

Inflation Pulse

# Türkiye | Inflation trend fell only limitedly

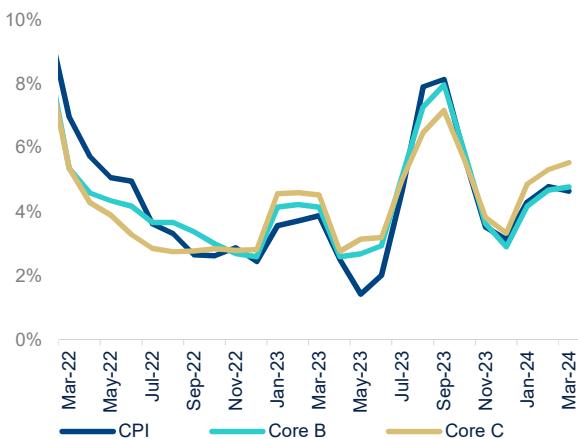
Adem İleri / Tugce Tatoglu / Gul Yucel  
3 April 2024

Consumer prices rose by 3.16% in March, both lower than our expectation and consensus (3.5% and 3.6%, respectively), while annual inflation accelerated to 68.5% from 67.07% the month before. The main deviation in our forecast was due to the slower than expected food inflation. Core inflation trend kept worsening, this time driven by basic goods prices due to the fast exchange rate pass-through. Our big data indicators show a most recent acceleration in goods consumption, led by durable goods. Besides, our financial conditions index has started to signal a tighter stance but the tightening occurs very slowly, making it hard to start anchoring inflation expectations. We expect annual consumer inflation to reach 45% by 2024 end under the assumption of 3.5% GDP growth this year, gradual currency depreciation, continuing demand restrictive policies and no substantial additional wage hikes. Though, given the increasing likelihood of more aggressive tightening after the election, we will assess risks on our exchange rate and inflation forecasts.

## Deterioration in basic goods prices' trend while inertia remained strong

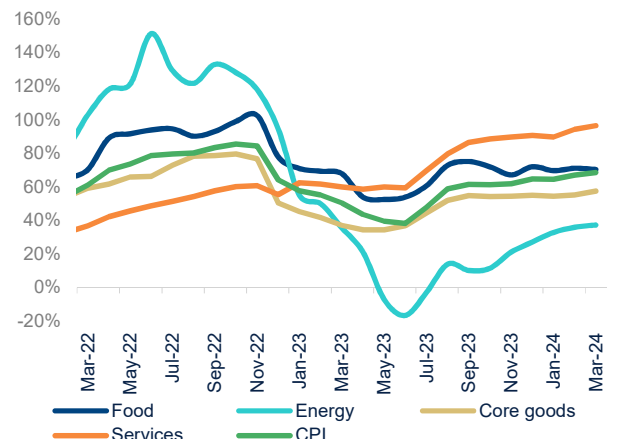
Core C inflation (excluding food, energy and gold) remained steady at 3.5% m/m in March thanks to the slight improvement in services inflation; while there was a deterioration in basic goods prices led by the exchange rate sensitive items. With this, annual core C inflation accelerated further from 72.9% to 75.2%. On seasonal adjusted series, core C inflation retreated limitedly to 3.9% m/m (vs 4.4% m/m in Feb.) but its 3-month trend deteriorated further to 5.5% (Figure 1). Despite previous month's slow-down, basic goods inflation climbed up to 2.9% m/m from 1.6% m/m (if seasonal adjusted, 3.2% m/m vs. 2.6% m/m in Feb) on the back of durable goods prices such as furniture (5% m/m) and auto prices (2.5% m/m), which supports our argument that the monetary policy tightening to cool down domestic demand is not adequate so far. As known from the past experience, a clear and sustained improvement in services inflation can only be attained after the gains in basic goods inflation. In this respect, services inflation fell to 4.2% m/m from 5.7% (if seasonal adjusted, 4% m/m vs 5.7% in Feb), mainly led by the negative monthly inflation in transportation services (-0.2% mom). Yet, other sub-items inflation remained solid. More specifically, rental prices rose by 6.3% m/m (7.1% prev.) following its unsustainable increase since Jul23 (7.7% on average), while restaurant & hotel prices maintained its strong increase with 4% m/m (5.4% m/m prev.). Other services inflation retreated to only 4.1%, mainly due to education inflation (13.1% m/m). The quarterly acceleration in services prices (21% q/q in 1Q24 vs. 15.2% q/q in 4Q23) confirmed the upward pressure from strong wage adjustments in January and strengthening inflation inertia in this period. All in all, annual services inflation gained pace to 96.5% from 94.4% in Feb and reached its historical peak.

Figure 1. CONSUMER INFLATION INDICATORS (seasonal adj., monthly, 3-month average)



Source: Garanti BBVA Research, TURKSTAT

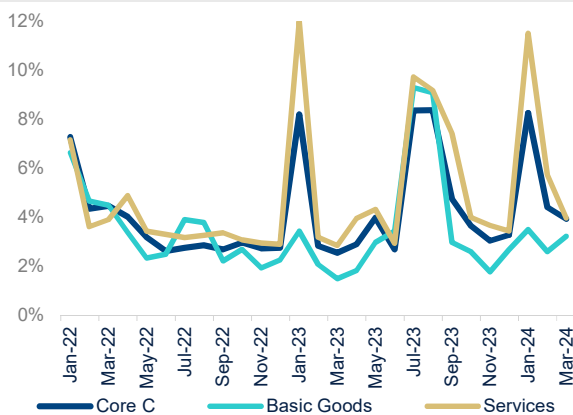
Figure 2. CONSUMER INFLATION SUBCOMPONENTS (YoY change)



Source: Garanti BBVA Research, TURKSTAT

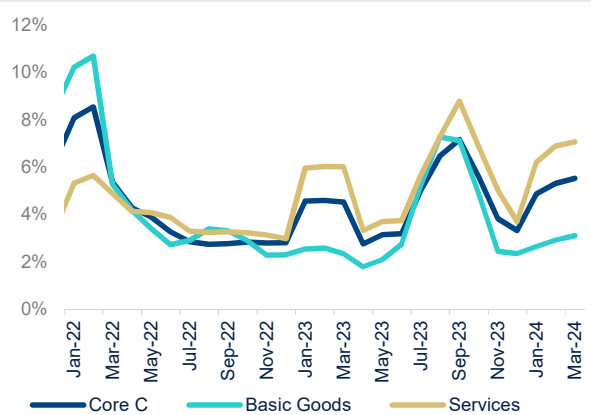
Food prices increased by 3.5% m/m (vs. 8.5% m/m in Feb) on top the rise in other unprocessed food prices (8.9% m/m vs. 6.5% m/m prev.), while fresh fruit and vegetable prices remained almost flat with 0.6% m/m (13.7% m/m prev.). The increase in processed food prices, on the other hand, remained limited with 1.4% m/m, following its previous realization of 7.3% m/m. Despite the decision at the beginning of the month that meat prices would remain unchanged in some markets during Ramadan, red meat prices accelerated by 17% m/m, which was the main driver for the acceleration in unprocessed food prices. Hence, annual food inflation stayed strong with 70.5% (vs. 71% previously). On the other hand, energy prices inflation slowed down further to 1.4% m/m (3% m/m previously) due to a relatively limited increase in gasoline price compared to last months. Yet, the low base effect led annual energy prices to climb up to 37.3% from 36% the month before. Last but not the least, cost push factors also underpinned the deterioration in inflation outlook as domestic producer prices rose by 3.3% m/m (3.7% m/m previously), and its annual inflation accelerated to 51.5% from 47.3%.

Figure 3. **CONSUMER INFLATION INDICATORS**  
(seasonal adj., monthly)



Source: Garanti BBVA Research, TURKSTAT

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



Source: Garanti BBVA Research, TURKSTAT

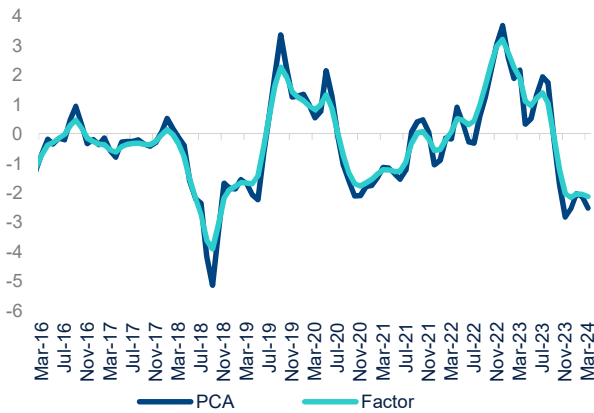
## Higher than expected inflation and strengthening dollarization led the CBRT to react

Despite the tightening in monetary policy until March, inflationary pressures have not yet shown signs of moderation. First, tightening in financial conditions is not enough to contain the acceleration in consumption ahead of the election (Figure 5). Therefore, domestic demand remained strong, as confirmed by our big data consumption indicators (Figure 6) and still strong consumption goods imports. Second, recent strong inflation realizations on top of solid demand led inflation expectations to deteriorate further. According to the March market participants' survey of the CBRT, inflation expectations for 2024 and 2025 year-end increased to 44% and 26% (Figure 7), remaining far above the CBRT interim targets of 36% and 14%, respectively. Third, high inflation expectations and solid demand also resulted in consumer prices to be highly sensitive to the exchange rate (Figure 8). Last but not the least, increasing foreign currency demand of the residents prior to the local election brought further pressure on the CBRT reserves, while the indirect measures of the CBRT to tighten the monetary stance backlashed and the CBRT was finally pushed to deliver the positively surprising rate hike of 500 bps in March MPC meeting with a wider interest rate corridor.

To attain 36% year end inflation target, average monthly inflation in the remaining nine months should be closer to 1.9%, while the recent trend (3 month avg.) is hovering around 4.5%. We expect the CBRT to keep its interim inflation targets of 36% and 14% for 2024 and 2025 in next inflation report (May 9). If so, we envisage the monetary policy to remain tight for longer with additional demand restrictive policies. In this respect, new macro-prudential measures, particularly on consumer credit cards would be implemented. Fiscal stance excluding the needed earthquake spending will likely become more restrictive and financial conditions will become tighter in the coming period.

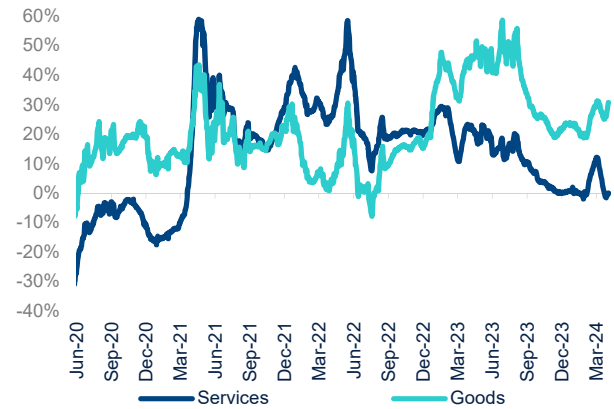
To sum up, we expect annual consumer inflation to reach 45% by 2024 year end under the assumption of 3.5% GDP growth, gradual currency depreciation, continuing restrictive policies and no substantial additional wage hikes. We assess an increasing likelihood of more aggressive tightening after the election, which might put downside risk on our exchange rate and inflation forecasts. If inflation eases below our expectation, the CBRT could start an easing cycle with very gradual steps in 4Q24.

Figure 5. **GARANTI BBVA FINANCIAL CONDITIONS INDEX<sup>1</sup>** (standardized, + easing, - tightening)



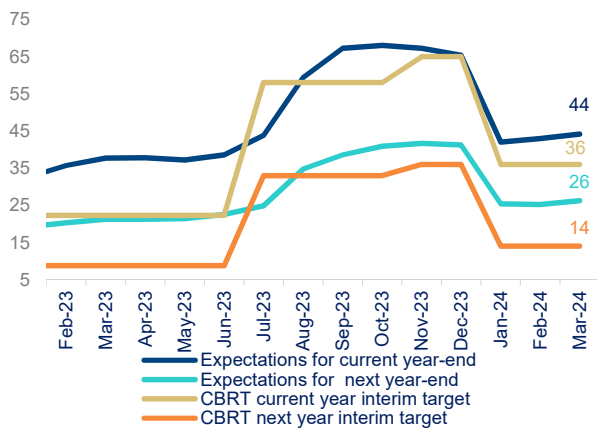
Source: Garanti BBVA Research, TURKSTAT

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



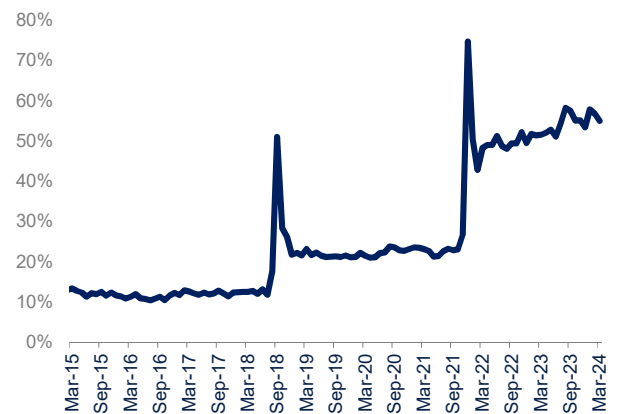
Source: Garanti BBVA Research, TURKSTAT

Figure 7. **CBRT MARKET PARTICIPANTS SURVEY INFLATION EXPECTATIONS (%)**



Source: Garanti BBVA Research, CBRT

Figure 8. **EXCHANGE PASS-THROUGH ON CORE D INFLATION (Recursive Method)**



Source: Garanti BBVA Research, BRSA

Figure 9. **CPI SUBCOMPONENTS**

	MoM	YoY
<b>Total</b>	<b>3.16%</b>	<b>68.50%</b>
Food & Non-alcoholic beverages	3.4%	70.4%
Beverage & Tobacco	0.0%	63.0%
Clothing & Textile	2.6%	50.1%
Housing	3.4%	51.2%
Household Equipment	3.2%	63.7%
Health	1.4%	80.3%
Transportation	1.7%	79.9%
Communication	5.6%	59.5%
Recreation & Culture	3.7%	66.8%
Education	13.1%	104.1%
Restaurants & Hotels	4.0%	95.0%
Misc. Goods & Services	3.2%	62.7%

Source: Garanti BBVA Research, TURKSTAT

Figure 10. **DOMESTIC PPI SUBCOMPONENTS**

	MoM	YoY
<b>Total</b>	<b>3.29%</b>	<b>51.47%</b>
Mining & Quarrying	3.3%	71.2%
Manufacturing	3.5%	58.9%
Food Products	4.4%	62.5%
Textiles	4.7%	58.4%
Wearing Apparel	2.7%	66.7%
Coke & Petroleum Products	-1.0%	65.9%
Chemicals	3.4%	54.6%
Other Non-Metallic Mineral	2.2%	42.4%
Basic Metals	3.9%	51.6%
Metal Products	3.7%	72.7%
Electrical Equipment	2.6%	59.6%
Electricity, Gas, Steam	1.4%	-18.9%

Source: Garanti BBVA Research, TURKSTAT

<sup>1</sup> 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, portfolio inflows, yield curve slope(10y-2y), real loans rate.

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### **ENQUIRIES TO:**

Garanti BANKASI A.Ş. Nispetiye Mah. Aydar Cad. No:2 34340 Levent Beşiktaş İstanbul.  
Tel.: +90 212 318 18 18 (ext 1064)  
[www.bbvarresearch.com](http://www.bbvarresearch.com)