% and energy price hikes of around 25% are compatible with the CBT's near-term inflation trajectory and an end-2025 forecast of 26%Y (see [Turkey: About to Turn a Corner](#), November 18, 2024).

We now expect the first rate cut in December, from January previously... Our reading of the statement is that the CBT intends to deliver a measured cut in December barring any significant upside surprises in November inflation, publicly set wages and prices, and FX volatility in the meantime (until the meeting on December 26). In view of the MPC's new forward guidance, and the balance of risks, we now expect rate cuts to start in December, from January previously. We see headline inflation declining to 46.5%Y (1.9%M) in November and 44.5%Y (1.5%M) in December, providing room for a 200bp rate cut in December that would keep the ex post real rate in positive territory. We expect the CBT to keep a 100-200bp pace

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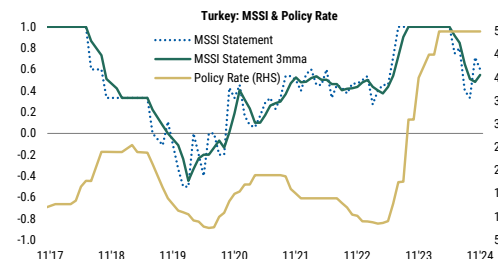
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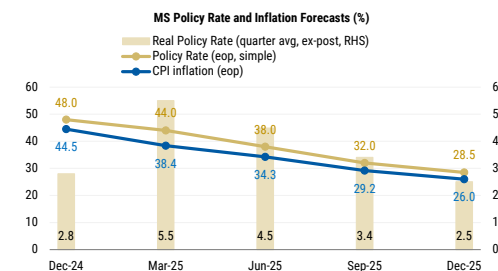
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Exhibit 1 : Our semantic index shows a softening in the tone of the statement compared to last month (dashed blue lines)



Source: Haver Analytics, Morgan Stanley Research; Note: For methodology, see [Eye, Robot – Introducing Our Semantic Index](#), March 28, 2023. MSSI declined to 0.6 from 0.7 in October, on a scale between -1 and 1, where 1 denotes the highest level of hawkishness.

Exhibit 2 : We bring forward our expectation for the first rate cut to December (200bp) from January, but see a similar real rate path in 2025 as in our outlook



Source: Haver Analytics, Morgan Stanley Research forecasts

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until the policy rate reaches 28.5% in December 2025 conditional on inflation declining towards our 26%Y end-2025 forecast. Our forecasts continue to imply a gradual decline in ex post real rates from an average of around 5% in 1H25 to sub-3% in 4Q25 as headline inflation comes below 30%Y as we have in our [2025 outlook](#).

...but uncertainty around appropriate tightness remains: Given uncertainty around what level of ex post or ex ante real rate would be sufficiently tight to ensure disinflation towards the CBT's forecast range (21-26%Y for end-2025), rate cuts could be paused sooner or the CBT could continue with smaller steps as and when the decline in inflation stalls.

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