

Macro-note – Industrial Production

Industrial production rises 2.9% mom and 1.5% yoy in November. While monthly production data remains mixed, we expect a gradual recovery given interest rate cuts.

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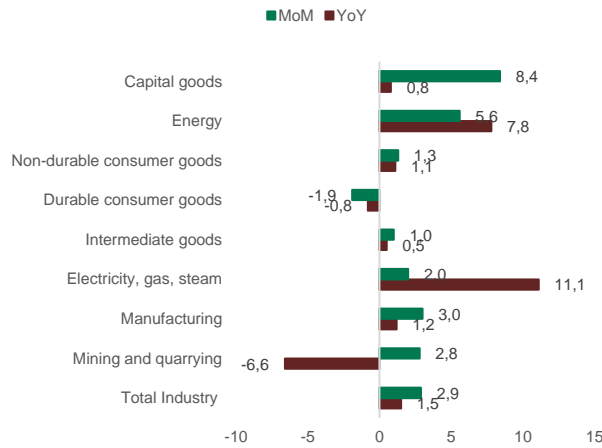
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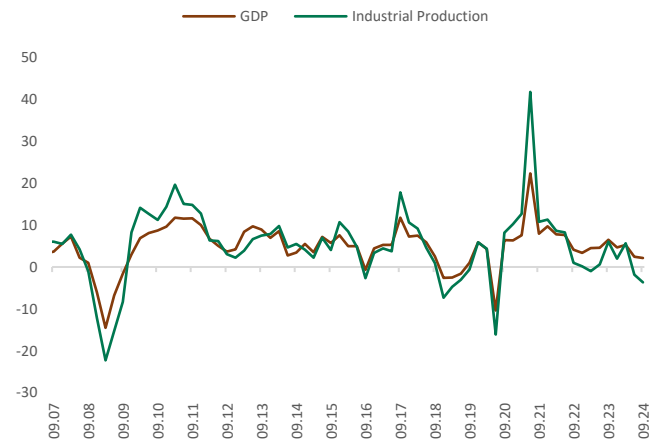
According to industrial production index data, seasonally- and calendar-adjusted production increased by 2.9% mom in November. Thus, annual production growth was realized as 1.5% (previous 3.1% contraction). We expected a limited recovery in monthly production data and a strong base effect in annual production data. We note that the data was in line with our expectations. Although the tight monetary policy did not affect pricing behavior at the expected pace, it had negative repercussions on production data. In this context, we will again see the positive reflections of the shift in monetary policy stance and interest rate cuts on industrial production. 2024 can be considered a lost year in terms of production. 2025 is a candidate for recovery where these losses are partially recovered. If foreign demand also contributes positively to the positive domestic mood, production data may improve beyond the forecasts. Current indicators suggest that this scenario is not remote. In particular, the measures taken to support production in Europe are an indication of this. The slowdown in economic activity and domestic demand has decelerated to expected levels, and interest rate cuts have paved the way for supporting production-side economic activities. The privilege enjoyed by commercial loan growth will also contribute to production activity. Throughout 2024, production indicators were sacrificed to ensure disinflation, while 2025 will be a year when production recovers and contributes to price dynamics. For a long time, we have experienced a period of negative divergence of industrial companies in financial markets, which has had a compounded effect of both financing costs and weakening production. We anticipate that this cycle will reverse as of the first months of 2025, and that we will enter a period in which industry decouples positively with the revival in economic activity. If the CBRT continues the interest rate cut cycle in line with market expectations, the manufacturing and industrial sectors will close the year with a significant recovery in profit margins and sales volumes.

Analyzing the sub-sectors, in November, the mining and quarrying sector index decreased by 6.6% yoy, the manufacturing industry index increased by 1.2%, and the electricity, gas, steam, and air conditioning production and distribution sector index increased by 11.1%. At monthly change levels, the mining and quarrying sector index increased by 2.8%, the manufacturing industry index increased by 3.0%, and the electricity, gas, steam, and air conditioning production and distribution sector index increased by 2.0% compared to the previous month. We consider it positive that the monthly change in the manufacturing industry was realized across all sector averages. The recovery in manufacturing is particularly important for sustainable growth. We observe that production in durable consumer goods remains far from the desired levels in monthly and annual series. This is a consequence of the pullback in demand. Indeed, one of the main objectives of the economic administration was to reduce price pressures by cooling demand. In the current situation, the pullback in demand is relatively smaller than the slowdown in production (supply). This supports our thesis of low growth and relatively high inflation. By 2025, we expect this gap to gradually close and inflation to be more subdued as we move towards balanced growth figures.

Table 1: Industrial Production Rate of Change (%)



Graph 1: Industrial Production and GDP Growth (YoY %)



The revival in domestic production activity will start to make a positive supply-side contribution to pricing behavior. We experienced an even more positive realization than our expectation of monthly production data revealing a limited recovery following the CBRT's interest rate cut signals. We can say that the negative atmosphere in real sector expectations has partially dissipated. Uncertainty regarding monetary policy has diminished, and a monetary and exchange rate policy has been designed to support production in 2025. The harmonization of the output gap with price mechanisms and the calming of demand inflation are among the main indicators of this. As stated in CBRT reports, while 2024 is the year of disinflation, 2025 is the year of rebalancing. As macro-financial stability is considered as a whole, the imbalance in the budget, current account balance, and other macro indicators has made price stability and cutting domestic demand a higher priority. We expect to close the year with industrial production in the 1.3-1.8 band.

In sum, industrial production increased by 2.9% mom in November, signaling a recovery in industrial production in line with monetary policy. The annual increase of 1.5% will converge to the 3-4% band in 2025, with a gradual improvement in the monthly series. The slowdown in economic activity led to a limited decline in inflation figures and a significant decline in production indicators throughout the year. Uncertainty in the main export markets and slowing demand were other factors weighing on production. We anticipate that the slowdown in both domestic and external demand will gradually have the expected consequences on inflation. The alternative cost of achieving the price stability target, or at least a cooling cycle in an overheated economy, would be to sacrifice growth targets. While year-end growth forecasts remain below potential growth, the slowdown in certain sectors has become more pronounced. Weakening production and recession concerns in global markets may mitigate the impact of the slowdown in domestic production. Coordinated tightening in monetary and fiscal policies will bring about price stability and financial stability. With the reduction in financing costs and the revival in domestic demand, we expect positive sentiment among industrial companies throughout 2025. We underline here that new decisions and implementations will prompt updates to our forecasts.

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