

Economic Watch

Turkey: Lower-than-expected July CPI on food

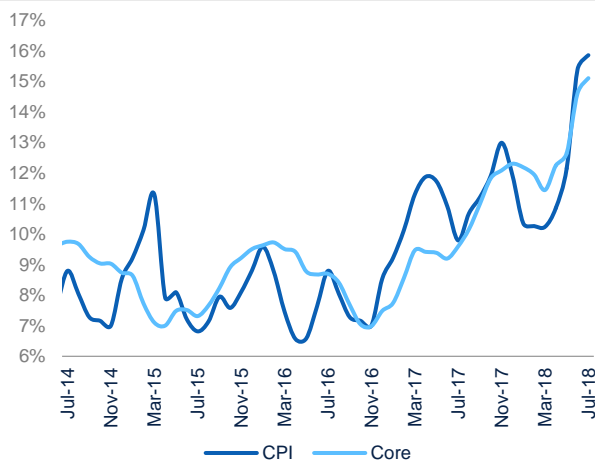
Adem Ileri / Serkan Kocabas / Seda Guler Mert / Alvaro Ortiz

Consumer prices increased 0.55% (mom) in July below our estimate and market consensus (0.9% vs. 1%), leading the annual figure to rise to 15.85% from 15.39% in June. The downside surprise came from the lower food inflation than our expectation, while the worsening in core inflation continued as annual core inflation reached 15.1%. Domestic producer prices also continued its upward trend, with 25% yoy, maintaining cost push factors on consumer inflation. Given the recent hikes in utility prices and rapid depreciation in TL, we may not have seen the peak in CPI yet and increasing trend could continue until TL stabilizes. Hence, risks on our year-end 14% inflation estimate are now on the upside by at least 1pp. Depending on the level of correction in food inflation (still continuing in August and relying on the potential hike in bread prices) and likely removal of the tax adjustment in fuel prices, risks could be even higher. The adjustment in the economy will help disinflation path in the coming period but monetary policy should also be supported by a comprehensive strategy to enhance transmission mechanism.

Inflation maintain upward risks on rapid depreciation and increasing costs

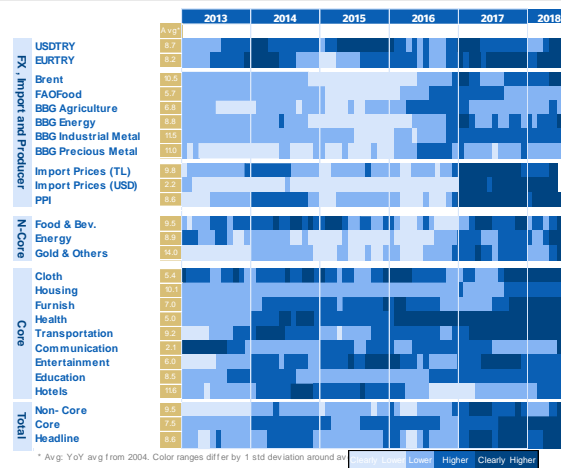
The downside surprise to our estimate was due to sizably lower food inflation than we initially estimated. Monthly food inflation realized at -0.4%, very close to its seasonal average vs. our estimate of 2.1% rise. Though, due to unfavorable base effects, annual food inflation rose to 19.9% from 19.4% in June. On the other hand, core inflation continued to deteriorate on top of ongoing exchange rate pass-thru, increasing cost-push factors and second round price effects and accelerated to 15.1% from 14.6% in June. The worsening remains across-the-board, with the highest contributions from furniture, restaurants & hotels, housing and clothing. Given the recent negative currency shock, cumulative pass-thru impact on consumer inflation could surpass 5pp in September. Recent hikes on utility prices will bring 0.4pp direct impact on consumer prices, while the indirect impact might be around 0.5pp from producer prices till the end of the year. According to our analysis, pass-thru from producer prices to consumer prices could reach 30-35%, observing the peak in the 5th month. Thus, recent figures of PPI including upside risks will keep the cost push factors upward on consumer prices in the short term.

Chart 1 Core Inflation and CPI (YoY)



Source: BBVA Research Turkey & Turkstat

Chart 2 Core Inflation Heat Map



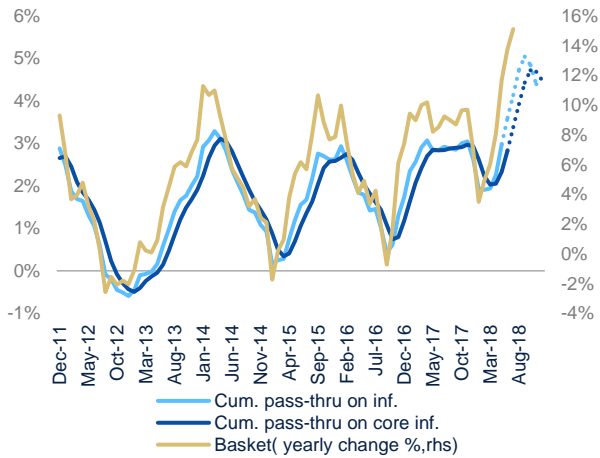
Source: BBVA Research Turkey & Turkstat

Worsening inflation outlook requires an urgent anti-inflation strategy

Given the recent rapid depreciation and price hikes on both consumer and producer side, risks on our year-end 14% inflation estimate are clearly on the upside. The adjustment in the economy will help disinflation path; though a collaborative anti-inflation strategy should be urgently followed and the measures in the new Medium Term Plan should be consistent to restore credibility to fight against macro imbalances.

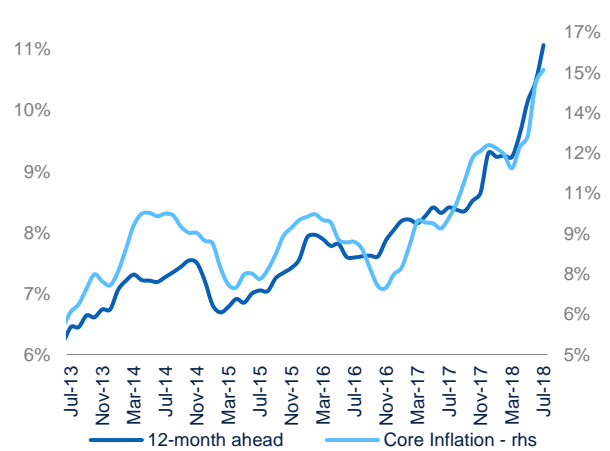
Creating Opportunities

Chart 3 Pass-thru on CPI and Core CPI



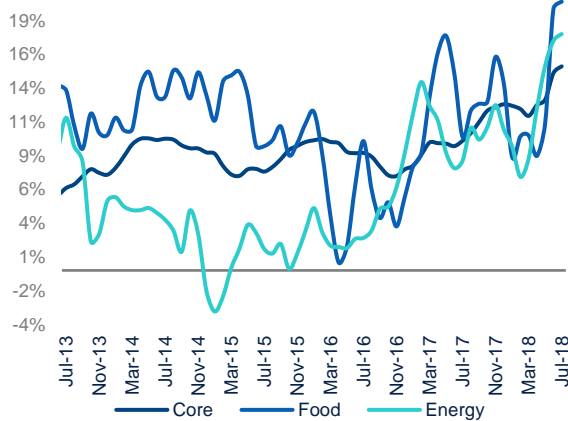
Source: BBVA Research Turkey Inflation Model & Turkstat

Chart 4 Core Inflation vs Inflation Expectations (YoY)



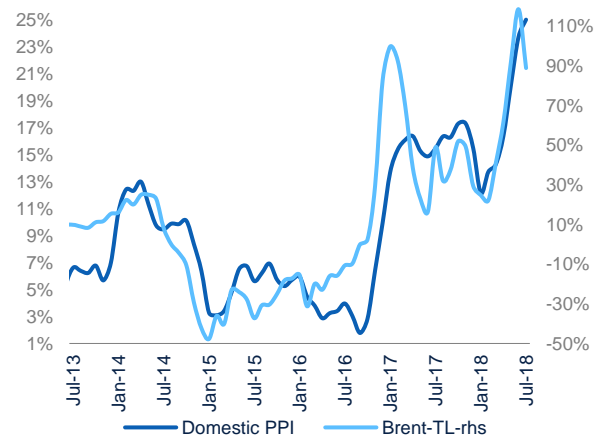
Source: CBRT & Turkstat

Chart 5 CPI Components (YoY)



Source: BBVA Research Turkey & Turkstat

Chart 6 Domestic PPI and Oil Prices in TL (YoY)



Source: BBVA Research Turkey, CBT & Turkstat

Chart 7 CPI in Subcomponents

CPI	MoM	YoY
Total	0.6%	15.8%
Food	-0.3%	19.4%
Beverage & Tobacco	0.8%	1.4%
Clothing & Textile	-3.1%	11.9%
Housing	1.1%	12.8%
Household Equipment	1.8%	20.3%
Health	1.2%	11.8%
Transportation	1.1%	24.2%
Communication	-0.1%	4.7%
Recr. & Culture	1.6%	9.7%
Education	1.1%	10.8%
Rest. & Hotels	2.3%	13.9%
Misc. Goods & Services	0.6%	17.2%

Source: BBVA Research Turkey & Turkstat

Chart 8 Domestic PPI in Subcomponents

Domestic PPI	MoM	YoY
Total	3.0%	25.0%
Mining & Quarrying	2.4%	24.9%
Manufacturing	3.2%	25.3%
Food Products	2.6%	12.7%
Textiles	3.7%	22.7%
Wearing Apparel	3.7%	14.5%
Coke & Petroleum Products	6.9%	85.3%
Chemicals	4.6%	32.3%
Other Non-Metallic Mineral	1.0%	20.3%
Basic Metals	5.0%	50.1%
Metal Products	3.4%	29.4%
Electrical Equipment	5.2%	25.0%
Electricity, Gas, Steam	2.0%	23.1%

Source: BBVA Research Turkey & Turkstat

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