Macro: Upward revision in interim targets; current stance and framework likely to be maintained for a long period

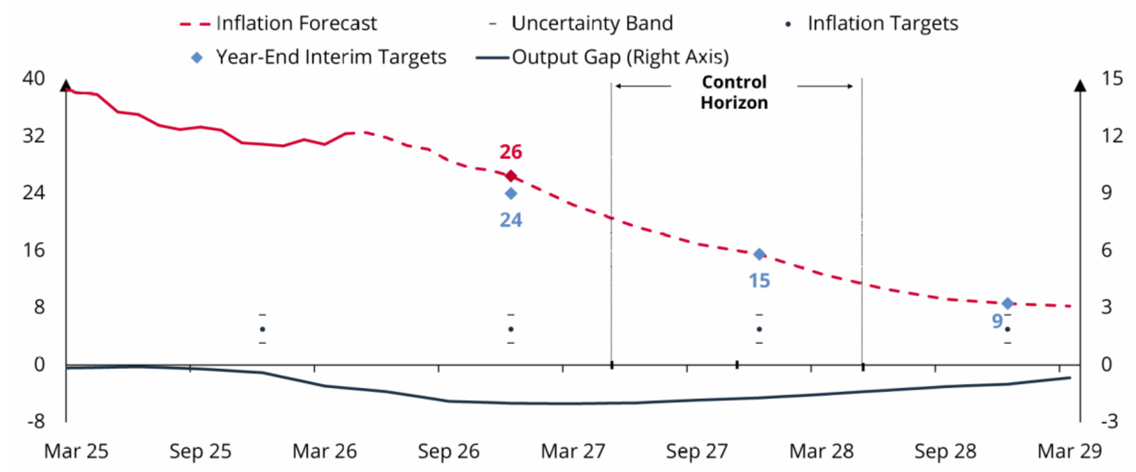
1. Forecasts

In the third inflation report of 2025, the CBRT changed the framework regarding the communication of medium-term forecasts; and separated 'interim targets', which are used as a reference in determining the monetary policy stance and indicate the levels to be achieved during the disinflation process, and year-end inflation forecasts. Within this framework, it was stated that inflation forecasts could be revised depending on the flow of data, while interim targets would not be changed between report periods unless extraordinary developments occur.

Referring to the extraordinary effects of geopolitical developments, the CBRT made various changes in its interim targets, inflation forecasts, and communication regarding the inflation forecasts. Accordingly

- **Interim targets** for 2026, 2027, and 2028 year-ends were updated to 24%, 15%, and 9%, respectively. Previous interim targets were 16%, 9%, and 8%, respectively.
- **Communication of inflation forecasts through forecast bands was suspended**. Instead, point forecasts were presented under the baseline scenario, and a descriptive narrative was preferred rather than numerical representation regarding the risk factors around these forecasts.
- Year-end inflation forecasts in the baseline scenario are 26% for 2026, which is above the interim target; and the same as interim targets for 2027 and 2028 (Chart 1). In the previous inflation report, the midpoints of the forecast band were 18%, 9%, and 8%, respectively.

Chart 1. 2026-II Inflation and Output Gap Forecasts



Forecast accounting: CBRT shared no numerical accounting regarding the change in the interim target and inflation forecasts. However, a forecast accounting within this scope was shared in the report introducing the interim targets. (Macro: 2025-III Inflation Report.) When we look at the changes in the baseline assumptions for 2026, the oil price assumption increased from $60.9 to $89.4 (up by 46.8%). According to the analysis in Box 2.4 in the report, this adds 4.7 points to inflation within one year under no sliding scale mechanism. However, given the sliding-scale mechanism in effect, the update in food assumptions, increases in other commodity prices, and the anticipated slowdown in the economic activity do not appear sufficient to explain a total forecast update of 8 points. We interpret the remaining difference, most probably, as a compensation for low forecasts in previous reports.

2. Assumptions

External demand: The export-weighted global growth assumption was updated from 2.3% to 1.7% for 2026 due to the limiting effect of geopolitical developments on the global growth outlook, especially in Gulf region (Table 1). While the external demand outlook weakened, for the sake of internal consistency, the growth update implied by output gap forecasts points to a stronger domestic demand, and therefore a more accommodative stance in economic policies.

Food prices: While the food inflation assumption for 2026 was updated from 19% to 26.3%, this update was largely based on realizations in the January-April period (Table 1). It was foreseen that normalization in food supply conditions would positively affect food prices in the upcoming period. Nevertheless, food inflation for 2027 was also increased from 11% to 19%.

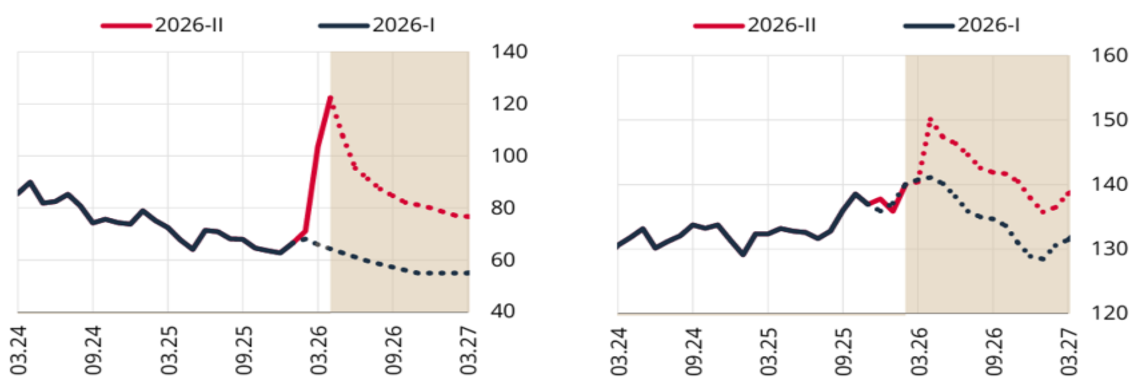
Fiscal stance: As before, it was assumed that fiscal policy would contribute to the disinflation process and that administered prices, as well as borrowing, tax, and income policies, would support the disinflation process. In this context, it was assumed that sliding-scale mechanism would continue in the upcoming period. However, past adjustments in other administered prices (energy, agricultural product procurement prices, etc.) indicate that risks through this channel remain upward.

Commodity prices: While assumptions regarding oil prices were revised significantly upward, an upward revision was also made to import prices for 2026 by taking developments in energy and other commodity prices into account (Chart 2, Table 1).

Table 1. Revisions to Main Assumptions

		IR 2026-I	IR 2026-II
Global Production Index* (Average Annual % Change)	2026	2.3	1.7
	2027	2.2	2.5
Oil Prices (USD, Annual Average)	2026	60.9	89.4
	2027	56.0	75.4
Import Prices (USD, Average Annual % Change)	2026	2.0	6.3
	2027	-0.9	-0.2
Food Prices (Year-End, % Change)	2026	19.0	26.3
	2027	11.0	19.0

Chart 2. Oil (left panel) and Import Price (right panel) Assumptions



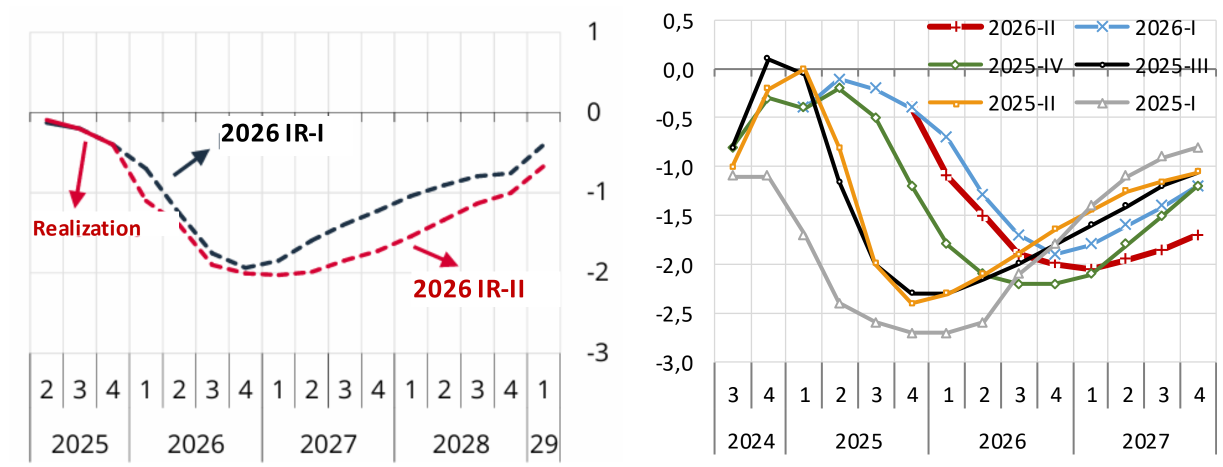
Source: Bloomberg, CBRT
* Shaded areas show the forecast horizon

Economic activity: Contrary to recent reports, a downward revision was made to output gap forecasts due to the effect of global uncertainties (Chart 3, left panel). According to output gap forecasts, growth is somewhat lower than in the previous report in the upcoming period. In addition, the cyclical trough appears to have shifted to the first half of 2027. Under different quarterly potential growth assumptions, the growth forecasts implied by the output gap projections are as follows (Table 2):

Table 2. Growth Forecasts Implied by Output Gap Forecasts (%)

	Quarterly Potential Growth (%)		
	0.8	**1.0**	**1.2**
2026	1.9	2.5	3.0
2027	3.0	3.8	4.7
2028	3.9	4.7	5.6

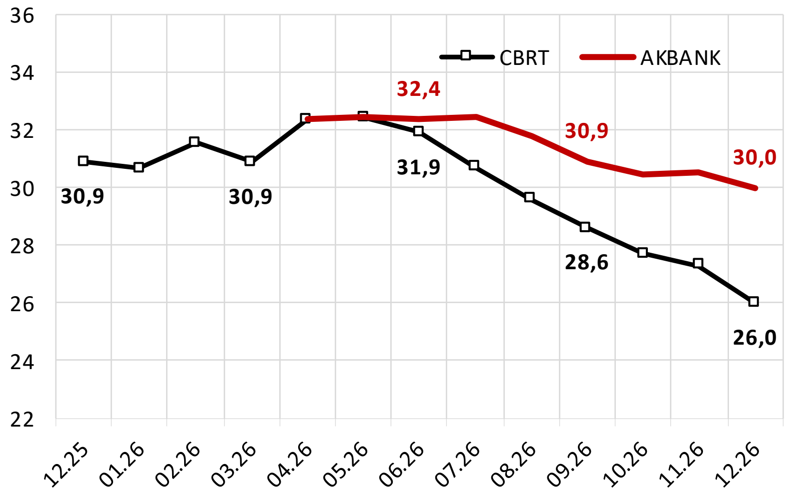
Chart 3. CBRT Output Gap Forecasts



3. Our Evaluations

- We find the magnitude of the upward revision made by the CBRT in interim targets and forecasts stronger than implied by the changes in baseline assumptions. Therefore, it can be said that the size of the update is an indication and compensation for past forecasts having remained low
- We also consider the update in the 2027 year-end inflation forecast important from the perspective of the monetary policy stance. The 2027 year-end interim target was increased by 6 points from 9% to 15%. A revision close to the short-term update in the control horizon of monetary policy weakens forecast credibility since it contains a message of passive monetary policy against inflationary shocks.
- In light of our past observations regarding the reaction function, , we interpret the statements in the Q&A section of the press conference regarding the next MPC meeting that “all options are on the table” and that there is “no dollarization risk” as “the status quo will be maintained unless there is strong dollarization.”
- In this regard, we do not change to our inflation and policy rate forecasts. When we apply the CBRT’s previous approach to its point forecast (26%) for end-2026, the upper bound of the forecast band woud reache a point close to our forecast at 29% (Chart 4). We assess that there is no room (or perhaps only a very limited room) for a policy rate cut until year-end.

Chart 4. Inflation Forecasts



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