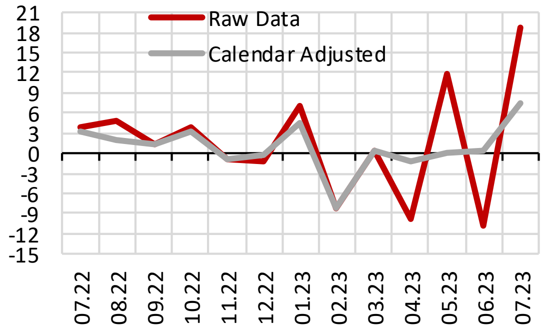
Macro: Industrial production decreased by 0.4% mom in July

The seasonally and calendar adjusted Industrial Production (IP) Index decreased by 0.4% in July on a monthly basis. However, due to calendar and base effects, it increased by 18.7% yoy. Adjusted for these two effects, the annual increase is close to that of the previous months, while the average monthly increase over the last two months is quite moderate at 0.4%. Divergences between different sectors prevail. Leading indicators (surveys) point to a decline in new orders and production due to rising costs and final product prices. Weakening external demand and monetary tightening steps are among the factors that will limit IP in the coming period. Nevertheless, construction-related sectors are expected to remain relatively strong and support IP in the short and medium term due to spending on earthquake-affected regions, as noted in MTP.

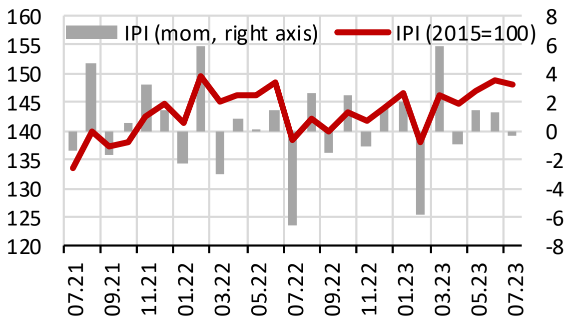
In July, the seasonally and calendar adjusted IP decreased by 0.4% mom and increased by 18.7% yoy (Charts 1 and 2). One of the factors behind the high annual rate of increase was the 2.5 more working days in July compared to July 2022 due to the shift of the Feast of Sacrifice from July to June. Adjusted for this calendar effect, IP increased by 7.4% yoy in July (Chart 1). This increase was mainly due to the base effect. In July 2022, the monthly IP had contracted by 6.6%. Therefore, it should be noted that the high annual rate of increase is not permanent and annual growth rates will normalize as these effects disappear in the remaining months of the quarter.

Chart 1. Industrial Production Index (IPI) (yoy)



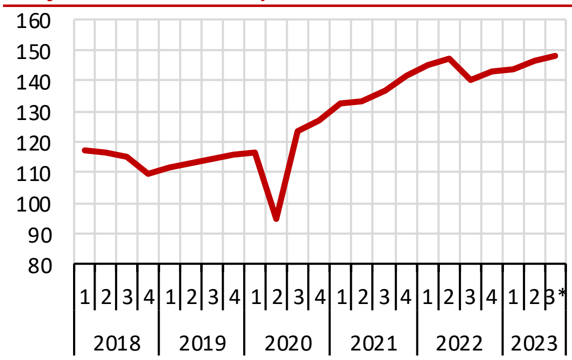
Source: Turkstat

Chart 2. IPI (seasonally and calendar adjusted)



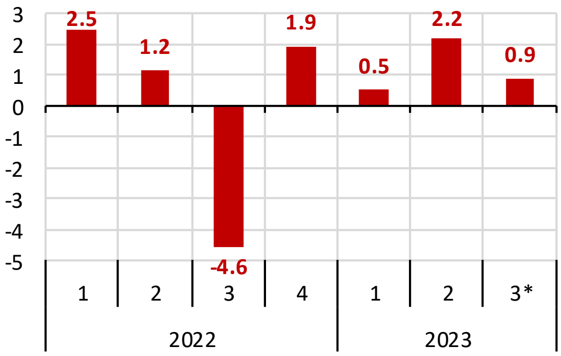
Source: Turkstat

Chart 3. IPI (seasonally and calendar adjusted. 2015=100)



Source: Turkstat

Chart 4. IPI (seasonally and calendar adjusted. qoq)



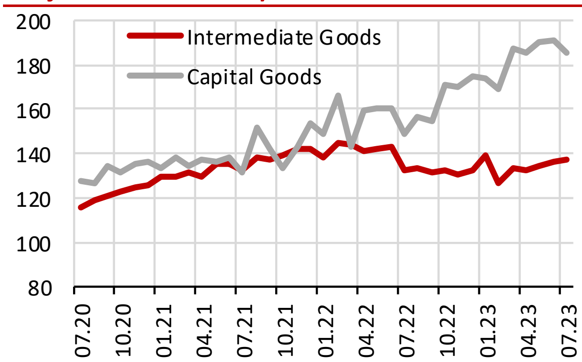
Source: Turkstat

Despite the monthly decline, the seasonally and calendar-adjusted level of production in July was 0.9% above the average for the second quarter (Charts 3 and 4). This looks like a slowdown in industrial production as the quarterly increase was slower than in the second quarter. However, as industrial production has been very volatile recently due to factors such as earthquakes, elections and shifting holidays, it is not enough to look only at quarterly changes to understand the extent of the slowdown.

Last month (Macro: Higher than expected increase in industrial production), we noted that bridge days had reduced IP by 1.2 pp in June and that this effect would be reversed in July. In this context, excluding the 1.2 pp upward effect of the bridge day, the decline in July rose from 0.4% to 1.6%, indicating a deeper monthly contraction in the underlying trend. Another way of analyzing the underlying trend by excluding the effects of the bridge day is to look at June and July together. The average monthly increase in IP over the last two months was 0.4%. This compares with the monthly average increase of 0.3% during April-May, which included Ramadan, and 0.0% between February-March during the earthquake period. Before the earthquake, the growth rate was quite high, above 1%. Therefore, although industrial production remains weak compared to the pre-earthquake period, there is no additional slowdown in July compared to the post-earthquake averages.

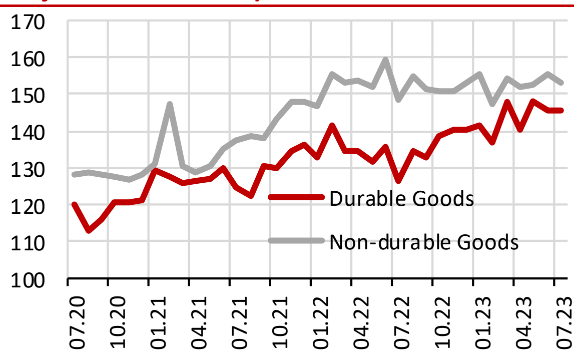
Looking at the Main Industrial Groupings (MIGs), the monthly decline in the IPI was driven by capital goods and non-durable goods. Durable goods remained flat in this period, while production of energy and intermediate goods increased (Charts 5 and 6, Table 1). According to sectoral breakdown, manufacturing recorded a sharper decline than in the IP, falling by 1.4% (Table 1). Intermediate goods saw a correction to the strong growth seen in the construction-related sectors in June. While the monthly decline for mineral products was 2.7%, the decline for ready-mixed concrete was more pronounced, falling by 11.0%. Again, while the monthly decline in basic metals was 2.9%, the contraction in its iron and steel sub-sector was more pronounced at 3.5%. On the other hand, there were relatively strong increases in intermediate goods for paper and wood and cork products (Table 1). However, chemicals and chemical products posted a sharp 5.1% month-on-month decline, following four months of stagnation. Following last week's MTP announcement, we expect the substantial spending on rebuilding the earthquake zone to support construction-related sectors in the period ahead.

Chart 5. IPI (seasonally and calendar adjusted. 2015=100)



Source: Turkstat

Chart 6. IPI (seasonally and calendar adjusted. 2015=100)

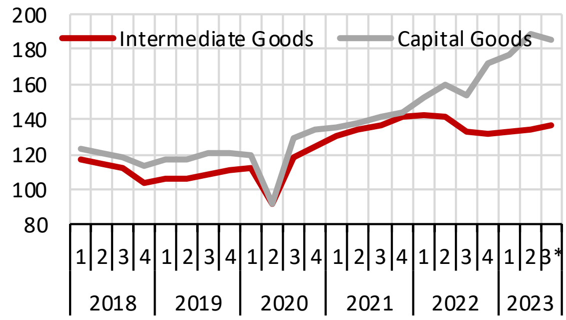


Source: Turkstat

The decline in **non-durable goods (1.5%)** was led by a 9.9% fall in the **clothing** sector, the largest monthly decline since the pandemic and spread across all sub-items in the sector. On the other hand, the outlook for **textiles** is flat, but the downward trend in weaving continues. These are both highly labor-intensive sectors that are highly sensitive to wage increases. We believe that the erosion of competitiveness due to rising costs is having a negative impact on these sectors. While **food**, the largest sector of consumer non-durables, rose by 0.3%, the 14.8% monthly increase in pharmaceuticals limited the negative impact of clothing to some extent. On the durable goods side, although the monthly outlook was flat, there was a divergence in sub-components; while output of **electrical equipment** fell, **furniture** rose (Table 1).

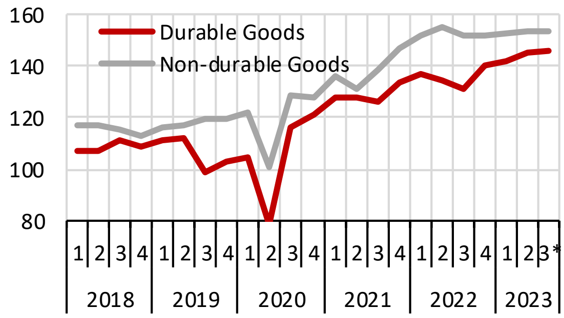
The most significant mom fall was for **capital goods**, which fell by 2.8%. However, the decline was due to sharp falls in **computer and optical products and other transport vehicles** (-10.7% and -17.9% respectively), which are always highly volatile. We estimate that these two sectors made a negative contribution of around 0.8 and 4.9 points to IP and capital goods, respectively. Therefore, there is no negative outlook for capital goods except for these two sectors. In fact, the production of **vehicles** increased by 4.5% mom, while the production of **machinery and equipment** increased by 1.2% mom, extending the streak to the 5th month.

Chart 7. IPI (seasonally and calendar adjusted. 2015=100)



Source: Turkstat

Chart 8. IPI (seasonally and calendar adjusted. 2015=100)



Source: Turkstat

Leading indicators signal that industrial production will weaken in August.

- The ICI manufacturing PMI index fell to 49 in August. The fall in new orders stood out.
- Capacity utilization rate (seas. adj.) fell by 1.2 points to 75.7% in August, with continued divergence between sectors.
- According to preliminary data, exports to Europe, our main export market, declined.
- The production of transport equipment will be significantly lower in August as a result of scheduled maintenance and repair work. This will temporarily lower the IPI on both a monthly and annual basis.

Table 1. Industrial Production Index (Seasonally and Calendar Adjusted)

	Monthly % Chg				Quarterly % chg			
	Apr.23	May.23	Jun.23	Jul.23	2022-Q4	2023-Q1	2023-Q2	2023-Q3*
IPI	**-0.9**	**1.4**	**1.2**	**-0.4**	**1.9**	**0.5**	**2.2**	**0.9**
Mining and quarrying	**-0.8**	**2.8**	**-6.0**	**10.5**	**3.9**	**-2.6**	**-2.9**	**7.0**
Mining of coal and lignite	4.3	-13.7	18.6	-0.2	3.9	-32.8	-8.2	6.1
Extraction of crude petroleum and natural gas	0.8	2.2	0.3	1.3	2.0	2.4	2.8	2.2
Mining of metal ores	1.2	5.9	-14.9	22.3	7.9	6.6	-1.0	11.7
Other mining and quarrying	-7.6	4.6	-1.4	0.7	-1.9	-2.5	-7.4	1.3
Manufacturing	**-1.1**	**1.2**	**2.0**	**-1.4**	**2.3**	**0.8**	**2.4**	**0.3**
Food products	-0.6	0.8	3.0	0.3	0.8	1.4	-0.5	2.5
Beverages	2.1	0.7	-5.0	6.7	7.9	-6.6	1.7	3.4
Tobacco products	11.1	0.8	-0.6	-1.9	6.6	-4.4	15.6	-2.0
Textiles	1.4	1.0	-0.2	0.0	-4.1	-3.1	5.1	0.2
Wearing apparel	-2.7	1.5	0.8	-9.9	-1.0	4.0	0.0	-9.0
Leather and related products	-4.0	-0.8	-1.0	-0.4	9.8	-0.9	-3.5	-1.3
Wood and cork products	-5.1	-4.3	4.4	1.8	-3.6	13.4	-3.2	3.3
Paper and paper products	-1.5	1.3	6.0	3.2	-3.2	-4.5	2.3	7.7
Printing and reproduction of recorded media	4.1	-4.1	-7.7	2.1	-6.7	-7.0	4.0	-4.7
Coke and refined petroleum products	-1.9	0.3	7.8	-1.0	-0.8	-7.1	1.8	4.1
Chemicals and chemical products	-0.4	-1.8	1.1	-5.1	-4.7	-1.9	0.0	-5.0
Basic pharmaceutical products	-4.0	4.6	2.3	14.8	1.7	-2.6	1.6	18.3
Rubber and plastic products	-1.6	0.4	2.3	-0.2	1.8	4.5	-1.1	1.5
Other non-metallic mineral products	-4.3	2.2	5.3	-2.7	-1.6	1.6	-2.4	1.4
Base metals	-1.4	2.5	6.5	-2.9	-2.8	1.4	3.4	2.0
Fabricated metal products	5.0	-2.1	-0.4	0.2	4.3	4.2	6.7	-0.8
Computer. electronic and optical products	-8.3	8.1	20.1	-10.7	25.8	-3.0	-0.5	2.9
Electrical equipment	-2.8	2.0	2.8	-1.9	6.2	4.4	0.1	0.6
Machinery and equipment	1.0	0.1	0.3	1.2	5.0	2.9	0.9	1.4
Motor vehicles.	-1.7	4.5	-4.6	4.5	3.5	4.7	4.9	2.7
Other transport equipment	-5.3	8.6	-1.2	-17.9	41.5	-3.4	28.5	-16.3
Furniture	-2.1	3.9	-2.9	2.8	7.9	-0.6	2.5	2.1
Other manufacturing	-2.7	-2.3	0.6	-2.6	3.5	2.6	0.8	-3.0
Repair and installation of mach. and equip.	0.6	0.3	3.8	7.0	10.3	5.8	2.9	9.7
Electricity. gas. steam	**0.7**	**2.2**	**-2.0**	**3.7**	**-4.3**	**1.7**	**2.7**	**3.1**
IPI	**-0.9**	**1.4**	**1.2**	**-0.4**	**1.9**	**0.5**	**2.2**	**0.9**
Intermediate Goods	-0.6	1.2	1.7	0.3	-0.5	0.7	1.1	1.8
Durable Consumer Goods	-4.8	5.4	-1.5	0.0	6.6	1.5	2.0	0.7
Non-durable Consumer Goods	-1.5	0.1	2.1	-1.5	0.0	0.6	0.6	-0.1
Energy	0.5	1.4	0.1	2.8	-3.1	-1.6	2.1	3.3
Capital Goods	-0.9	2.5	0.6	-2.8	12.1	2.8	6.7	-1.6
Low Technology	-1.1	0.9	1.0	-0.8	-0.4	-0.3	1.3	0.1
Medium-Low Technology	-0.9	0.9	3.7	-0.5	1.2	2.4	1.8	2.2
Medium-High Technology	2.0	-0.3	-1.6	1.0	4.7	1.7	3.3	-0.2
High Technology	-15.7	14.1	15.6	-18.6	21.4	-2.8	10.8	-6.9

* As of July
Source: TURKSTAT

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