

Economic Watch

Turkey: Consumer inflation end 2020 at %14.6

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Consumer prices increased by 1.25% in December, slightly higher than expectations (1.2% BBVA Research, 0.9% Consensus), leading the annual inflation to reach 14.6% up from 14% in November. The lagged impact of exchange rate pass thru and the unfavorable food inflation resulted in one of the highest monthly inflation levels for December. Besides, cost push factors maintained upside risks on inflation outlook as domestic producer prices rose by 2.3% mom and resulted in an annual inflation of 25.1%. The recent hikes in utility and toll ticket prices could have minor impact on inflation but the high increase in minimum wage (21.6% yoy) might increase stickiness on inflation through especially services prices. The tight monetary policy stance accompanied by consistent commitment from the government could maintain stabilization in currency and result in deceleration in domestic demand. However, still alive inertia, ongoing cost push factors, unsupportive global commodity and food prices, and unfavorable base effects till April 2021 would lead the headline inflation to rise around 15.5% in April 2021 before a gradual disinflation path thereafter. We expect consumer inflation to end 2021 at 10.5%.

The rise in inflation on the lagged impact of pass-thru and unfavorable food prices

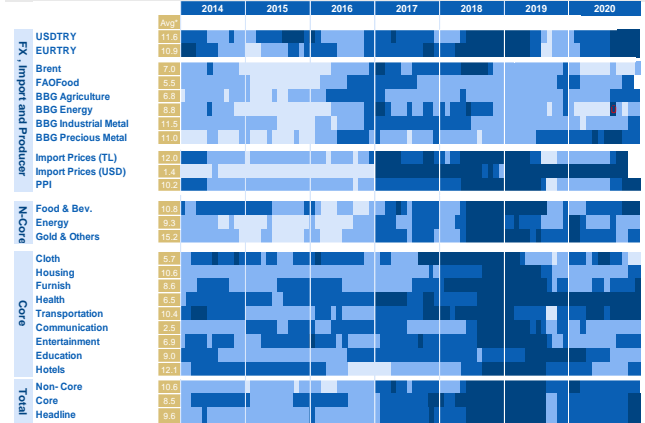
Food inflation continued to be one of the main factors on upside surprise in inflation as it increased by 2.7% mom (season avg. 1.8%) on the back of both unprocessed (3.4% mom) and processed food inflation (1.7% mom). However, led by base effects, annual food inflation slightly retreated to 21.2% from 21.7% in November. Also, the acceleration in oil prices led energy inflation to rise by 1.5% mom but annual energy inflation remained subdued at 5.6%. Core prices rose by 1.1% mom on lagged impact of exchange rate pass-thru on certain sensitive items such as furniture (3.5% mom) and transportation (2.6% mom); though clothing prices decreased by 3.2% mom on relatively weak demand. Therefore, annual core C inflation jumped to 14.3% from 13.3%. Also, inertia remained alive as annual services inflation increased to 11.6% from 11.4% in November. Last but not least, cost push factors could maintain upside risks on inflation outlook as domestic producer prices (2.4% mom) upsurged to 25.1% from 23.1% in November. The recent hikes on electricity (6%), natural gas (1%) and toll ticket prices could have minor impact (near 0.2pp) but the rise in minimum wage (21.6% yoy) might increase stickiness on inflation through especially services prices. The high level of trend inflation (close to 13.5% yoy, Chart 5) signal that the remaining impact of the exchange rate pass-thru could be limited but the long-awaited cost factors could result in some upward price adjustments at the start of the year, making it difficult to manage already worsening inflation expectations.

Chart 1. Core Inflation and CPI (YoY)



Source: BBVA Research Turkey, Turkstat

Chart 2. Inflation Heat Map

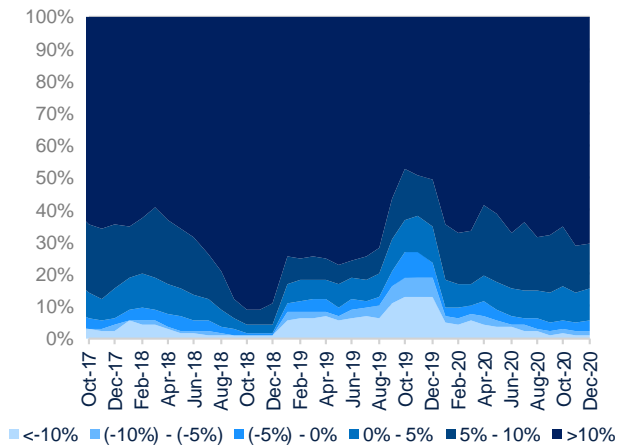


Source: BBVA Research Turkey & Turkstat

Worsened inflation outlook requires a more coordinated policy mix

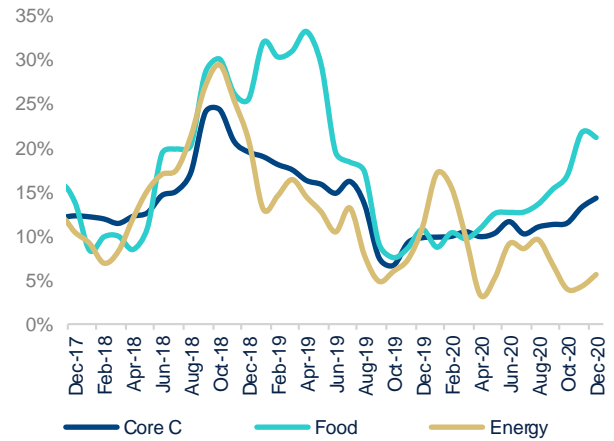
Cost push factors, high inertia, unfavorable base effects, higher than expected price adjustments like the minimum wage hike could dominate the impact of the recent currency stabilization and decelerating domestic demand in the very short term as we expect inflation to increase till May 2021 before a gradual disinflation path thereafter and end the year at 10.5% helped by sizable positive base effects in 4Q21. Therefore, tight monetary stance should be maintained and accompanied by a coordinated policy mix of authorities in order to accelerate disinflation process.

Chart 3. **Consumer Inflation Diffusion Map, YoY**



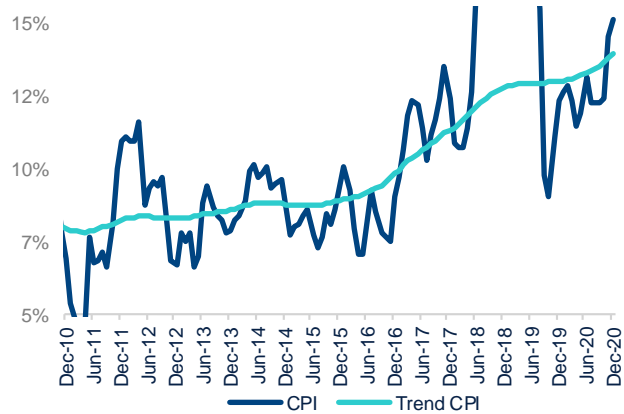
Source: BBVA Research Turkey, Turkstat,

Chart 4. **CPI Components, YoY**



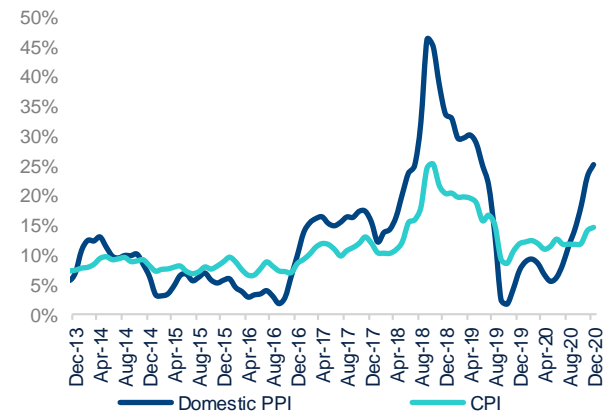
Source: BBVA-Research Turkey, Turkstat,

Chart 5. **CPI and Trend Inflation, YoY**



Source: BBVA Research Turkey UCSV-MA Model, Turkstat

Chart 6. **CPI vs PPI, YoY**



Source: BBVA Research Turkey, Turkstat

Chart 7. **CPI in Subcomponents**

	MoM	YoY
Total	1.25%	14.60%
Food & Non-alcoholic beverages	2.5%	20.6%
Beverage & Tobacco	0.0%	0.7%
Clothing & Textile	-3.2%	-0.3%
Housing	0.7%	9.6%
Household Equipment	3.5%	18.0%
Health	0.8%	16.7%
Transportation	2.6%	21.1%
Communication	0.8%	5.7%
Recreation & Culture	0.1%	10.4%
Education	0.0%	6.8%
Restaurants & Hotels	0.5%	12.7%
Misc. Goods & Services	-0.6%	28.1%

Source: BBVA Research Turkey & Turkstat

Chart 8. **Domestic PPI in Subcomponents**

	MoM	YoY
Total	2.36%	25.15%
Mining & Quarrying	0.0%	19.0%
Manufacturing	2.7%	27.3%
Food Products	1.8%	24.9%
Textiles	0.5%	25.2%
Wearing Apparel	-0.4%	6.7%
Coke & Petroleum Products	10.7%	4.8%
Chemicals	2.3%	27.1%
Other Non-Metallic Mineral	3.2%	15.5%
Basic Metals	6.5%	56.3%
Metal Products	4.8%	35.4%
Electrical Equipment	1.2%	28.8%
Electricity, Gas, Steam	-1.2%	0.2%

Source: BBVA Research Turkey & Turkstat

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