Creating Opportunities

Inflation Pulse

Türkiye | Much faster improvement in CPI trend

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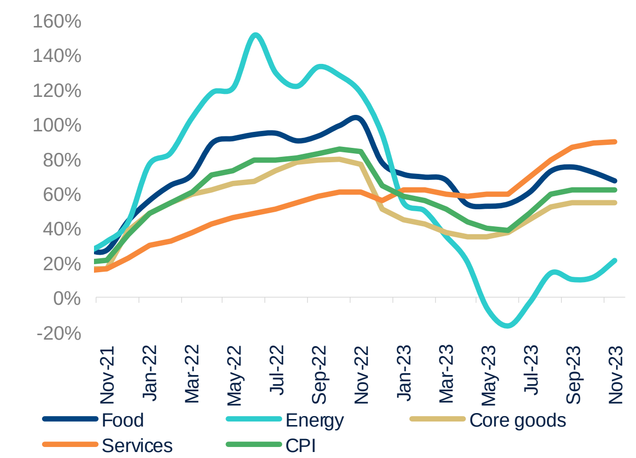
Consumer prices rose by 3.28% m/m in November, lower than both our expectation (4.0%) and market consensus (3.7%), while its annual inflation accelerated slightly to 61.98% from 61.36% the month before. The main deviation in our forecast was mainly due to core inflation being much weaker than expected, while food inflation was in line with our expectation. Both basic goods prices and services inflation lost pace on the back of limited depreciation of the currency and slowing domestic demand. Households' natural gas consumption, which was fully subsidized by the government up to 25m^3, started to exceed this threshold led by the colder weather conditions. We calculate the direct impact of natural gas usage on CPI as nearly 1.25pp. Considering the lower than expected October and November realizations coupled with the recent positively surprising policy rate hikes, the year-end consumer inflation could materialize high likely around 65%. Wage adjustments, administrative price hikes, the pace of currency depreciation and the fiscal stance especially before the local election will determine the path of inflation outlook. We expect consumer inflation to slow down to near 45% at the end of 2024 with a strengthening bias to the downside, led by the recent faster decline in monthly inflation trend and more restrictive monetary policy stance.

Core prices eased while energy prices put further pressure on inflation

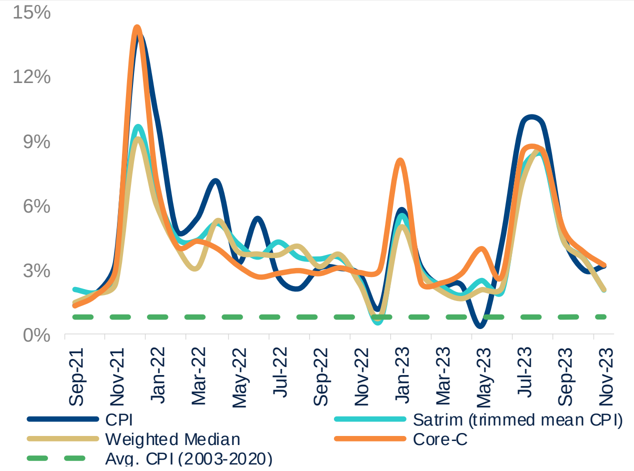
Turkstat had announced in May23 that the price of the natural gas being used by households would be equal to 0 nullifying the impact of energy consumption on consumer inflation, as the initial 25m^3 of monthly consumption would be fully subsidized until May24 as part of the election promises. Since households' consumption started to exceed this threshold, led by the colder weather conditions, the impact of the natural gas price was included in the calculations of CPI as of Nov23. We calculate the direct impact of this increase on the monthly inflation to be around 1.25pp with a monthly energy prices inflation accelerated to 10%. Therefore, annual energy inflation climbed up to 21.2% from 11.6% the month before. Domestic producer prices also accelerated to 2.8 m/m from 1.9% m/m in October after the deceleration recorded in the last four months, which led to an annual inflation gearing up to 42.2% (39.4% prev.) and confirmed the continuing cost factors on consumer prices.

Figure 1. **CONSUMER INFLATION SUB-COMPONENTS (YoY)**



Source: Garanti BBVA Research, TURKSTAT

Figure 2. **CONSUMER INFLATION INDICATORS (sa, monthly changes)**



Source: Garanti BBVA Research, TURKSTAT

Core prices (C index) surprised to the downside, decelerating to 2.0% m/m in November from 3.7% m/m the month before. Despite remaining almost flat compared to previous month (69.9% y/y), annual core prices inflation is still very close to the its record level of 70.4% in Oct22. In sub-details, monthly services prices slowed down limitedly to

2.8% from 3.8%, while its annual inflation accelerated to 89.7% (vs. 88.6% in Oct.). Following an average increase of 8.2% m/m in the last four months, rental prices continued to remain strong increasing by 6.0% m/m. The increase in restaurant & hotel prices lost pace with 2.5 m/m due to most likely much weaker demand as signaled by our Big Data services consumption proxy. On the other hand, the slow-down in basic goods prices (1.1% m/m vs. 3.6% m/m prev.) was more evident due to both the contraction in clothing and footwear prices (-0.3% m/m vs. 13.7% m/m prev.) and limited increase in durable goods prices (0.7% m/m vs. 0.4% m/m prev.), which stemmed from the limited depreciation of the currency and cooling domestic demand. Our inflation trend indicators keep improving but continue to highlight risk from inertia indicating the more limited slow-down in core inflation trend compared to other headline indicators. Given the expected administrative price hikes and wage adjustments at the start of the year, inflation inertia might remain strong and limit the pace of deceleration in services prices inflation going forward.

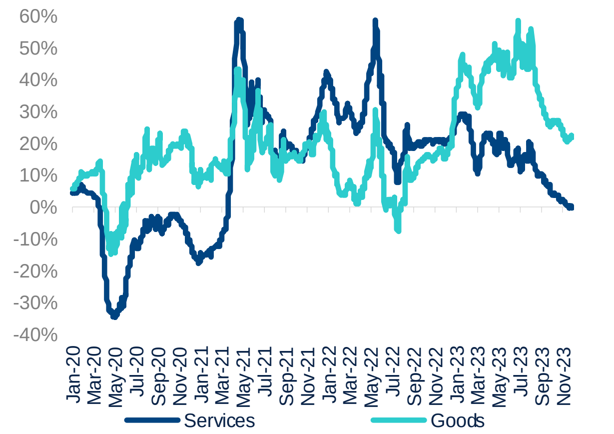
Food prices increased by 2.8% m/m mainly due to the acceleration in processed food prices (4.9% m/m vs. 2.5% m/m prev.) mainly led by the recent price hikes in dairy products stemming from a 25% hike in raw milk prices. On the other hand, unprocessed food prices were almost unchanged (0.3% m/m), as the increase in other unprocessed food prices (2.0% m/m) offset the contraction in fresh fruit and vegetable prices (-2.7% m/m). Although annual food inflation still remains very high, it continued to lose pace with 67.3% y/y (vs. 72.1% prev.).

Hawkish stance in monetary policy may help alleviate inflationary pressures

In the latest Monetary Policy Committee (MPC) meeting in Nov23, the Central Bank (CBRT) reinforced its commitment to fight against inflation by surprising to the upside with 500 bps hike in the policy rate. According to the forward guidance by the CBRT, the pace of monetary tightening will slow down and the tightening cycle will be completed in a short period of time. We observe faster than expected deceleration in inflation as a result of cooling domestic demand and managed depreciation of the currency. Led by slower than expected Oct. and Nov. inflation realizations, the end of the year consumer inflation will likely get nearer to 65% in the absence of any substantial shock. Though, uncertainties remain on fiscal stance, exchange rate outlook, wage adjustments of next year and accordingly second-round price effects. This is why inflation expectations would require more time to show that aimed convergence toward the CBRT's interim target of 36% by the end of 2024. According to the November market participants' survey of the CBRT, inflation expectations for the next 12 months and 24 months slightly improved to 43.9% and 25.1%, down from 45.3% and 25.8%, respectively. This is why the tight stance should be maintained as long as needed to ensure sustained price stability.

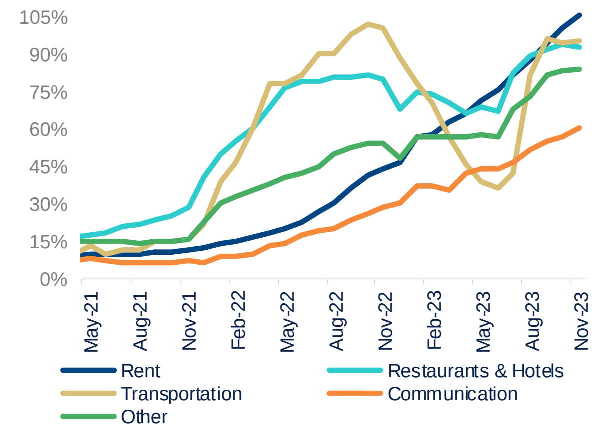
On the rebalancing of the activity, our recent monthly GDP nowcasts have demonstrated slight quarterly contraction for 4Q23. Despite the observed correction in the imbalance between aggregate demand and aggregate supply, positive output gap still continues to present challenges over the inflation outlook. The growth pattern for 2024 is rather unclear with differing projections from the Medium Term Program (MTP) and the CBRT, hence there is uncertainty over the pace of the stabilization. Therefore, the fiscal stance will be decisive over the disinflation pace. If the CBRT remains hawkish and keeps TL deposit rates much more restrictive with regulations, and any potential populist action remains to be suppressed ahead of the election, we would acknowledge the downside risks on our most recently revised inflation projections of 45% for the end of 2024.

Figure 3. **GARANTI BBBA BIG DATA CONSUMPTION INDICATORS** (28-day sum, real, YoY)



Source: Garanti BBVA Research, TURKSTAT

Figure 4. **SERVICES CPI INFLATION** (YoY)

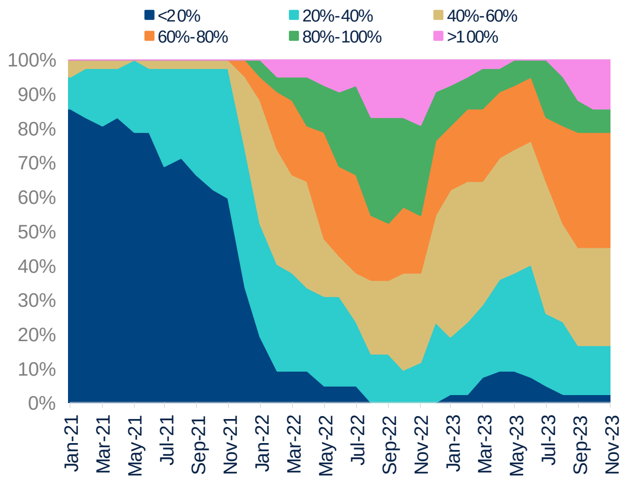


Source: Garanti BBVA Research, TURKSTAT

Figure 5. **CBRT MARKET PARTICIPANTS SURVEY** (12 and 24 Month Ahead Inflation Expectations)

Source: Garanti BBVA Research, CBRT

Figure 6. **CPI DIFFUSION ANALYSIS** (YoY)



Source: Garanti BBVA Research, TURKSTAT

Figure 7. **CPI SUBCOMPONENTS**

	MoM	YoY
Total	**3.28%**	**61.98%**
Food & Non-alcoholic beverages	2.8%	67.2%
Beverage & Tobacco	9.2%	71.4%
Clothing & Textile	-0.3%	40.7%
Housing	11.2%	37.5%
Household Equipment	2.3%	59.9%
Health	1.5%	82.1%
Transportation	0.2%	70.0%
Communication	3.4%	48.2%
Recreation & Culture	2.1%	56.9%
Education	0.6%	81.5%
Restaurants & Hotels	2.5%	92.9%
Misc. Goods & Services	2.3%	59.8%

Source: Garanti BBVA Research, TURKSTAT

Figure 8. **DOMESTIC PPI SUBCOMPONENTS**

	MoM	YoY
Total	**2.81%**	**42.25%**
Mining & Quarrying	2.7%	65.5%
Manufacturing	2.3%	54.1%
Food Products	3.0%	64.9%
Textiles	3.1%	45.3%
Wearing Apparel	3.2%	51.8%
Coke & Petroleum Products	-3.5%	30.5%
Chemicals	2.0%	44.2%
Other Non-Metallic Mineral	1.9%	52.3%
Basic Metals	2.1%	40.2%
Metal Products	2.2%	59.0%
Electrical Equipment	2.8%	65.0%
Electricity, Gas, Steam	11.0%	-30.0%

Source: Garanti BBVA Research, TURKSTAT

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