Deepening Mortgage Crisis and Increasing Worries About the US Economy Continue to Shake the Markets …

The action to close ruling AKP increased volatility in the domestic markets…

The deepening liquidity crisis indicated by the Bear Stearns bailout by J.P. Morgan for US$ 2 a share and increasing worries about the US economy contributed to the continuing turmoil in the global financial markets throughout March. FED's consecutive cuts of 25 bps in discount and 75 basis points in fed funds target rates and further measures to pump liquidity into the markets caused temporary recovery in the markets. However weak US economic data caused the recovery to be temporary and the market volatility continued to increase.

In the domestic agenda, the supreme court of appeals chief prosecutor's action to close ruling AKP further contributed to the volatility in the domestic markets and the ISE suffered heavy losses as a result. We expect the issue to cause pressure on the markets in the mid to long run due to the increasing number of speculations and scenarios regarding the outcome of the closing action and rising political tension.

FED cut the benchmark interest rate by another 75 bps in March…

As the mortgage crisis deepens, the markets' focus moved to the financial industry following Bear Stearns bailout. The grim outlook cleared out a little bit after better than expected earnings releases by US financial institutions and OFHEO's approval to decrease the capital adequacy ratio to 20% from 30% for Fannie Mae and Freddie Mac, the two largest U.S. mortgage finance companies, practically enabling them to pump an additional US$200 billion to distressed mortgage markets.

The commodity prices declined after reaching an all time high due to increased expectations about a slow down in US economy for the 1st quarter. The current benchmark rate reached to 2.25% after recent rate cuts. On the other hand, we observe that FED's rate cuts start to have a relatively shorter effect on stabilizing the markets. We believe that we have to wait for the US economic data releases in order to assess the effects of FED rate cuts on the US economy as a whole. We expect the current high level volatility to continue dominating markets until the economic data shows serious signs of recovery in the US economy.

IMF peg...

The government couldn't succeed to pass the Social Security Reform bill from the Parliamentary General Assembly in March, due to increasing protests by the labor unions. While Labor & Social Security Minister Celik kept negotiating with executives from the confederations of civil servants and workers regarding the Social Security and General Health Insurance draft law, IMF executives stated that the remaining reviews of Turkey's program would probably be united.

On the other hand, we observe that the nature of relations with IMF after the completion of the stand by agreement on May 2008 does not seem to be clarified so far. We believe that it is critical for Turkey to keep close relations with IMF for the continuing stability of Turkish economy, considering the increased domestic political tension following the action to close ruling AKP and subsequent developments.

EU peg...

After the release of the EU progress report on Turkey on the 7th of November 2007, Turkish EU relations were strained by French President Sarkozy's negative remarks regarding Turkey's EU membership prospects. The tension increased further on December 2007 when the EU leaders signed a final declaration of an EU summit which failed to refer to Turkey's "membership" and its "accession process".

The relations were then normalized again as the EU decided to open two new negotiation chapters and the approval of the new foundation Law by the Turkish Parliament. Despite these positive developments, we remain worried about a slowdown in Turkish EU relations due to the increasing uncertainty caused by increasing domestic political tension. We believe that the resolution of domestic political tension and further developments in the political reform process will have critical importance for the course of Turkish EU relations in the near future.

Our portfolio recommendation for April…

Deepening effects of the mortgage crisis and increasing worries about the US economy continued to dominate the markets in March. In this context, we expect the high volatility to continue throughout April. Hence, we maintain our portfolio recommendation of 15% fx, 20% stock and 65% treasury bill for April.