



# An insider's take on Turkey's economic crisis

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*Turkey is a case study in missteps. And it proves that successful investing always comes back to fundamentals.*

Economic problems in Turkey have been making headlines, and news like this is unnerving for people who are invested in emerging markets. But it's particularly relevant to me personally. I was born and raised in Izmir, one of Turkey's largest cities. My family continues to be deeply involved in the business community. And although I haven't lived there since 1997, my relatives and friends in Turkey provide me with feedback on what's going on in my home country. For quite some time, I've been hearing about mistrust in the government's fiscal and economic policies, along with anxiety about Turkey becoming an increasingly polarized society. But it's only been recently that these concerns are making their way into the news here in the U.S.

## What's happening in Turkey's economy

The Turkish lira lost more than 42% of its value against the dollar this year as of the end of August against a backdrop of deteriorating relations with the United States. Investors had been wary of developments in Turkey since its failed coup, mainly due to structural issues. Looking at Greece's debt presents some troubling numbers: While overall government debt is modest (as a percentage of GDP it's been falling and is about 30% of GDP), Turkish banks and the private sector are significant debtors.

The sharp fall in the Lira has sparked fears of contagion in broader emerging markets. Previous actions by the Turkish government to stabilize the lira have been ineffective, and inflation in Turkey now exceeds 15% — well above the Turkish central bank's target of 5%. But we're beginning to see signs of policy improvement, as the Turkish Central Bank recently increased interest rates above expectations. Turkey's stock market is 0.6% of the MSCI EM index and it's even more relevant for fixed-income indices, where it constitutes a 3.5%-4.5% weight depending on the index.<sup>1</sup>

## Turkey is an isolated issue

While Turkey's predicament might sound like a classic emerging market crisis (in



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terms of owing too much), it is very much a Turkish crisis. Even given the current situation, I don't believe that Turkey falls into the same category of concern as the recent Greek debt crisis or that the problems in Turkey are a threat to other economies. Greece was a member of the eurozone, and its default would have called into question the sustainability of the eurozone itself (i.e., there was a large systemic risk in letting Greece default). Turkey doesn't pose the same level of systematic risk.

### **Our outlook is focused on the long term**

I don't believe that things will be corrected immediately. Right now, a political agenda is driving economic policy and perpetuating the mistakes that are being made. I don't think anything will be resolved in the short term (12–18 months). But in the longer term, I think competitive market forces will prevail and the market will correct itself — there's just a lot happening right now and many moving parts that need to be ironed out.

### **Bottom line**

Even though it saddens me, as an investor I'm reminded that Turkey is a case study in how poor governance and policy mistakes can turn into a crisis. For investors, the lesson is clear: whether it's a company or a country, pay attention to the fundamentals and watch for signs of poor decision-making. If you're invested in benchmark-tracking passive emerging market strategies, you're exposed to foreseeable risks like Turkey. A solid investment strategy should be informed by research and rigorous analysis. And both companies and countries should be governed with integrity and transparency.

<sup>1</sup> Source: Columbia Threadneedle Investments as of August 23, 2018



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