Inflation Pulse

Türkiye | Worsening inflation trend keeps challenges

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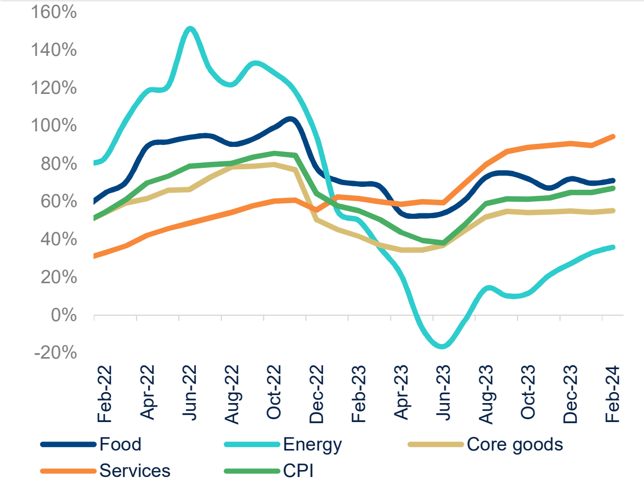
4 March 2024

Consumer prices rose by 4.53% in February, higher than our expectation and consensus (4.0% both), while annual consumer inflation accelerated to 67.07% from 64.86% the month before. The main deviation in our forecast was due to core inflation, led by services prices. According to our big data indicators, private consumption has most recently started to gain pace; and our financial conditions index signals somewhat an easing in overall financial conditions, keeping the challenges on inflation outlook. In the post-election period, we believe some level of fiscal prudence will be implemented and additional macro-prudential policies and quantitative measures will be used in order to strengthen the monetary transmission mechanism. Under the assumption of a gradual currency depreciation, expectations of household energy price hikes and the current policy rate throughout the year, we expect annual consumer inflation to reach 45% by 2024 year end. Following the most recent communication of the CBRT, we also assess that the likelihood of hiking the policy rate above 45% has increased. If so, we will revise our projections, accordingly.

Tighter financial conditions are needed to contain inflationary pressure

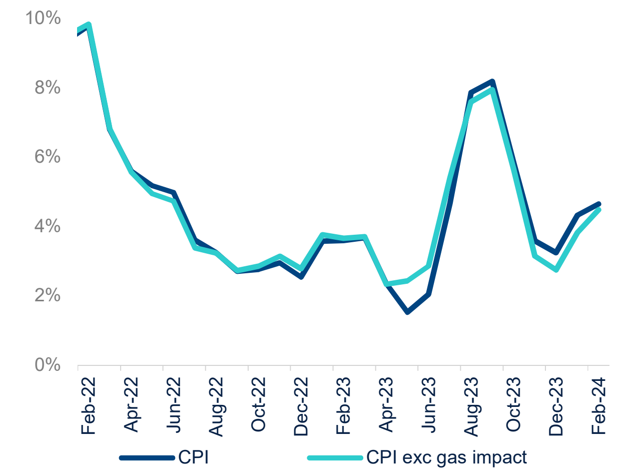
After the worsening in January (7-8% m/m if seasonal adjusted), core inflation (both B and C indexes) remained strong with almost 4% m/m in seasonal adjusted terms and resulted in an acceleration towards 5% in 3-month averages (vs. 4-4.5% in January and the CBRT target of 1.5% for 4Q24), according to our calculations. Therefore, annual core B inflation accelerated to 70.3% from 67.7%; and core C from 70.5% to 72.9%. The strong realizations in services prices confirm the continuing impact from second round effects mainly driven by the recent high adjustment in wages and strengthening inflation inertia. In monthly terms, services inflation stayed robust with 5.7% m/m (vs. 12.1% prev.) due to the continuation of sharp increases in rent (7.1% m/m) and restaurant & hotel prices (5.4% m/m). Given the resilient services prices (if seasonal adjusted, 3-month average of 7.2%), annual services inflation reached its historical peak with 94.4% (vs. 89.7% prev.). On the other hand, the slowdown in basic goods prices (1.6% m/m vs. 3.6% m/m prev.) was noteworthy thanks to durable goods (1.5% m/m) and clothing and footwear prices (0.1% m/m). The seasonal adjusted monthly goods inflation improved to the level below its Dec23 realization; however, its 3-month average trend still rose to 2.9% (vs. 2.6% in January). All in all, our indicators signal that inflation trend has started to worsen since the beginning of the year (from around 3% in Dec23 to almost 4.5% in Feb24), confirming the need for tighter financial conditions.

Figure 1. **CONSUMER INFLATION SUBCOMPONENTS** (YoY change)



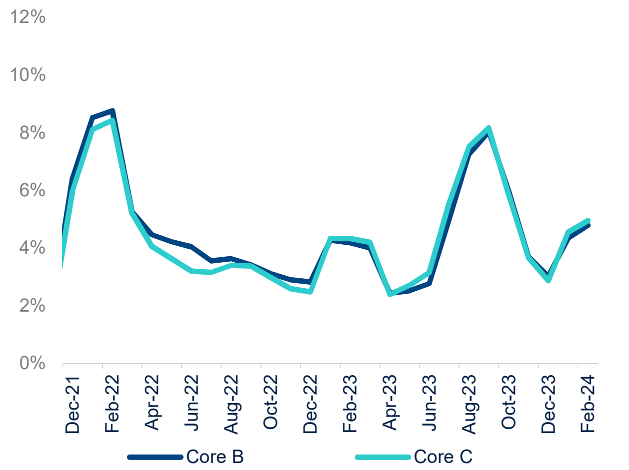
Source: Garanti BBVA Research, TURKSTAT

Figure 2. **CONSUMER INFLATION INDICATORS** (seasonal adj., 3-month avg.)



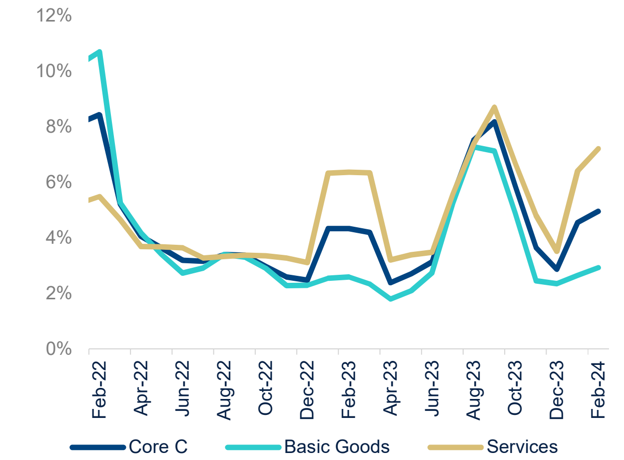
Source: Garanti BBVA Research, TURKSTAT

Figure 3. **CONSUMER INFLATION INDICATORS** (seasonal adj., 3-month avg.)



Source: Garanti BBVA Research, TURKSTAT

Figure 4. **CONSUMER INFLATION INDICATORS** (seasonal adj., 3-month avg.)



Source: Garanti BBVA Research, TURKSTAT

Food prices rose by 8.5% m/m, driven by a broad-based acceleration in its sub-items. More specifically, unprocessed food prices geared up to 9.3% m/m (vs. 7% m/m prev.), while processed food prices, which increased by 3.6% m/m on average in the last five months, accelerated to 7.3% (vs. 3.6% prev.). The lagged effects of the price hikes in dairy products coupled with increases in red and white meat prices (most likely seen ahead of Ramadan) were the main drivers of the strong realizations in food prices. Hence, annual food inflation gained pace to 71% (vs. 69.6% prev.).

Energy prices slowed down to 3.0% m/m (6.1% m/m prev.) due to a more moderate increase in gasoline prices compared to last month. On the other hand, annual energy inflation climbed up to 36% y/y from 32.9% y/y the month before, mainly led by low base effects. Meanwhile, domestic producer prices rose by 3.7% m/m (4.1% m/m prev.), confirming the continuation of cost push factors on consumer inflation, and led to an acceleration in its annual inflation to 47.3% from 44.2% in January.

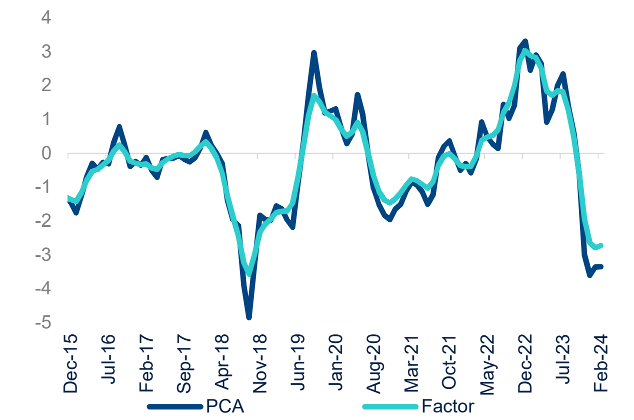
Reinforced hawkish stance, though the pressure of inflationary factors lingers on

In the latest MPC meeting, the CBRT maintained the policy rate at 45%. However, the messages in the MPC press release involved a more hawkish tone with a more concerned view on the inflation outlook. In the press meeting of the first Inflation Report of the year, the CBRT governor had pointed to the 3-month average seasonal adjusted inflation moving at around 4% in January and mentioned about the target of reducing it to 1.5% in 4Q24. In this respect, the CBRT repeated the commitment to keep the current policy rate until there is a significant and sustained decline in the monthly inflation trend and until inflation expectations converge to the projected forecast range (30-42% for 2024 end, 7-21% for 2025 end). They also strengthened their communication by adding that they are ready for further tightening if the inflation trend does not improve as targeted but primarily refer to additional macro-prudential measures and quantitative tightening tools in order to strengthen the monetary transmission mechanism.

In this regard, we assess that the challenges on inflation outlook have recently increased: First, the financial conditions, which had shown the signs of tightening in the last quarter of 2023, do not tighten further (Figure 5). Second, our big data consumption indicators point to some acceleration in consumption (Figure 6), slowing down the needed rebalancing in the economy. Third, according to the February market participants' survey of the CBRT, inflation expectations for 2024 end and 2025 end stood at 43% and 25%, far above the CBRT interim targets of 36% and 14% (Figure 7). This is why we believe that the likelihood of raising the policy rate above 45% has increased and put an upward bias on our expectation of a constant policy rate throughout the year.

All in all, high course of food inflation, stronger than expected wage adjustments and administrative price hikes led to a continuing deterioration in inflation trend in February. Under the assumption of a gradual currency depreciation, expectations of significant household energy price hikes and the current policy rate throughout the year, we expect annual consumer inflation to reach 45% by 2024 year end. If a clearer commitment against inflation prevails with more restrictive economic policies in post-election period, we will revise our projections, accordingly.

Figure 5. **GARANTI BBVA FINANCIAL CONDITIONS INDEX**[1] (standardized, + easing, - tightening)

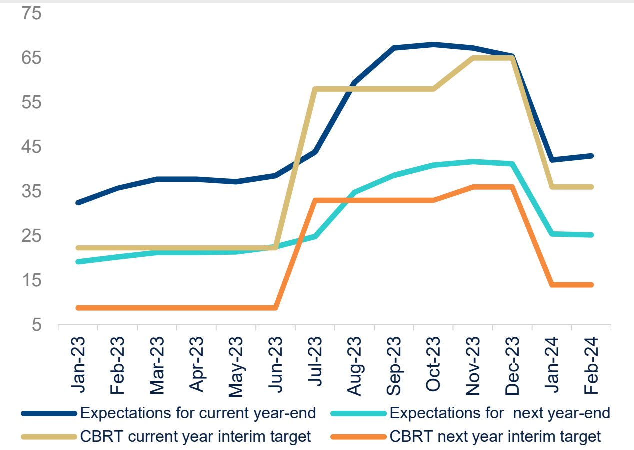


Source: Garanti BBVA Research, TURKSTAT

Figure 6. **GARANTI BBVA BIG DATA CONSUMPTION INDICATORS** (28-day sum, real YoY)

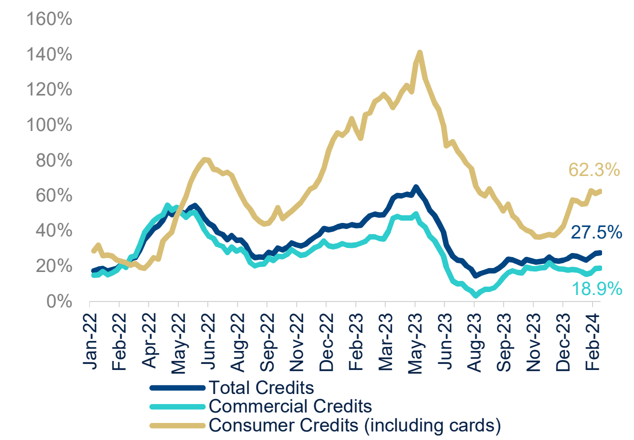
Source: Garanti BBVA Research, TURKSTAT

Figure 7. **CBRT MARKET PARTICIPANTS SURVEY**



Source: Garanti BBVA Research, CBRT

Figure 8. **TOTAL CREDIT GROWTH** (13-Week Annualized Trend)



Source: Garanti BBVA Research, BRSA

Figure 9. **CPI SUBCOMPONENTS**

	MoM	YoY
Total	**4.53%**	**67.07%**
Food & Non-alcoholic beverages	8.3%	71.1%
Beverage & Tobacco	0.5%	63.1%
Clothing & Textile	0.2%	43.4%
Housing	3.4%	49.1%
Household Equipment	3.0%	62.9%
Health	3.6%	81.3%
Transportation	2.8%	78.0%
Communication	4.3%	51.9%
Recreation & Culture	3.2%	65.4%
Education	12.8%	91.8%
Restaurants & Hotels	5.4%	94.8%
Misc. Goods & Services	3.5%	61.9%

Source: Garanti BBVA Research, TURKSTAT

Figure 10. **DOMESTIC PPI SUBCOMPONENTS**

	MoM	YoY
Total	**3.74%**	**47.29%**
Mining & Quarrying	4.3%	68.1%
Manufacturing	4.6%	56.7%
Food Products	6.0%	62.8%
Textiles	3.7%	53.3%
Wearing Apparel	5.2%	64.4%
Coke & Petroleum Products	10.3%	59.7%
Chemicals	3.1%	50.1%
Other Non-Metallic Mineral	3.9%	42.1%
Basic Metals	5.0%	50.4%
Metal Products	2.8%	69.2%
Electrical Equipment	2.8%	57.5%
Electricity, Gas, Steam	-5.0%	-30.7%

Source: Garanti BBVA Research, TURKSTAT

[1] Based on the study done by Bahçeşehir University Financial Research and Implementation Center (BFRC), we calculate the financial conditions index. The following variables are included; CDS, ex-ante 2 year yield (real), real exchange rate, real stock price, portfoli inflows, yield curve slope(10y-2y), real loans rate.

BBVA Research

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