

Turkey: CPI surprised on the upside with 36.1%

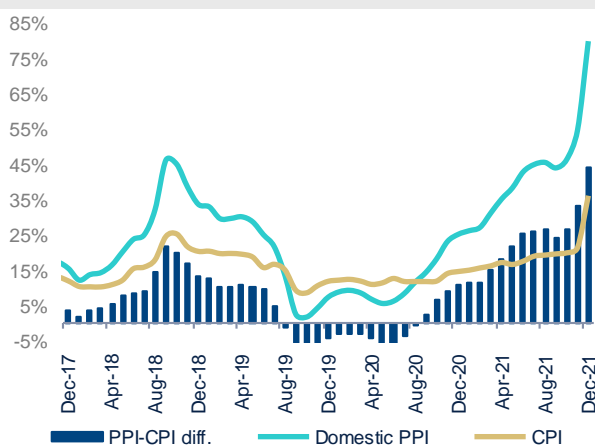
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3 January 2022

Consumer prices increased by 13.58% in December significantly above expectations (BBVA Research 10%, Consensus 8.5%) and resulted in an annual inflation of 36.1% up from 21.3% the month before. Our main deviation stemmed from core prices inflation, which confirmed faster than expected pass-thru from cost factors. Domestic producer prices also surprised on the upside, which will likely accelerate further due to energy price hikes and pressures from recent currency depreciation. Looking ahead, continuing exchange rate pass-thru led by the high volatility in the currency, strengthening cost-push factors from recent utility price hikes, high food inflation and reinforced pressures from imported prices clearly raise upside risks and uncertainty on the inflation outlook. On the other hand, ongoing consumption growth supported by the recent wage hikes and significantly deteriorating inflation expectations will keep inflationary risks alive. We expect consumer inflation to hover above 40% throughout the year before slowing down to near 30% at the end of the year, helped by the favorable base impact in December.

Sharp acceleration in producer and core prices led by currency depreciation

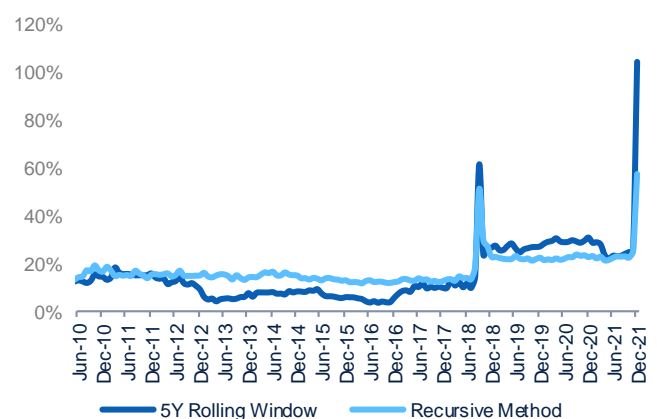
Food inflation recorded a record level of acceleration on the back of 15.5% unprocessed and 16.5% processed food monthly inflation, where the annual figure jumped to 44.7% from 27.5%. Energy prices similarly resulted in a 9.8% monthly and 42.9% annual inflation on the back of sharp currency depreciation followed by the series of price hikes. Core prices accelerated as well driven by the currency depreciation where core C prices increased by 13.2% monthly and 31.9% annually, reflecting a historically peak on pass-thru even surpassing the 2018 currency shock (Figure 2). Moreover, cost push factors reached a record high level of 19 years, jumping 19.1% on monthly basis carrying the annual PPI to 79.9%. The pressure from cost push factors will strengthen further given the strong price hikes in utility prices (electricity prices increased on average by 120% and natural gas prices increased by 25% for residential and 50% for industry) in addition to the strong minimum wage hike (50%). The impact of producer prices inflation has already gained momentum in the last quarter (Figure 6). Inflation expectations keep worsening as 12-month CPI and 24-month ahead expectations reached 21.39% and 14.41%, respectively, which will likely keep a reinforced inertia in the longer run. All in all, currency depreciation, high cost push factors accompanied with high demand and worsening expectations (also supported by the recent acceleration in credit growth and brought-forward demand), and continuing supply side problems maintain risks clearly on the upside for the inflation outlook.

Figure 1. CPI vs Domestic PPI, YoY



Source: Garanti BBVA Research, Turkstat

Figure 2. Exchange Rate Pass-Thru to Core-D Inflation

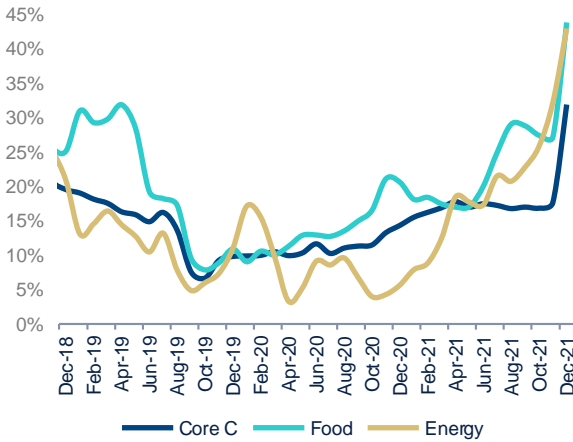


Source: Garanti BBVA Research, Turkstat

A clear top risk for 2022: Inflation

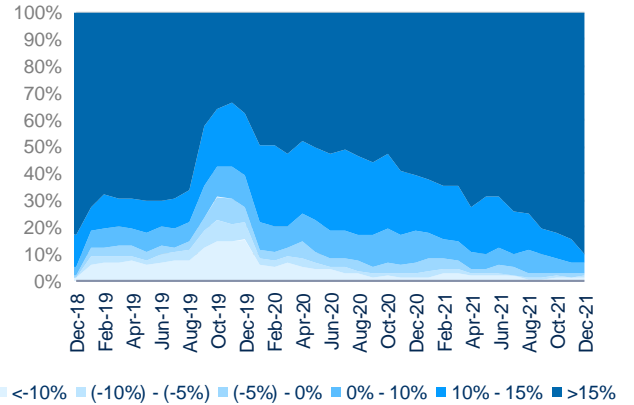
Given the latest price hikes on several items (4-4.5pp direct impact from utility, tobacco & alcohol, services items etc.) and continuing pass-thru effects, we expect annual consumer inflation to realize above 40% as soon as January, which will likely keep the inflation path high throughout the year. Therefore, it will be more challenging to keep current loose monetary and fiscal policies when the foreign yields are also rising and global inflation remains stubbornly high. Finally, the persistent high food inflation will bite into households' pocketbooks.

Figure 3. **CPI Components, YoY**



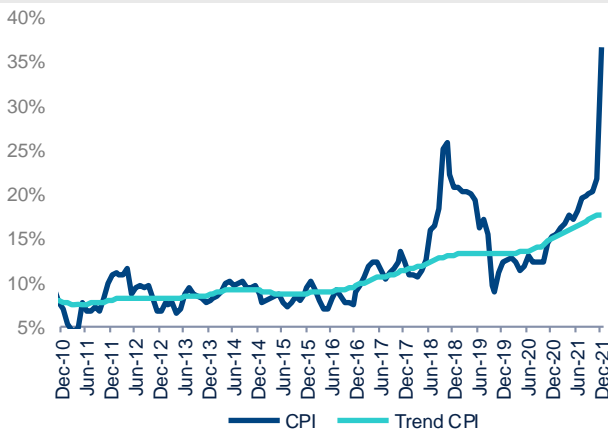
Source: Garanti BBVA Research BVAR Inflation Model, Turkstat

Figure 4. **Consumer Inflation Diffusion Map, YoY**



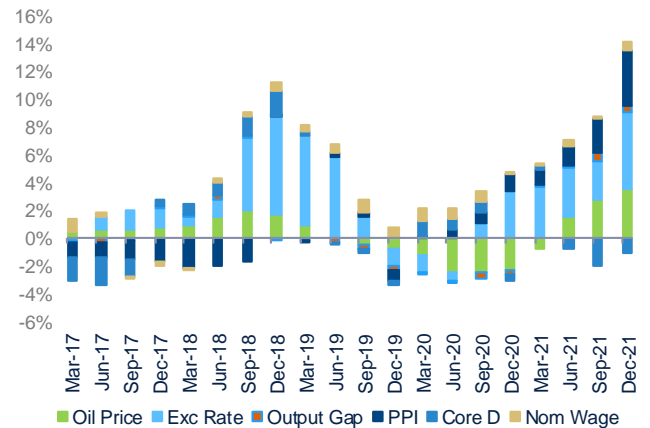
Source: Garanti BBVA Research, Turkstat

Figure 5. **CPI & Trend CPI, YoY**



Source: Garanti BBVA Research Time Varying BVAR and BVAR Core Inflation Models, Turkstat

Figure 6. **Historical Decomposition of Core-D Inflation (Quarter Avg., YoY)**



Source: Garanti BBVA Research BVAR Core Inflation Model, Turkstat,

Figure 7. **CPI in Subcomponents**

	MoM	YoY
Total	13.58%	36.08%
Food & Non-alcoholic beverages	16.0%	43.8%
Beverage & Tobacco	11.2%	20.0%
Clothing & Textile	7.4%	20.1%
Housing	4.6%	28.6%
Household Equipment	16.5%	40.9%
Health	3.6%	20.5%
Transportation	28.5%	53.7%
Communication	3.6%	8.8%
Recreation & Culture	10.2%	25.5%
Education	0.1%	17.2%
Restaurants & Hotels	9.8%	40.8%
Misc. Goods & Services	13.7%	35.4%

Source: Garanti BBVA Research, Turkstat

Figure 8. **Domestic PPI in Subcomponents**

	MoM	YoY
Total	19.08%	79.89%
Mining & Quarrying	12.7%	62.8%
Manufacturing	18.9%	77.4%
Food Products	20.1%	64.8%
Textiles	23.9%	89.9%
Wearing Apparel	7.5%	21.4%
Coke & Petroleum Products	17.9%	161.9%
Chemicals	22.3%	100.9%
Other Non-Metallic Mineral	13.9%	67.3%
Basic Metals	1.1%	130.9%
Metal Products	19.6%	67.1%
Electrical Equipment	17.9%	70.9%
Electricity, Gas, Steam	24.4%	117.1%

Source: Garanti BBVA Research, Turkstat

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