

Turkey: Inflation jumps to highest level in three years

CPI inflation in November jumped to the highest level in the last three years, while the underlying trend showed a significant acceleration, reflecting exchange rate developments and consequent pass-through



Shoppers in Istanbul

CPI came in at 3.51% last month, the highest November reading in the current inflation series and above the market consensus of around 3%, though significant currency volatility made inflation forecasting quite challenging. Accordingly, annual inflation jumped to 21.3% from 19.9% a month ago. When we look at the core inflation indicators, both B (excluding unprocessed food, energy, alcoholic beverages, tobacco and gold) and C (excluding energy, food and non-alcoholic beverages, alcoholic beverages, tobacco and gold) core inflation indices recorded lower increases than the headline rate, at 19.7% and 17.6%, respectively. The underlying trend for both indicators, on the other hand, showed a significant acceleration in comparison to a month ago, but remained below levels seen after the volatility of August 2018.

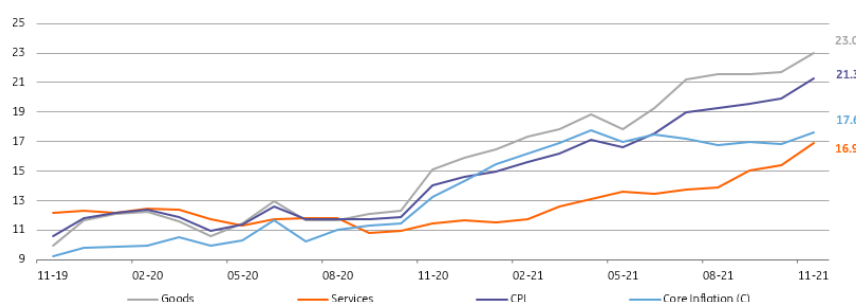
In the breakdown of the CPI, we see 1) goods inflation moving up to 23% with the impact of currency weakness weighing on energy, gold, processed food, and core goods while large base effects from last year were also in play 2) services inflation accelerating to 16.9% with an underlying trend at the highest since late-2018 on the back of exchange rate pass-through,

deteriorating pricing behaviour and backward indexation, along with the continuing impact of reopening

The November Domestic Producer Price Index (D-PPI) recorded one of the highest monthly increases at 10.0% and pulled the annual figure up to 54.6%, an all-time high in the current inflation series. The difference between CPI and PPI is now at a record level, 33.3ppt, showing unabatingly high cost-push pressures driven by the strength in commodity prices, cumulative exchange rate effects and continuing supply constraints in some sectors.

Evolution of Annual Inflation (%)

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

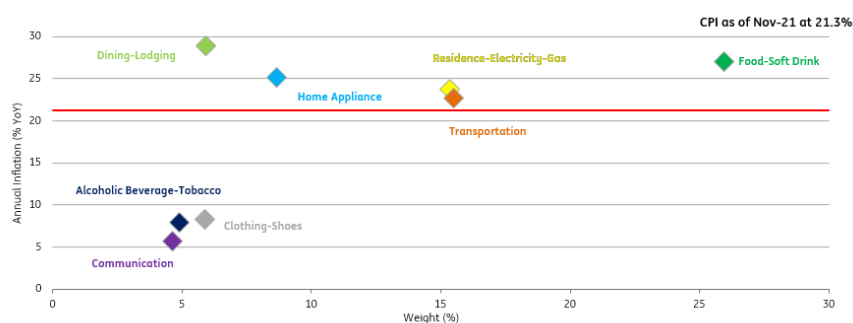


Source: TurkStat, ING

The main expenditure groups showed across-the-board price increases last month:

- Food prices provided the biggest contribution to the headline rate (1.05ppt) attributable to processed food while bread and cereals recorded the highest November reading in the current 2003=100 series. Showing a relatively benign change, fresh fruit and vegetables limited the impact on the headline from the food group. Given a recent adjustment to raw milk prices of close to 47%, dairy products (which have a 2.4% share in the CPI basket) will likely lead to further pressure in food inflation in December.
- Reflecting the impact of currency movements, transportation pulled the headline up by 0.95ppt driven by significant price hikes in automobiles and energy products.
- Housing and household equipment were among the other drivers, raising the monthly inflation rate by 0.5ppt and 0.3ppt, respectively. For the former, rent, water fees and coal prices were the main drivers. Despite the jump in global natural gas prices, the impact on the housing group is negligible as the government hiked prices only for industrial users and power plants while consumers have not been affected. However, keeping natural gas prices unchanged for longer would be challenging for the government given the higher fiscal burden. This increases risks to the inflation outlook.

Annual inflation in Expenditure Groups



Source: TurkStat, ING

Inflation will likely remain high in the near term and at elevated levels in the first half of next year before starting to moderate into year-end 2022 with the support of large base effects. While the broad-based rise in prices (due to import prices and higher trend inflation) increases upside risks for next year, the most important driver of the outlook is the path of the lira. The Central Bank of Turkey is not comfortable with currency movements as banks have directly intervened for the first time after many years. Given this backdrop, the governor reiterated in the latest investor meeting that there was limited room for another rate cut though this will be determined by developments ahead of the December meeting.

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