

Turkey: Core inflation returns to single digits

Annual inflation dropped in April thanks to lower energy prices and moderating demand, despite higher FX volatility. Annual core inflation also changed direction, falling into single digits

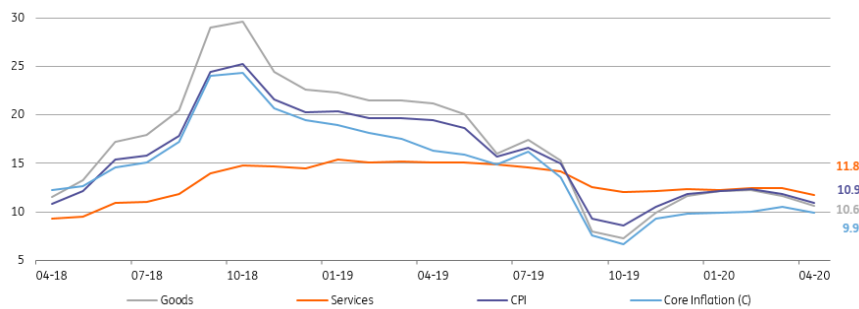


Source: Flickr

In April, monthly inflation came in at 0.85%, slightly higher than the consensus and our call (0.75% and 0.7%, respectively), pulling the annual figure down to 10.9% from 11.9% a month ago. More importantly, despite higher FX volatility impacting certain sensitive items of the CPI basket like white goods and automobiles, annual core inflation also changed direction and fell into single digits at 9.9% from 10.5% a month ago, likely on the back of deteriorating demand conditions.

Evolution of Annual Inflation (%)

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



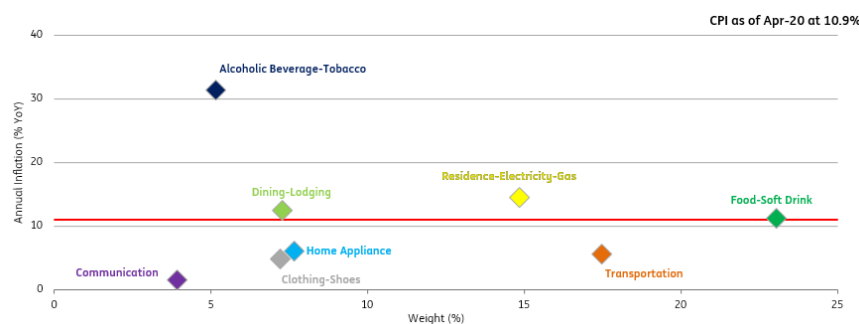
Source: TurkStat, ING

In the breakdown, we see 1) a decline in annual goods inflation to 10.6%, driven by energy as a result of the large drop in oil prices last month and core goods 2) services inflation, on the other hand, moderated to the lowest level since mid-2018, at 11.8%, with across the board weakness in subgroups, showing the impact of shutdowns and quarantine measures.

Regarding the main expenditure groups, among the positive drivers:

- The food group stood out as the major driver lifting the headline by 61 basis points. Also, the monthly change was significantly above the long-term April average, reflecting increasing demand under lockdown conditions and short curfews imposed at the weekends. Accordingly, we saw higher increases in both unprocessed and processed food prices.
- Another major contributor was the clothing group, with a 25bp impact on the monthly reading, though the monthly price change was very low in comparison to earlier years.
- On the flip side, as expected, transportation dragged the headline down by -27bp, thanks to the oil effect, though price increases in automobiles amid weakness in the Turkish lira limited the extent of the drop.

Annual inflation in Expenditure Groups



Source: TurkStat, ING

Overall, we saw a fall in annual inflation in April amid supportive energy prices, while underlying price developments also showed an improvement despite the impact of currency movements on certain items. Going forward, softer domestic demand conditions

will remain supportive for disinflation, along with lower oil prices and the second round effects. On the other hand, exchange rate developments will be one of the major determinants of the inflation outlook, though FX pass-through should be relatively limited during the slowdown. Given the downside revision to end-year inflation forecasts and the central bank's determination to contain the adverse impact of the coronavirus shock on the economy, the bank will likely maintain its easing bias and announce with further cut(s).

Author

Muhammet Mercan

Chief Economist, Turkey

muhammet.mercan@ingbank.com.tr

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