

## PRESS RELEASE

### FEBRUARY INFLATION, FORWARD-LOOKING EXPECTATIONS AND INTEREST RATES

#### I. GENERAL EVALUATION

1. In February 2002, monthly increases in the CPI and WPI were realized at 1,8 percent and 2,6 percent respectively. Annual inflation figures, which materialized at 73,1 percent in CPI and 91,8 percent in WPI, have slowed down for the first time since March 2001. (Table 1).

2. Apart from agricultural and food prices, in the price indexes we may more clearly see that inflation have entered into a downward trend during the last couple of months. As a matter of fact, in February the increase in CPI (excluding food) was 1,3 percent, while the increase in WPI (excluding agriculture) was 0,6 percent.

3. The slowing-down process we have seen in recent months in the Annual Inflation Tendency, which is calculated by annualizing the de-seasonalized consumer and wholesale price indexes according to the quarterly moving averages, has become more evident in February. As of February, the annual inflation trend has fallen to 50,6 percent in CPI, and 54,1 percent in WPI. The downward trend is more evident in WPI (excluding agriculture) and in CPI (excluding food), which are realized at 20,6 percent and 41,7 percent respectively.

Table 1: CPI, WPI and Sub-items

|  | (Yearly % Change) |             | (Monthly % Change) |            |            |
|--|-------------------|-------------|--------------------|------------|------------|
|  | 2001              | 2002        | 2001               | 2002       | 2002       |
|  | February          | February    | December           | January    | February   |
| <b>CPI</b>                             | <b>33,4</b>       | <b>73,1</b> | <b>3,2</b>         | <b>5,3</b> | <b>1,8</b> |
| CPI (Goods)                            | 28,7              | 89,5        | 3,7                | 6,4        | 1,5        |
| CPI (Services)                         | 41,7              | 47,0        | 2,4                | 3,2        | 2,3        |
| CPI (Excluding Food)                   | 35,5              | 66,6        | 2,0                | 3,9        | 1,3        |
| <b>WPI</b>                             | <b>26,5</b>       | <b>91,8</b> | <b>4,1</b>         | <b>4,2</b> | <b>2,6</b> |
| WPI (Public)                           | 20,6              | 99,4        | 0,8                | 2,5        | 0,5        |
| WPI (Private)                          | 28,7              | 89,2        | 5,5                | 4,8        | 3,3        |
| WPI (Private Manufacturing)            | 27,9              | 91,7        | 2,4                | 2,1        | 0,7        |
| WPI (Excluding Agriculture)            | 25,4              | 94,3        | 1,8                | 2,3        | 0,6        |
| WPI (Excluding Agriculture and Energy) | 24,6              | 93,1        | 1,6                | 1,9        | 0,7        |

Source: CBRT, SIS

#### Developments in Consumer Prices

4. In February, the increase in the CPI lagged well behind the last four years average, which was considerably below the market expectations. Besides the successful implementation of the Transition Program for Strengthening the Turkish Economy, the risk premium began to

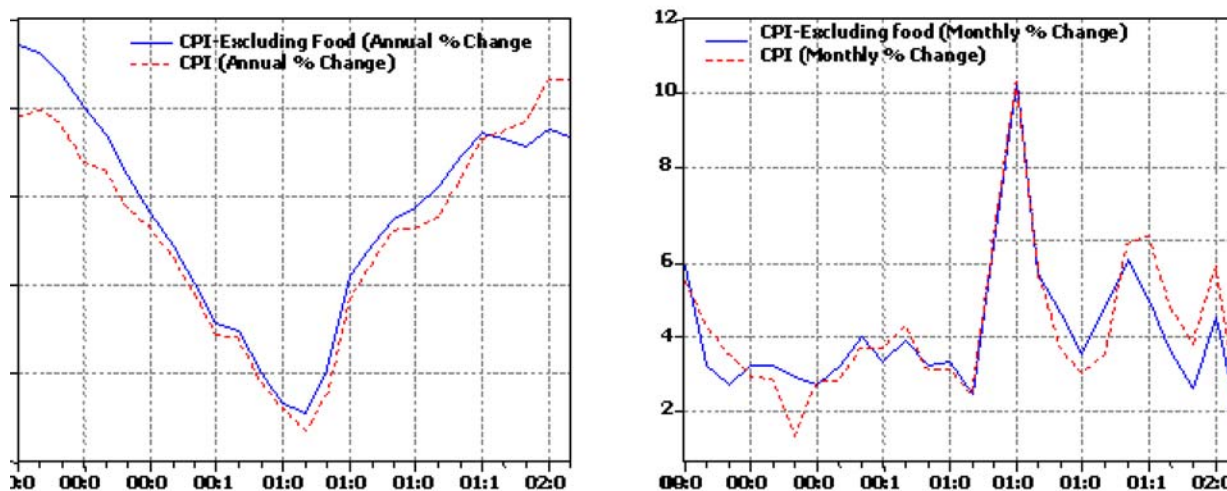
diminish resulting from the increased confidence in the continuation of fiscal and monetary discipline in 2002, which had already started in October 2001. These positive developments have helped the inflation expectations to come close to targets by strengthening the plausibility of the economic program.

5. Moreover, the reduction of VAT ratios in durable goods that had been raised in January leading to high price increases, and the persisting subdued demand have limited the CPI monthly increases.

6. Although agricultural prices went up significantly at the end of 2001 and in January and February 2002 due to adverse weather conditions, the price increases in food sector slowed down in February and stood at 3,2 percent. The fact that consumers have switched to substituting goods and the prices of processed foods have slowed down due to low demand may explain the reason why the prices in food sector remained limited despite high price increases in fresh vegetables and fruits. Despite the slowing-down trend in February, food prices have shown an increase of 59,3 percent in the 6 month-period covering September 2001 - February 2002.

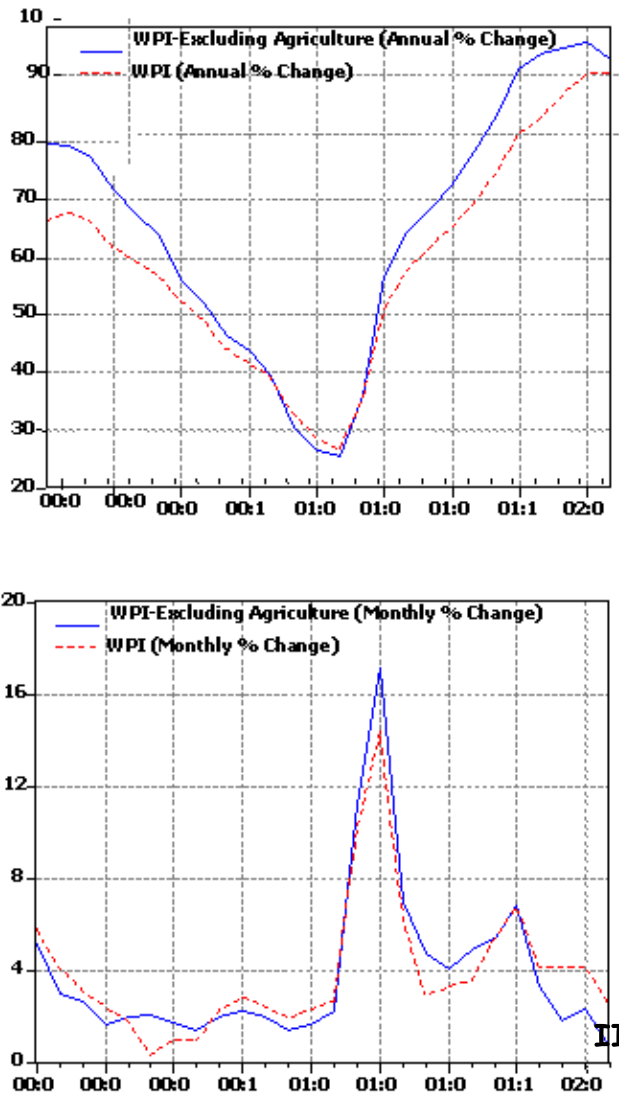
**Figure 1: CPI and CPI (Excluding Food)**

Source: CBRT, SIS.



7. Monthly price movements in the CPI goods basket were mostly greater than those of in the service basket in the wake of the February 2001 crisis. However, a reverse trend was observed in February 2002 and the monthly increase in goods prices remained below the increase in service prices. In February, the goods prices increased by 1,5 percent, while service prices increased by 2,3 percent. If we omit the food sector, the increase in goods prices has materialized at 0,5 percent. Lower than expected food price increases on one hand, and the price increases in house rents, hospital services, medical services and restaurant services on the other hand have caused the service sector prices to materialize above the goods sector prices, despite the seasonally lowered clothing sector prices.

## Developments in Wholesale Prices



**Figure 2: WPI and WPI (Excluding Agriculture)**

Source: CBRT, SIS.

8. The main element affecting the wholesale inflation in February was the increase in agricultural prices by 8,9 percent. However, the increase in WPI remained below the expectations, despite the rise in agricultural prices. The appreciation of Turkish Lira during the last four months on one hand, and the decreasing trend in public sector price adjustments on the other hand, which was helped also by positive exchange rate developments, have led to a decline in production costs. Therefore, the downward trend observed in private manufacturing industry price increases persisted in February and prices in this sector rose by only 0,7 percent.

## II. FORWARD-LOOKING EXPECTATIONS

9. We consider the February inflation as an important development, completely removing the possible adverse effects of the high price increases in January on the expectations and supporting the belief that the year-end inflation target would be hit.

**Figure 2: Year-end Inflation Expectations According to the CBRT Survey of Expectations (Mean)**

|      | Appropriate Mean* | Mean |      |
|------|-------------------|------|------|
| 2001 | 08-1              | 63,0 |      |
|      | 08-2              | 63,7 |      |
|      | 09-1              | 63,9 |      |
|      | 09-2              | 64,8 |      |
|      | 10-1              | 68,8 |      |
|      | 10-2              | 68,4 |      |
|      | 11-1              | 72,5 |      |
|      | 11-2              | 72,0 |      |
|      | 12-1              | 69,7 |      |
|      |                   |      | 63,0 |
|      |                   |      | 63,7 |
|      |                   |      | 63,9 |

|      |      |      |      |
|------|------|------|------|
|      | 12-2 | 69,8 | 70,8 |
|      | 01-1 | 48,3 | 48,5 |
|      | 01-2 | 47,3 | 47,9 |
| 2002 | 02-1 | 47,6 | 48,5 |
|      | 02-2 | 47,5 | 48,3 |
|      | 03-1 | 43,6 | 43,6 |

Source: CBRT

\* The selection of the appropriate mean is done by comparing mean, median, mode, and alpha-trimmed mean.

10. An overall look into the recent data gathered by surveys for inflation expectations reveals that the general downward tendency that had started in the last months of 2001 continues to do so (Table 2).

11. According to the January 2002 CBRT Business Tendency Survey, which covers the WPI expectations, the expected inflation rate for the 12 months onward has declined to 55,3 percent from 58,1 percent in December 2001. The expected year-end WPI is 57,6 percent.

12. According to the results of the CBRT Survey of Expectations for the first period of March, the expected CPI rate for the 12 months onward has declined to 39,8 percent from 43,3 percent. The expected year-end CPI has receded to 43,6 percent. [\[1\]](#)

13. It is expected that the continuation of stability in the exchange rate in the months to come and the moving of public sector prices in tandem with the targeted inflation will improve the inflation expectations even further. However, the rises we are observing in oil prices might create a risk for inflation in the future months.

14. Realizations in the monetary base and in the primary consolidated budget surplus are in conformity with the previously announced targets. This reality is increasing the credibility of the economic program and is improving the expectations. In line with these developments, our positive stance is also supported by the continuation of structural reforms. The preparation of a public sector borrowing draft-law is an example of this.

### III- CENTRAL BANK INTEREST RATES

15. In the light of evaluations for the period ahead of us, we have decided to decrease the short-term interest rates we apply in the Interbank Money Market and in the Istanbul Stock Exchange Repurchase - Reverse Repurchase Market effective 14 March 2002 as following:

- a) **Overnight Interest Rates:** Our borrowing rate has been decreased from 57 percent to 54 percent, and our lending rate has been decreased from 62 percent to 61 percent.
- b) **Weekly Interest Rates:** Our borrowing rate for one week has been decreased from 59 percent to 55 percent.

---

[1] The difference between the inflation expectation values obtained from two surveys is noteworthy. The first reason is that the one measures WPI expectations, while the other one measures CPI expectations. The second reason is that the Business Tendency Survey is conducted once in a month and the data at hand show the survey results that were sent to respondents in the first week of January and answered before the end of the third week of February. On the other hand, the Survey of Expectations is conducted twice a month and shows the results of the first period of March. The third reason is the existence of a two different respondent groups. The first survey covers 1.000 big industrial firms, while the second one gives emphasis on financial sector.