

**The BIST has moved in parallel with the emerging markets, reaching new record highs...**

**The BIST has moved in tandem with EMs in May testing a new record high of 98,794...**

Having started the month below 95,000 levels, the BIST100 has reached a new record high of 98,794 within the month, thanks mainly to increasing fund flows towards the EMs, closing the month on a 3% gain at 97,574. The monthly index rise was supported by the 3.3% average rise among the industrial stocks, while the banking index has decoupled negatively, underperforming the market with a monthly increase of 1.5%. The expectation of a continuing abundance of liquidity with the expectation that the US Federal Reserve will not hasten, but continue to increase its policy rates gradually, declining political risk following the referendum and tension with the EU and government measures to support the economy with facilities such as the credit guarantee fund have all contributed to the index breaking its highest records in the month.

**The Fed has left policy rates steady between 0.75%-1.00%...**

The Fed has held policy rates steady between 0.75%-1.00% with a unanimous vote. The minutes of the Fed's May meeting indicated that members have judged that it would be prudent to await additional evidence indicating that the recent slowing in the pace of economic activity had been transitory before taking another step in removing accommodation. FOMC members have agreed to reduce the Fed's balance sheet in a gradual and predictable manner. The odds of a rate increase at the Fed's meeting on June 13-14 have, however, declined from 100% to 80% following the investigation into President Trump and the recent, relatively more dovish comments from Fed members.

**The CBRT has increased the average funding rate to 11.97%...**

After having raised the late liquidity window (LON) interest rate by 50bps to 12.25% at its April meeting, the CBRT has gradually increased the weighted average funding rate to 11.97% in May, addressing inflation. There were no MPC meetings during the month.

**Markets will follow the Fed's policy decision and FOMC members' statements in June...**

In June, the markets will mainly concentrate on the US Federal Reserve's FOMC meeting of June 13-14, focusing on both the Bank's rate decision and the dot plots, and also on Chair Yellen's comments after the meeting. The markets have taken a rate increase decision almost as certain, and attention would, thus, mainly be on the pace of future rate increases and the disclosures of the Bank regarding its intention to reduce its balance sheet. Should the number of rate increase expectations be raised to 4 for 2017E, the EMs could face selling pressure. Conversely, a reduction in the number of expected rate increase decisions would strengthen fund flows towards the EMs. Markets will maintain their focus on President Trump as well, as they have since his inauguration. Increasing expectations of the President's removal from office as a result of investigations could create turbulence and selling pressure on the markets. Meanwhile, the development of geopolitical risk due to North Korea will also be followed. Overall, after having decoupled positively in May, fund flows towards the EMs are expected to continue, although their pace of increase is expected to be relatively lower than in the previous month. Risk appetite towards EMs is expected to grow stronger should the increasing trend in commodity prices gain strength, and any hawkish comment from the Fed would deplete this risk appetite. The EMs, especially the BIST and other TRY-based assets, would benefit from any further rise in risk appetite.

**The BIST may face some profit taking in June...**

Domestically, the focus will be on the Government's 180-day programme, expected to be announced by the end of June, and possible changes in Cabinet members. Should Cabinet members include familiar and reputable names, the changes are likely to be welcomed by the markets. Conversely, any surprising appointments might lead to some profit taking. The CBRT's decisions will also be followed, especially on whether the Bank will maintain its tight stance following the Fed decision towards mid-month.

**We maintain the distribution of our portfolio in June...**

The BIST is expected to continue decoupling positively with intermittent corrections, should fund flows towards the EMs continue. The past 6 years' trend indicates that the index moves within a rather narrow band in the month of June, and closes with a slight decline. However, with increasing global risk appetite, the index may test new highs in June as well. Yet, we rather consider that the possibility of profit takings has increased following the markets' strong performance in May. In this respect, while expecting the BIST to perform almost in tandem with other EMs, we may expect a slightly negative decoupling in June.

In light of these expectations, we maintain the distribution of our portfolio at 55% in bonds, 15% in FX and 30% in equities.