

Türkiye | Encouraging surprises, underlying strains in July CPI

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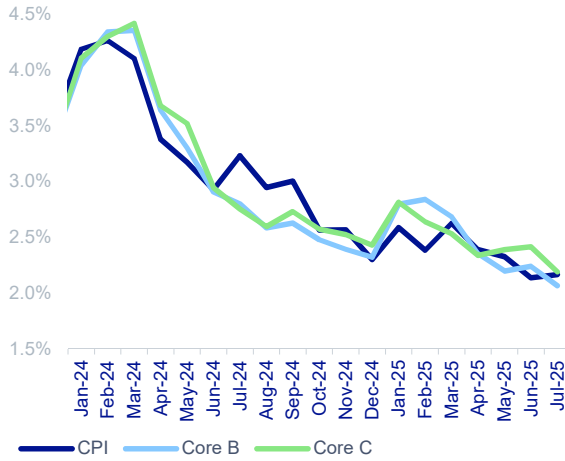
- According to our calculations, seasonally adjusted (s.a.) monthly consumer inflation considerably accelerated with 2.6% m/m (up from 2.0% in June). When excluding the impact of one off factors (s.a. 0.9pp) stemming from administered prices, seasonally adjusted monthly consumer inflation stayed below 2%.
- While the deterioration in seasonal adjusted services inflation continued, but at least not broad based, the improvement in basic goods inflation was marginal despite the support from clothing inflation. Hence, core inflation remained steady at around 2.2% (almost the same in the last 3 months).
- Despite the acceleration in processed food inflation, the deflation in the fresh fruit and vegetable prices and other unprocessed food supported the improvement in food inflation. Furthermore, cost push factors remained limited.
- Weaker domestic demand contributes to disinflation; however, risks to the inflation outlook remain elevated due to unanchored high inflation expectations, backward-looking pricing behavior, limited support from fiscal policy so far, and ongoing uncertainties surrounding energy and food prices driven by geopolitical risks and the impact of frost.
- Recent monthly inflation figures were lower than expected, creating downside risk to our near term inflation forecasts. Nevertheless, persistent uncertainties surrounding the inflation outlook keep us prudent. Therefore, assuming adequate real interest levels via gradual policy rate cuts, we have revised downside our year end inflation forecast to 30% from 31%.

Headline Up on Administered Prices, Core Holds Steady

Consumer prices rose by 2.06% m/m in July (vs. 1.37% in June) with an acceleration on the back of administered prices and services, which still surprised to the downside relative to both the consensus (2.40%) and our expectation (2.50%) due to weaker than expected food prices. As a result, annual inflation eased to 33.5% in July from 35.05% in June. Favorable dynamics in fresh food and clothing helped dampen the headline figure, despite administered prices contributing around 1pp, and services inflation remaining elevated.

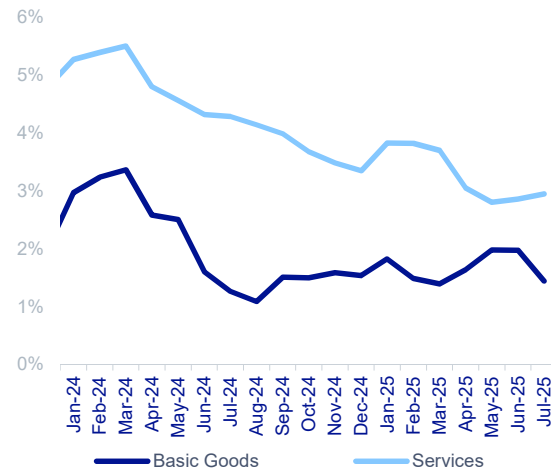
According to our calculations, seasonally adjusted CPI materialized as 2.6%, compared to 1.9% previously. Therefore, when excluding the impact of one off factors, seasonally adjusted monthly consumer inflation stayed below 2%. The 3-month headline trend slightly edged up to 2.17% in July from 2.14% in June, as the base still reflects the high April inflation, which was impacted by the pass-through of currency depreciation in late March.

Figure 1. Consumer Inflation Indicators
(seasonal adj., monthly, 3-month average)



Source: Garanti BBVA Research, TURKSTAT

Figure 2. Core C Inflation Indicators
(seasonal adj., monthly, 3-month average)

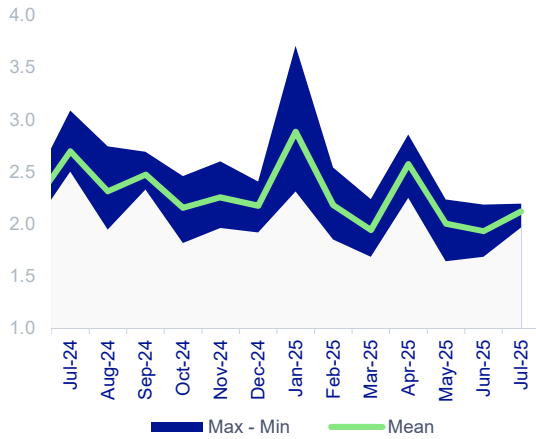


Source: Garanti BBVA Research, TURKSTAT

According to our calculations, the average of the underlying trend indicators monitored by the CBRT worsened, rising to 2.1% in July from 1.9% previously. Underlying trend indicators excluding extreme values also deteriorated, suggesting broad-based upward price adjustments in July. The median rose to 2.0% from 1.9%, satrim increased to 2.0% from 1.7%, and v_1 climbed to 2.2% from 1.7%. However, as the upper-end exclusions mainly reflect administered items and the lower-end exclusions are concentrated in categories like clothing, the data suggests that pricing behavior may be improving amid weaker demand. Supporting this view, the 3rd quantile declined to 2.8% from 3.2%, while the 1st quantile increased slightly to 0.9% from 0.8%, which constitutes only a limited deterioration given the timing of wage adjustments and the high share of adjusted prices in July. Core C inflation remained stable around 2.2%, as improvements in basic goods inflation offset the deterioration in services. Core B inflation, however, rose to 2.2% from 2.0% due to a rise in processed food prices. The dynamic factor model also points to stable inflation dynamics around 2.2%, though with a slight downward drift.

Overall, the 3-month trend of underlying inflation only marginally eased to 2.0% from 2.2%, largely due to the exclusion of the high April figure. The data indicates that firms refrained from increasing prices amid weak demand; however, unanchored inflation expectations continue to exert upward pressure, especially on less frequently adjusted services prices such as education and rent. Looking ahead, as a significant portion of price adjustments took place in July, we expect the inflation trend to slow in August. The trajectory will be shaped primarily by inflation expectations, as demand-related pressures already appear restrictive.

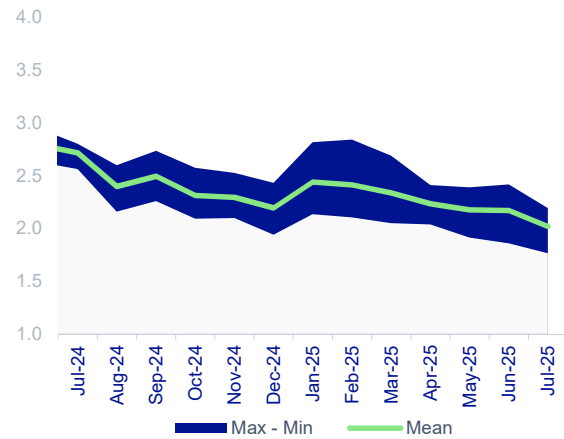
Figure 3. Consumer Inflation Indicators*
(seasonal adj., monthly)



Source: Garanti BBVA Research, TURKSTAT

* Mean represents the average of different trend indicators including seasonally adjusted B, C, SATRIM, Median, inflation excluding volatile items and dynamic factor. The highlighted area shows the maximum and minimum range.

Figure 4. Consumer Inflation Indicators*
(seasonal adj., monthly, 3-month average)



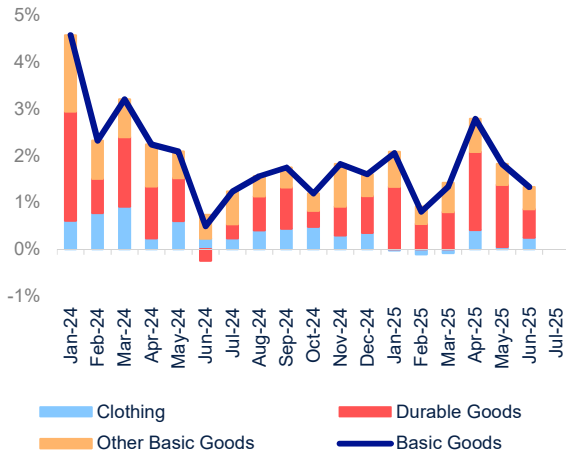
Source: Garanti BBVA Research, TURKSTAT

In seasonally adjusted terms, basic goods inflation declined slightly to 1.2% from 1.3%, reflecting the effects of deflation in clothing (-0.8% vs. 1.16%), relatively moderate increases in durable goods prices (1.6% vs. 1.2%), and somewhat subdued inflation in other basic goods (2.0% vs. 1.6%). These outcomes highlight the dampening effect of weak demand under tight financial conditions and limited purchasing power. On the other hand, services inflation deteriorated to 3.2% from 3.0%, primarily due to a sharp increase in communication services inflation (5.7% vs. 1.5%), along with a more modest rise in restaurant and hotel inflation (2.2% vs. 2.0%). In contrast, rent inflation declined slightly to 4.2% from 4.3%, transportation to 2.25% from 2.9%, and other services to 3.2% from 3.4%, although all remain at elevated levels. The persistence of high inflation in less frequently adjusted services categories, despite weak demand, underscores the role of backward-looking inflation expectations as a key obstacle to disinflation.

Seasonally adjusted food and non-alcoholic beverage inflation declined to 1.2% in July from 1.4% in June, contributing positively to the headline figure. This improvement was driven primarily by fresh food deflation, which came in at -2.5% (vs. 3.3%), due to excess supply in certain items. However, inflation in other food categories increased: unprocessed food inflation rose to 1.5% from 1.2%, while processed food inflation accelerated to 2.2% from 1.0%. Given the expected impact of agricultural frost on fresh food prices and the absence of significant improvement in other food items, food inflation remains a risk to the overall outlook.

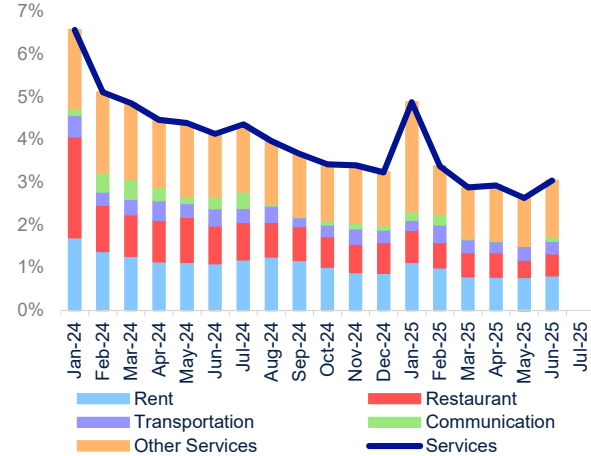
Energy inflation jumped to 7.35% in July, largely reflecting a 24.6% increase in natural gas prices and the rise in special consumption tax on fuel at the beginning of the month. On the producer side, domestic PPI rose by 1.7% m/m in July, with annual inflation slightly declining to 24.19% from 24.5%. Increases in natural gas prices (7.9%) and fuel contributed to intensifying cost-push pressures. Nevertheless, subdued domestic demand suggests that the pass-through to consumer prices may stay limited.

Figure 5. Contributions to Basic Goods Inflation (seasonal adj., monthly, pp)



Source: Garanti BBVA Research, TURKSTAT

Figure 6. Contributions to Services Inflation (seasonal adj., monthly, pp)



Source: Garanti BBVA Research, TURKSTAT

The pace of disinflation will depend on the effectiveness of policy mix

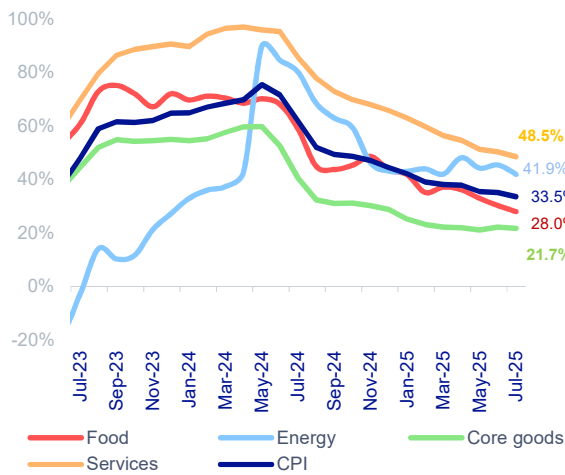
July consumer inflation revealed an acceleration on the back of both goods reflecting the administered price hikes and the recent appreciation of Euro and services inflation keeping strong inflation inertia with its seasonally adjusted 3-month average nearing 3% since February. Once the one-off effects are excluded, seasonally adjusted monthly inflation stayed below 2%, which still requires a high level prudence since core inflation trend stood at nearly 2.2% in the last 3 months, fueled by the stickiness of services on the back of backward indexation.

Secondly, inflation expectations, being an important factor in achieving disinflation, remain elevated despite some improvement among market participants and real sector. According to the market participants survey of the CBRT, 12- and 24-month annual inflation expectations declined only very slightly with 23.39% (vs. 24.56% prev.) and 17.08% (vs. 17.35% prev.), respectively while the year-end inflation expectations for 2025 materialized as 29.7%. While 12 month ahead real sector expectations fell only marginally to 39.0% from 39.8%, households' expectations worsened to 54.5% (vs. 53.0%). Overall, both market participants, real sector and households continue to expect inflation levels above the CBRT forecast range (19-29% for 2025 end). We will closely monitor the inflation and output gap projections, as well as the Central Bank's messages regarding potential policy actions, in the third inflation report to be published on August 14.

Despite fastening inflation in both unprocessed and processed food inflation, the deflation in fresh food and vegetables limited the pressures over the food inflation. However, the potential impact from the agricultural frost has not yet been fully reflected and may be more clearly seen in the upcoming months, preserving the uncertainty regarding food inflation. The high volatility in energy prices stemming from geopolitical and global uncertainties continue to pose risk on inflation outlook. Finally, the support from fiscal policy has so far remained limited so the Medium Term Program (MTP), likely to be announced in early September, could shed more light on the extent of fiscal consolidation in the upcoming near future.

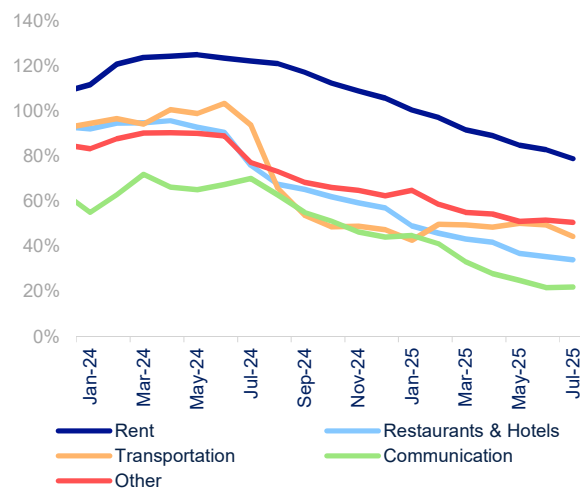
Although recent monthly inflation figures were lower than expectations—creating downside risk to our inflation forecast—the known unknowns are clouding the disinflation outlook. Hence, we expect the CBRT to preserve its cautious stance with gradual rate cuts, allowing real interest rates to remain at adequate levels. We have slightly revised our 2025 year-end inflation expectation from 31% to 30%, considering the better-than-expected realizations in the previous months. However, the magnitude of rate cuts in the upcoming MPC meetings and the degree of fiscal consolidation will be key factors to support disinflation going forward.

Figure 8. Consumer Inflation Subcomponents (YoY)



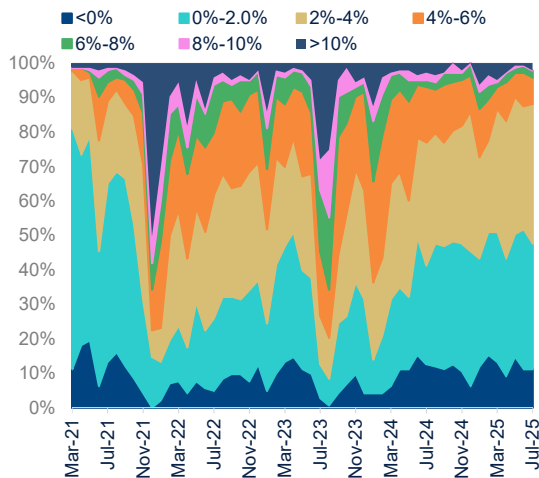
Source: Garanti BBVA Research, TURKSTAT

Figure 9. Services Inflation (YoY)



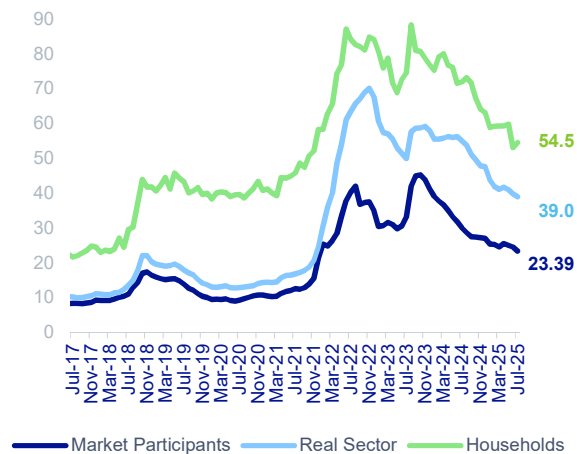
Source: Garanti BBVA Research, TURKSTAT

Figure 10. CPI Diffusion Index



Source: Garanti BBVA Research, TURKSTAT

Figure 11. Inflation Expectations (12 Month Ahead, %)



Source: Garanti BBVA Research, TURKSTAT

Figure 12. CPI Subcomponents

	MoM	YoY
Total	2.06%	33.52%
Food & Non-alcoholic beverages	0.1%	28.0%
Beverage & Tobacco	5.7%	27.8%
Clothing & Textile	-5.8%	10.7%
Housing	5.8%	62.0%
Household Equipment	1.6%	30.1%
Health	2.8%	37.5%
Transportation	2.9%	26.6%
Communication	4.2%	19.6%
Recreation & Culture	2.1%	27.5%
Education	2.7%	75.5%
Restaurants & Hotels	2.2%	34.2%
Misc. Goods & Services	1.9%	34.9%

Source: Garanti BBVA Research, TURKSTAT

Figure 13. PPI Subcomponents

	MoM	YoY
Total	1.73%	24.19%
Mining & Quarrying	3.7%	28.3%
Manufacturing	1.6%	24.0%
Food Products	0.2%	25.1%
Textiles	1.7%	17.2%
Wearing Apparel	3.2%	28.2%
Coke & Petroleum Products	6.4%	10.7%
Chemicals	2.7%	24.7%
Other Non-Metallic Mineral	1.3%	17.2%
Basic Metals	0.8%	16.7%
Metal Products	3.0%	25.8%
Electrical Equipment	1.8%	25.6%
Electricity, Gas, Steam	2.2%	22.1%

Source: Garanti BBVA Research, TURKSTAT

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