Turkey Outlook

Highlights/Takeaways:

- Turkey's challenges today are driven by years of economic mismanagement and President Recep Tayyip Erdogan's actions following his recent consolidation of power.
- Recent issues present little risk of a "contagion effect". Further, Turkey is not a barometer for global economic health.

On Friday, 10th August, Turkish markets plummeted -15% —most likely tied to the lira's -13% drop and the Trump administration's announcement to double aluminium and steel tariffs. While this news may seem alarming, Turkish markets and the lira have been gradually declining over the last five years. Turkey's real problems are much deeper, driven by years of economic mismanagement and President Erdogan's recent consolidation of power, including his refusal to raise interest rates despite inflation. However, Turkey is an isolated example of political and economic mismanagement with little risk of contagion and is no barometer for global economic health.

To better understand how Turkey got here, context is necessary. Following June's elections, the country transitioned from a parliamentary system to a presidential system. Erdogan then laid out thousands of pages of decrees, centralising power with the president with almost no legislative oversight. One of these decrees allowed him to hire/fire the head of the central bank without confirmation. Though extant Governor Murat Centinkaya presently remains in that position, Erdogan hired his son-in-law as finance minister. Additionally, Erdogan has sought to influence monetary policy despite Centinkaya's continued leadership, holding a press conference where he outlined his policy on interest rates, claimed high-interest rates caused inflation, and said the best way to reduce inflation was to cut rates. The spectre of diminishing central bank independence, combined with Erdogan's backward take on monetary policy, has led to a massive loss of investor confidence in the Turkish lira. While the revved up sanctions add fuel to the fire in the short term, the consistent and continued declines have more to do with the defiant tone Erdogan maintains on his view of the Turkish economy and monetary policy.

But, to put Turkey's issues in perspective, Turkish stocks represent just 0.07% of the MSCI ACWI Index, and its economy just 1% of global GDP—nowhere near wallop potential. Moreover, late-cycle Emerging Market currency turmoil like this is not uncommon (e.g., 1998's Asian currency crisis.) Emerging Markets can drive some short-term uncertainty, and Turkey seems no different than past instances.

Additionally, spillover effects of Turkish problems are minimal. Some European banks have exposure to Turkish banking investments, such as Spanish Financials holding Banco Bilbao Vizcaya Argentaria (BBVA)—which derives about 15% of its profits from Turkey and was down ~7% on the news as of Friday, 10th August 2018. But BBVA hedges ~50% of its Turkish income from currency impacts. For example, if the lira depreciated 50%, BBVA profits would decrease only 3.75%. Further, loans to Turkey's government make up less than 1% of BBVA's Turkish loans—isolating BBVA from real trouble.

Looking forward, Turkish currency swings and political headlines likely continue to garner headlines. But while currency swings can seem worrisome, they aren't a major global economic driver, good or bad. In our view, Turkey's problems likely remain isolated to Turkey, aside minimal, non-bear-market-inducing, short-term spillover effects.

This material may also be found posted on the Fisher Investments Europe web-site at www.fisherinvestmentseurope.com. If your firm wishes to be removed from receiving these materials in the future or wishes to pay for this material, please contact Fisher Investments Europe.

Fisher Investments Europe Limited (FIE) is authorised and regulated by the Financial Conduct Authority. It is registered in England, Company Number 3850593. FIE is wholly-owned by FI, which is wholly-owned by Fisher Investments, Inc.

Fisher Investments (FI) is an investment adviser registered with the securities and Exchange Commission. As of 30 June 2018, FI managed over $98 billion, including assets sub-managed for its wholly-owned subsidiaries. FI and its subsidiaries maintain four principal business units – Fisher Investments Institutional Group (FIIG), Fisher Investments Private Client Group (FIPCG), Fisher Investments International (FII), and Fisher Investments 401(k) Solutions Group (401(k) Solutions). These groups serve a global client base of diverse investors including corporations, public and multi-employer pension funds, foundations and endowments, insurance companies, healthcare organisations, governments and high-net-worth individuals. FI's Investment Policy Committee (IPC) is responsible for investment decisions for all investment strategies.

For purposes of defining "years with Fisher Investments," FI was established as a sole proprietorship in 1979, incorporated in 1986, registered with the US SEC in 1987, replacing the prior registration of the sole proprietorship, and succeeded its investment adviser registration to a limited liability company in 2005. "Years with Fisher Investments" is calculated using the date on which FI was established as a sole proprietorship through 30 June 2018.

FI is wholly owned by Fisher Investments, Inc. Since Inception, Fisher Investments, Inc. has been 100% Fisher-family and employee owned, currently Fisher Investments Inc. beneficially owns 100% of Fisher investments (FI), as listed in Schedule A to FI's form ADV Part 1. Ken Fisher beneficially owns more than 75% of Fisher Investments, Inc. as noted in Schedule B to FI's Form ADV Part 1.

FIE delegates portfolio management to FI. FI's Investment Policy Committee is responsible for all strategic investment decisions. FIE's Investment Oversight Committee (IOC) is responsible for overseeing FI's management of portfolios that have been delegated to FI. Matters arising pursuant to FI's portfolio management policies are elevated to the IOC.

The foregoing information has been approved by Fisher Investments Europe.

The foregoing information constitutes the general views of FI and FIE and should not be regarded as personalised investment advice or a reflection of the performance of FI or its clients. Investment in securities involves the risk of loss. Past performance is no guarantee of future returns. Other methods may produce different results, and the results for different periods may vary depending on market conditions and the composition of a portfolio or index. If you have asked us to comment on a particular security then the information should not be considered a recommendation to purchase or sell the security for you or anyone else. We provide our general comments to you based on information we believe to be reliable. There can be no assurances that we will continue to hold this view; and we may change our views at any time based on new information, analysis or reconsideration. Some of the information we have produced for you may have been obtained from a third party source that is not affiliated with FI. FI does not provide tax advice and is not registered as a tax advisor. FI requests that this information be used for your confidential and personal use.

FISHER INVESTMENTS EUROPE™

Investing in securities involves the risk of loss and there is no guarantee that all or any capital invested will be repaid. Past performance is never a guarantee nor reliable indicator of future results. The value of investments and the income from them will fluctuate with world equity markets and international currency exchange rates. Other methods may produce different results, and the results for individual portfolios and for different periods may vary depending on market conditions and the composition of the portfolio.