

Inflation Pulse

Türkiye | Inflation trend improves on food prices

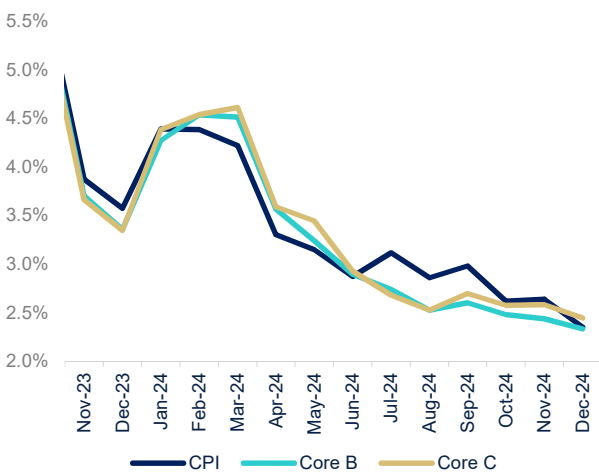
Adem İleri / Berfin Kardeşler / Gül Yücel
3 January 2025

Headline inflation eased to 1.03% m/m (vs. 2.24% prev.), lower than consensus and our expectation (both at 1.6%), leading year-end inflation to materialize at 44.4%. While the headline inflation was supported by food and core prices, seasonally adjusted data indicate that the correction primarily stemmed from fresh fruit and vegetable prices. On the other hand, only a moderate improvement is observed in the core inflation trend, driven by services and core goods but this improvement is not broad-based and appears to result from the impact of some specific sub-items. A 30% increase in the minimum wage, a lower adjustment of the fuel tax hike compared to the past six months of PPI inflation, and potential adjustments in administered prices, particularly for natural gas and electricity, which may be determined in line with inflation target of 2025, pose downside risks on our inflation forecast. Despite recent improvement, unanchored elevated inflation expectations, the signaling impact of revaluation rate set at 43.9%, strong inertia, high likelihood of real interest rates to be lower than our previous expectations and uncertainty regarding the magnitude of fiscal policy support could be upside risks. Hence, we maintain our year-end inflation forecast for 2025 at 26.5%. We will closely monitor the effects of price adjustments and dynamic factors on the inflation outlook in the first quarter of 2025. Our expectation of some improvement in annual inflation in the 1Q25 could create room for CBRT to continue to easing cycle with 250 bps cut in January. Still, we believe that a cautious stance should persist, ensuring sufficient positive real interest rates to maintain the attractiveness of TL assets.

Inflation trend shows relief from fresh food prices, yet core pressures persist

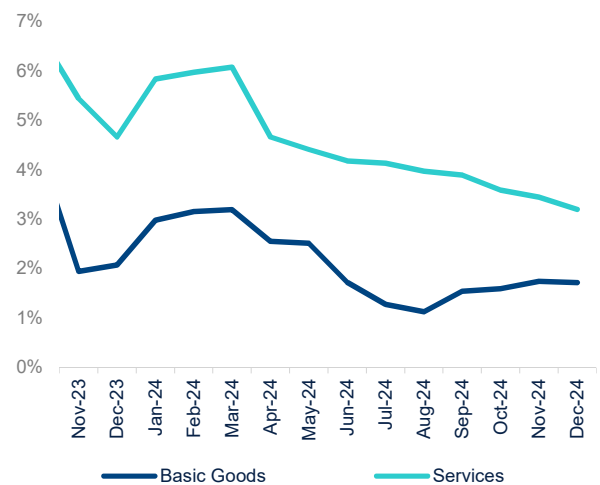
Monthly headline inflation decreased to 1.03% m/m (prev. 2.24%), driven by a decline in fresh food, other basic goods and rent inflation. Our calculations also indicate an improvement in the seasonally adjusted CPI, which decreased to 1.84% from 2.80%, lowering the three-month inflation trend to 2.35% from 2.64%. The improvement in fresh food inflation only accounts for 0.8 percentage points of the decrease in the seasonally adjusted headline inflation. Consequently, such promising improvements are not observed for core indicators excluding that category. Core C inflation decreased to 2.36% (prev. 2.69%), insufficient to establish a significant downward trend; the three-month core inflation trend eased only to 2.45% (prev. 2.58%).

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)

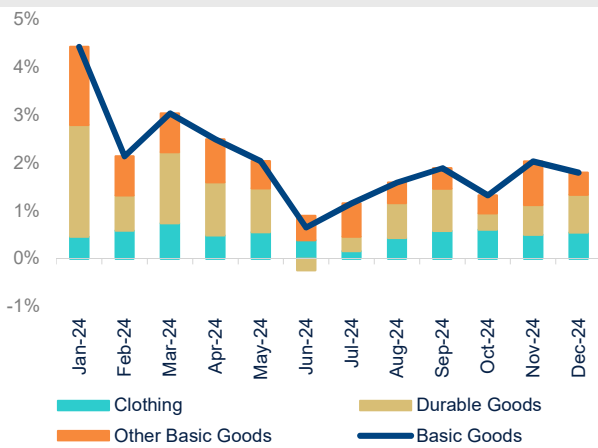


Source: Garanti BBVA Research, TURKSTAT

Both main components of Core C inflation – basic goods and services - experienced a decrease, with basic goods inflation retreated to 1.80% (prev. 2.03%), and services inflation declining to 2.93% (prev.3.37%). This kept the basic goods inflation trend stable around 1.7%; while services inflation slightly fell to 3.20% (prev. 3.45%), leading to a restricted improvement in the Core C inflation trend (down to 2.45% from 2.58%). The monthly improvement in Core C inflation is primarily driven by rent prices (down to 3.35% from 5.29%) and other basic goods (down to 1.56% from 3.08%). However, durable goods (up to 1.62% from 1.27%) and restaurant and hotel prices (up to 2.45% from 2.06%) exerted upward pressures. High inflation expectations, coupled with slowing but resilient demand and currency appreciation, may explain the deterioration in non-durable goods and restaurant and hotel prices.

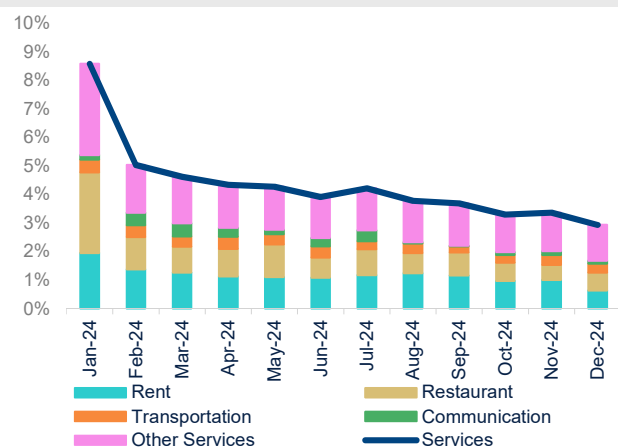
Fresh fruit and vegetable inflation decreased sharply to -1.52% from 15.34%, contributing almost entirely to the decline in food and non-alcoholic beverage inflation (down to 1.44% from 4.52%). Meanwhile, the impact of unprocessed food prices on food inflation remained positive, rising to 1.71% from 1.57%.

Figure 3. **CONTRIBUTIONS TO BASIC GOODS INFLATION** (seasonal adj., monthly, pp)



Source: Garanti BBVA Research, TURKSTAT

Figure 4. **CONTRIBUTIONS TO SERVICES INFLATION** (seasonal adj., monthly, pp)



Source: Garanti BBVA Research, TURKSTAT

Cost push factors remained weak based on our trend calculation, despite being relatively higher than what headline PPI implies (0.40% m/m and 28.5% y/y). Energy prices decreased further in December (-5.8% m/m vs. -3.6% m/m prev.). In January, upward adjustments in the special consumption tax in fuel prices, increasing municipal water prices in the metropolitan cities, including Istanbul's dynamic price hikes according to the average of CPI and PPI realizations, and minimum wages may increase the cost pressures. Still, supportive oil prices and stable currency may compensate for these upside risks. Additionally, 30% minimum wage hike point that the upside pressure on costs in the short run may remain lower than our previous expectations (35%).

Fiscal support would be crucial for inflation outlook as CBRT starts easing cycle

Our heatmap analysis (Figure 5) on the underlying inflation trend across sub-categories points that the improvement is not broad based. The recovery in the inflation trend has been driven by food prices, while core inflation has shown only very limited improvement. The upward trend in basic goods since June has merely stabilized while despite the some improvement, services inflation remain solid on backward-looking indexation. In these circumstances, in December, the Central Bank started easing cycle with a 250 bps rate cut, exceeding the market's limited cut expectations but at least it emphasized that future decisions will be inflation-focused, cautious, and evaluated on a meeting-by-meeting basis. Therefore, as the monetary policy easing cycle begins, support from the fiscal policy becomes increasingly crucial for the fight against inflation. First, the 30% increase in the minimum wage could result in lower inflationary pressures than our previous expectation (35%). Also, special consumption tax on fuel prices were raised by 6%, slightly below the 7.6% PPI inflation over six months. Last but not least, Finance Minister Şimşek stated that some administered prices, particularly electricity and natural gas, could be adjusted in line with the 2025

inflation target. Therefore, fiscal policy focused to support disinflation in the short term by implementing relatively modest price or tax adjustments for items with high weights in the consumer basket. Fiscal consolidation is expected to become more evident in the second half of the year. The scale of consolidation will be another factor for the inflation outlook.

On the other hand, the revaluation rate remained at 43.9%, contrary to our downside adjustment expectation. Although its direct impact on the consumer inflation is more limited, we considered its signaling impact, particularly on inflation expectations, to be important. The inflation expectations remain unanchored, signaling the likelihood of distorted pricing behavior to continue in the near future. In December survey (Figure 7), professional forecasters' expectations for 2025 year-end inflation increased to 27.07% (vs. 26.22%, prev.). On the other hand, the real sector's and households' expectations for 12-month ahead inflation improved very limitedly to 47.6% and 63.1%, respectively (47.80% and 64.05% previously) but still remained elevated compared to the CBRT targets. In addition, 24 month ahead and 5 year ahead, increased further to 18.47% and 11.34% (vs. 18.33% and 11.13% prev.). Also, despite some moderation, the demand conditions remains stronger than supply, maintaining the inflationary pressures and the financial conditions seem to be more restrained on the production side. Even though weaker than expected minimum wage hike may limit the cost pressures in the services sector, still robust demand and backward indexation could lead services inflation to remain high. All in all, persistently high inflation expectations, strong inertia, the possibility of real interest rates remaining below our previous anticipation, geopolitical risks, and the potential distortions may rise from Trump's protectionist trade policies keep upside risks alive.

To sum up, we believe that the risks on inflation outlook are more balanced. Hence, we kept our year-end inflation forecast of 26.5% for 2025. We will closely monitor price adjustments in the first quarter and their secondary effects and revise our inflation forecast accordingly.

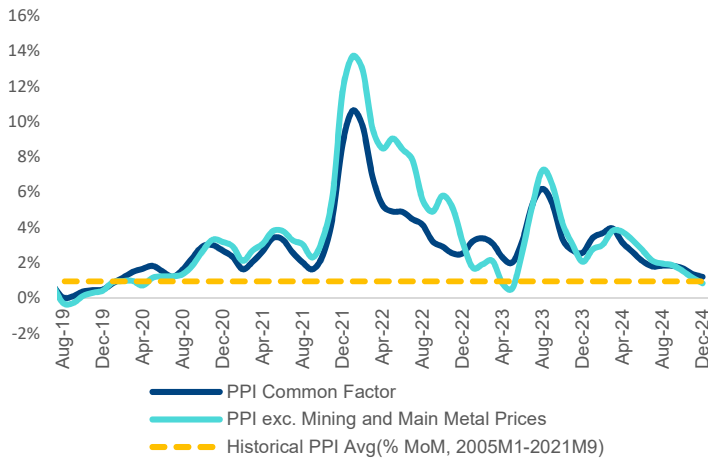
Figure 5. **CONSUMER PRICES HEAT MAP** (% , seasonal adj., 3 month moving avg.)*

	Mean	2023												2024											
		Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
CPI	1.3	3.7	3.4	3.6	2.4	1.6	2.4	4.9	7.9	7.9	5.7	3.9	3.6	4.4	4.4	4.2	3.3	3.2	2.9	3.1	2.9	3.0	2.6	2.6	2.4
CORE-B	1.3	4.1	3.9	3.8	2.6	2.8	3.2	5.3	7.3	7.5	5.6	3.7	3.4	4.3	4.5	4.5	3.6	3.2	2.9	2.7	2.5	2.6	2.5	2.4	2.3
CORE-C	1.2	4.1	3.9	3.7	2.6	3.1	3.7	5.8	7.5	7.5	5.5	3.7	3.3	4.4	4.5	4.6	3.6	3.4	2.9	2.7	2.5	2.7	2.6	2.6	2.4
Goods Prices	1.3	3.3	3.2	3.4	2.0	1.2	1.8	4.3	7.6	8.1	6.1	3.9	3.1	4.2	4.4	4.6	3.3	3.2	2.8	3.0	2.9	3.2	2.9	2.3	1.7
Energy	1.3	0.3	0.0	0.9	-0.9	-8.2	-6.9	-1.3	0.4	10.3	7.2	5.8	5.4	6.3	3.9	3.5	1.4	2.1	2.1	5.4	6.1	5.8	2.9	0.9	0.9
Food and Non Alcoholic Bev Prices	1.5	4.0	3.9	4.5	3.8	2.8	3.3	5.2	7.8	7.6	5.8	3.2	3.4	3.6	4.7	4.0	3.5	2.7	2.9	3.2	2.2	2.2	2.6	3.8	3.2
Unprocessed Food Prices	1.7	3.8	4.0	5.3	5.2	4.4	5.6	7.7	9.5	8.3	5.6	2.4	3.4	3.3	4.9	3.9	3.5	3.1	3.0	3.3	1.8	2.1	3.2	6.2	4.8
Processed Food Prices	1.4	4.3	3.8	3.9	2.6	1.5	1.3	3.0	6.3	7.1	5.9	3.9	3.4	3.8	4.5	4.1	3.5	2.3	2.8	3.0	2.5	2.2	2.1	1.8	1.8
Basic Goods Prices	1.1	2.8	2.7	2.4	1.8	2.1	3.1	5.6	7.6	7.0	4.3	1.9	2.1	3.0	3.2	3.2	2.6	2.5	1.7	1.3	1.1	1.5	1.6	1.7	1.7
Clothing	0.8	1.3	1.4	0.9	0.7	1.4	2.4	3.4	5.4	5.2	5.0	2.7	2.6	2.2	2.3	2.8	2.8	2.7	2.2	1.7	1.5	1.8	2.5	2.6	2.6
Durable Goods	1.2	3.1	3.1	3.0	2.4	2.7	4.4	7.5	9.0	7.6	3.6	1.2	1.3	2.7	3.0	3.1	2.3	2.4	1.2	0.7	0.5	1.3	1.3	1.3	1.2
Other Basic Goods	1.2	3.2	2.9	2.6	1.6	1.5	1.4	3.9	6.9	7.1	5.0	2.6	3.0	4.0	4.0	3.6	2.8	2.5	2.2	2.0	1.8	1.7	1.4	1.9	2.0
Services Prices	1.4	5.5	5.1	5.1	3.4	4.0	4.3	6.1	7.3	8.2	6.7	5.4	4.7	5.8	6.0	6.1	4.7	4.4	4.2	4.1	4.0	3.9	3.6	3.4	3.2
Rent	1.4	5.5	5.0	5.6	4.5	5.5	5.8	6.3	6.8	7.4	7.6	7.5	6.5	7.4	7.5	8.1	6.6	6.2	5.9	5.9	6.2	6.3	5.9	5.5	4.6
Restaurant	1.6	6.5	6.2	6.0	3.3	4.3	4.4	7.4	7.9	8.2	5.7	4.3	4.1	6.2	6.5	6.3	3.9	3.9	3.6	3.6	3.0	3.2	2.8	2.6	2.3
Transportation Services	1.4	3.5	3.3	3.2	3.0	3.0	3.0	4.1	10.6	11.8	11.4	4.9	4.0	4.0	4.2	4.1	4.1	3.9	4.0	3.5	3.4	2.8	2.8	2.8	3.2
Communication Services	0.8	4.0	3.4	3.5	3.4	4.0	4.6	3.2	3.9	4.8	4.9	4.9	4.1	3.5	3.9	5.1	5.8	4.4	3.6	4.0	3.4	2.1	0.8	1.2	1.6
Other Services	1.3	5.5	5.2	4.9	2.9	3.4	3.7	6.1	6.9	8.2	6.1	5.4	4.4	5.7	5.7	5.6	4.2	4.0	3.8	3.8	3.8	3.8	3.7	3.6	3.4

Contraction Slow-down Growth Boom

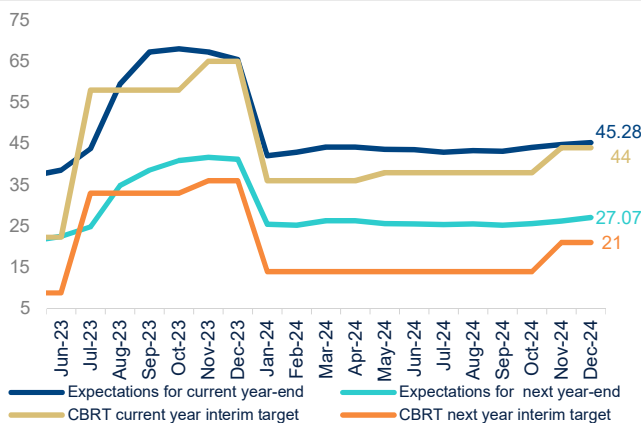
Source: TURKSTAT, Garanti BBVA Research, *Mean and standard deviation based on data period from 2005-2024 realization so far.

Figure 6. **PPI TREND INDICATORS (3 MONTH MOVING AVERAGE, %, MOM)**



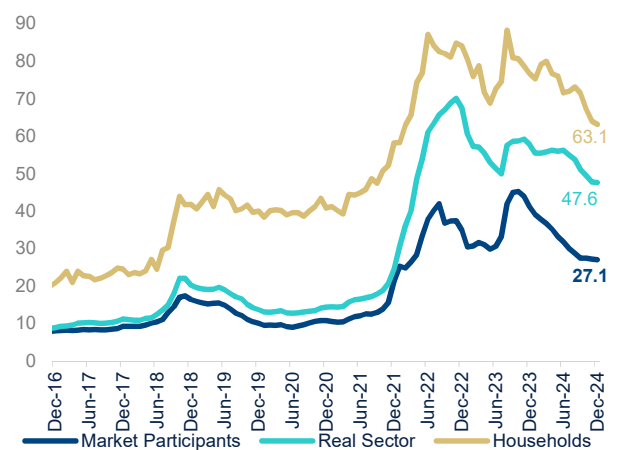
Source: Garanti BBVA Research, TURKSTAT

Figure 8. **CBRT MARKET PARTICIPANTS SURVEY INFLATION EXPECTATIONS (%)**



Source: Garanti BBVA Research, CBRT

Figure 7. **CBRT MARKET PARTICIPANTS SURVEY INFLATION EXPECTATIONS (%)**



Source: Garanti BBVA Research, CBRT

Figure 9. **CPI SUBCOMPONENTS**

	MoM	YoY
Total	1.03%	44.38%
Food & Non-alcoholic beverages	1.3%	43.6%
Beverage & Tobacco	0.0%	39.3%
Clothing & Textile	-0.7%	32.3%
Housing	1.7%	69.0%
Household Equipment	2.8%	38.7%
Health	0.9%	47.6%
Transportation	-0.4%	25.9%
Communication	1.8%	34.1%
Recreation & Culture	1.5%	37.6%
Education	0.1%	91.6%
Restaurants & Hotels	1.4%	57.1%
Misc. Goods & Services	1.5%	43.3%

Source: Garanti BBVA Research, TURKSTAT

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