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Could the outcome of Turkish parliamentary elections lead to increased volatility?

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The upcoming parliamentary elections on Sunday in Turkey could force Erdogan to postpone his plan for a new constitution and could lead to new political leaders in the Ministry of Finance and the Ministry of Economics. This would trigger an increase in uncertainty and consequently a higher degree of volatility for the Turkish Lira and the Istanbul stock Exchange.

Four main political parties are running for government: the ruling AKP (Justice and Development), the main opposition party CHP (Republican People's Party), MHP (the Nationalist Action Party) and the Kurdish HDP (Kurdish People Democratic Party).

Erdogan wants to strengthen his influence

Two major uncertainties affect the elections this year: firstly, whether HDP, the Kurdish Party, will be able to exceed the 10% threshold to make it into parliament and, secondly whether AKP will be able to acquire enough seats (276) to form a single party government.
Depending on the outcome, AKP may be willing to shift to a presidential system. If Erdogan manages to hold on to power in a single party government, this might lead to an amendment of the constitution, which would furnish him with more authority.

A coalition government would lead to higher uncertainty

A possible coalition government could cause more political turmoil after the election period. The capital market may be concerned with the question of who is going to replace Ali Babacan, the Deputy Prime Minister responsible for Economics, and Mehmet Simsek as the Minister of Finance. It seems that continued political stability and, hence a further improvement of consumer sentiment would ease the pressure on the Turkish lira and in turn have a positive impact on the economy.

This year economic growth will be at 3%, down from 4.5% in 2014. Turkey is feeling the weakness of its major trading partners such as Russia and the Middle East. The equity market has been moving sideways this year, with the Turkish lira depreciating sharply against many other emerging markets currencies. Therefore the economy failed to benefit from the cheaper oil imports.

Recent polls indicate that HDP's popularity hovers around 10% and AKP's votes to fluctuate around 40-43%. Given this outcome, AKP would fall short of 330 seats needed to call a referendum on amending the constitution.

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