Turkey’s economy continued to experience volatility in Q2 2018. According to the Turkish Statistical Institute (TurkStat), annual consumer inflation reached 15.39 percent, the highest increase in the last 15 years. The inflation rate for food and non-alcoholic beverages was 18.89 percent.

The highest increase in year-over-year Consumer Price Index was in Hatay, Kahramanmaraş and Osmaniye regions with 17.38 percent.

The Turkish Lira lost 15 percent of its value against the US dollar in Q2, reaching a 20 percent loss for the first half of the year.

The Minimum Expenditure Basket (MEB) cost an average of 2,307 TL for a household of six, or 385 TL per capita. When deflated to reflect refugee actual expenditure, the MEB cost is 1,767 TL for a household of six, or 295 TL per person.

**Turkey Macroeconomic Context**

Turkey’s economy continued to experience volatility in Q2 2018. According to the Turkish Statistical Institute (TurkStat), annual consumer inflation reached 15.39 percent, hitting a record for the last 15 years. The monthly inflation (2.61 percent) was higher than expected, raising concerns for the rest of the year. Prices for the food and non-alcoholic beverages recorded their highest increase in June with 5.98 percent on a monthly basis. The yearly increase in food prices was 18.89 percent. Hatay, Kahramanmaraş and Osmaniye experienced the highest (17.38 percent) consumer price index increases when compared to the same month last year, June 2017. These provinces also have the highest increase in CPI (12.58 percent) since the beginning of 2018.

Among the consumer price index components, transportation prices rose by 24.26 percent in June, registering the highest year-on-year increase. This was followed by furnishing and household equipment by 18.91 percent, housing prices by 12.01 percent, health services by 10.83 percent, and education by 10.79 percent.

Even though the announcement of the June presidential election results after the first round eliminated political uncertainty and temporarily reversed the losses in the value of the Turkish lira, the global risk perception surrounding the Turkish economy prevented a sustained recovery of the currency.1 The ongoing devaluation of the Turkish lira continues to affect the economy negatively. Within the second quarter, the Turkish Lira lost 15 percent of its value against the US dollar. The accumulated loss in the value of the TL during the first half of the year reached 20 percent.

The Central Bank of Turkey (CBRT) raised its policy rates by 1.5 percent to 17.75 percent in June, to rein in the rising inflation. Following the most recent increase, the cumulative rise in the policy rates reached 5% since April.

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Turkey’s trade deficit narrowed by 8.9 percent on an annual basis in June, in line with the devaluation in the currency. On the other hand, the country’s current account deficit, a measure that encompasses trade balance as well financial transfers such as net portfolio inflows and FDI (foreign direct investment), continued to widen for the third month in a row in early July, reaching 5.5 percent of GDP. A higher current account deficit implies increased vulnerability to potential external shocks, such as reversals in investor sentiment, or sudden outflows of foreign capital.

Citing the high inflation rate, devaluation of the Turkish Lira and increase in the energy prices as the primary reasons, Moody’s has reduced the expected growth rate in 2018 from 4 percent to 2.5 percent for Turkey. Moody’s had already downgraded Turkey’s credit rating from Ba1 to Ba2 in March 2018, two notches below investment grade.

During the first five months of 2018, the budget performance deteriorated slightly. In this period, the budget revenues expanded by 18.3 percent while the budget expenditures increased by 20.9 percent, creating a 9 billion TL increase in the budget deficit that reached 20.5 billion TL for the five month period. In 2017, Turkey’s budget deficit was 1.5 percent of GDP, below the target indicated in the country’s Medium Term Economic Programme. Currently, the budget deficit stands at 1.6 percent of GDP and the year-end target is 1.9 percent of the country’s gross domestic product. Analysts maintain that fiscal discipline will be particularly important in the upcoming period, at a time of rising interest rates and deteriorating current account deficit.

According to the unemployment data for March 2018 (released in June 2018), the unemployment rate in Turkey was 10.1 percent, lower than the 11.7 percent registered for the same period of the previous year. Non-agricultural employment stood at 11.9 percent, whereas youth unemployment rate was 17.7 percent. Labour force participation rate for males remained substantially above that of females, with 77.5 percent and 37.5 percent respectively. The rate of unregistered unemployment (those working without a social security scheme) was 32.4 percent in March 2018.

While Turkey’s calendar-adjusted industrial production index rose by 6.2 percent in April, the pace of growth slowed down for the fourth consecutive month since December. The slowdown in the industrial sector was also reflected in the Manufacturing Purchasing Managers’ Index (PMI), which reached its lowest level since April 2009. The slowdown in industrial production and manufacturing activity are indicative of an upcoming slowdown in the previous high growth rates in the country.

In contrast, the consumer confidence index increased by 0.6 percent from 69.9 in May to 70.3 in June 2018. Compared with the previous month’s results, consumers reported expecting an improved overall economic situation within the next 12 months, as well as a “better financial situation in the household” and a decline in the number of unemployed persons. On the other hand, consumers reported a lower probability of savings for the next 12-month period.

The current economic conjuncture implies a looming slowdown in the previous high growth rates, and elevated inflation levels. This is expected to decrease the living standards and diminish the purchasing power of Turkish consumers and refugees alike, particularly affecting more vulnerable segments of the society, which traditionally lack access to safety nets which guard them during times of economic difficulty.

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*The total may not be 100% as the percentages are rounded up.
Minimum Expenditure Basket

Based on the data from TurkStat, the weighted average cost of the MEB has increased by 2 percent from Q1 to Q2, and 11.6 percent on an annual basis.

The MEB cost has been calculated using the methodology revised at the beginning of 2018. (Please refer to Q1 2018 Market Bulletin for details).

Figure 1 indicates the actual MEB costs in June 2018, across the eight regions included in the analysis. The orange line indicates the percentage price change between Q1 and Q2. The average weighted MEB for a household size of six is calculated as 2,307 TL per month for Q2, indicating 2.03 percent increase compared to Q1.

In addition to Istanbul, Izmir and Ankara which are the most expensive regions, Bursa, Eskisehir and Bilecik also have higher MEB prices than average, becoming equal fourth most expensive regions in Q2. In Istanbul the MEB cost has reached 3,032 TL.

Mardin, Batman, Sırnak, Siirt, Sanliurfa, Diyarbakir, Hatay, Kahramanmaras and Osmaniye provinces are the least expensive locations, with an MEB below 2100 TL. However, the annual MEB cost increase was the highest in Hatay, Kahramanmaras– and Osmaniye in June 2018, with a 14.3 percent increase, followed by Izmir with 13.5 increase. The lowest rate of increase in MEB was seen in Mardin, Batman, Sırnak and Siirt with 9.4 percent and Gaziantep, Adıyaman and Kilis with 9.5 percent. Among the four regions that have MEB costs higher than the average, Ankara experienced the lowest increase; yet this was also 9.8 percent.

Figure 1: MEB Cost per Region in Q2 2018

The quarterly changes of the weighted average MEB costs over the past 12 months are demonstrated in Figure 2.

The MEB costs increased gradually during this period. The average weighted MEB has increased by 11.6 percent from June 2017 to June 2018. This was lower than the rise in CPI (15.39 percent), as the CPI is more comprehensive and includes items and services that are not covered by the MEB.

Figure 2: MEB Costs between 2017 –2018
Food Prices

The prices for food and non-alcoholic beverages, which make up 23 percent of the CPI, increased by 18.89 percent in the last twelve months, significantly impacting the annual inflation rate.

In June 2018, the annual increase in the food and non-alcoholic beverage inflation was 18.89 percent. This is reflected in the monthly food basket as equivalent to a 20 TL increase per person compared to the same month of last year. In Central Bank of the Republic of Turkey (CBRT)’s analysis, the increase in the unprocessed food prices led by fresh fruit and vegetables was cited as the driving factor behind high inflation rates. According to experts, the unusual weather conditions underlie the increase in the food prices and override the seasonal reversing effect, which was -2 percent between May and June 20186.

TurkStat announced the year-on-year inflation rate for the processed food prices as 14.47 percent. The price increase for bread, which is an essential processed food, was relatively lower compared to other items, at 11.74 percent. The quarterly change in bread prices between Q1 and Q2 2018 was 1.85 percent.

The price of rice, the second leading component in the food basket, increased by 3.55 percent from Q1 to Q2 2018, and 15.1 percent annually. Bulgur (wheat) prices increased by 3.19 percent annually and the quarterly change was 0.03 percent. Dry bean prices registered an annual decrease of 9.4 percent; following a declining trend since Q3 2017.

Energy Prices

Overall energy prices continued to increase in the second quarter of 2018. Cooking gas prices that had declined in Q1 increased by 4.5 in Q2 2018.

The energy prices continued to increase in Q2 2018. The annual inflation rates for petrol, diesel and cooking gas prices were 30.1 percent, 24.4 percent, and 19.7 percent respectively. The quarterly increase in diesel prices was 9.9 percent, followed by petrol prices with 9.1 percent. Following a decline registered during the first quarter of 2018, cooking oil prices rose by 4.5 percent in the second quarter, reaching its 2017 year-end levels. Since Turkey imports a significant proportion of its energy needs, the recent devaluation in the currency was also carried over to the energy price inflation rates. Figure 4 depicts the quarterly energy prices since 2016.

6. BBVA Inflation Report for June 2018
The ESSN program aims to help the refugee population in Turkey meet their basic needs through cash transfers. At the end of June 2018, 1,361,343 beneficiaries received ESSN assistance. The ESSN cash transfer value is calculated based on the cost of the MEB; WFP VAM and M&E monitor the developments in the Turkish economy to determine whether the assistance provided continues to meet the needs of beneficiaries.

The MEB cost 64 TL more per household in Q2 compared to Q1, having reached 2,307 TL for a household of six. As noted above, this data is collected from the Turkish Statistical Institute. Due to a variety of factors, including limited purchasing power, refugee consumption choices differ from those of the host community. Therefore, using refugee expenditure data, the MEB has been deflated to reflect actual expenditure decisions (please refer to Q1 2018 Market Bulletin for more details). The Q2 MEB for refugees was 1,767 TL, with a 2.1 percent increase that is equal to 68 TL.

The MEB cost per person in Q2 2018 was therefore 295 TL. The pre-assistance baseline data from February – May 2017 on refugees indicate that even the poorest households are able to generate an income that provides 132 TL per person, leaving a 163 TL gap (295 — 132 TL). The ESSN transfer value is 120 TL per month and reaches an average of 133 TL per month when the quarterly top-ups are included. While the ESSN assistance was covering 85 percent of the basic needs of the refugees in Q1 2018, the increase in the MEB in Q2 reduced it to 82 percent, and almost one fifth (18 percent) of the identified gap remains unmet.

Therefore an average refugee household was short of 30 TL per person per month in Q2 (163 TL gap versus 133 TL provided) in order to meet its minimum basic needs. Furthermore, the impact of the rising energy prices are likely to be felt more substantially following the summer months. Given the rising food and energy prices, elevated core inflation levels (which covers rent, clothing, education, health, communication and transportation prices), combined with the expected slowdown in growth and other risks surrounding the Turkish economy, it is of utmost importance to continue providing support for the most vulnerable segments of the refugee population. The projected reduction in the purchasing power of the refugees is concerning and indicates the value of the assistance should be revised in order to protect households against the rising prices and deteriorating economic outlook.

Emergency Social Safety Net Programme Implications