Inflation Pulse

Türkiye | Slight improvement in inflation trend

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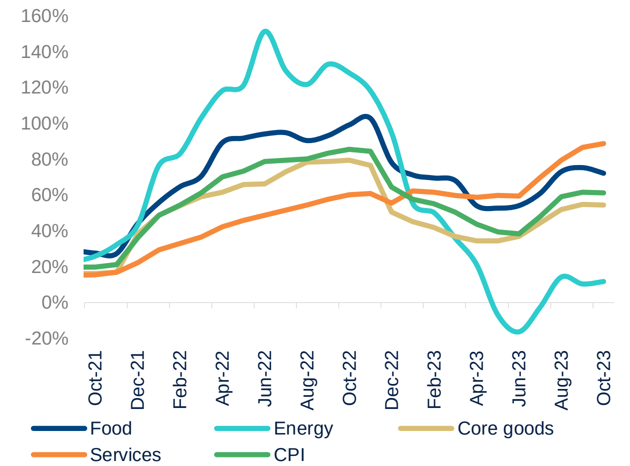
Consumer prices rose by 3.43% m/m in October, lower than both our expectation (4.5%) and market consensus (4.1%), which led to the annual inflation decelerating slightly to 61.36% from 61.53% previously. The downward surprise stemmed from weaker than expected realizations of both food and core inflation. Managed depreciation in the currency and strong but relatively weaker cost-push factors have started to feed into slower inflation in exchange rate sensitive goods prices, whereas services prices maintained pressure from ongoing inflation inertia and annual core C inflation accelerated to 69.8%. Given the implementation of "zero price" in households' natural gas consumption for levels below a certain threshold, the seasonally excessive gas usage will add further pressure on inflation in the upcoming months. Led by slower than expected October realization and likelihood of postponing utility price hikes for households after the local election in March 2024, we now acknowledge slight downside risk on our current year-end inflation forecast of 70%. Preferences over the course of economic growth, depreciation pattern of the currency, wage adjustments, administrative price hikes and inflation expectations will be decisive on inflation outlook. We expect consumer inflation to be realized closer to the upper bound of the Central Bank's (CBRT) revised inflation projections in the near term and finish next year at near 50%.

Core prices maintain high inflationary pressure

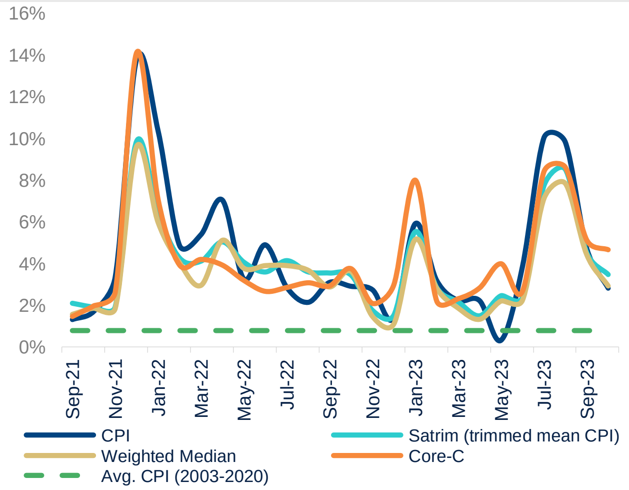
Despite the downward trend on a monthly basis, core prices (C index) remained strong increasing by 3.7% m/m (vs. the average of 7.9% m/m in the last 3 months). Therefore, annual core prices inflation accelerated to 69.8% (vs. 68.9% in September). In detail, services prices continued to signal solid inflation inertia with an increase of 3.8% m/m, following an average increase of 9.0% m/m in the last 3 months, which led to an annual inflation climbing up to 88.6% from 86.5% the month before. The increase in rent (7.9% m/m vs. 9.5% m/m prev.) and restaurant & hotel prices (3.5% m/m vs. 4.1% m/m) were more pronounced, which confirmed the continuation of second round effects. On goods front, basic goods prices accelerated to 3.6% m/m mainly due to the sharp increase in clothing and footwear prices (14.0% m/m) due to seasonal factors. On the other hand, durable goods prices (excluding gold) remained almost flat (0.4% m/m) thanks to the limited depreciation of the currency and much weaker domestic demand. Our SATRIM estimations on inflation trend shows differentiation across groups with core inflation showing a relatively more limited slow-down compared to overall CPI, which confirms that high inertia might keep stickiness on prices and contribute to additional inflationary pressure.

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

Food prices increased by 3.1% m/m mainly due to the acceleration in other unprocessed food prices (6.3% m/m) led by the price hikes in both red and white meat (lamb: 8.8%, beef: 4.9%, poultry: 5%) and egg prices (10.8%). Fresh fruit and vegetable prices remained well below our expectation and increased by only 0.4% m/m. Thanks to the gradual currency depreciation and weakening cost-push factors, processed food prices continued to slow down, increasing by 2.5% m/m. Thus, annual food inflation slightly lost pace with 72.1% y/y (vs. 75.7% prev.).

Energy prices rose by 3.6% m/m on the back of the households' natural gas usage above 25m^3 and other solid fuels despite a clear decline in gasoline prices in October. Meanwhile, producer prices decelerated considerably both on monthly (1.9% vs. 3.4% prev.) and annual terms (39.4% vs. 47.4% prev.). 20% price hike in natural gas and electricity for industrial users announced by the state-run Petroleum Pipeline Corporation (BOTAŞ) was put into effective as of October, which could still keep spill-over effects on cost factors going forward.

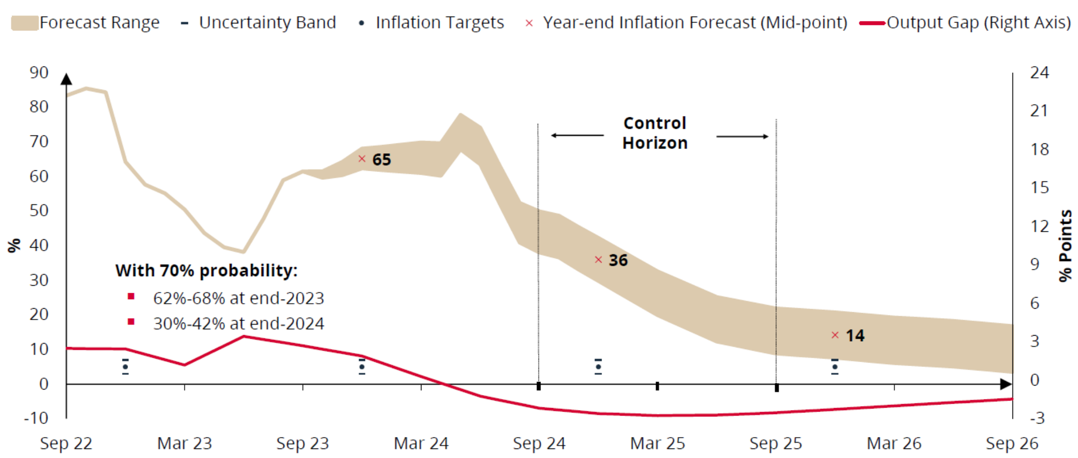
The CBRT revised its inflation projections on the upside

The Central Bank (CBRT) released the last inflation report of the year and made upward revisions on their inflation projections (interim targets) within a much wider range indicating higher uncertainty over the forecasts. 2023 year-end inflation forecast was hiked up by 7pp to 65%, slightly below the consensus of 68%, with the forecast range revised upward to 62-68% band from 54-62% in the previous report released in July. On the other hand, 2024 inflation forecast was raised slightly to 36% from 33% (with a wider range of forecasts spanning from 30% to 42%), remaining far from the market expectation range of 40-45%. The 2025 forecast was predicted to decrease slightly from 15% to 14%, indicating no likelihood of achieving the official single digit inflation target of 5% during the forecast horizon.

In 2024 revisions of the CBRT, forecast deviation and changes in forecasting approach (+1.5pp), TL based import prices (+1.8pp) and administered prices (+1.5pp) pushed up their forecast; whereas food prices (-1.0pp) and a negative output gap (-0.7pp following a more positive update of the previous years) pinned down the projection. We welcome the communication about a wider forecast range highlighting uncertainties on the inflation outlook and the trade-off given on growth rather than inflation to show a clearer fight against inflation. Though, the previous statements and the commitment of the government in the Medium Term Program (MTP) on avoiding a recession (4% GDP target of 2024 and 4.5% on average in medium run) have become inconsistent with the CBRT's clearly downward revised growth assumptions implying 1-1.5% growth in 2024 and ongoing below potential projections even during 2026.

During her presentation, the CBRT Governor emphasized the importance of anchoring inflation expectations and stressed that the monetary policy tightening will continue. If the market participants' survey is considered, the range of 12-month ahead inflation and policy rate expectations remain quite large. The current high uncertainty shows the need to strengthen forward guidance and confirm with actions. Otherwise, it will be difficult to anchor inflation expectations especially to attain inflation level below 30% in 2025.

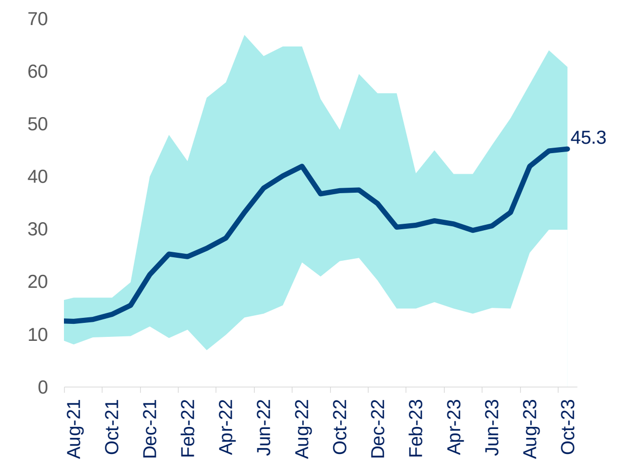
CBRT MEDIUM TERM INFLATION PROJECTIONS (YoY)



Preferences on economic policies will determine the inflation outlook

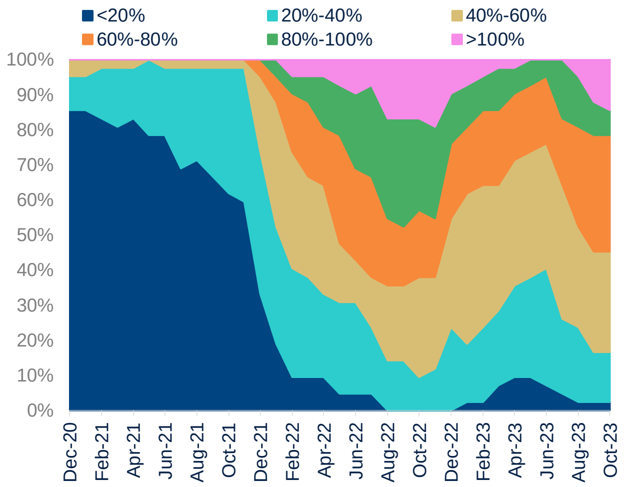
Given the managed depreciation of the currency helped by the reinforced regulations on the banking sector, we observe a slow deceleration in monthly trend inflation, which proves to be stickier in the case of the core prices. Led by slower than expected October realization and likelihood of postponing utility price hikes for households after the local election in March 2024, we now acknowledge slight downside risk on our current year-end inflation forecast of 70%. Preferences over the course of economic growth, depreciation pattern of the currency, wage adjustments, administrative price hikes and inflation expectations will be decisive on inflation outlook. We expect consumer inflation to be realized closer to the upper bound of the Central Bank's (CBRT) revised inflation projections in the near term and finish next year at near 50%, led by a delayed adjustment in the currency. If a gradual depreciation pattern is preserved with the help of an ongoing course of macro-prudential measures, a lower inflation path will likely be achieved in absence of any other substantial shock. Under that scenario, a clearly tighter stance in economic policies will be finally required to achieve a stabilization in the economy and start a clearer exit from the current regulations.

Figure 3. **CBRT MARKET PARTICIPANTS SURVEY INFLATION EXPECTATIONS** (12-month ahead, YoY)



Source: Garanti BBVA Research, CBRT

Figure 4. **CPI DIFFUSION ANALYSIS** (YoY)



Source: Garanti BBVA Research, TURKSTAT

Figure 5. **CPI SUBCOMPONENTS**

	MoM	YoY
Total	**3.43%**	**61.36%**
Food & Non-alcoholic beverages	3.2%	72.0%
Beverage & Tobacco	0.1%	62.0%
Clothing & Textile	13.7%	39.1%
Housing	7.5%	26.0%
Household Equipment	2.6%	61.0%
Health	2.6%	81.3%
Transportation	-0.2%	72.0%
Communication	2.7%	46.7%
Recreation & Culture	2.3%	57.0%
Education	0.3%	80.8%
Restaurants & Hotels	3.5%	94.1%
Misc. Goods & Services	3.1%	60.3%

Source: Garanti BBVA Research, TURKSTAT

Figure 6. **DOMESTIC PPI SUBCOMPONENTS**

	MoM	YoY
Total	**1.94%**	**39.39%**
Mining & Quarrying	3.4%	69.2%
Manufacturing	2.3%	53.7%
Food Products	4.2%	64.7%
Textiles	1.8%	42.1%
Wearing Apparel	5.3%	50.7%
Coke & Petroleum Products	-3.2%	32.6%
Chemicals	2.6%	43.5%
Other Non-Metallic Mineral	3.9%	55.4%
Basic Metals	1.1%	36.4%
Metal Products	2.7%	60.7%
Electrical Equipment	1.9%	66.2%
Electricity, Gas, Steam	-4.4%	-40.2%

Source: Garanti BBVA Research, TURKSTAT

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