

Turkish inflation likely to have reached the cyclical peak

Annual inflation in Turkey maintained the upwards trend in July but is likely to have reached its cyclical peak. Therefore, we expect the central bank to remain on hold in August and the coming few months



19%

Annual Inflation

(as of July)

Higher than expected

Inflation in Turkey in July came in higher than our call at 1.4% and market consensus at 1.54%.

The July inflation showed an upside surprise with a 1.8% MoM change - the highest July reading in the current inflation series. The figure pulled annual CPI inflation up to 19%, reaching the peak since early 2019, from 17.5% a month ago.

On the other hand, core inflation recorded a drop to 17.2% YoY, while its underlying trend on a

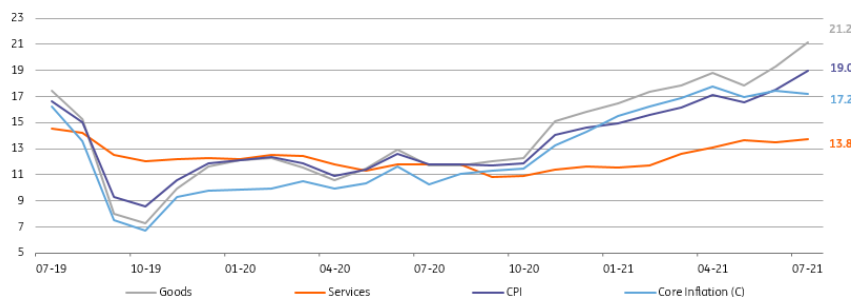
seasonally adjusted basis (3m-ma, annualised) also improved, after a pickup in June. The trend of services inflation has remained sticky and elevated, reflecting deterioration in pricing behaviour in recent months.

The breakdown shows goods inflation exceeding 21% in July, attributable to energy, and food, while price hikes in other sub-items were relatively strong showing broad-based pricing pressures
 2) services inflation at 13.8% moving up further driven by catering, and transportation services.

The domestic producer price index (D-PPI) has now reached almost 45% with another significant monthly increase at 2.5% in July. The difference between CPI and PPI expanded further to the peak in recent years at 26ppt, at an all-time peak, indicating elevated producer-price-driven cost impact on the inflation outlook driven by rising commodity prices, exchange rate effects and supply constraints in some sectors.

Evolution of annual inflation (%)

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

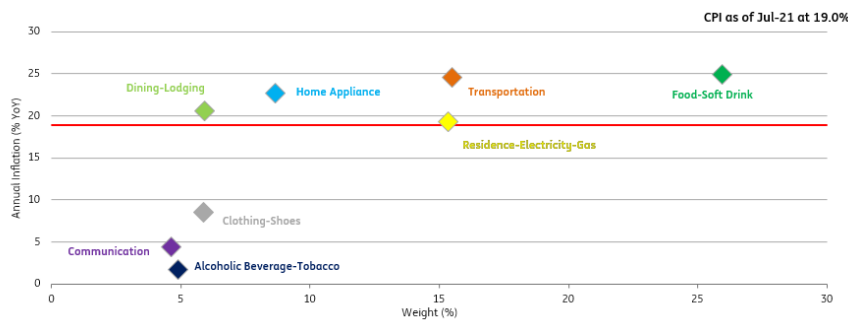


Source: TurkStat, ING

Regarding the main expenditure groups

- Housing inflation was the biggest contributor to the headline at 77bp, as expected, due mainly to utility price hikes. Accordingly, annual inflation in the group went up to 19.3% from 14.6%.
- We see a 73bp impact from food prices driven by both unprocessed foods (with large hikes in fresh fruits and vegetables) and processed foods, the latter recording the biggest July increase in 2003=100 inflation series. Annual inflation in food group jumped to 24.9% (vs the CBT's 15% call for end-2021 in the latest inflation report).
- Other key drivers of the headline figure were transportation (on the back of impacts from transportation services and LPG) and catering (likely attributable to price adjustments following unwinding pandemic control measures) with a 17bp contribution from each group.

Annual inflation in Expenditure Groups



Source: TurkStat, ING

Overall, driven by food inflation and administrative price adjustments impacting housing inflation, annual inflation maintained the uptrend in July.

The data show broad-based deterioration in price dynamics with buoyant demand conditions, elevated services inflation and the impact of normalisation of the pandemic. July inflation is likely to be the cyclical peak, while we expect the headline figure to remain above 18% until November before recording a pronounced decline in the last two months with base effects.

Given this backdrop, we expect the central bank to remain on hold in August and the coming few months and focus on a measured cut given its guidance that the current stance would be maintained until there is a significant fall in inflation. Accordingly, we see the policy rate at 18% this year with a 100bp cut in November.

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