

Summary of the Monetary Policy Committee Meeting

30 June 2022, No: 2022-30

Meeting Date: 23 June 2022

Inflation Developments

1. Consumer prices rose by 2.98% in May, while annual inflation increased by 3.53 points to 73.50%. Up across all subcategories, annual consumer inflation was mostly driven higher by core goods and services. Annual inflation increased in all subcategories of core goods. On the services front, annual inflation was relatively flat for transportation services, but went up in other subcategories, especially in restaurants-hotels. As for the food category, annual inflation declined in unprocessed food due to the partial correction in vegetable prices, but continued to rise in processed food. The outlook for energy inflation was largely dominated by changes in municipal water tariffs and fuel prices. Producer prices increased further due to international commodity prices, rising domestic energy prices and ongoing supply chain disruptions. Thus, annual inflation went up in B and C indices.
2. Prices of food and nonalcoholic beverages increased by 1.63% in May, while annual inflation rose by 2.53 points to 91.63% in this category. Annual inflation fell by 3.06 points to 97.61% in unprocessed food but increased by 7.92 points to 86.01% in processed food. Across items of unprocessed food, seasonally adjusted prices of fresh fruits and vegetables recorded a decline due to the correction in vegetable prices. Across items excluding fresh fruits and vegetables, prices of red meat, white meat, milk, rice and dried nuts saw an increase, whereas egg prices dropped. Despite the decline in unprocessed food inflation, processed food inflation remained on the rise. In the bread and cereals item, where the effects of grain price developments were observed, annual inflation was realized at 90.69 percent, as prices increased by 3.65 percent. Monthly price hikes were more pronounced for processed food items excluding bread and cereal due to fats-oils, tea-coffee, meat products, sugar and related products, and especially cheese and other dairy products.
3. Energy prices rose by 2.90 % in May, and annual energy inflation increased by 3.01 points to 121.21%. This was mostly driven by administered municipal water tariffs and fuel prices led by Turkish lira-denominated oil prices. In this period, solid fuel prices continued to increase, especially for coal, while bottled gas prices were slightly down relative to international butane and propane prices.
4. Prices for services rose by 3.73% in May, and annual services inflation rose by 3.60 points to 45.78%. Annual inflation was relatively flat in transportation services, but was higher in other subcategories, with restaurants-hotels in the lead. Annual inflation increased by 7.57 points to 76.83% in restaurants-hotels, but remained flat at 78.16% in transportation services due to the base effect. Prices for the other services subcategory rose by 2.97% on the back of package tours dominated by pilgrimage tours that are about to resume, while seasonally adjusted data indicate that there has been some acceleration in monthly rent increases.
5. The annual core goods inflation increased by 3.74 points to 65.32% in May. Annual inflation rose across all subgroups. Durable goods prices were up by 2.14% in May, led by furniture,

automobile and white goods. Thus, annual inflation in durable consumption goods reached 76.75%. Monthly inflation in the other core goods group stood at 3.94%. While this was mainly driven by household-related cleaning materials, personal care products and housing maintenance and repair materials, price increases spread across the group. Clothing and footwear prices rose by 4.63% in May, driving annual inflation up by 3.52 points to 29.27%.

6. In May, alcoholic beverages and tobacco products increased by 6.53% and annual inflation rose to 66.62%. While this rise was determined by the price increases by producer firms, the contribution of this group to monthly consumer inflation stood at 0.28 points.
7. According to the June results of the Survey of Market Participants, the current year-end inflation expectation rose by 6.67 points to 64.59% and the 12-month-ahead inflation expectation increased by 4.63 points to 37.91%. The 24-month-ahead inflation expectation is 22.04%.

Factors Affecting Inflation and Risks

8. The escalating geopolitical risks were adversely realized in the first half of the year and caused a weakening in the worldwide economic activity. Global growth forecasts for the upcoming period are being revised downwards.
9. Increasing concern over global food security driven by trade restrictions, high course of commodity prices, the persistence of supply constraints in some sectors, particularly in food and energy, and high transportation costs have led to producer and consumer price increases internationally. The effects of high global inflation on inflation expectations and international financial markets are closely monitored. Moreover, central banks in advanced economies emphasize that the rise in inflation may last longer than previously anticipated due to rising energy prices and imbalances between supply and demand. The divergence in monetary policy steps and communications of central banks in advanced economies increased due to their diverse economic outlook. It is observed that central banks have increased their efforts to develop new supportive measures and tools to cope with the increasing uncertainties in financial markets.
10. Regarding portfolio flows to emerging economies, bond and equity markets both continued to register outflows in June in tandem with the global risk appetite. However, the volatility in long-term bond rates in advanced economies and the course of global financial conditions keep the risks to portfolio flows to emerging economies alive. The impact of such risks through the portfolio flows channel towards Türkiye is expected to remain relatively limited, considering the current levels of non-residents' portfolio positions.
11. Increase in inflation is driven by rising energy costs resulting from geopolitical developments, temporary effects of pricing formations that are not supported by economic fundamentals, strong negative supply shocks caused by the rise in global energy, food and agricultural commodity prices.
12. As a result of geopolitical developments, the high levels seen in commodity prices, primarily in energy and agricultural products, the ongoing disruptions in supply chains and increases in domestic energy costs continue to affect producer prices. Across main industrial categories, annual inflation was almost flat in intermediate goods, but was up in other subgroups, energy in particular. The energy producer prices increased by 27.65% month-on-month, driven by the rise in natural gas prices.
13. Economic activity remained strong in the first quarter of 2022. In this period, the Gross Domestic Product (GDP) increased by 7.3% year-on-year, and by 1.2% quarter-on-quarter in seasonally and calendar adjusted terms. On the production side, the main determinants of annual growth in the first quarter were services and the industry sectors, while the

construction sector limited growth. On the expenditures side, the main driver of annual growth was the final domestic demand led by private consumption, while the contribution of net exports was 3.5 points. Machinery-equipment investments, a component of total investments, continued to grow on a yearly basis. As a matter of fact, as of the first quarter of the year, the share of machinery-equipment investments and net exports in GDP reached its highest level over the last decade.

14. Level of capacity utilization and other leading indicators show that robust growth in the beginning of the year continues in the second quarter as well, with the support of external demand. Industrial production adjusted for seasonal and calendar effects remained flat in April compared to the previous month. Thus, production grew by 0.3% in April compared to the previous quarter. The industrial production of sectors with higher export shares posted a strong growth in this period. Industrial turnover indices also revealed that external demand continued to support industrial production. Meanwhile, retail sales volume indices were up in April compared to the previous quarter, indicating the ongoing recovery in domestic demand.
15. Investment tendencies of manufacturing industry firms for the next twelve months remain high. Firms' registered domestic and external orders and future order expectations reveal that external demand maintains its supportive course in the second quarter. On the other hand, card spending data confirm the recovery trend in domestic demand for the April-May period.
16. Developments in the labor market are in tandem with the outlook of economic activity. In April, the seasonally-adjusted total employment rate rose by 1.4% (approximately 408 thousand people) month-on-month. As the labor participation rate increased by 0.7 percentage points, the seasonally-adjusted unemployment rate has remained almost flat since the previous month at 11.3%. Survey indicators and high-frequency data indicate that the upward trend in employment is maintained.
17. The recent strong course of energy imports still affects the current account balance. In April 2022, the Current Account Balance (CAB) registered a deficit of USD 2.7 billion, while the annualized current account deficit rose by USD 1.2 billion to USD 25.7 billion. According to the provisional external trade data, exports remained strong in May, while imports remained high due to energy prices. On the other hand, it is observed that short-term regional losses caused by the conflict are compensated by the increase in exports to other countries thanks to the dynamic capacity and market diversification flexibility of exporting firms and regional exports exceeded pre-conflict levels. Despite the increase in the foreign trade deficit led by the surge in commodity, mainly energy, prices the ongoing upward trend in services revenues further supports the current account balance. While share of sustainable components of economic growth increases with tourism-related improvements, risks on current account balance due to energy prices continue. Sustainable current account balance is important for price stability.

Monetary Policy

18. The monetary policy stance will be determined by taking into account the evaluations on the source and permanence of risks, along with the extent to which they can be contained by monetary policy, and with a focus on achieving the sustainable price stability target, in a cautious manner.
19. In formulating the monetary policy towards achieving the sustainable price stability objective, a liraization-oriented approach will be maintained that also addresses risks to financial stability. Credit growth and allocation of funds for real economic activity purposes are

closely monitored. The Committee will continue to implement the strengthened macroprudential policy set decisively and take additional measures when needed.

20. The Committee expects disinflation process to start on the back of measures taken and decisively implemented for strengthening sustainable price and financial stability along with the decline in inflation owing to the base effect and the resolution of the ongoing regional conflict. Accordingly, the Committee has decided to keep the policy rate unchanged.
21. To create an institutional basis for sustainable price stability, the comprehensive review of the policy framework continues with the aim of encouraging permanent and strengthened liraization in all policy tools of the CBRT. The focus of this process will be on developing policy instruments to support the improvement of Turkish lira deposits, to increase Turkish lira-denominated assets in the collateral structure of OMO funding, to gradually reduce the volume of swaps, and to strengthen foreign exchange reserves.
22. The collateral and liquidity policy actions, of which the review process is finalized, will continue to be implemented to strengthen the effectiveness of the monetary policy transmission mechanism. Following these actions, it is observed that interest rates of long-term fixed-income and TL-denominated securities converged to policy rates and yield curve shifted downward in all maturities, increasing the effectiveness of monetary policy. Similarly, the Committee considers that the improvement in financing costs of loans, which provide efficiency gains in targeted areas, is important for increasing the efficiency of the monetary transmission mechanism.
23. Accordingly, the effects of liquidity and distribution developments of the Turkish lira on deposits and loan pricing, the effects of exchange rate developments on inflation, and the impact of the developments regarding FX-protected deposit products on reverse currency substitution, the depth and stability of the foreign exchange market and price stability are being analyzed and necessary policy measures are being taken.
24. The CBRT will continue to use all available instruments decisively within the framework of the liraization strategy until strong indicators point to a permanent fall in inflation and the medium-term 5 percent target is achieved in pursuit of the primary objective of price stability.
25. Stability in the general price level will foster macroeconomic stability and financial stability through the fall in country risk premium, continuation of the reversal in currency substitution and the upward trend in foreign exchange reserves, and durable decline in financing costs. This would create a viable foundation for investment, production and employment to continue growing in a healthy and sustainable way.
26. The Committee supports building strong policy coordination and a holistic macro policy mix involving all stakeholders in order to achieve price stability.
27. The Committee will continue to take its decisions in a transparent, predictable and data-driven framework.