TURKEY: BOOM-MARKET OR FALSE FRONT?

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Last year Turkey's stock market outpaced Europe with a positive performance of +58 percent. There are a number of reasons for this outstanding achievement, specifically ample liquidity, high GDP growth and low indebtedness. And the most experts are in complete agreement: The potential of Turkey's growth is not yet exhausted. By 2023, Turkey wishes to become one of the top ten global economies, for which it is required to grow at the rate of 6-7 percent in the medium to long term.

In November 2012 the London-based rating agency **Fitch** upgraded Turkey's

- long term foreign currency issuer default rating (IDR) from BB+ to **BBB-**,
- long-term local currency IDR from BB+ to **BBB**,
- short-term foreign currency IDR from B to **F3,**
- and its country ceiling from BBB- to **BBB**.

Beyond that, Fitch set the outlooks on the ratings as **stable**. Thus Turkey received its first "**investment grade"** ranking since 1994. In 1994 Turkey's economy was plunged into a deep crisis. On January 14, 1994, both Standard & Poor's and Moody's downgraded Turkey's credit rating from "investment grade" to "speculative grade".

But what do these terms and ratings mean?

Definition of Ratings

The terms "investment grade" and "speculative grade" have established themselves over time as market conventions and describe the categories "AAA" to "BBB" (investment grade) and "BB" to "D" (speculative grade).

Rating organizations such as the Fitch Group, Moody's or Standard & Poor's (S&P) help investors and other market participants around the world make sound financial decisions and evaluate the financial stability of a company or a country.

The rating organization publishes opinions on a variety of scales, the most common of which are credit ratings. Credit ratings are generally used by investors as indications of the likelihood of receiving the money owed to them in accordance with the terms on which they invested. International credit ratings assess the capacity to meet foreign currency or local currency commitments. Both "foreign currency" and "local currency" ratings are internationally comparable assessments. The local currency rating measures the likelihood of repayment in the currency of the jurisdiction in which the issuer is domiciled and hence does not take account of the possibility that it will not be possible to convert local currency into foreign currency or make transfers between sovereign jurisdictions.

Fitch-Ratings[1]

Long-Term Rating Scale:		Short-Term Rating Scale:	
AAA:	Highest credit quality	**F1:**	Highest short-term credit quality
AA:	Very high credit quality	**F2:**	Good short-term credit quality
A:	High credit quality	**F3:**	Fair short-term credit quality
BBB:	Good credit quality		
BB:	Speculative	**B:**	Speculative short-term credit quality
B:	Highly speculative		
CCC:	Substantial credit risk		
CC:	Very high levels of credit risk	**C:**	High short-term default risk
C:	Exceptionally high levels of credit risk		
RD:	Restricted default	**RD:**	Restricted default
D:	Default	**D:**	Default

A plus or minus sign added to the rating (e.g. B+) shows strength or weakness within a major rating category. AAA to BBB- (long-term) and F1 – F3 (short-term) indicate relatively low to moderate credit risk and are also known as "investment grades". BB+ to D (long-term) and B to D (short-term) signal a higher level of credit risk or that default has already occurred. For example "B" means that material default risk is present, but a limited margin of safety remains and financial commitments are currently being met. "CCC" shows that default is a real possibility and the credit risk is present.

Future of Turkey's Economy

The World Bank

Fitch Managing Director Ed Parker (London) noted that the upgrade in November 2012 "reflects a combination of an easing in near-term macro-financial risks as the economy heads for a soft landing" and that "the Turkish economy is on track to return to a sustainable growth rate, having narrowed the current account deficit". This upgrade in 2012 should reflect the fact that after two years of fluctuating growth rates, Turkey's fundamentals are expected to pave the way for steady, long-term growth of 4-5%. And this will not only enable Turkish investors to do business: Turkey will be in position to receive favorable loans and investments from abroad. Especially investment funds, private equity funds and sovereign wealth funds are turning to Turkey to avoid Europe's worsening debt crisis. The conditions appear to be favorable.

[1] Fitch Ratings – Definitions of Ratings and Other Forms of Opinion – Feb 2013, available for download here: www.fitchratings.com

The “Global Economic Prospects 2013” of the World Bank has predicted growth rates for Turkey in 2013. In regard to expectations in the Turkish economy, the Global Economic Prospects touched that Turkey’s economy would grow about

- **4 percent in 2013**,
- **4.5 percent in 2014**
- and “princely” **5 percent in 2015**.

For comparison: The Euro Zone expects 0.1 % in 2013[2]. The World Bank also added in its report that Turkey made a significant progress in the scope of reducing inflation momentum.

Furthermore, the World Bank mentioned that Turkey’s current account deficit ratio to gross domestic product (GDP) was predicted to be

- **7 percent in 2013**,
- **6.8 percent in 2014**
- and **6.5 percent in 2015**.

Fitch Group

Yesterday (Thursday, 7 March 2013) Fitch Ratings senior director **Paul Rawkins** said in an interview in London (speaking at a Fitch briefing on Turkey) that Turkey would need to lower its current account deficit and inflation to secure another rating upgrade.

"We don't see the current account deficit improving much from here, at least not in the next couple of years, it will be a long term process," Rawkins said. "The way the current account deficit evolves and its funding trend will be important for this credit rating. It's important to see more long term flows," he added.

The Central Bank of Turkey is trying to limit loan growth to avert an expansion in the current account deficit, which surged to about 10 percent of gross domestic product in 2011. Turkey’s rate of loan expansion is about 20 percent. The Central Bank of Turkey aimed 15 percent this year. The Turkish Stock Exchange[3] reacted immediately: The index fell 0.41 percent to 81,834.73 points (the index was starting the day with 82,348.26 points). The Lira gained 0.1 percent to 1.7962 per dollar at 5:10 p.m. in Istanbul, paring its loss on the year to 0.7 percent.

International Monetary Fund & Global Comparison

The International Monetary Fund (IMF) praises Turkey’s economic achievements, too. IMF’s Turkey director Mark Lewis talked to The Anadolu Agency (AA): "Your macroeconomic foundations are strong and your role in the International Monetary Fund will grow. Turkey plays an important role in offering solutions to economic and fiscal problems international community faces". Turkey has reduced its debt to the IMF from 23.5 billion US-Dollars to 400 million US-Dollars.

[2] http://ec.europa.eu/news/economy/121107_en.htm.
[3] Istanbul Menkul Kıymetler Borsası (IMKB), 100 Endeksi.

The IMF predicted in its “Global Prospects and Policy Challenges Report” that

- **Turkey**’s economy will grow **3.4 percent in 2013** and **4.2 percent in 2014**;
- the **EU** would grow 0.2 percent in 2013 and 1.4 percent in 2014;
- the **Euro Zone** would shrink 0.2 percent in 2013 and grow 1 percent in 2014;
- **France**’s economy will grow 0.3 percent in 2013 and 0.9 percent in 2014;
- **Germany**’s economy will grow 0.6 percent in 2013 and 1.4 percent in 2014;
- **Britain**’s economy will grow 1 percent in 2013 and 1.9 percent in 2014;
- **China** will grow 8.2 percent in 2013 and 8.5 percent in 2014;
- **Russia** will grow 3.7 percent in 2013 and 3.8 percent in 2014;
- **US** will grow 2 percent in 2013 and 3 percent in 2014.

Conclusion

Only 10 years remain until 2023, the 100th anniversary of the establishment of the Turkish Republic. The Turkish government has set as a national objective to have Turkey in 2023 become one of the 10 largest economies in the world (Turkey is ranked 16th today). Due to its economic and demographic strength Turkey’s significance within the global economy is gradually increasing. In the last decade, the country's economy has nearly trebled in size. Just 10 years ago, the average Turk had one-fifth the income of the average European. Today, Turks are only 30% less wealthy than European Union citizens. Given Europe's financial straits, Turkey could catch up in the coming years and realize its 4-centuries-old dream of becoming a great power again. The country is a rare haven of economic growth and political stability in a region in turmoil. This increase can be enhanced by a shift to renewable energy, which would reduce Turkey’s dependency on foreign energy sources (especially imported oil and gas). Both (foreign and domestic) investors and Turkey need to seize all opportunities.

If you have any questions, please don’t hesitate to contact me,

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