Lloyds Chambers
1 Portsoken Street
London E1 8HZ
Tel: 020 7702 0888 Fax: 020 7702 9452
www.hermes.co.uk

INVESTMENT NOTE **17 FEBRUARY 2014**

Why we have taken 'cheap' Turkey to an overweight

Gary Greenberg, Lead Portfolio Manager and Head of Hermes Emerging Markets, explains why the team has moved to an overweight position in Turkey, which has suffered significant equity market and currency falls in recent weeks and months.

Markets and currency have plummeted
"The combination of tapering and political unrest has hit the Turkish market hard, resulting in a 30% drop in dollar terms from the peak in May 2013. Turkey's currency has lost more than 25% since May 2013, when tapering was first mentioned. Six month Turkish Libor has jumped from 5.1% to 9.4% over this period, and the economy duly slumped. Given these headwinds, the market has de-rated and is now looking cheap.

"The Central Bank of the Republic of Turkey continues tightening to defend the currency against Fed tapering. Turkey has achieved a large devaluation of its currency, re-establishing competitiveness versus the euro. Technological innovation would have been our preferred method, but it looks like the job has essentially been done for now."

Benefiting from recovery in Europe
"As most exports are directed to the Eurozone – primarily autos, textile, white goods and steel – Turkey stands to benefit from any European recovery. The country does not produce many commodities – it is an importer of oil, iron ore and coal. Therefore, any softening of Chinese growth could also have the knock-on effect of lowering further the costs of imports. This would have a significant impact, as the combination of electricity, gas, other fuels, and transportation account for another 22% of a typical Turkish consumer's overall expenditures."

Political strife
"The political situation is quite fluid and thus difficult to handicap, but on a tactical basis we believe a political solution will be found and companies will find a way to grow profits. Europe's recovery will help exports, China's slowdown should ease pressure on commodity prices, and the growing global interest in energy extraction from shale can only help Turkey's current account.

"This all means Turkey becomes an overweight position, on the assumption politics do not seriously derail the economy and the market's valuation reverts to the mean."

Stocks we own include **Aygaz**, **Arcelik** and **Halkbank**.[1]

Aygaz currently distributes propane gas. However, it is becoming a more diversified gas distribution and power generation company. Trading under 9x earnings and with a 10.6% yield, we think this is well valued, with a business plan that could see earnings grow significantly.

---

[1] Figures from Bloomberg

Arcelik is the number one white goods company in Turkey, South Africa and Romania, with leading market share in home appliances in the UK, and third place in Europe. The stock has a 4.8% yield and trades at 11.7x earnings, with a 17.3% return on equity.

Halkbank is a well-run though government-owned bank which lost its chairman and 20% of its market cap to a scandal recently. Recent interest rate hikes and the upcoming economic slowdown have reduced estimates for profitability and earnings for this year, but the stock trades at book value and 6x earnings, yields 3.4%, and should earn a return on equity of 17.9% this year.

-ENDS-

For further information, please contact:

Hermes Fund Managers

Jean Dumas
+44 (0)20 7680 2152
j.dumas@hermes.co.uk

Melanie Shelley
+44 (0) 20 7680 2110
m.shelley@hermes.co.uk

Notes to Editors:

Hermes Fund Managers
Hermes is a unique fund manager – we have been an industry leader in Responsible Investing for over thirty years and offer clients the unparalleled combination of:

- Our **Multi-Boutique Structure** gives institutional and pension fund clients globally the benefit of access to a broad range of specialist, high conviction investment teams operating within an established and robust operating platform.
- Our **Investment Office** is a crucial function, acting as a performance risk 'radar' for all boutiques' investment activity and is central to our mission to deliver Sustainable Risk-Adjusted Alpha to all our clients.
- Our commitment to behaving as a **Responsible Asset Manager**, not merely by being a 'Responsible Investor' in quoted companies but also by applying these principles across all asset classes and by behaving as a 'good fiduciary' on behalf of our clients.

Hermes' investment solutions include:

- **Bonds**: Inflation-Linked, Government Bonds, Investment Grade, High Yield
- **Alternatives**: Commodities, Hedge Fund Solutions, Real Estate, Private Equity, Infrastructure
- **Equities**: Global, Emerging Markets, Small & Mid Cap, Europe, Japan

Hermes manages assets on behalf of more than 170 clients* across these investment areas with £26.3 billion* assets under management. Additionally, we support pension funds and other global institutional investors worldwide in meeting their ESG responsibilities through our market leading Hermes Equity Ownership Services, which takes on a stewardship role engaging globally on more than £98 billion* of assets.

*Please note the total AuM figure includes £3.4bn of assets managed or under an advisory agreement by Hermes GPE LLP ("HGPE"), a joint venture between Hermes Fund Managers ("HFM") and GPE Partner Limited. HGPE is an independent entity and not part of the Hermes group. £0.4bn of total group AuM figure represents HFM mandates under advice. Source: Hermes as at 31 December 2013.