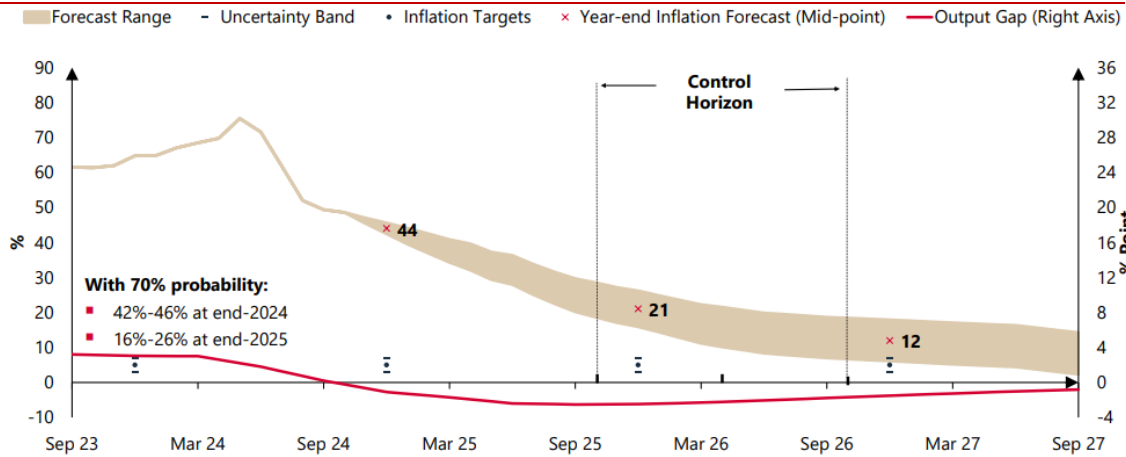


Macro: CBRT revised inflation forecasts upwards but will not respond to the inflationary outlook with a tighter monetary stance

1. Forecasts

In the 2024-IV Inflation Report, the CBRT raised its year-end inflation forecasts for 2024, 2025 and 2026 to 44%, 21% and 12%, respectively (Chart 1). In the previous Inflation Report, the forecasts were 38%, 14% and 9%, respectively. The uncertainty band around the inflation forecasts has been revised to 42%-46% for 2024 and 16%-26% for 2025, while it has been set at 6%-18% for 2026.

Chart 1. 2024-IV Inflation and Output Gap Forecasts



Sources of forecast revision: The significant upward revision in the year-end inflation forecasts for 2024 and 2025 was mainly driven by the ‘initial conditions, underlying inflation and inertia’ item, as the improvement in the underlying trend did not materialize at the expected pace, and the upward revision in the food inflation assumption. Apart from these, changes in TL-denominated import prices and output gap forecasts also raised inflation forecasts.

The assumption of administered price adjustments for 2025 also contributed 0.9 points to the forecast revision. In the report, it was stated that ‘the regulations on electricity pricing dynamics had an upward impact on consumer inflation compared to the assumptions in the previous inflation report. In addition, assumptions for administered prices were also revised due to the upward revision in the inflation forecast’.

Table 1. Revisions to Inflation Forecasts

	2024	2025
IR 2024-III Year End Forecast (%)	38	14
IR 2024-IV Year End Forecast (%)	44	21
Forecast Revision as Compared to IR 2024-III Period (% Point)	6	7
Sources of Forecast Revisions (% Point)		
Food Prices	+1.6	+1.9
Import Prices in Turkish Lira	+0.2	+0.5
Output Gap	+0.3	+0.2
Administered Prices	-	+0.9
Initial Conditions, Underlying Inflation and Inertia	+3.9	+3.5

2. Assumptions

External demand: The assumption for the external demand outlook remained unchanged. Expected export-weighted global growth is 2.0% for 2024 and 2.4% for 2025, below the historical average.

Food prices: The 2024 and 2025 food inflation assumptions were revised upwards to 41.8% and 22.5% (previously 35.5% and 15%), respectively (Table 2). We had previously emphasized that the food assumption remained optimistic in our macro notes earlier this year. This revision confirms our previous projections.

Since the cumulative increase in food prices in the first 10 months of this year was 34.9%, the cumulative price increase in the remaining two months should be 4.9% for this year's assumption to hold. Such an increase implies a slowdown in seasonally adjusted monthly food inflation. We find this forecast achievable if there is a correction for the recent acceleration in fresh fruits and vegetables. Nevertheless, we think that unprocessed food-driven upside risks to the inflation forecast also persist.

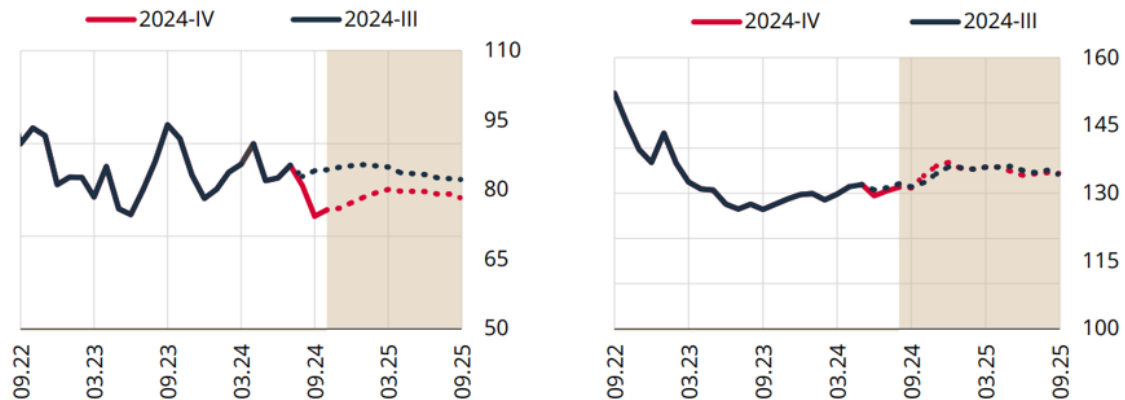
Table 2. Assumption Updates*

		IR 2024-III	IR 2024-IV
Global Production Index* (Average Annual % Change)	2024	2.0	2.0
	2025	2.4	2.4
Oil Prices (USD, Annual Average)	2024	84.2	81.1
	2025	82.9	78.8
Import Prices (USD, Average Annual % Change)	2024	0.7	0.8
	2025	2.8	2.8
Food Prices (Year-End % Change)	2024	35.5	41.8
	2025	15.0	22.5

* Based on the growth rates and export shares of 110 countries to which Türkiye exports.

Commodity prices: Oil prices remained below the assumption in the last reporting period. Accordingly, the average oil price assumption for 2024 was lowered from \$84.2 to \$81.1 and for 2025 from \$82.9 to \$78.8 (Table 2 and Chart 2). Despite the decline in energy commodity prices, the outlook for non-energy commodity prices turned more negative, which limited the revision in assumptions for import prices in general.

Chart 2. Oil (left panel) and Import Price (right panel) Assumptions

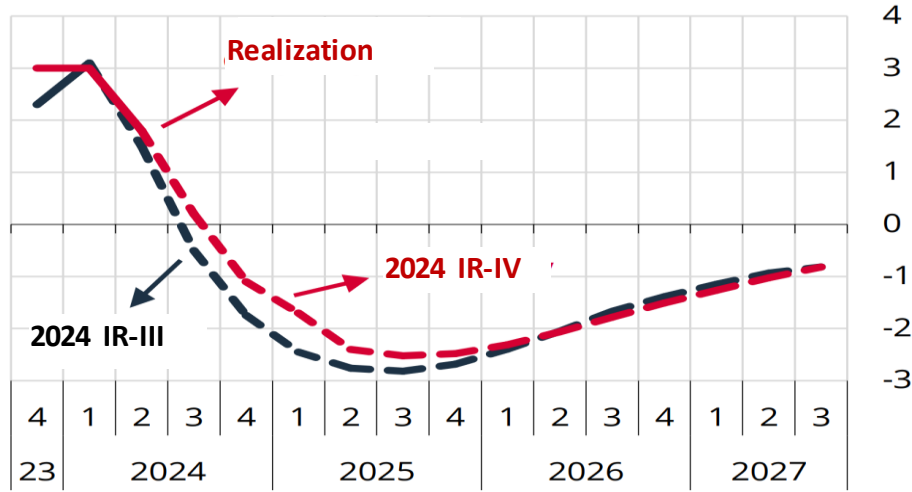


Source: Bloomberg, CBRT

* Shaded areas show the forecast horizon

Economic activity: As in previous reports, output gap forecasts were revised upwards based on realizations (Charts 1 and 3). Therefore, the disinflationary impact of demand conditions on economic activity has diminished compared to the previous report.

Chart 3. CBRT Output Gap Forecasts



- We calculate that output gap forecasts point to a quarter-on-quarter contraction (negative quarterly growth) in Q3 and a flat outlook in Q4. Until the last quarter of 2025, the disinflationary contribution of aggregate demand conditions is expected to increase with “below-potential quarterly growth (deepening negative output gap). Starting from the last quarter of 2025, the quarterly growth of economic activity is expected to reach its potential and then exceed it.
- We estimate that the presented output gap path is consistent with a growth forecast of around 2.5% for 2024. In the previous report, it was 3.0%. This downward revision reflects the base effect from the revision of 2023 growth from 4.5% to 5.1%. For 2025, we calculate the implied growth forecast as 1.5%.
- When converting output gap forecasts into growth forecasts, the potential growth assumption is important. Table 3 shows the growth forecasts implied by the output gap under different quarterly potential growth assumptions:

Table 3. Growth Forecasts Implied by Output Gap Forecasts (%)

	Quarterly Potential Growth (%)		
	0.8	1.0	1.2
2024	2.2	2.4	2.6
2025	0.0	0.7	1.5
2026	3.6	4.5	5.3

Exchange rate: Although not explicitly shared in the inflation reports, we believe that the CBRT's exchange rate assumption has not changed significantly compared to the previous reporting period. We assess that the current forecasts imply a value around 35.0 for end-2024 and 41.0 for end-2025 for the USD/TL exchange rate.

3. Our Evaluations

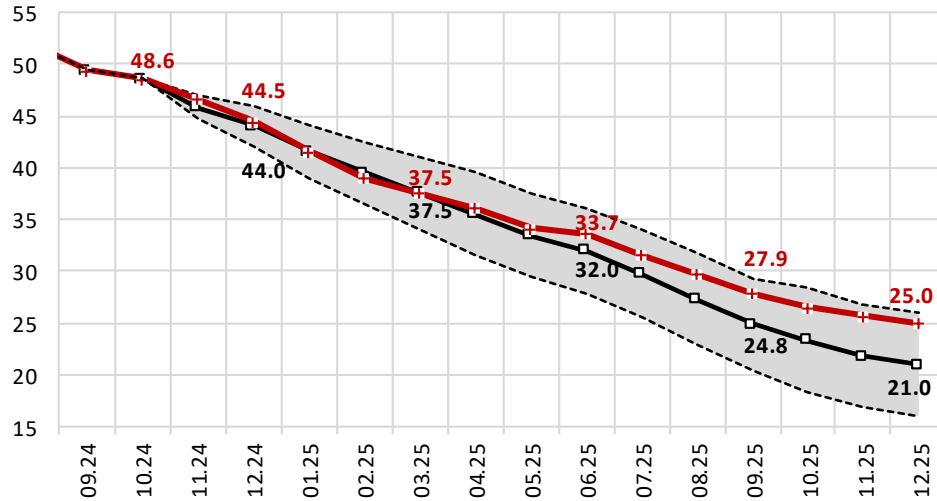
Forecasts are more dovish than in the past in terms of the monetary stance and support the intention to cut interest rates in December.

- While the year-end inflation forecast for 2024 was revised upwards by 6 points, that for 2025 was revised upwards by 7 points, which means that the CBRT will not respond to the short-term inflationary outlook with a tighter monetary stance.
- Thus, the CBRT recognizes that it will not be able to reach the degree of monetary tightness (very high real interest rates and sacrifice of growth) required to bring inflation below 20% in 2025.

When we compare our forecasts with the monthly inflation path derived from the CBRT's fanchart, we observe that our forecasts are quite close to each other in the first five months of the year (Chart 4).

- Although our forecasts remain within the CBRT's uncertainty band throughout the year, they diverge from the official path starting from June. We believe that this divergence stems from growth and exchange rate projections that are not explicitly shared in the report. The CBRT forecasts a growth rate of around 1.5%, which would lower end-2025 inflation to 21%, but the growth forecast in the MTP is much higher at 4.0%. If growth realizes above CBRT's forecast, inflation will come closer to our forecast.

Chart 4. Annual Inflation Forecasts (Akbank vs. CBRT)



Source: CBRT, Akbank.

Note: CBRT forecast path is derived from the Chart in the Inflation Report by ourselves.

Red line shows Akbank forecast, while black line shows CBRT forecast. Grey area shows the uncertainty band around CBRT's forecast.

This report is prepared by Akbank Economic Research

Economic.research@akbank.com

Çağrı Sarıkaya– Chief Economist

Cagri.Sarikaya@akbank.com

Çağlar Yüncüler

Caglar.Yunculer@akbank.com

M. Sibel Yapıcı

Sibel.Yapici@akbank.com

Alp Nasır

Alp.Nasir@akbank.com

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