Inflation Pulse

Türkiye | Inflationary trend improved only limitedly

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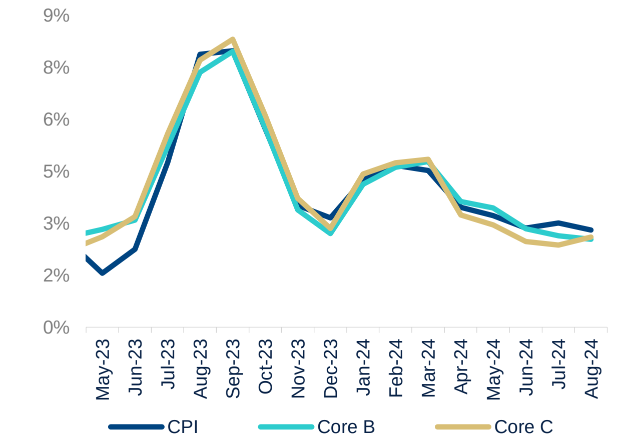
Consumer prices rose by %2.47 m/m in August, higher than our expectation (2.2%) and consensus (2.3%). As a result, annual consumer inflation came down to 51.97% from 61.78% previously. According to our calculations, underlying consumer inflation trend slightly eased to 2.8% from the previous 3%, supported by the decline in food prices; while core prices trend worsened led by services inflation reflecting backward indexation and second round effects. Energy inflation remained strong due to the natural gas price hike for residential use in August and lagged effects of July price hikes, adding new dynamic effects on the headline. We forecast inflation trend to improve; reaching 1.5-2% monthly in 4Q24 and finish the year annually at 43% in 2024 and 25% in 2025. Even though rebalancing in economic activity has become clearer with further normalization in domestic demand, unanchored inflation expectations, strong inertia in services and increasing pressure over the currency maintain risks to the upside on inflation outlook.

Acceleration in core inflation trend point to risks on the upside

Underlying consumer inflation trend (3-month moving average of seasonally adjusted inflation) slightly eased to 2.8% from 3% previously, supported by the decline in food prices (1.6% m/m). Negative monthly inflation in fresh fruit & vegetables (-10.0 m/m) on seasonal effects and other unprocessed food (-1.7% m/m) helped, whereas processed food inflation remained more or less unchanged at 2.4% m/m. On the other hand, energy inflation stayed strong (6.8% m/m) due to 24% natural gas price hike for residential use (0.6pp direct impact on headline inflation) in August and lagged effects of July price hikes, adding new dynamic effects on the headline. Along with backward indexation and second round effects especially on services prices, monthly seasonal adjusted core inflation (both B and C) worsened to above 3%, according to our calculations (Figure 1 & 2).

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)

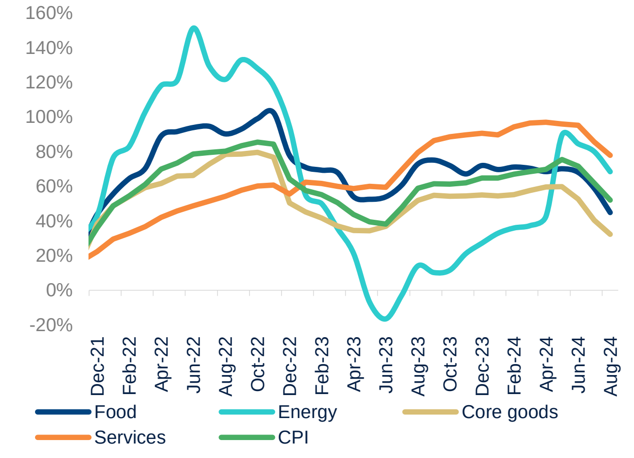
Source: Garanti BBVA Research, TURKSTAT

Services prices were the main contributor to August inflation, increasing by 4.6% m/m (sa), pointing to strong inertia and backward indexation. The rent inflation remained elevated at 7.4% m/m (7.0% m/m in July), in the presence of the removal of 25% rent hike ceiling as of July. Another important component fueling services inflation was the education prices, increasing by 11.3% m/m on the back of upward adjustments in school tuition fees. Since we were expecting this impact to go into effect in September, our inflation expectations diverged considerably from the realization. Finally, transportation prices geared up (9.2% m/m vs. 4.8% m/m prev.) due to price hikes in subway, intercity train lines, taxi cab fares and other related transportation medium prices. Overall, the 3-month average trend in services inflation worsened to 3.8% (3.5% previously).

Basic goods price inflation was also somewhat higher in August (1.2% m/m vs. 0.4% m/m prev.), primarily led by durable goods (1.5% m/m) and a slight increase in clothing prices (0.3% m/m). Still, the trend inflation in basic goods eased to 1.1% (1.4% prev.) thanks to the ongoing moderation in domestic demand.

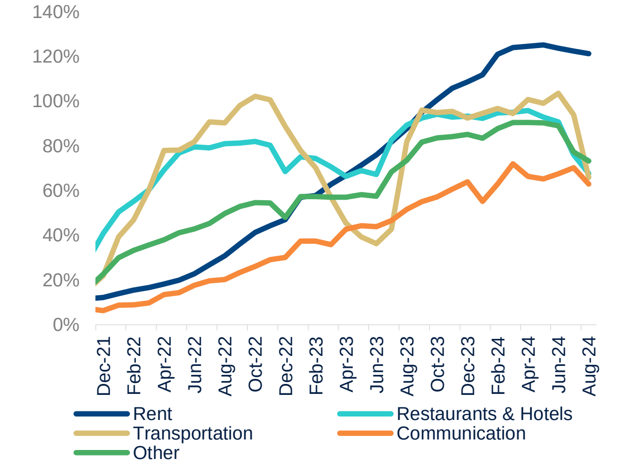
Regarding cost push factors, monthly producer price inflation eased further to 1.68% in August, resulting in an annual inflation of 35.8%. Despite August's uptick, deceleration in yearly currency depreciation compared to previous months and weaker commodity prices reduce the cost pressure on consumer prices.

Figure 3. **CONSUMER INFLATION INDICATORS** (YoY)



Source: Garanti BBVA Research, TURKSTAT

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



Source: Garanti BBVA Research, TURKSTAT

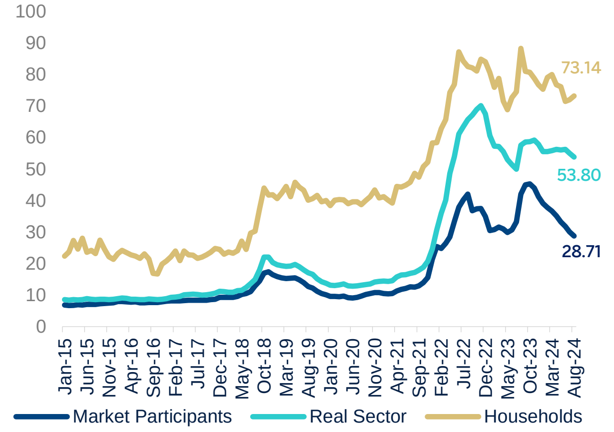
Not yet a favorable space for monetary easing

Even though the rebalancing in economic activity has become clearer with further normalization in domestic demand, unanchored inflation expectations, strong inertia in services and increasing pressure over the currency maintain risks to the upside on inflation outlook. In the last MPC document, the Central Bank (CBRT) had assessed domestic demand as slowing down and reducing its inflationary impact but highlighted the high level and the stickiness of services inflation, while also emphasizing the need for an alignment of inflation expectations with their projections. In this respect, output gap turning into negative clearly as of 3Q24 will help alleviating risks as signalled by our monthly nowcasts on consumption pointing to possible declines as of August. However, stickiness of services prices and resistance from inflation expectations will require a restrictive stance for longer to maintain a sustained disinflation path.

In the August survey, professional forecasters' expectations for 2024 and 2025 year-end inflation inched upward to 43.31% and 25.55% (vs. 42.95% and 25.4%, previously). Even though, the real sector's expectation for 12-month ahead inflation fell back to 53.8% from 55% in July, the households remain unconvinced over the improvement of inflation, with their expectation for 12-month ahead increasing to 73.14% (from the previous 71.98%). Overall, inflation expectations remain well above the upper bound of the CBRT targeted inflation range (42% and 21%, respectively), confirming the resistance due to the widened credibility gap of the previous years.

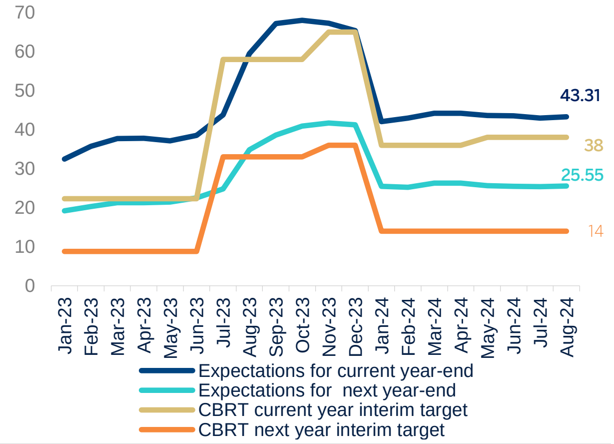
All in all, the challenging inflation outlook narrows down the opportunity window for a premature monetary easing cycle. Given our expectations of output gap turning into negative and a real appreciation trend, we expect inflation trend to decline to slightly below 2% by end 2024 (vs. 1.5% target of the CBRT in 4Q24). Our call to a moderate rate cut in late 4Q24 is still likely, given the increasing likelihood of looser external financial conditions and the most recent faster than expected adjustment in economic activity. Yet, inflation risks continue to be challenging and the expected fiscal consolidation is still missing, which we hope to see in the New Medium Term Plan (MTP) to be released on 5th of September.

Figure 5. **CBRT SECTORAL INFLATION EXPECTATIONS** (%, 12 MONTH AHEAD, ANNUAL)



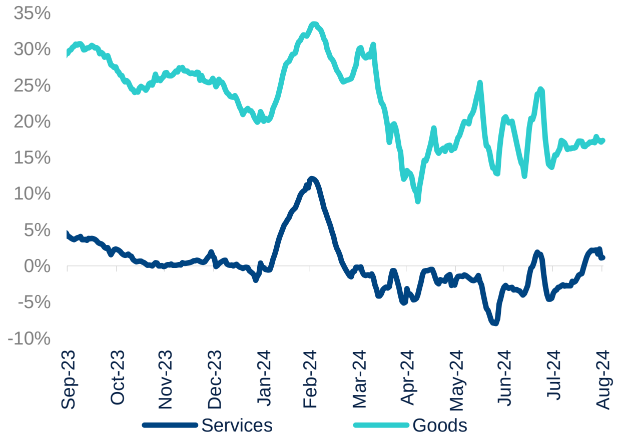
Source: Garanti BBVA Research, CBRT

Figure 6. **CBRT MARKET PARTICIPANTS SURVEY INFLATION EXPECTATIONS** (%)



Source: Garanti BBVA Research, CBRT

Figure 7. **GARANTI BBVA BIG DATA CONSUMPTION INDICATORS** (28-day sum, real YoY)



Source: Garanti BBVA Research, TURKSTAT

Figure 8. **CPI SUBCOMPONENTS**

	MoM	YoY
Total	**2.47%**	**51.97%**
Food & Non-alcoholic beverages	-1.1%	44.9%
Beverage & Tobacco	4.5%	60.9%
Clothing & Textile	0.4%	29.4%
Housing	8.5%	101.5%
Household Equipment	1.1%	44.7%
Health	1.7%	53.5%
Transportation	2.9%	29.0%
Communication	0.6%	42.8%
Recreation & Culture	2.6%	47.2%
Education	11.3%	120.8%
Restaurants & Hotels	2.0%	67.7%
Misc. Goods & Services	2.1%	47.7%

Source: Garanti BBVA Research, TURKSTAT

DISCLAIMER

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