

February CPI: Feeding inflation

Monthly CPI posted a 1.45% MoM rise in February, much higher than the market consensus of 0.64% (Şeker Securities: +0.30%), on the back of an extraordinary rise (5.01% MoM) in food prices. The figure even exceeded the upper limit of the market participants' estimates at 1.00% MoM rise. Food prices alone contributed 1.45 percentage points to the monthly headline CPI rise. Tobacco and alcohol products continued to rise by 3.72% MoM in February, partly due to the recent tax hikes on the related products while seasonal price contraction in clothing (5.25% MoM decline) prevented a further rise. **Thus, annual CPI jumped to the double-digit territory to 10.13% in February from 8.19% in January.** One can put the blame on the supply-side shocks such as high food prices, tax rate hikes for rising headline inflation, **but the core indices, which exclude the one-off price effects, do not look good either.** The annual core index (I) – that excludes food, energy, tobacco and gold prices – increased to 4.05% in February from its record of 3.83% in January. **On the monetary policy front, despite the upward risks on the annual inflation outlook, the CBRT will preserve its policy rate at its current level for a while. Moreover, the CBRT is more responsive to rising inflation expectations than the headline inflation. We had argued that IMF program with considerable financing might allow the CBRT to postpone the rate hiking cycle later this year. But, if the deal does not appear on the horizon in 1Q10, it might be difficult to manage the inflation expectations.**

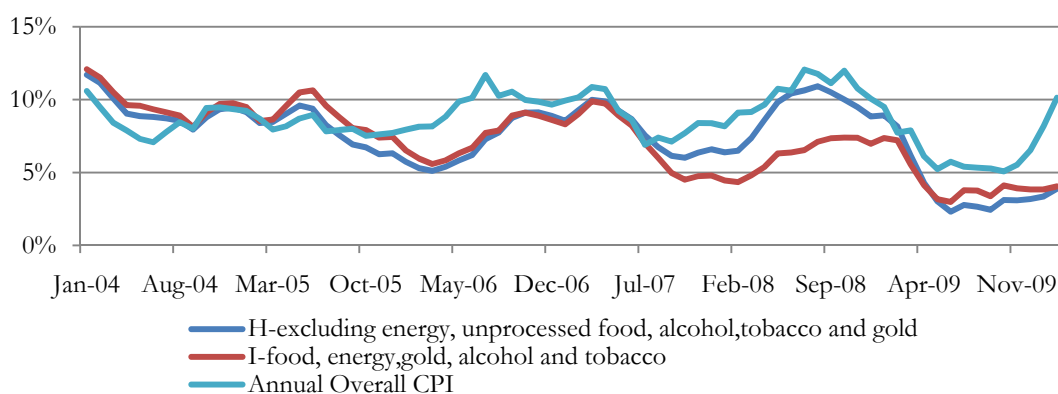
Exhibit 1: Monthly inflation figures

	Previous month	This month	Next month	2010E	2011E
CPI (MoM%)	1.85%	1.45%	na		
CPI (MoM%) consensus	0.97%	0.64%	0.67%	7.37%	6.48%
CPI (MoM%) Şeker	0.80%	0.30%	0.50%	7.50%	6.00%
CPI (YoY%)	8.19%	10.13%			
WPI (MoM%)	0.58%	1.66%	na		
WPI (MoM%) consensus	1.05%	0.70%	0.83%	7.25%	5.35%
WPI (MoM%) Şeker	na	na	na		
WPI (YoY%)	6.30%	6.82%	na		

Source: Turkstat, CNBC-e, Şeker Securities

- Housing expenditure rose by 0.4% MoM rise in February while rents – the most rigid component of non-tradable inflation – rose by 0.30% MoM. Its annual figure continued to decline and eased to 4.8% in February.
- Furniture, health and entertainment sectors posted monthly declines in their price movements while transportation, communication prices saw limited hikes. Restaurants& hotel prices jumped more than 1.00% MoM in February.
- The core indices, which exclude the one-off price effects, do not look good either as the annual core index (I) – that excludes food, energy, tobacco and gold prices – increased to 4.05% in February from its record of 3.83% in January. This ends its four month declining trend.

Exhibit 2: Core Inflation Indices (YoY%)



Source: Turkstat

The bottom line: The benchmark yields at the secondary markets become more sensitive to monthly inflation data going forward. **The yields are likely to test above 9.00% in the short-term on the back of disturbing February inflation realizations. On the monetary policy front, despite the upward risks on the annual inflation outlook, the CBRT will preserve its policy rate at its current level for a while. Thus, a long pause period for the policy rate is ahead whereas the hottest issue is the timing for the CBRT to restart interest rate increases.** As the economy recovers, inflation will become more important this year. The CBRT has considerably revised upward its short-term inflation forecasts on the back of energy, food and administrative price adjustments at its first quarterly inflation report of the year. It saw the year-end CPI for 2010 at mid-point of 6.9%, up from its previous estimate of 5.4% on the back of energy, food and administrative price adjustments. **Our year end CPI estimate stood at 7.5% for 2010.** Note that the official inflation target for 2010 is at 6.5%. **At this juncture, trying to manage expectations through relatively dovish statements is probably the best approach. However, rising headline inflation in 1H10, combined with a return of economic growth are likely to affect inflation expectations significantly. Given the still hold position on the IMF deal process, the inflation outlook may lead the CBRT to revisit its stance on the rate decision earlier than expected.**

PPI by Sector (%)	Feb-10	Jan-09	Feb-09
PPI	1.66	0.58	1.17
Agriculture	4.04	2.54	1.63
Industry	1.16	0.18	1.07
Mining	0.28	1.26	2.76
Manufacturing	0.39	0.22	0.33
Oil products	-0.83	2.90	4.41
Others	0.48	-0.09	-0.14
Energy	9.14	-0.62	8.76
CPI by Sector (%)	Feb-10	Jan-09	Feb-09
CPI	1.45	1.85	-0.34
Food & non-alcoholic bev.	5.01	1.58	0.02
Alcoholic bev.& tobacco	3.72	22.04	0.10
Clothing	-5.25	-8.20	-5.58
Housing	0.39	1.51	-0.99
Furniture	-0.11	0.71	-1.00
Health	-0.20	-0.11	0.10
Transportation	0.42	3.53	1.40
Communication	0.11	-0.24	-1.18
Entertainment	-0.57	-0.27	-0.17
Education	0.02	0.07	-0.34
Restaurant, hotel	1.17	1.11	0.59
Others	0.22	0.23	3.43

Source: Turkish Statistics Institution



Şeker Yatırım Menkul Değerler A.Ş. İnönü Cad. Tımşah Han No: 36 Beyoğlu - İSTANBUL

Phone: +90 (212) 334 33 33 Fax: +90 (212) 334 33 34

E-mail: research@sekeryatirim.com

Web: www.sekeryatirim.com

For additional information, please contact:

Hakan Karacıgan Group Head of ICM and Research 90 (212) 334 91 01 hkaracigan@sekeryatirim.com

Sales

Batuhan Alpman Senior Sales Trader 90 (212) 334 91 03 balpman@sekeryatirim.com

Atakan Andic Sales Trader 90 (212) 334 91 02 aandic@sekeryatirim.com

Belit Taşdemir Sales Trader 90 (212) 334 91 01 btasdemir@sekeryatirim.com

Macro Economy

Seher Fazlioglu Economist 90 (212) 334 91 04 sfazlioglu@sekeryatirim.com

Research

Kadir Tezeller Head of Equity Research 90 (212) 334 33 33 ktezeller@sekeryatirim.com

Volkan Muhurcuoğlu Analyst 90 (212) 334 33 33 vmuhurcuoglu@sekeryatirim.com

Aktug Sami Baloglu Analyst 90 (212) 334 33 33 abaloglu@sekeryatirim.com

Burak Demirbilek Analyst 90 (212) 334 33 33 bdemirbilek@sekeryatirim.com

Selahattin Aydın Analyst 90 (212) 334 33 33 saydin@sekeryatirim.com

Engin Değirmenci Database Associate 90 (212) 334 33 33 edegirmenci@sekeryatirim.com

BASIS FOR 12m RECOMMENDATIONS

BUY: Requires 15% or more estimated upside.

SELL: Requires 10% or more downside.

HOLD: When estimated relative return is limited between -10% and 15% in either direction.

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