

# Turkey: Another pick-up in core inflation

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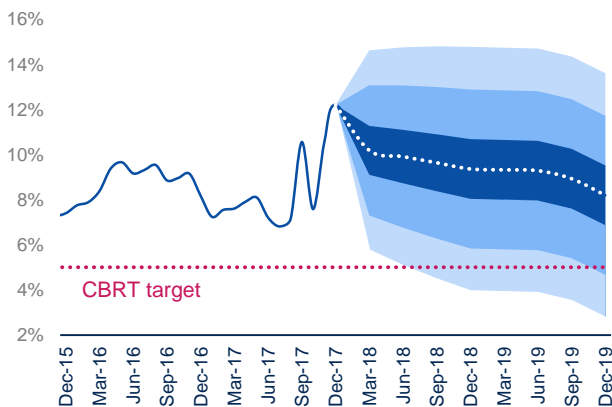
3 January 2018

Consumer prices increased by 0.69% (mom) in December 2017, higher than median market expectation and BBVA-GB forecast (both 0.5%). Thanks to favorable base effects, annual consumer inflation fell to 11.9% from 13.0% in November. The upside surprise came from core prices, whose annual inflation reached 12.3% rising from 12.1% the month before. Exchange rate pass-thru (especially on the items sensitive to euro) and solid domestic demand continued to be the key factors behind. Looking ahead, while the worst could be over, cumulative lagged effects of currency depreciation and positive output gap will keep core inflation high, possibly at two-digits until the last quarter of the year. We expect the headline to ease towards slightly below 10% by the end of 1Q and stay close to these levels until 4Q before falling to around 9% at the end of the year.

## Core inflation outlook stays worrying

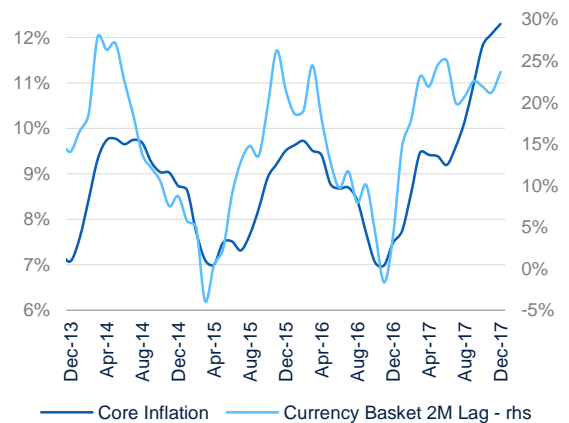
Base effects on food and exclusion of the tax hike on tobacco in this period helped annual headline inflation fall by near 1pp at the end of 2017. Despite still being high, annual food inflation eased to 13.8% from 15.8%. Energy inflation was also supportive on base effects, however, it still implies upward risks over higher oil prices on improving global demand in 2018. Surprising pick-up in core inflation, on the other hand, limited the expected decline in the headline. Core inflation climbed to 12.3% from 12.1% the month before, especially on top of the items sensitive to Euro pricing. The pick-up in automobile and white goods prices (3.5% and 3.8% mom, respectively) took the lead in the deterioration. Lagged effects of lira depreciation and cost-push factors remained to be the impulsive force as domestic producer prices annual inflation continued to be high at 15.5%. We expect core inflation to fall slightly below 11% at best by end 1Q18 and stay possibly at two-digits until the last quarter of the year.

**Figure 1** BBVA-GB Inflation Expectations (3M, YoY)



Source: Garanti Research & Turkstat

**Figure 2** Core Inflation and Currency basket



Source: Garanti Research Inflation Model & Turkstat

## Upside risks on inflation should maintain the CBRT on alert

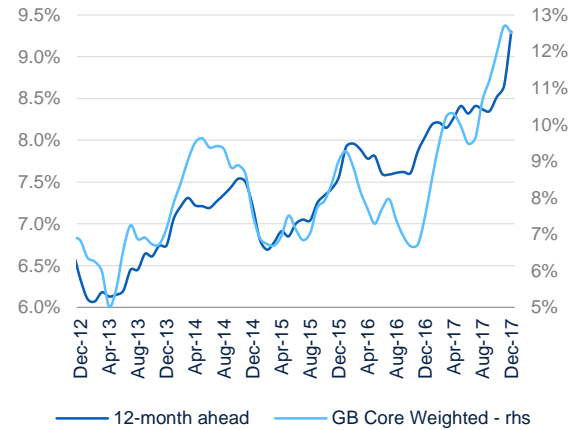
Cumulative effects of the exchange rate depreciation, stronger increases than inflation in wages, higher energy prices, cost-push factors from producer prices and lagged pressures from robust domestic demand conditions will likely keep inflation high, possibly close to two-digits until the last quarter of the year. Favorable base effects on food will help especially in the first quarter, which will bring the headline to slightly below 10% at best. Considering the upward risks on inflation, we expect the Central Bank (CBRT) to maintain the tight stance throughout the year.

**Figure 3** BBVA-GB and CBRT Core Inflation (YoY)



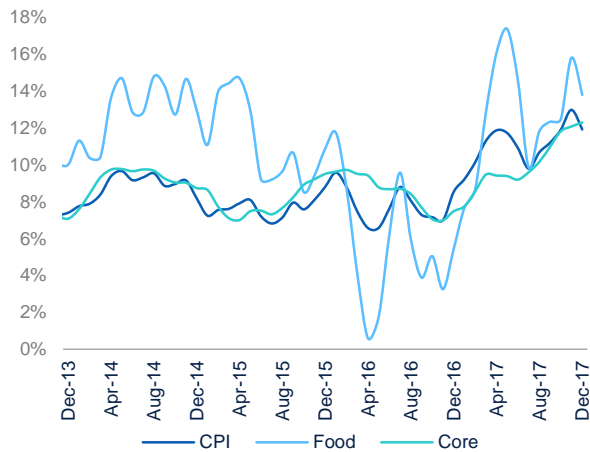
Source: Garanti Research Inflation Model & Turkstat

**Figure 4** Inflation Exp. and GB-Core Inflation (YoY)



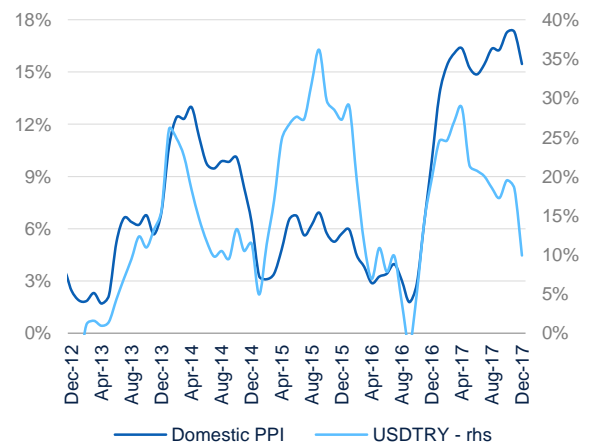
Source: Garanti Research Inflation Model & Turkstat

**Figure 5** CPI and Components (YoY)



Source: Garanti Research & Turkstat

**Figure 6** Domestic PPI and USDTRY (YoY)



Source: Garanti Research, CBRT & Turkstat

**Figure 7** CPI in Subcomponents

CPI	MoM	YoY
<b>Total</b>	<b>0.7%</b>	<b>11.9%</b>
Food	1.5%	13.8%
Beverage & Tobacco	0.0%	2.9%
Clothing & Textile	-2.4%	11.5%
Housing	0.8%	9.6%
Household Equipment	1.2%	12.7%
Health	0.2%	11.9%
Transportation	1.7%	18.2%
Communication	-0.2%	1.4%
Recr. & Culture	0.0%	8.4%
Education	0.0%	10.5%
Rest. & Hotels	0.5%	11.5%
Misc. Goods & Services	0.0%	12.8%

Source: Garanti Research & Turkstat

**Figure 8** Domestic PPI in Subcomponents

Domestic PPI	MoM	YoY
<b>Total</b>	<b>1.4%</b>	<b>15.5%</b>
Mining & Quarrying	1.9%	16.1%
Manufacturing	1.3%	16.6%
Food Products	0.8%	5.3%
Textiles	1.1%	18.4%
Wearing Apparel	-0.3%	8.5%
Coke & Petroleum Products	1.2%	32.5%
Chemicals	1.1%	20.8%
Other Non-Metallic Mineral	1.3%	11.4%
Basic Metals	3.3%	35.8%
Metal Products	0.9%	19.1%
Electrical Equipment	2.5%	19.3%
Electricity, Gas, Steam	1.7%	0.4%

Source: Garanti Research Inflation Model & Turkstat

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