

Economics

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Turkey Macro View

Trip Notes: Investors are waiting in the wings

- We saw 15 clients in London between June 11 and 15. Given the relatively favorable performance of Turkish assets to date, we were expecting to see a more enthusiastic crowd. Investors, however, were distracted by the euro zone debt crisis and the outcome of the critical leadership election in Greece. The mood among investors was in stark contrast to that observed during our previous visit in late January, when they were more upbeat. A rather worrisome observation in this regard was investors' rising concerns about the global growth outlook, as their faith in liquidity-based measures seems to be diminishing.
- Based on our meetings, investors appear to lack strong conviction for Turkish assets due to the combination of the ongoing euro zone woes and Turkey-specific factors. Concerning the latter, uncertainties about the external adjustment process and the highly discretionary monetary policy seem to be the main drivers behind investors' hesitance. As one investor put it, *"Turkey wanted to be a 5-5-5 economy: 5% growth, 5% inflation and a current account deficit of 5% of GDP. Instead, we are probably looking at a 3-7-8 type of economy"*.
- What about *"the yields are too high to ignore"* view? Although investors concur that Turkey's yields are definitely attractive, an abrupt move in the lira is a non-negligible risk owing to the uncertain global environment and the country's large external financing requirements. In this respect, a few investors pointed out that they would start getting uncomfortable about the lira if 1-month FX implied yields were to drop considerably below 8%.
- Investors' hesitancy is also confirmed by the light positioning in Turkish assets. According to a poll that we carried out among the 15 investors during our visit, in which we asked them to classify their exposure on a scale of -10 to +10 (with - and + representing short and long exposure, respectively), the average exposure on FX and rates is around 1.5 and 1.3, respectively (please refer to Figures 1 and 2 for details). Compared with our previous poll results, investors seem to be somewhat more constructive on the rates front than they were in late January.
- All in all, our meetings confirmed that investors remain wary of tail events, as their investment horizon is now much shorter than before. With this caveat in mind, investors continue to view the lira as an attractive carry trade, as Turkish assets are likely to benefit from investors' enthusiasm for EM countries and their quest for yield. Nonetheless, it is worth highlighting that investors' interest in Turkish assets, which seems to be largely driven by high yields, is not underpinned by a coherent macroeconomic story. Consequently, we think investors should enjoy the carry, while remaining alert since Turkish assets are likely to remain at the mercy of global financial markets.

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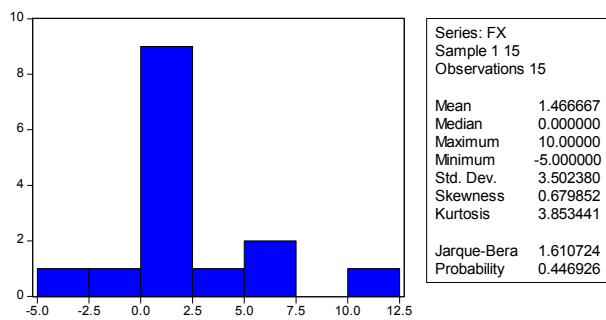
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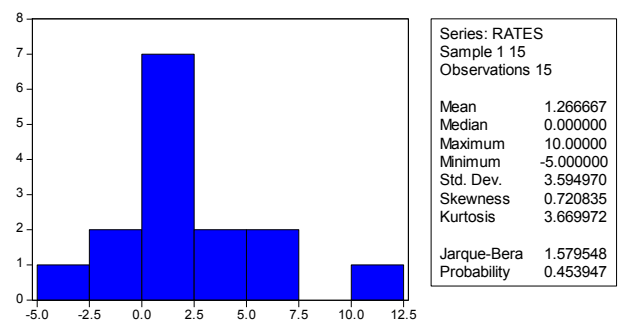
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Figure 1. Turkey: FX Exposure (Histogram and Charts)



Source: CIRA. Note: On a scale to -10 to 10.

Figure 2. Turkey: Rates Exposure (Histogram and Charts)



Source: CIRA. Note: On a scale to -10 to 10.

Appendix A-1

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