

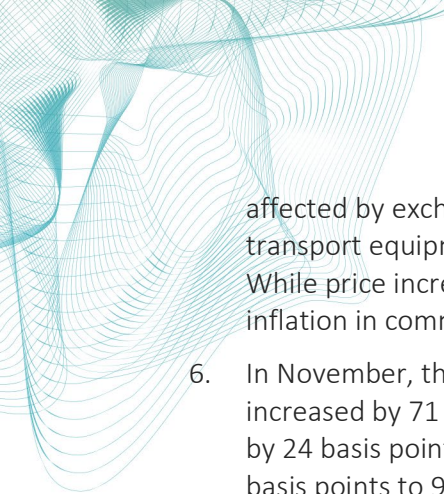
Summary of the Monetary Policy Committee Meeting

26 November 2020, No: 2020-70

Meeting Date: 19 November 2020

Inflation Developments

1. In October, consumer prices rose by 2.13%, while annual inflation increased by 0.14 points to 11.89%. Annual inflation increased in food and core goods groups, while it decreased in the energy group and remained flat in the services group. While the rise in food inflation stemmed from both unprocessed and processed food prices, the rise in core goods inflation was mainly driven by durable goods. Annual energy inflation decreased owing to the base effect in electricity prices. Against this background, while annual inflation in B and C indices increased, the trend of the B index remained almost flat and the trend of the C index slightly decreased.
2. In October, annual inflation in food and non-alcoholic beverages increased by 1.56 points to 16.51%. Due to the rally in international food prices and exchange rate developments, annual inflation in unprocessed food group increased by 1.31 points to 18.78% and that of processed food prices increased by 1.70 points to 14.49%. Eggs, pulses and rice played a major role in the increase in unprocessed food prices. In the processed food group, prices of bread and cereals as well as other processed foods posted high monthly increases. The adverse outlook in the latter was mainly driven by fats and oils.
3. Energy prices increased by 2.09% in October, yet annual inflation in the energy group decreased by 2.79 points to 3.88%. In this period, although electricity prices rose by 5.76%, annual inflation in the group decreased owing to the base effect. In October, international oil prices posted a limited decrease; however, depreciation of the Turkish lira led to a rise in fuel-oil prices and curbed a more favorable outlook in the energy group inflation.
4. In October, prices of core goods increased by 3.29% and group's annual inflation rose by 0.41 points to 12.09%. Owing to exchange rate developments and the lagged effects of the strong credit impulse, the uptrend in the annual inflation in durable goods group continued, led by furniture, automobiles and white goods, and increased by 2.41 points to 19.79%. Meanwhile, monthly and annual inflation in the clothing and footwear remained weak also due to the sectoral demand conditions. In other core goods, although annual inflation remained relatively low at 9.40%, the effects of exchange rate developments have been observed in monthly price increases.
5. Services prices was up 0.71 percent in October and annual inflation in the group rose by 0.08 points to 10.92%. Annual inflation decreased in communication and transport services, while it increased in restaurants-hotels, rents and other services. Other services group prices were

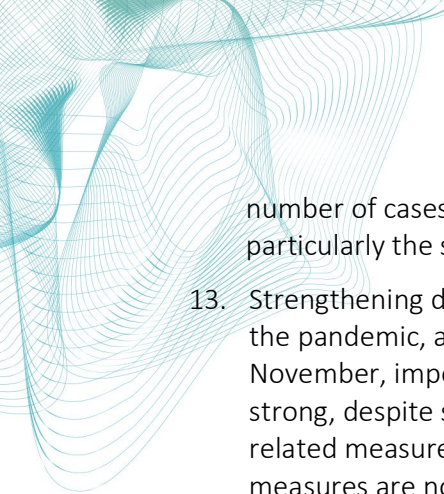


affected by exchange rate developments, meanwhile, maintenance and repair of personal transport equipment as well as health services continued to be the most prominent items. While price increases in communication and transport services were moderate, annual inflation in communication decreased on the back of the base effect.

6. In November, the rise in inflation expectations continued. The year-end inflation expectation increased by 71 basis points to 12.47%; the 12-month-ahead inflation expectation increased by 24 basis points to 10.77%, and the 24-month-ahead inflation expectation increased by 15 basis points to 9.20%.

Factors Affecting Inflation and Risks

7. Global economic activity has recovered partially in the third quarter. However, uncertainties regarding global economic activity heightened due to the recent increases in Covid-19 cases. The recently elevated pandemic-related restrictions in the European countries keep downside risks to external demand and export outlook in place. Moreover, uncertainties remain regarding the possible effects of the pandemic and health measures on consumption habits and general spending behavior. In case of prolonged normalization due to delays in widespread vaccination, the recovery in the global activity may be slow and the global risk appetite may fluctuate.
8. Although crude oil prices are still below the pre-pandemic period levels, they have risen since the previous MPC Meeting. Besides, the upward trend in commodity prices excluding energy, specifically industrial metals and agricultural commodities, increases the upward cost pressure on consumer inflation. Developments in international prices as well as the exchange rate have an adverse effect on the trend inflation, particularly in food and core goods groups.
9. Advanced and emerging economies maintain their expansionary monetary and fiscal stances. While long-term interest rates remain at historic lows across advanced economies, both central bank statements and market expectations suggest that the low interest rate environment is likely to continue for a long period. The effectiveness of these policies on financial markets, growth and employment will depend on the course of the pandemic and the available policy room in each country.
10. Portfolio inflows to emerging economies have continued at an increasing scale since the previous MPC meeting due to improved risk sentiment. However, excluding China, inflows to bond markets increased at a limited extent, while those to equity markets remained relatively weak. Reinforced perceptions that policy rates will remain low in advanced economies and possible incentive packages are likely to improve portfolio flows to emerging economies in the upcoming period.
11. Domestic economic activity posted a marked recovery in the third quarter. According to September data, industrial production index increased by 1.7% month-on-month and by 30.3% quarter-on-quarter, exceeding its pre-pandemic levels. Considering together with the developments in turnover indices, economic activity recovered with a wide sectoral diffusion led by sectors sensitive to financing conditions and those producing goods for the domestic market. Nevertheless, the weak trend continued in goods and services sectors strongly tied to the tourism sector.
12. The recovery in economic activity continues. However, leading indicators and high-frequency data suggest that economic activity has been decelerating since mid-October. Recently, exports slowed down due to pandemic-driven limitations in Europe while domestic demand remained relatively strong. Meanwhile, partial restrictions introduced due to the increasing

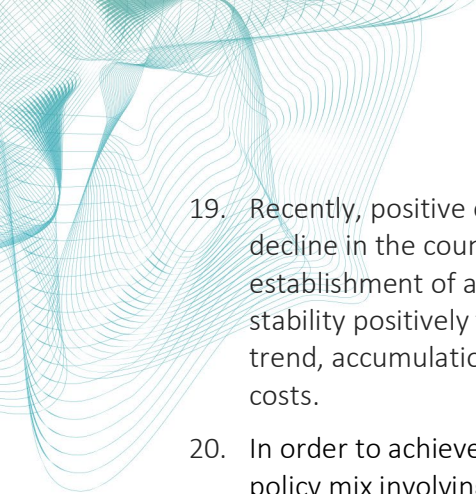


number of cases heighten uncertainties on the short-run outlook of economic activity, particularly the services sector.

13. Strengthening domestic demand due to the lagged effects of strong credit impulse during the pandemic, affects the current account balance adversely through the imports channel. In November, imports excluding gold remains almost flat, while imports of gold has still been strong, despite some slowdown. On the other hand, the restraining effects of pandemic-related measures introduced in Europe have started to be observed; however, since measures are not as tight as those introduced at the early stages of the pandemic and the activity in manufacturing industry continues, the favorable outlook particularly in exports of intermediary goods is maintained. The Committee underscored the importance of the course of the current account balance in terms of a lasting recovery in economic activity and financial stability.
14. The recovery in economic activity has a positive effect on the labor market. In August, non-farm employment increased across sectors, while so far, employment losses have been partially compensated. In this period, both the labor force participation rate posted an increase on the back of economic recovery and unemployment rates receded. Leading indicators reveal that new job posts increased and employment opportunities continued to improve.

Monetary Policy

15. The Committee emphasized that, within the inflation targeting framework, it will decisively use all of its policy tools in order to achieve and maintain price stability, by taking into account all factors affecting inflation and the increased risks.
16. The lagged effects of depreciation in Turkish lira, increasing international commodity prices and deterioration in inflation expectations affect the inflation outlook adversely. While tracked data for November point to an increase in inflation due to the recent exchange rate volatility, this is assessed to be temporary with the decisive monetary policy stance. Accordingly, the Committee has decided to implement a transparent and strong monetary tightening in order to eliminate risks to the inflation outlook, contain inflation expectations and restore the disinflation process. In this context, the one-week repo auction interest rate, which is the policy rate, is increased from 10.25 percent to 15 percent. In the periods ahead, all factors affecting inflation will be taken into account, and tightness of monetary policy will be decisively sustained until a permanent fall in inflation is achieved. The Central Bank will continue to use all available instruments in pursuit of the price stability and financial stability objectives.
17. In addition to monetary tightening, the Committee decided to adopt a simple operational framework to enhance transparency and predictability, and decided to provide all funding at the one-week repo auction rate, which is the main policy rate. In this regard, the funding currently provided by the CBRT via traditional method repo auctions with one-month maturity and late liquidity window facilities will instead be provided via one-week quantity repo auctions, which is the principal monetary policy tool as of 20 November 2020.
18. In line with the primary objective of price stability, the Committee assessed the need for a revision in the reserve requirement policy in order to enhance the effectiveness of monetary transmission mechanism.

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19. Recently, positive expectations regarding monetary policy have been contributing to the decline in the country risk premium. The Committee assessed that the permanent establishment of a low inflation environment will affect macroeconomic and financial stability positively through the fall in country risk premium, reversal in the dollarization trend, accumulation of foreign exchange reserves and the perpetual decline in financing costs.
 20. In order to achieve price stability, a strong policy coordination and an integrated macro policy mix involving all stakeholders are required.
 21. It should be emphasized that any new data or information may lead the Committee to revise its stance.