

Turkey: Broad-based inflationary pressures continue

Inflation in Turkey, standing at slightly below 80% in June, continues to face a challenging outlook given an accommodative monetary policy stance and elevated cost-push pressures



Standing at 4.95% month-on-month, the June inflation reading came in better than the consensus forecast (5.38% MoM), though slightly above our projection (4.8% MoM). Annual inflation, on the other hand, moved up to 78.6% from 73.5% a month ago. The rapid uptrend, which has been in place since the fourth quarter of 2021, is attributable to the pass-through effects of a weak currency following significant monetary easing as well as worsening inflation expectations and external factors, which have weighed on import prices. With the latest data, the (ex-post) real policy rate drops further into negative territory. The policy rate stands at 14% currently, implying a need for a correction in the monetary stance.

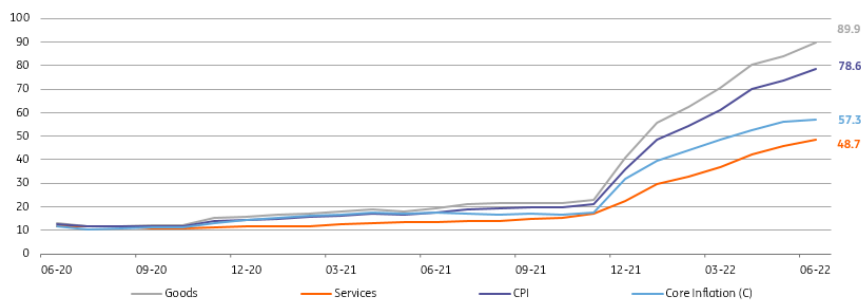
Regarding the core indicators, both B and C indices continued to rise, reaching 64.4% year-on-year and 57.2% YoY, respectively - their highest levels as we continue to witness a broad-based deterioration in price dynamics. While the underlying trend has been in retreat since February, it is still markedly high, showing the extent of the challenges on the inflation front.

On the PPI side, the trend remains strong with a 6.8% MoM increase, leading to a further rise in

annual inflation to 138.3%. This points to the strength of cost-led inflationary pressures which could further weigh on the CPI outlook in the coming months. Given the possibility of higher energy prices, ongoing supply-side challenges, and currency-related uncertainties, the risks lie to the upside.

Evolution of annual inflation (%)

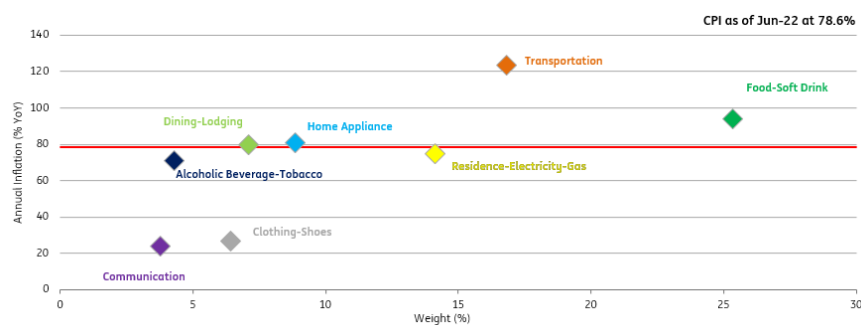
(Core = CPI excluding energy, food & drinks, alcoholic beverages, tobacco, gold)



Source: TurkStat, ING

According to the breakdown of the main expenditure groups, transportation was the biggest contributor, adding 188bp to the headline rate. Annual inflation is now at 123.4% due to higher fuel prices and adjustments in transportation services. Housing was the second biggest contributor, adding 117bp to the inflation rate, driven by electricity fees and natural gas prices. The volatile food group pulled the headline up by 57bp mainly on the back of processed food. As a result, goods inflation hit 89.9% given the spike in energy inflation, processed food and durable goods. Regarding services, annual inflation is at the highest level in the current 2003=100 series, at 48.7%, with price adjustments in all groups, particularly in rent, catering and transportation services.

Annual inflation in expenditure groups



Source: TurkStat, ING

Inflation data in June showed that the accommodative monetary policy stance and elevated cost-push pressures are continuing to drive prices higher. Despite a recently announced price cap on residential rent hikes until July 2023 and other measures to try to replicate some parts of the monetary transmission mechanism and pull lending rates up, inflationary risks have remained elevated amid deteriorating pricing behaviour, the impact

of exchange rate developments and higher trend inflation. Given the rapid and increasing FX pass-through in recent months, currency moves will be key for the inflation outlook.

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