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GLOBAL MARKET THOUGHTS: A FOCUS ON TURKEY

Please reference below for Beacon Pointe's summarized thoughts on the current global market environment, specifically focused on the recent news in Turkey.

Summary

1. Turmoil in Turkey has led to economic disruption and significant depreciation of the lira.
2. Investors concerned about contagion impacting other emerging economies have sold off assets in those markets.
3. European banks are under scrutiny due to potential fallout from Turkish banks which now face higher funding costs.
4. To regain confidence by global investors who have fled Turkish assets, the Central Bank has increased interest rates – just not as much as the markets expected. Turkey's president Recep Tayyip-Erdogan is opposed to the higher interest rates and is trying to control fiscal and monetary policy.
5. US tariffs on Turkish steel and aluminum have added to economic difficulties but are not the sole problem.

Since his reelection, Mr. Erdogan has taken steps to control Turkey both politically and economically. He has used the attempted coup last year to jail opponents, has appointed his son-in-law as the Finance Minister, and has consolidated power in his own hands. Because of these actions, foreign direct investments have slowed, and the Turkish lira has sold off, leading to a decline in the currency earlier this year. With the depreciation in the currency, inflation in Turkey climbed precipitously and is now over 15%. The depreciated lira has raised the cost of funding for Turkish banks precisely at the time when the economy needs stability.

The spat with the US on the non-extradition of Fethullah Gulen, who resides in the US, and is thought by Mr. Erdogan to have perpetrated the coup, escalated with the arrest of the US Pastor Andrew Brunson. Pastor Brunson is accused of furthering Mr. Gulen's agenda to topple Mr. Erdogan. The US retaliated with tariffs, aggravating further the already deteriorating economic situation.

Global investors are now concerned about certain European banks which have exposure to Turkish banks. These banks include, but are not limited to, UniCredit, BNP and BBVA. The impact on Italian banks is especially worrisome. Italy has already undergone its own credit struggles as the new populist government is looking to expand fiscal policy, increasing the country's deficit. The European Central Bank will certainly provide liquidity to Italy if needed since Italy appears to have the resources to pay back any loans.

For investors, it is likely that volatility in emerging and European markets will continue. There are concerns about European banks' exposure to Turkey, as well as Turkey's impact on other emerging markets. However, the level of trade between Turkey and other emerging markets is small. This makes it less likely that the turmoil will spill over to those markets. Turkey has said it will support its currency, which gave some relief to the lira. Additionally, Qatar has pledged $15 billion to Turkey, signaling Mideast support of Turkey. This is hardly surprising given the large ownership of assets in Turkey by Mideast investors. However, the troubles in Turkey should not derail the global growth narrative, which will be supportive for stock markets in general. For now, investors are being cautious until there is more clarity on how these political alliances and posturing by Mr. Erdogan, Mr. Trump, the EU, and Mr. Putin work out. The economy in Turkey should recover, and the impact on most portfolios will be minimal. Emerging market currencies have come under pressure recently as Turkey's crisis has escalated, but historically these types of negative reactions tend to be brief.

Please feel free to call Beacon Pointe should you need additional information or have any questions.