Turkey's annual inflation remains flat in October

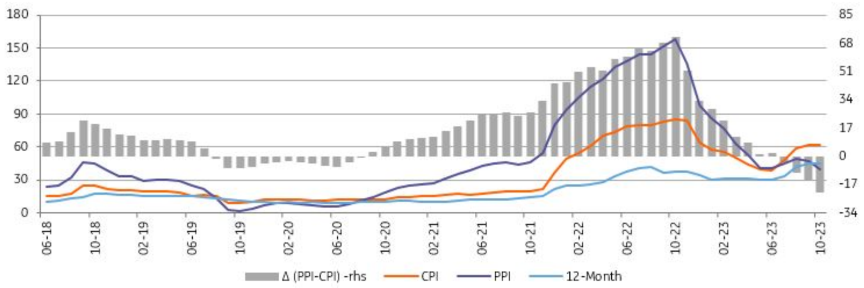
Annual inflation remained practically unchanged in October, while the underlying trend showed an improvement over the previous month

With a better-than-expected monthly inflation rate coming in at 3.4%, Turkey's annual figure remained broadly unchanged at 61.4% in October. The data reflects continuing deterioration in price dynamics with significant pressure in services and clothing, though deceleration in food and transportation limited the monthly inflation increase. In the last inflation report of the year, the Central Bank of Turkey (CBT) raised its year-end and 2024 inflation forecasts by 7pp to 65% and by 3pp to 36% respectively, while the band of uncertainty around the forecasts widened on the back of higher geopolitical risks and uncertainties surrounding administered prices.

Core inflation (CPI-C) came in at 3.7% month-on-month, rising to 69.8% on an annual basis on the back of worsening pricing behaviour and inertia in services prices. However, the underlying trend (as measured by 3m-ma, annualised percentage change, based on seasonally adjusted series) improved not only for the core but also the headline rate in October, in line with the CBT's expectations as specified in the MPC note. Given that the CBT also pledged that the policy rate will be determined in a way that will create the monetary and financial conditions necessary for ensuring a decline in the underlying trend of inflation, we should not rule out a possibility of deceleration in the pace of hikes in the upcoming MPC.

October PPI, on the other hand, stood at 1.9% on a monthly basis, translating into 39.4% year-on-year. The decline in annual PPI from close to triple digits at the end of last year shows improvement in cost pressures, despite the increase in the TL equivalent of import prices over recent months due to commodity price developments and exchange rate increases. While the sharp drop in October also reflecting favourable base effects is a positive development, limited moderation in domestic demand so far hints that producers will likely continue to pass their cost increases to consumers.

Inflation outlook (%)

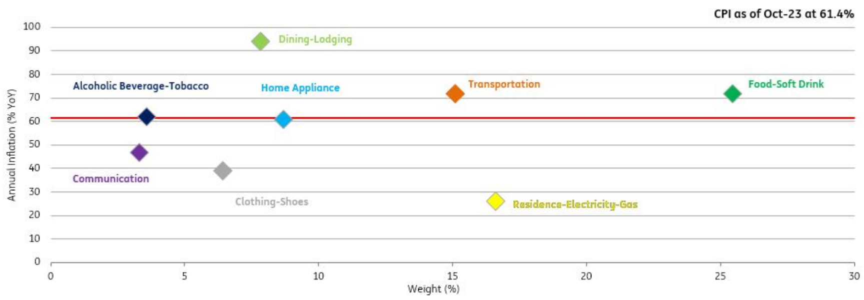


Source: TurkStat, ING

In the breakdown, all main expenditure groups – with the exception of transportation – positively affected the headline. Among them, the housing group turned out to be the major contributor with 0.93ppt, due mostly to natural price increases along with continuing rises in rents and adjustments in water fees. This was followed by food (0.84ppt) as a result of benign prices for fresh fruits and vegetables, close to the minimum of the October increases in the current inflation series.

In the latest reading, the annual inflation of these groups reached 72%, versus the CBT's expectations of 66.7% as outlined in the November inflation report. Clothing also stood out by lifting the headline 0.74ppt and recorded a strong 13.7% MoM, but annual inflation in this group remained relatively subdued at 39.2% YoY. On the flipside, transportation recorded a slight price decline on the back of benign gasoline and automobile prices. As a result, goods inflation went down to 51.5% YoY. Annual inflation in services – which is influenced by domestic demand and minimum wage hikes – maintained its uptrend and reached another peak at 88.6% YoY, despite a loss in momentum in comparison to the recent months.

Annual inflation in expenditure groups



Source: TurkStat, ING

The pass-through effects from the post-election adjustment in FX, wages and taxes has been “largely completed” as indicated by the CBT, but a deterioration in pricing behaviour, exchange rate-related risks, and likely pressure in oil prices due to geopolitical developments hint that inflation will likely remain elevated in the near term. However, the continuation of recent stability in the lira, a moderation in domestic demand and subsidies provided to consumers in electricity and natural gas prices will all prove supportive for the inflation outlook.

In this environment, the CBT has taken steps towards normalisation in interest rates and exchange rate policy after the elections. The latest rate hikes were significant and likely raised expectations for the final level in the current cycle. Following the signal of additional macroprudential measures in the October MPC (and thanks to progress in the monetary tightening process, with rates being high enough to control lending and support de-dollarisation) the CBT has taken significant steps to reinforce rate hikes in recent days. These moves and their impact on deposits and loans will be important for tightening financial conditions and controlling domestic demand.

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