Turkish inflation unexpectedly falls

In contrast to expectations, Turkish inflation for May marked a downward turn with an improvement in the underlying trend for both the headline and core figures. However, in the short term, there are still upside risks

People walk in an open market in Istanbul, Turkey

Source: Shutterstock

Turkish inflation for May showed a big downside surprise at 0.89% vs market consensus at 1.46% and our expectation of 1.3%, pulling annual CPI inflation down to 16.6% from 17.1% a month ago. Core inflation also recorded a drop to 17.0% YoY, while its underlying trend on a seasonally adjusted basis (3m-ma, annualised) has continued to improve with a deceleration last month. The trend of services inflation has remained sticky though stabilised lately, reflecting further deterioration in pricing behaviour with increasing backward indexation.

As of May, the difference between CPI and PPI expands further to the peak in recent years at 22ppt

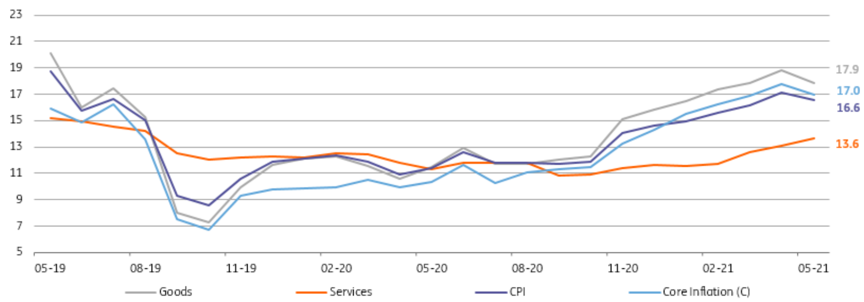
In the breakdown, we see: 1) goods inflation at 17.9%, down from the highest level since mid-2019 a month ago attributable to energy, clothing, durables and other core goods along with base effects from last year; and 2) services inflation at 13.6% inching up further, driven by rent as well as catering, transportation and communication services, showing that price pressures have remained high in this group.

Continuing its rapid uptrend on the back of the impact of exchange rate developments, rising commodity prices and strong base effects, the Domestic Producer Price Index (D-PPI) now exceeds 38% with another significant monthly increase of 3.9% May. The outlook indicates elevated producer-price-driven cost pressures on the inflation outlook driven by rising commodity prices, exchange rate effects and supply constraints in some sectors.

As of May, the difference between CPI and PPI expands further to the peak in recent years at 22ppt.

Evolution of annual inflation (%)

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

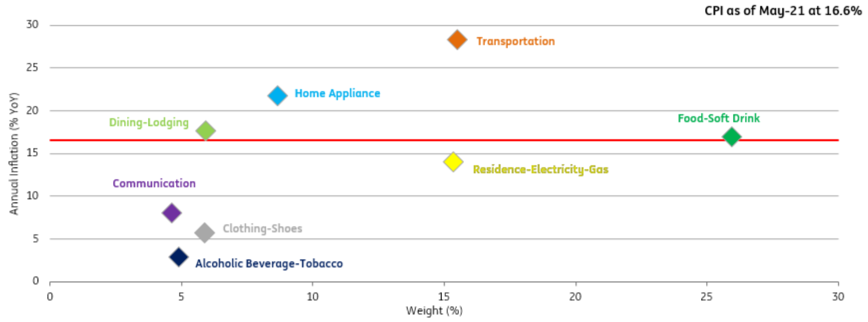


Source: TurkStat, ING

Regarding the main expenditure groups

- Transportation was the most significant contributor to the headline figure at 39bp, as expected. Given the recent fuel price hike, the government decided to pass on some of the price increase having been absorbing the price shock from the oil price via an automatic tax adjustment. However, annual inflation in the group showed some moderation to 28.4%, with a significant base effect from last year despite also the impact of currency weakness in automobile prices.
- We see a 12bp impact from housing prices, increasing rent and further adjustment in natural gas.
- Clothing pulled the headline up by 10bp, though the monthly change in this group at 1.8% was the lowest May figure in the current series, showing a relatively limited impact.
- Among heavyweights, food provided a modest lift to the May figure of 8bp, attributable to processed foods, while the monthly reading of unprocessed food turned negative due to a drop in fresh fruits and vegetable prices. As a result, annual inflation in the food group remained broadly unchanged at 17% (vs the CBT's 13% call for end-2021).

Annual inflation in expenditure groups



Source: TurkStat, ING

Although differing from expectations, the latest data shows a downward turn with some improvement in the underlying trend for both headline and core inflation. However, upside risks have remained with demand conditions, elevated services inflation, the recent uptrend in commodity prices, TRY weakness and supply constraints. Therefore, in the June investor meeting yesterday, the central bank provided clearer timing related to the latest guidance that “the current monetary policy stance will be maintained until the significant fall in the April Inflation Report’s forecast path is achieved”.

According to the Governor, “the significant fall” is expected at the end of the third quarter or the beginning of the fourth quarter. So, the expected rate cut should be announced around this time at the earliest.

Author

Muhammet Mercan
Chief Economist, Turkey
muhammet.mercan@ingbank.com.tr

Disclaimer