

INFLATION PULSE

Turkey: inflation stable yet the core improved

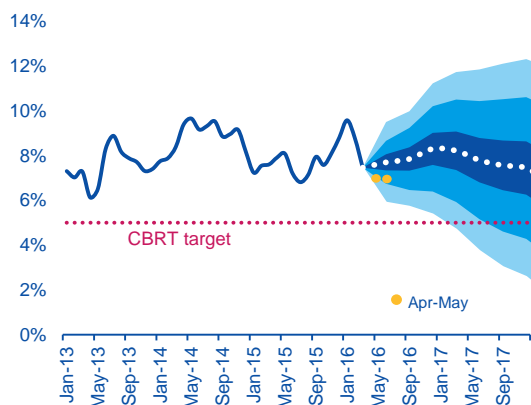
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In May monthly consumer prices rose 0.6%, slightly lower than market expectations of 0.7%. Annual inflation stayed stable at 6.6%. Although the headline remained constant, underlying factors improved compared to the previous month.. Central Bank’s core-I indicator fell to 8.8% in May from 9.4% of April, reflecting the slowdown of exchange rate pass-through and favorable pass-through of low food prices. We expect the headline to pick up due to reversal of base effects on food and energy.

Improvement in core indicators is positive news

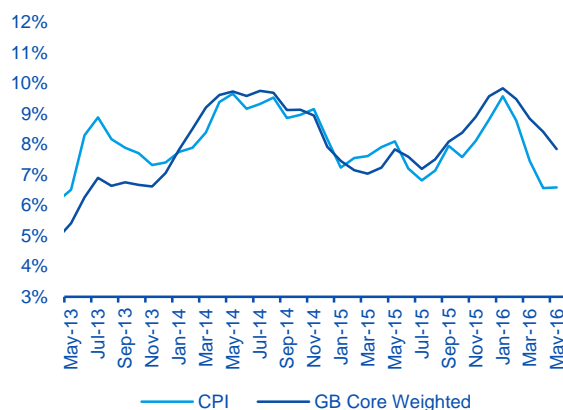
Although remained elevated, some 60bps improvement in the core-I indicator was the good news of the month. Several factors were behind the improvement. Less than its seasonal average increase in clothing and footwear; diminishing impact of exchange rate pass-through on imported goods and lower restaurant and hotel inflation due to depressed food prices and decreased hotel occupancy were the most striking ones. Meanwhile, annual food inflation bottomed out and rose to 1.8% from 0.6% of the previous month, as the favorable base effects waned out. Annual energy inflation remained low at 1.1% as favorable base effects persist. Assuming the current \$50 per barrel Brent prices and a constant exchange rate, we should expect the base effects on energy inflation to turn negative in August and increase towards the end of the year.

Figure 1
Turkey: inflation Forecasts
 (YoY, 20% & 50% uncertainty band forecasts)



Source: Garanti Research Inflation Model & Turkstat

Figure 2
Turkey: headline and BBVA-Garanti Core Inflation
 (YoY)

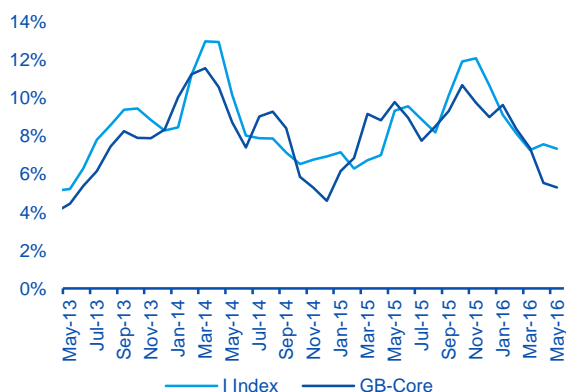


Source: Garanti Research Inflation Model & Turkstat

Risks are tilted towards the downside on our 8.5% year-end forecast

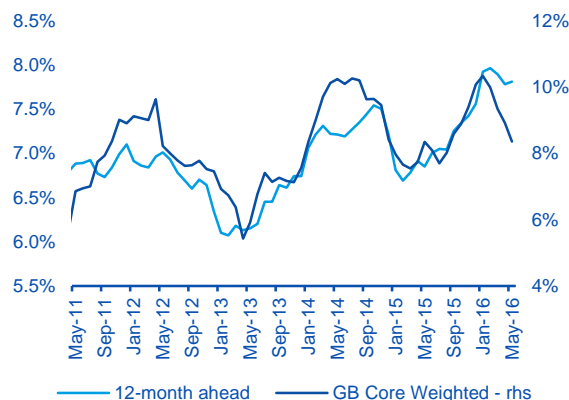
The lower margin for currency appreciation, cost push impacts of minimum wage hike and the narrowing output gap will likely limit a further significant correction in core inflation. However, favorable pass-through of persistently low food prices on restaurant prices and decreased hotel occupancy levels due to contracting tourist arrivals, pose downside risks. This would make the Central Bank more comfortable to continue lowering the marginal funding rate.

Figure 3
Turkey: core Inflation (3-MA, annualized)



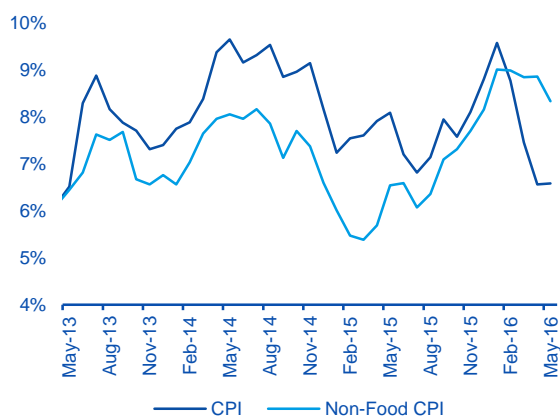
Source: Garanti Research Inflation Model & Turkstat

Figure 4
Turkey: inflation Exp. and GB-Core (YoY)



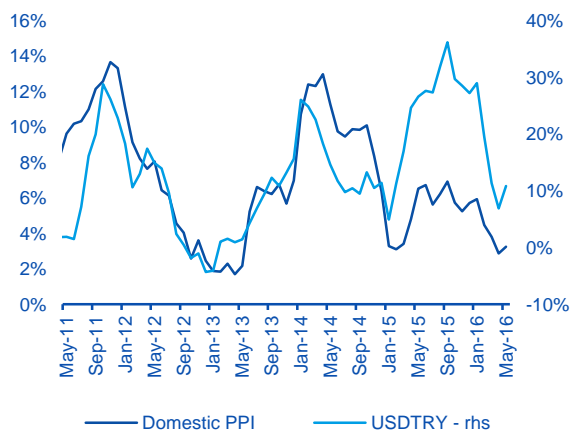
Source: Garanti Research Inflation Model & Turkstat

Figure 5
Turkey: inflation and Non-Food Inflation (YoY)



Source: Garanti Research & Turkstat

Figure 6
Turkey: domestic PPI and USDTRY (YoY)



Source: Garanti Research & Turkstat

Table 1
Turkey: CPI in Subcomponents

CPI	MoM	YoY
Total	0.60%	6.60%
Food	-1.60%	2.50%
Beverage & Tobacco	0.00%	12.80%
Clothing & Textile	8.00%	7.30%
Housing	0.40%	6.50%
Household Equipment	-0.30%	9.20%
Health	0.20%	9.60%
Transportation	1.10%	5.70%
Communication	0.90%	2.90%
Recr. & Culture	0.90%	9.00%
Education	1.00%	7.60%
Rest. & Hotels	0.50%	10.60%
Misc. Goods & Services	0.90%	11.90%

Source: Garanti Research & Turkstat

Table 2
Turkey: domestic PPI in Subcomponents

Domestic PPI	MoM	YoY
Total	1.5%	3.2%
Mining & Quarrying	2.4%	-0.4%
Manufacturing	1.9%	4.5%
Food Products	1.5%	2.8%
Textiles	0.3%	6.7%
Wearing Apparel	-0.8%	4.5%
Coke & Petroleum Products	14.6%	-22.0%
Chemicals	0.8%	2.3%
Other Non-Metallic Mineral	0.7%	2.5%
Basic Metals	5.9%	1.1%
Metal Products	1.3%	7.4%
Electrical Equipment	0.9%	7.8%

Source: Garanti Research & Turkstat

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