Creating Opportunities

Turkey: Annual CPI got closer to 80%

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Consumer prices increased by 4.95% in June, slightly lower than market consensus (5.7%) and our expectation (5.5%), which resulted in an annual figure of 78.6%. The downside surprise was due to lower food prices, particularly processed food conflicting with the recent hikes in certain administrative food prices. Besides, domestic producer prices accelerated further by climbing up 6.8% mom and 138.3% yoy, keeping the cost push factors high. Looking ahead, we expect consumer inflation to accelerate above 90% in the coming months led by loose economic policies and significantly deteriorating inflation expectations. By year-end, we expect inflation to slow down to near 70% given positive base effects in the last two months of the year, assuming no substantial shocks on the foreign exchange rate. Furthermore, potentially longer than expected upsurge in global commodity prices and additional price hikes in administrative prices would worsen this outlook, implying that inflation would climb even higher.

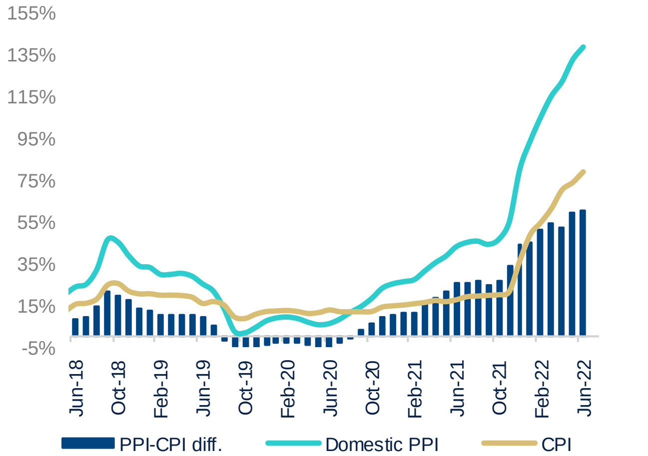
Lower realization on seasonal food prices and limited increase in core prices

Food prices continued to rise in June (1.4% mom) and led the annual figure to reach a new record level of 94.3%. Although both processed (7.5% mom) and other unprocessed food prices (3.4% mom) kept climbing due to price hikes in global food and commodity prices, seasonal factors contributed to the decrease in fresh fruit and vegetable prices (-15.2% mom). Energy prices continued to accelerate by 16.2% mom, resulting in an annual energy inflation of 151.3% on the back of utility and fuel price hikes during the month.

Consistent with our expectations, core prices slowed down compared to previous months but still remained high both in monthly (3.3% mom) and annual terms (57.26%), led by stronger cost push factors, ongoing robust domestic demand and currency depreciation. On the one hand, basic goods inflation decelerated to 2.8% mom, mainly due to weaker clothing and footwear (0.1% mom), whereas durable goods prices maintained a much stronger rise (3.6% mom). On the other hand, services price inflation deteriorated across the board rising 4% mom and 48.7% yoy, and signaling reinforced stickiness over core prices. Finally, despite domestic producer prices gearing down in monthly terms (6.8%), the annual PPI inflation reached 138.3%.

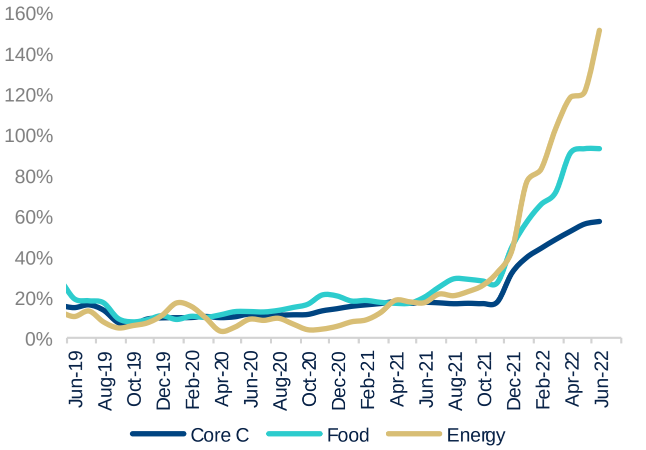
All in all, worsening inflation expectations, high global inflation and commodity prices, loose domestic policies, exchange rate depreciation and second round effects keep upside risks on the inflation outlook. The interim hike in minimum wages by near 30% will keep a spiraling effect on CPI, reaching 4.5pp mostly transmitted in the next two quarters, with 15% pass-thru from wages to CPI in our calculations.

Figure 1. **CPI vs Domestic PPI, YoY**



Source: Garanti BBVA Research, Turkstat

Figure 2. **CPI Components, YoY**

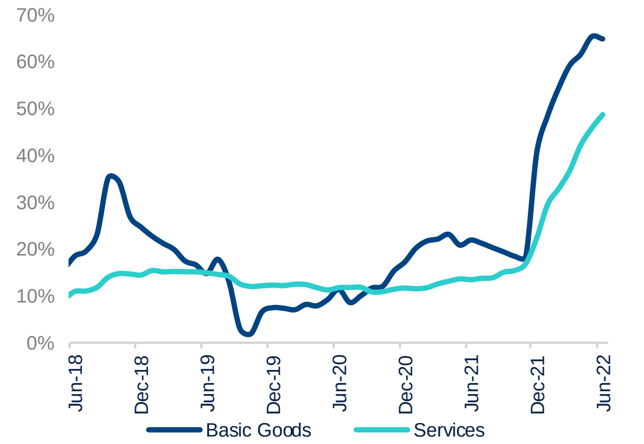


Source: Garanti BBVA Research, Turkstat

Inflationary pressures alive due to both domestic and global factors

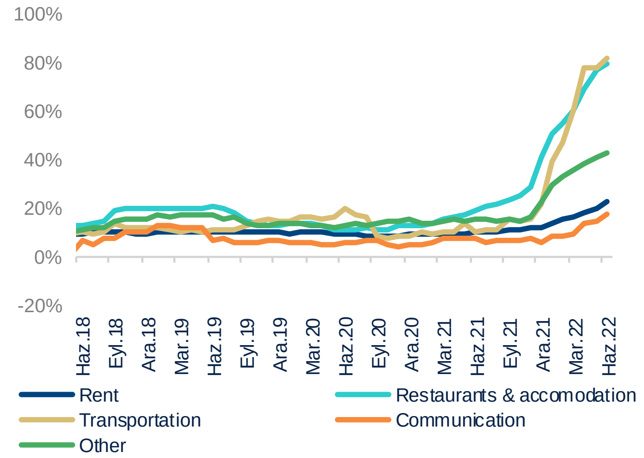
Domestic consumption stays strong on top of credit impulses and other loose economic policies and keeps pressure high on consumer prices without any anchor on price setting mechanism. Besides, longer than expected war conditions and post-pandemic supply side problems keep global commodity prices high. As a result, stronger cost push factors lead companies to easily pass them to consumer prices. Also, reinforced external financing needs and high dollarization in the economy keep the pressure on the exchange rate, which might well fuel the negative loop by means of both inflation expectations and production costs. Last but not least, wage adjustments remain crucial so it is obvious that inflationary pressures will likely strengthen more until a clear policy reaction is taken. We revise our year-end inflation forecast to near 70%, still with risks clearly on the upside. Therefore, the benefits from base effects at the end of the year get slimmer as price pressures remain elevated.

Figure 7. **Basic Goods and Services Inflation, YoY**



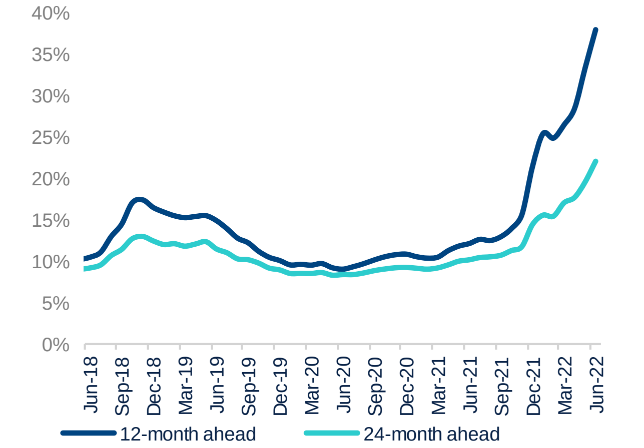
Source: Garanti BBVA Research, TURKSTAT

Figure 8. **Services Inflation, YoY**



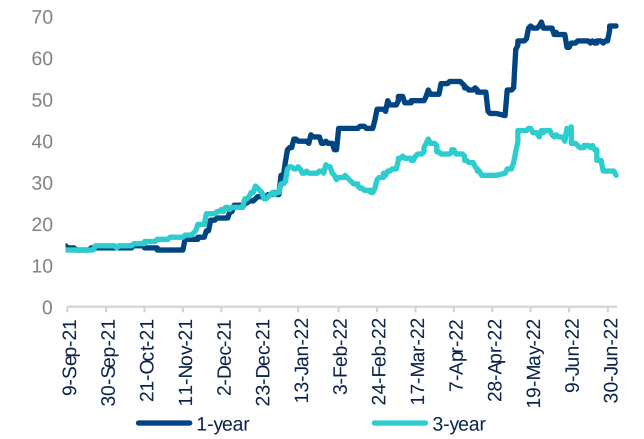
Source: Garanti BBVA Research, TURKSTAT

Figure 9. **Survey Based Inflation Expectations, YoY**



Source: Garanti BBVA Research, TURKSTAT

Figure 10. **Market Implied Inflation Expectations, YoY**



Source: Garanti BBVA Research, TURKSTAT

Figure 11. **CPI in Subcomponents**

	MoM	YoY
Total	**4.95%**	**78.62%**
Food & Non-alcoholic beverages	2.1%	93.9%
Beverage & Tobacco	2.6%	71.0%
Clothing & Textile	0.2%	27.0%
Housing	8.3%	75.1%
Household Equipment	4.0%	81.1%
Health	2.0%	39.3%
Transportation	10.6%	123.4%
Communication	3.6%	23.7%
Recreation & Culture	2.0%	50.5%
Education	2.4%	27.8%
Restaurants & Hotels	5.4%	79.6%
Misc. Goods & Services	4.4%	63.7%

Source: Garanti BBVA Research, Turkstat

Figure 12. **Domestic PPI in Subcomponents**

	MoM	YoY
Total	**6.77%**	**138.31%**
Mining & Quarrying	7.0%	142.7%
Manufacturing	6.3%	120.5%
Food Products	5.5%	131.7%
Textiles	7.7%	121.4%
Wearing Apparel	4.8%	49.6%
Coke & Petroleum Products	24.9%	297.3%
Chemicals	8.3%	130.2%
Other Non-Metallic Mineral	6.5%	183.6%
Basic Metals	1.1%	121.0%
Metal Products	5.2%	108.3%
Electrical Equipment	5.5%	98.2%
Electricity, Gas, Steam	9.5%	369.2%

Source: Garanti BBVA Research, Turkstat

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