July 2020 Inflation Report: Main Sections

- Overview
- International Economic Developments
- Inflation Developments
- Supply and Demand Developments
- Financial Conditions and Monetary Policy
- Public Finance
- Medium Term Projections
July 2020 Inflation Report: Boxes

- Measures during the Pandemic, Public Health and Economic Activity
- An Evaluation of Recent Unit Cost Developments
- Weekly Economic Conditions Index (WECI)
- Survey of the Effects of the Pandemic on the Real Sector
- The CBRT’s Bond Purchases in Response to the Pandemic
- Pandemic-Driven Supply and Demand Shocks and Their Impact on Potential Output and Output Gap
Macroeconomic Developments
Global Economic Outlook

- Global economic activity has shown signs of partial recovery after normalization steps, yet uncertainties remain high.
- Portfolio outflows from emerging countries continued in the second quarter, albeit at a slower pace.

Global PMI (Seasonally Adjusted, Level)

Portfolio Flows to Emerging Economies (Billion USD, 4-Week Cumulative)
Financial Developments

- While exchange rate volatility has declined due to the improvement in global risk appetite, credit growth has accelerated on the back of monetary and financial measures.

**Implied FX Volatility** (1 Month, %)

**Credit Growth Rates** (13-Week Moving Average, Adjusted for Exchange Rate, %)

*Emerging economies include Brazil, Chile, Colombia, Mexico, Poland, The Philippines, Malaysia, S. Africa, Indonesia, Romania and Hungary.*
Economic Activity and Current Account Balance

- Economic recovery, which started in May following gradual steps towards normalization, is gaining pace.
- The recovery in exports of goods and low levels of commodity prices will support the current account balance in the upcoming periods.

Weekly Economic Conditions Index

Current Account Balance (CAB, Billion USD)
Labor Market

- While unemployment rates increased, the fall in the labor force participation rate limited the increase.

Unemployment and Labor Force Participation Rates (Seasonally Adjusted, %)

Source: HLFS, TURKSTAT

* As of April period.
Consumer inflation and core inflation (B Index) were above the April forecasts in the second quarter of the year.

April 2020 Inflation Forecast and Actual Inflation* (%)

April 2020 Forecast and Actual Rates for Inflation Excl. Unprocessed Food, Energy, Alcohol-Tobacco and Gold (B Index)* (%)

* Shaded region indicates the 70 percent confidence interval for the forecast.
Inflation

- Consumer inflation increased in the second quarter due to core goods and food groups.
- Pandemic-related rise in unit costs have led to an increase in the trends of core inflation indicators.

**Contribution to Annual CPI (% Point)**

**Indices B and C (Seasonally Adjusted, Annualized 3 Month Average % Change)**

Source: CBRT, TURKSTAT

* Core Goods: Goods excluding food, energy, alcoholic beverages, tobacco and gold.
** Tobacco and Gold: Alcoholic beverages, tobacco and gold.
Inflation Expectations

- Year-end inflation expectations increased in July, while medium-term expectations remained relatively flat.

Inflation Expectations (%)

Distribution of Inflation Expectations (12-Month-Ahead)

* Data from the CBRT Survey of Expectations responded by the representatives of the real and financial sectors.

Source: CBRT
Monetary Policy

- Policy rate was kept unchanged at 8.25 percent in June and July on the back of inflation outlook.
- Funding composition has changed after the introduction of new facilities in open market operations.

CBRT Rates and Short Term Interest Rates (%)

CBRT Open Market Operations (Two-Week Moving Average, Billion TL)

Source: BIST, CBRT

Source: CBRT
Main Assumptions and Forecasts
Assumptions for External Variables

- While international crude oil price assumptions were revised upwards, USD-denominated import price assumptions were revised downwards.

Revisions to Oil Price Assumptions* (USD/Barrel)

Revisions to Import Price Assumptions* (Index, 2010=100)

* Shaded area shows the forecast period.

Source: Bloomberg, CBRT

Source: CBRT, TURKSTAT
## Revisions in Assumptions

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<thead>
<tr>
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<th>April 2020</th>
<th>July 2020</th>
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<tbody>
<tr>
<td><strong>Output Gap (Percent)</strong></td>
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<tr>
<td>2020 Q1</td>
<td>-1.5</td>
<td>-1.5</td>
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<tr>
<td>2020 Q2</td>
<td>-7.8</td>
<td>-6.4</td>
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<td><strong>Export-Weighted Global Production Index</strong></td>
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<td>(Average Annual Percent Change)</td>
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<tr>
<td>2020</td>
<td>-4.75</td>
<td>-7.56</td>
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<tr>
<td>2021</td>
<td>4.38</td>
<td>5.83</td>
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<td><strong>Oil Prices (Average, USD)</strong></td>
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<tr>
<td>2020</td>
<td>32.6</td>
<td>41.6</td>
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<tr>
<td>2021</td>
<td>36.8</td>
<td>43.8</td>
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<td><strong>Import Prices (USD, Average Annual Percent Change)</strong></td>
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<tr>
<td>2020</td>
<td>-5.1</td>
<td>-6.2</td>
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<tr>
<td>2021</td>
<td>7.3</td>
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<td><strong>Food Prices (Year-end Percent Change)</strong></td>
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<tr>
<td>2020</td>
<td>9.5</td>
<td>10.5</td>
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<tr>
<td>2021</td>
<td>7.0</td>
<td>8.0</td>
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Inflation and Output Gap Forecasts* (%)

Under the current monetary policy stance and strong policy coordination, inflation is projected to converge gradually to the targets.

Inflation is projected to be 8.9% at end-2020 and fall to 6.2% at end-2021, before stabilizing around 5% in the medium term.

Accordingly, inflation is expected to be
- between 6.9% and 10.9% (with a mid-point of 8.9%) at end-2020
- between 3.9% and 8.5% (with a mid-point of 6.2%) at end-2021

with 70% probability.

Source: CBRT, TURKSTAT

* Shaded region indicates the 70 percent confidence interval for the forecast.
Inflation and Output Gap Forecasts* (%)

- Forecast Range*
  - Inflation Targets
  - Year-end Inflation Forecast (Mid-point)

Drivers of the revision in 2020 year-end inflation forecasts relative to previous Report:
- +0.5 points from TL denominated import prices,
- +0.2 points from food inflation,
- +0.3 points from output gap,
- +0.2 points from real unit costs,
- +0.3 points from the underlying trend of inflation.

Accordingly, the inflation forecast for end-2020 was revised upwards by 1.5 percentage points.

Source: CBRT, TURKSTAT

* Shaded region indicates the 70 percent confidence interval for the forecast.
Factors that affect 2021 year-end inflation forecasts, relative to previous Report:

- TL denominated import prices by +0.1 points,
- Food inflation by +0.2 points,
- Output gap by +0.2 points,
- Underlying trend of inflation by +0.3 points.

Accordingly, the inflation forecast for end-2021 was revised upwards by 0.8 percentage points.
Overview

- Economic recovery, which started in May following gradual steps towards normalization, is gaining pace.

- The recovery in exports of goods and low levels of commodity prices will support the current account balance in the upcoming periods.

- Despite the restraining effects of aggregate demand conditions, pandemic-related rise in unit costs have led to an increase in the trends of core inflation indicators.

- As the normalization process continues, supply-side factors, which have prevailed recently due to pandemic-related restrictions, will phase out.

- The forecast that demand-driven disinflationary effects will become more evident in the second half of the year is preserved.

- Credit growth and its composition are closely monitored for their effect on internal and external balance.

- Maintaining a sustained disinflation process is a key factor for achieving lower sovereign risk, lower long-term interest rates, and stronger economic recovery.
Briefing on 2020-III Inflation Report

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