

# Summary of the Monetary Policy Committee Meeting

20 September 2018, No: 2018-41

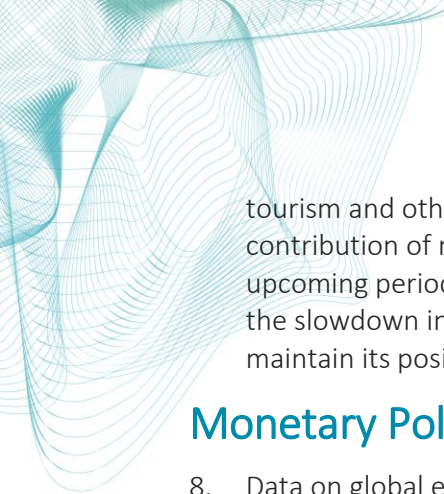
Meeting Date: 13 September 2018

## Inflation Developments

1. In August, consumer prices rose by 2.30 percent and annual inflation increased by 2.05 points to 17.90 percent. The rise in annual inflation was widespread across subcategories, with the most significant contribution coming from core goods and energy groups due to exchange rate developments. In the recent period, cost pressures have elevated, economic units' tendency to raise prices has become stronger.
2. Annual inflation in food and non-alcoholic beverages rose by 0.35 points to 19.75 percent in August. In this period, seasonally adjusted unprocessed food prices remained almost flat. Meanwhile, processed food prices increased by 2.12 percent in August, mainly due to exchange rates and developments in the prices of products used as input for processed food.
3. In August, energy prices increased by 5.37 percent and annual inflation in this group increased by 3.85 points to 21.34 percent. The rise was mainly driven by increments in electricity and natural gas prices as well as increased fuel oil prices due to Special Consumption Tax (SCT) arrangements.
4. Annual core goods inflation rose by 3.60 points to 23.18 percent in August. The durable goods and other core goods prices continued to increase across subcategories due to exchange rate developments. Prices of durable consumption goods increased by 5.49 percent. The seasonal sales in clothing group remained limited compared to previous years.
5. Annual services inflation increased by 0.80 points to 11.84 percent. Transportation services inflation went up on the back of rapid rises in tourism and fuel-oil prices. Meanwhile, the uptrend in accommodation services continued due to exchange rate developments and robust tourism activities.

## Factors Affecting Inflation

6. In the second quarter of 2018, Gross Domestic Product (GDP) increased by 0.9 percent quarterly and by 5.2 percent annually. Thus, economic activity slowed down to converge to its underlying trend and rebalanced in terms of its composition. In the second quarter, the main driver of the quarterly growth was net exports backed by the recovery in tourism.
7. Recently released data indicate a more significant rebalancing trend in the economic activity. According to the third quarter data, external demand maintains its strength. Amid a stable global growth outlook, rising external demand and flexibility in diversifying export markets continue to stimulate exports. The Committee noted that the recovery in revenues from



tourism and other services is rather strong, and under these circumstances, the positive contribution of net exports to quarterly growth may increase also in the third quarter. In the upcoming period, exports of goods and services are expected to boost growth further and the slowdown in import demand resulting from the subdued domestic demand is likely to maintain its positive impact on the current account balance.

## Monetary Policy and Risks

8. Data on global economy indicate that growth has stabilized and remained strong, offering a positive outlook for the year end. Despite the rise in commodity and energy prices due to positive global growth, consumer and core inflation rates continue to follow a moderate course worldwide. Downside risks to the global growth outlook are assessed to be more evident in the upcoming period. Geopolitical developments and increased discourse of protectionism in foreign trade stand out as the main risk factors that may deteriorate the global growth outlook.
9. An assessment of global inflation risks reveals that geopolitical developments and uncertainties about foreign trade policies may pose an upward risk to commodity prices, particularly energy and metal prices. Moreover, the likelihood of an acceleration in wages in advanced economies due to falling unemployment rates is also one of the most important risk factors for inflation in these countries.
10. Financial conditions in advanced economies have tightened in the recent period. The probability of acceleration in inflation due to strong demand and the rise in commodity prices creates a risk that may trigger a faster-than-expected tightening in the monetary policies of these economies. In particular, the ongoing positive growth performance and the new tax law in the US that can be seen as an expansionary fiscal policy increases the probability of Fed to expedite the monetary policy normalization process.
11. In sum, geopolitical uncertainties, weakening capital flows towards emerging economies, and the expansion of protectionism discourse in foreign trade continue to affect the outlook in emerging economies.
12. In this period of high volatility in financial markets, cost pressures and their second-round effects have negatively affected the inflation outlook. Accordingly, the Committee has delivered a strong monetary tightening in September to support price stability and raised the policy rate (the one-week repo auction rate) to 24 percent from 17.75 percent. It has also announced that the Central Bank funding, which used to be provided through overnight lending, will be provided via one-week repo auctions.
13. The Central Bank will continue to use all available instruments in pursuit of the price stability objective. The tight stance in monetary policy will be maintained decisively until the inflation outlook displays a significant improvement. Inflation expectations, pricing behavior, lagged impact of recent monetary policy decisions, contribution of fiscal policy to the rebalancing process, and other factors affecting inflation will be closely monitored and, if needed, further monetary tightening will be delivered.
14. The enhanced coordination between monetary policy and fiscal policy is believed to play an important role in disinflation efforts and macroeconomic rebalancing. Moreover, continued structural steps focusing on reducing rigidity and volatility in inflation will contribute to price stability and social welfare.