

Turkey: CPI touched 70% in April

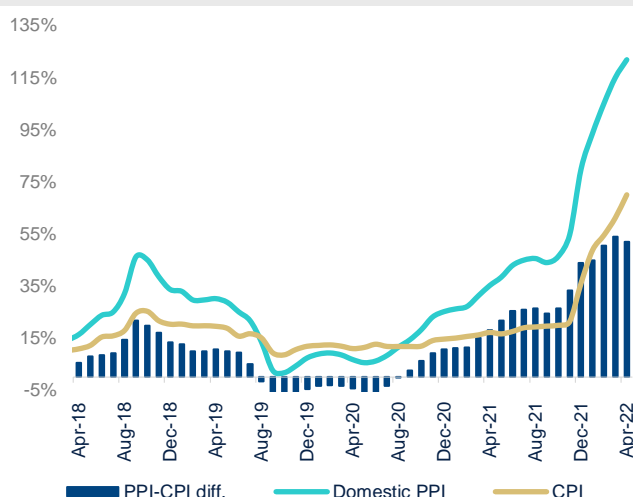
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5 May 2022

Consumer inflation increased by 7.25% mom in April, well above both the market expectation (5.75%) and our expectation (6%), leading annual inflation to reach 70%. While the surprise deviation in our forecast was mainly due to the high increase in food prices, the core inflation came in line with our expectations. Core inflation reached 52.4% yoy, up from 48.5% in March on the back of cost push factors, second round effects and the exchange rate pass thru. Cost pressures continue to increase as producer prices rose by 128% annually. High commodity prices, stronger cost-push factors, second round price effects, sharply deteriorated inflation expectations and the fact that global supply-side problems on pandemic will continue to remain for a while despite the easing, increase the upside risks on our inflation expectation, anticipating inflation to hover above 70% till November before declining to 50% at the end of the year on the base effect.

Higher food prices and further strengthened cost-push factors

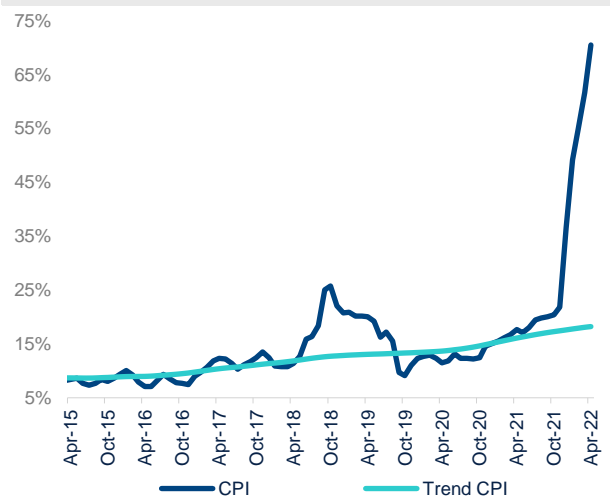
Both unprocessed and processed food prices increased by 16.8%(fresh food and vegetables, 20.8% mom) and 9.9% monthly, respectively, due to rising global food and commodity prices, price hikes in meat and dairy products and the fasting month of Ramadan. Therefore, the food inflation rose by 13.6% mom, led annual figure to reach 91% from 71.6% in March. Energy prices also continued to rise by 7.5% mom, resulting in annual energy inflation to get 118% due to high commodity prices, hikes in natural gas and water prices. Taking into account ongoing war in Ukraine and despite the diminishing but still negative impact of pandemic on global supply chain, global commodity and food prices may keep upside risks on energy and food prices alive. Furthermore, the lagged impact of exchange rate pass-thru, cost push factors, and second round effects on top of still strong demand caused core inflation to increase by 4.5% mom and upsurged annually to 52.4% in April from 48.5% in March. Basic goods prices increased by 4.4% mom especially on durable goods such as furniture(11.7% mom) and auto prices(4.1% mom). Inertia and cost push factors are intensified further. Services prices rose to 42.2% yoy(4.7% mom) from 36.7% in March, indicating that the inertia strengthened more. Due to high inflation realization, the new adjustment in wages in the rest of the year could reinforce this trend. In addition, cost push factors have increased further as producer prices have risen 7.7% mom, leading annual figure to reach 121.8%. The recent price hikes in natural gas prices and likelihood of further price hikes because of the high subsidization in energy prices could weighed more on the upside. All in all, worsening inflation expectations, high global commodity prices, continuing exchange rate pass through on top of still strong demand, high inertia and accelerated cost push factors would keep upside risks on the inflation outlook.

Figure 1. CPI vs Domestic PPI, YoY



Source: Garanti BBVA Research, Turkstat

Figure 2. CPI vs Trend CPI, YoY



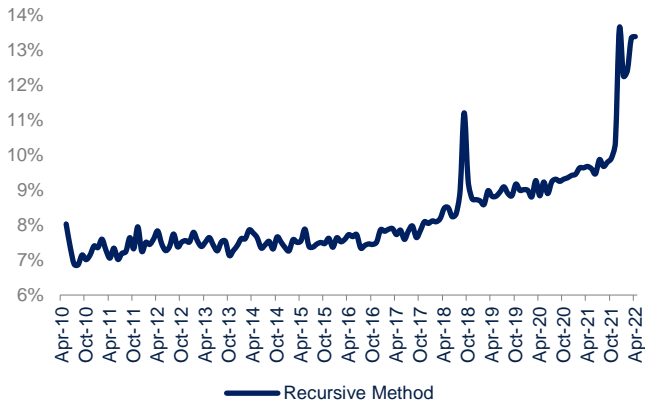
Source: Garanti BBVA Research, Turkstat

The rise in long-run inflation level could challenge CBRT on interim targets.

Trend CPI(exc. seasonal, cyclical and other idiosyncratic factors) continued to increase further close to 18%(Figure 2), supported by the evolution of long run equilibrium level for Core-D inflation throughout the year based on Bayesian

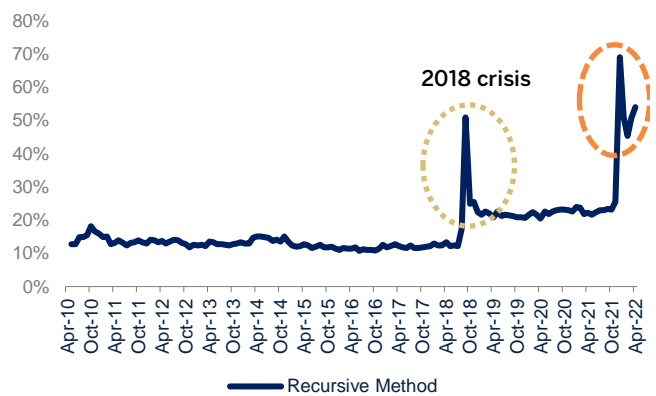
VAR(Figure 3). Despite the some stabilization in currency on the back of liraization strategy, exchange rate pass-through rose further in April (Figure 4) stemmed from the ongoing worsening inflation expectations. The impact of energy prices(import weighted of oil and natural gas prices) on core inflation has also increased (Figure 5). The Central Bank (CBRT) released the second Inflation Report of the year and revised inflation forecasts significantly on the upside as its year-end inflation forecast for 2022 by 19.6pp to 42.8% (midpoint of the forecast range of 38.7% and 46.9%) and for 2023 by 4.7pp to 12.9%. However, without anchoring inflation expectations with clear monetary policy framework, to reach both short run and long run targets would be extremely difficult as we mentioned the permanent inflation factors are shifting on the upside.

Figure 3. Long Run Equilibrium Level, Annual Core-D



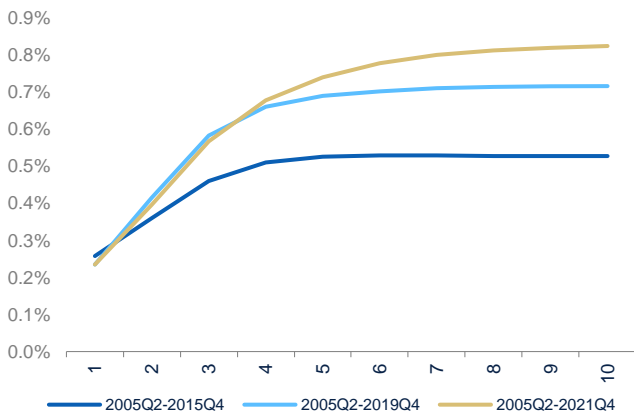
Source: Garanti BBVA Research, Turkstat, BVAR recursive method

Figure 4. Exchange Rate Pass-thru on Core D



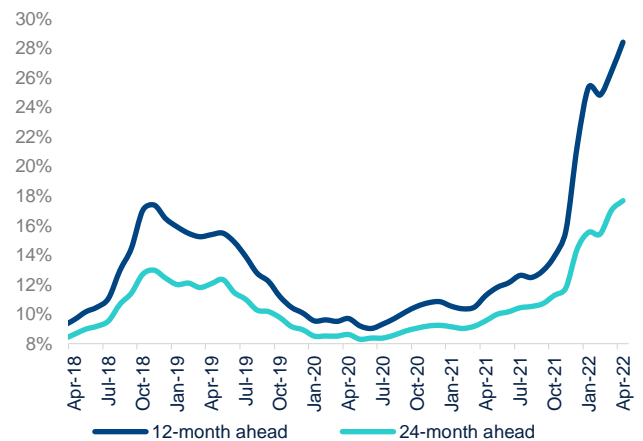
Source: Garanti BBVA Research, Turkstat, BVAR recursive method

Figure 5. Cumulative Impact of 10% rise in Energy Prices on Core D Inflation



Source: Garanti BBVA Research, Turkstat, BVAR

Figure 6. Inflation Expectations, annual %

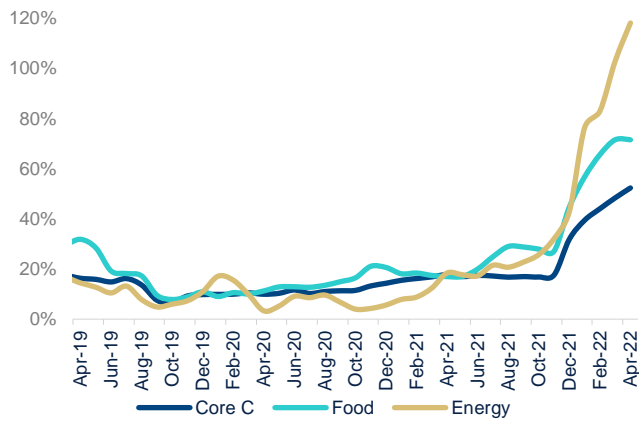


Source: Garanti BBVA Research, CBRT

Inflation outlook is getting more gloomy on intensifying upside risk factors

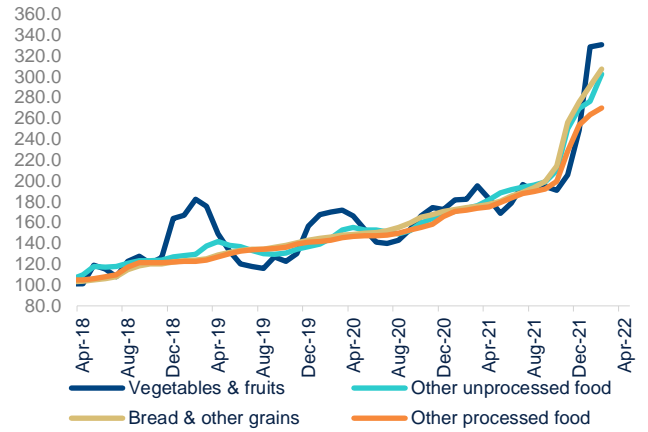
Global commodity prices and agricultural prices could remain elevated level for a while based on the Ukrainian war and still negative impact of global supply chain distortions stemmed from pandemic. Also, the stress on currency could increase further on the back of faster than expected monetary policy normalization in advanced economies(especially the FED), widened current account deficit accompanied with low reserves and deterioration in inflation expectations. We expect consumer inflation to hover above 70% till November before declining to 50% in December on the back of base effects. However, we acknowledge that the current dynamics and the negative factors put clear upside risks on our expectation.

Figure 7. **CPI Components, YoY**



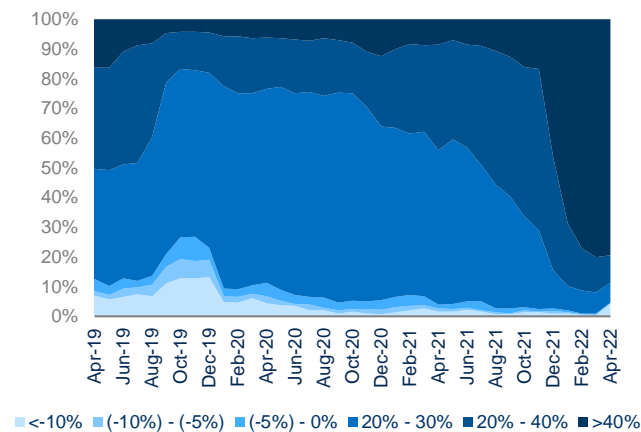
Source: Garanti BBVA Research, TURKSTAT

Figure 8. **Food Prices, January 2018 = 100**



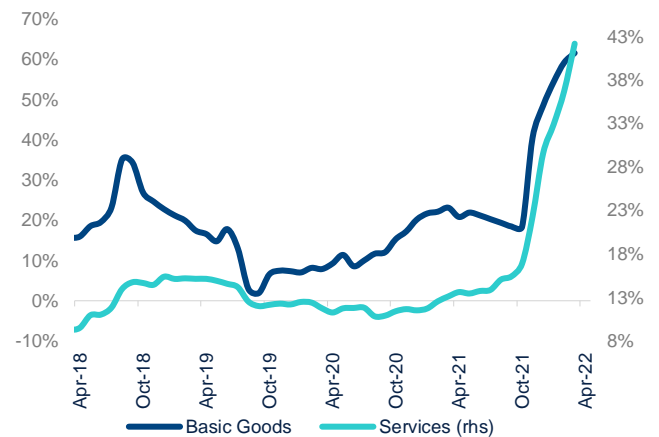
Source: Garanti BBVA Research, TURKSTAT

Figure 9. **Consumer Inflation Diffusion Map, YoY**



Source: Garanti BBVA Research, TURKSTAT

Figure 10. **Basic Goods and Services Inflation, YoY**



Source: Garanti BBVA Research, TURKSTAT

Figure 11. **CPI in Subcomponents**

	MoM	YoY
Total	7.25%	69.97%
Food & Non-alcoholic beverages	13.4%	89.1%
Beverage & Tobacco	4.0%	56.4%
Clothing & Textile	7.0%	26.2%
Housing	7.4%	61.1%
Household Equipment	4.9%	77.6%
Health	1.3%	36.0%
Transportation	5.1%	105.9%
Communication	2.9%	18.7%
Recreation & Culture	3.2%	43.3%
Education	2.9%	27.7%
Restaurants & Hotels	6.9%	69.3%
Misc. Goods & Services	0.9%	58.7%

Source: Garanti BBVA Research, Turkstat

Figure 12. **Domestic PPI in Subcomponents**

	MoM	YoY
Total	7.67%	121.82%
Mining & Quarrying	12.8%	125.9%
Manufacturing	7.3%	112.1%
Food Products	13.9%	115.2%
Textiles	4.6%	109.6%
Wearing Apparel	3.4%	42.1%
Coke & Petroleum Products	3.3%	249.6%
Chemicals	6.5%	115.4%
Other Non-Metallic Mineral	14.6%	159.1%
Basic Metals	1.1%	141.7%
Metal Products	4.8%	106.2%
Electrical Equipment	2.7%	99.7%
Electricity, Gas, Steam	8.0%	247.5%

Source: Garanti BBVA Research, Turkstat

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