ECONOMIC DIALOGUE

# Turkey

ECONOMIC, POLITICAL AND CULTURAL MAGAZINE ● YEAR 34 ● ISSUE 66 ● OCTOBER 2017

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## “THE WORST IS BEHIND US”

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**MEHMET ŞİMŞEK**
Deputy Prime Minister

The path to price stability: An integrated approach

**Murat Çetinkaya**
Governor of Central Bank

**5.1 Percent growth in first half of the year**
Turkey fourth fastest growing economy in Europe

AEGEAN ECONOMIC FORUM

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Author of Capital Failure

## Regional Vision in the Light of Global Developments

25-26 October 2017, Swissotel İzmir - Turkey

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**Publisher**
On behalf of Özgencil Yayıncılık
Tanıtım Organizasyon A.Ş
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Phone: +90 (212) 241 70 84 - 85

**Printed by**
Mim Ofset Basım
Litros Yolu, II. Matbaacılar Sitesi ZE - 4
Topkapı / İstanbul / Tel: +90 (212) 612 44 04

**Type of publishing:**
Local, periodical, yearly

ECONOMIC DIALOGUE TURKEY

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OCTOBER 2017 // YEAR 34 // ISSUE 66





*Honorary Chairman of Forum Istanbul*
*Yavuz Canevi*

# FUTURE'S BLESSING WILL ONLY COME WITH THE GLOBAL PEACE

Peace is the only option so far, and it is within our grasp, but we need leaders who believe in it and will be at the cost of being worse of themselves but being better of globally. This is not just a great idea and / or wishful thinking but it will be our only option to save the world we know to survive.

## GLOBAL MEDIUM TO LONG-TERM OUTLOOK

We have to recognize that currently populism's role in shaping the economic conditions will probably be more powerful than classic monetary and fiscal policies. We also recognize that a decade ago, most analysts considered ''political risk'' to be something that only infected the emerging markets world.

However, in the aftermath of the shocking results from last year's popular votes in the US, UK, Italy and this year's election in Holland, not to mention the possible developments in the upcoming November election in Germany, showed that populism is also a phenomenon for the developed countries, as well. Remember France was the only country in Europe recently, to avoid a populism victory at the last moment with a new, young and promising leader like Macron.

Have you ever wondered why is the world appears to be unsettled in the recent years? It is time to ask this question again and again and try to identify the real, deep-seated structural reasons which are related for the changing political, economical, social, technological and geo-strategical (security and natural resources wise) environment in an unprecedented manner.

This issue cannot be addressed unless we accept the fact that the world has already entered a new age of multipolarity which requires a totally different rules and mind-sets to navigate securely.

Today the lack of hegemonic rivalry over leadership of the global system is behind us. Therefore, primacy of one or two states or blocks has eroded and multipolarity is beginning to be at work. In fact, the current era is distinctively, if not dramatically, different. One obvious difference is the following; the revival of populist and authoritarian challengers to the liberal, free market system, and the reemergence of ideological and cultural-religious differences as both an aspect and driver of intensified geo-political and ideological competition.

The complexity of transnational problems seems to be outpacing the capacity of existing global institutions and mechanism to cope with. ''The Global Governance Gap'' is the new term to describe this bottleneck.


*Yavuz Canevi, Honorary Chairman of Forum İstanbul.*

From elections in key EU member states to the post-constitutional referendum in Turkey, on both sides we are likely to witness serious political developments and possible changes. The truth is that anti-globalisation is re-surfacing in advanced economies.

New global leadership in multilateralism to emerge is not a choice but a must in order to keep things rolling in the right direction. So the issue is not ''IF'' but ''WHEN'' will this happen. Economic history is the best witness of the destructive path of protectionism and populism. The record is one of almost unrelieved failure. Policy makers never seem to learn anything from these failures. Once this vacuum of new ''shared global leadership'' is left unmanaged, protectionism will spill over and the world will encounter another worse global recession. We can be alarmist and indeed pessimistic but never can we allow ourselves to become ''defeatist''. We still have a tiny room to be hopeful, even if there may be an element of ''mission impossible''. Let us admit that the future's blessing will only come with the global peace, otherwise we will have no future at all.

Peace is the only option so far to the world and it is within our grasp, but we need leaders who believe in it and to be willing to share at the cost of being worse of themselves but being better of globally. This is not just a great idea and/or wishful thinking but it may be our only option remaining to save the world we know to survive.

Can we expect that our leaders would have the courage and willingness to make this option at work? Why not! Global economic and

**The world's exposure not only to natural catastrophes but to political and economic downturns also is rising, but our ability to deal with these shocks is decreasing due to the weakened fiscal positions of many governments coupled with slow growth and lack of leadership.**

environmental developments are gradually evolving towards two ''perfect storms''. What is critical is that these two storms are on a collision course: Global Governance Failure.

The world's exposure not only to natural catastrophes but to political and economic downturns also is rising, but our ability to deal with these shocks is decreasing due to the weakened fiscal positions of many governments coupled with slow growth and lack of leadership.

**STORM I: Economic**

- Unjustified deglobalisation and rising protectionism.
- Severe income disparity at national and global level.
- Fast urbanization and demographics (aging population in DCs.), chronic labor market imbalances.
- Unmanageable foreign exchange volatility and movement of ''Hot Money''
- Managing Industry 4.0 and controlling ''cyber'' aggression.

**STORM II: Environmental and Social-Ideological-Political Challenges**

• Failure of climate change adaptation (Food and water shortage, rising gas emission, etc.)

• Rising Radical trends (Extreme right wing movements, populism, etc.)

• Terrorism (clash of civilization)

• As the most part of the world is not suffering only from the lack of basic education-cum-ignorance, but is not properly and adequately

prepared to embrace the next augmented technological up-swing.

In fact, new technologies such as AI (Artificial Intelligence), gene editing, nanoscale manufacturing, robotics and embedded computing are going to redefine the next age of humanity. Therefore, the immediate challenge for the whole world will be redesigning the learning / education strategy before it is too late.

**GLOBAL SHORT-TERM OUTLOOK**

Five ''Black Box'' Story is going to dominate the sceen in the short run:

**1.** Good Trump versus Bad Trump

*• Good Trump: Pro-Business, Pro-Structural investments, Pro-Wall Street, Pro-Strong Dollar.*

*• Bad Trump: Trade War with China, withdrawal From NASDAC, TTIP, TPP, increased protectionism.*

**2.** FED interest rate policy's dominance on global markets. There are signs that a clash between FED and Trump is brewing.

An aggressive interest rate hike would hurt EMs. Predictability is the key.

**Last couple of years were rather challenging years for Turkey as the security risks and geopolitical issues remained high on the agenda as opposed to the structural reforms which were properly listed in the 10th Development Plan for the period of 2014-2018.**

**3.** How EU's next structure will be affected with Brexit and will there be other exits?

**4.** Oil Price developments still remain as one of the key determinants of the global growth.

**5.** Terror will continue to be an important disturbing element to global peace and stability.

To conclude we can say that history provides several testimonies to show that the initiators of political or economic aggression or even the proponents of political and economic isolation cum protectionism never become victors.

Therefore, a united, collective action is needed, not building walls and fences. But it seems that the world has to live with this cyclic wave towards a deglobalised era, till as long as it may take to reverse the process again.

What is needed a re-born version of WTO, a more equitable, a more transparent and a more inclusive global development oriented system.


## TURKEY'S CHALLENGE: MOVING FORWARD

*Politics/Geopolitics*

Last couple of years were rather challenging years for Turkey as the security risks and geopolitical issues remained high on the agenda as opposed to the structural reforms which were properly listed in the 10th Development Plan for the period of 2014-2018. In fact Turkey has held two general elections, one regional election, presidential election and two referendums during this period. In the same period terror has accelerated and taken hostage of peace process. Meanwhile Syrian war has also accelerated and more than three million Syrian refugees flood has become the Turkey's burden. Also the country has also suffered seriously from the aftershocks of the Russian plane crash in Syria. And then, July 15, 2016 failed coup attempt and its subsequent ramifications were enough to divert country's focus from reforms to security and stability. Let us remember that Turkey has waited 19 years to get the ''Investable Grade'' from the international rating agencies and we could only enjoyed it three years. In 2016 we lost it again.

What is also worrisome is the recent tensions with our main trading and FDI partners, EU countries. As the 60th Anniversary of the EU, it is clear that the longstanding belief in closer integration toward a federal EU, is being challenged with an idea of a looser ''multi-speed'' governance for the bloc. Therefore, it is now essential more than ever that Turkey's anchor with the EU, during this redesigning phase, should continue at a rational level, away from stress and domestic policy debates. In fact this is not the right time to burn the bridges with the EU.

*Economics / Fiscal Space / Growth*

One should recognize the fact that Turkey is no longer a ''stand alone'' country anymore. Turkey is a global actor due to its:

• Links with EU, more so in economic sense than political
(Customs Union)

• Integration with the western security alliance, NATO

• Strategic position in terms of Middle East Peace, stability and migration

• Being in a key position in Energy pipelines and transportation.

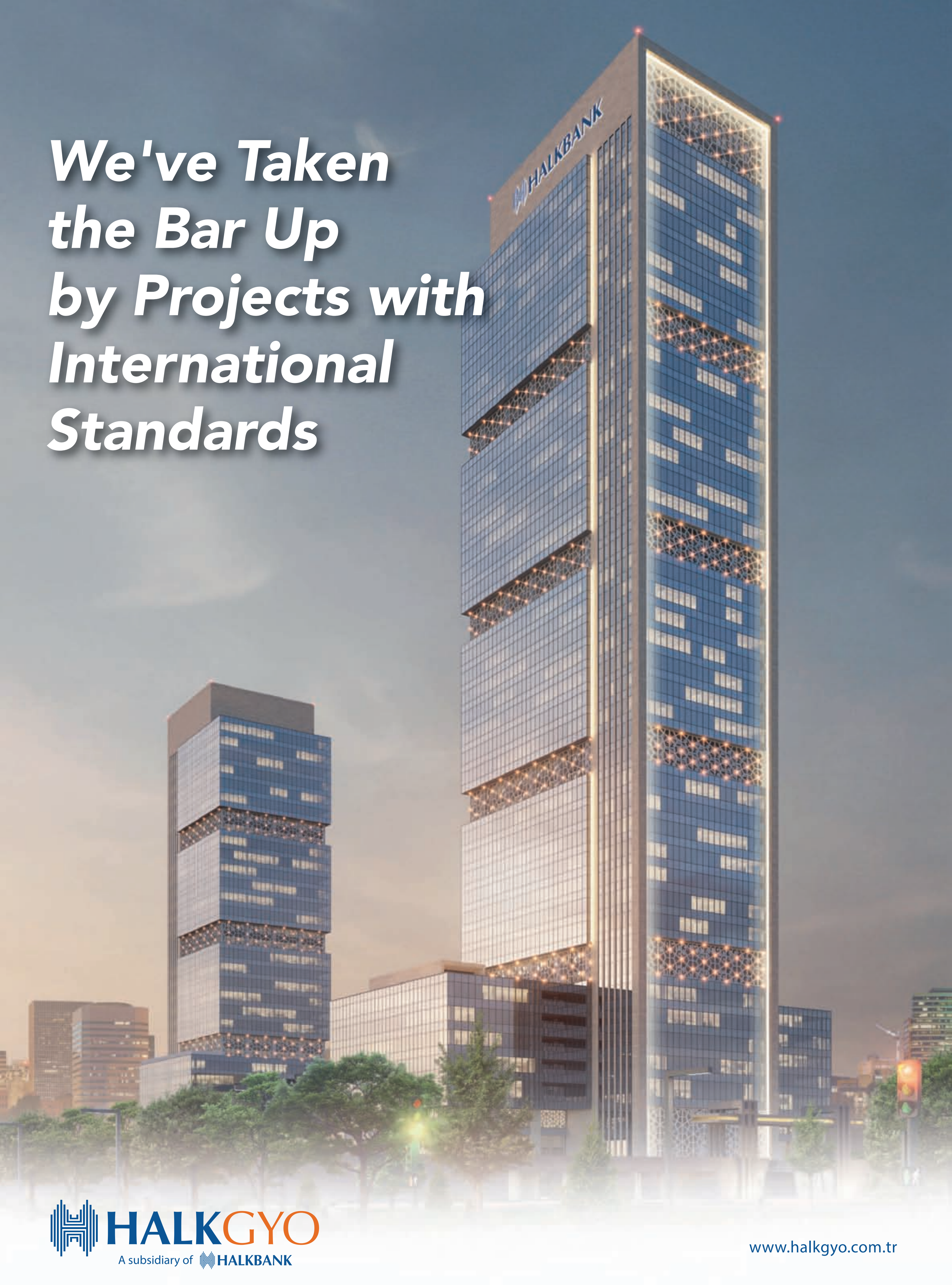
Therefore Turkey's actions should be and will be within these boundaries and in line with her commitment to western values.

With this understanding, according to a recent PWC report ''if Turkey can overcome its short-term political uncertainties and focus its attention on reforms in all needed areas, as it was listed on the 10th Development Plan, the country can provide great long-term business opportunities with its favorable demographics and geopolitical position. According to our estimates, Turkey has the potential to grow at an annual average rate of around 3% over the next 34 years compared to 1.7% on average for the G-7. Therefore the country is projected to become the world's 14th largest economy as of 2030. Turkey could also maintain its second position in 2050 within the E7 countries in terms of GDP per capita in PPP terms ''.

*Middle Income Trap and Industry 4.0*

To manage complex, multi- dimensional change in the value chain and in the face of the threat from competitor EMs and at the same time satisfying investors' demand, both domestic and international, for safety, security, accountability and naturally sustainable profitability requires a totally new strategy by raising the bar further in all fronts which should be able to deal with the existing complex and rapidly changing environment.

Because innovative technologies constantly are reshaping the landscape, that is why in this new era momentum and speed are vital. In this unprecedently complex and competitive environment digitalization and Industry 4.0 seems to be the way out. Turkey cannot afford to miss this Fourth Industrial Revolution. Private sector has already shown that they are aware of this unique opportunity. TUSİAD and BCG (The Boston Consulting Group) report of March- 2016 was the best proof of this awareness. EDT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*Today, the portfolio size of our Company is close to 2 billion TL consisting real estate properties with regular rent income, as well as qualified office, residential and hotel projects. We always raise the bar by signing projects with international standards. It is a great source of pride for us to be one of the biggest stakeholders of the **Istanbul International Finance Center Project**, which is aimed to be primarily the regional and ultimately the global financial center.*

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IIFC, the heart of the financial world, is located at the intersection of two main arteries, the TEM highway in the east and the E5 connection in the south. IIFC, rising in a region surrounded by living spaces, social centers, cultural and entertainment areas will increase the vitality of the region it is in. When the project is completed, there will also be an increase in the number of financial institutions, cultural centers, hotels, and residences. The project, which is carried out under the coordination of the Ministry of Environment and Urbanization, will contribute to the brand awareness of our sector at the global level. Istanbul will become a center of attraction for multinational corporations and investors. IIFC project will make Istanbul one of the leading centers of the world while raising our country's position in the global finance world. We believe that this giant project that will actualize a dream for Turkey will put Istanbul in between the first ranking cities of global financial centers such as New York, London, Hong Kong, Singapore, Tokyo, Toronto.

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## A Modern Building That Enriches City Life and Lives 24 - Hour

With the Istanbul International Finance Center, institutions like Halkbank, Vakifbank, Ziraat Bank, BRSA, CMB and Central Bank will be located all together in a financial hub. IIFC will be a multifaceted financial center with A class office standards and will increase the economic activity of the region by creating new jobs for thousands. The project, also planned on social and cultural aspects, will enrich the city life and rise in the heart of the city with its 24-hour-living modern structure. As Halk REIT, we are the largest stakeholder in this giant project which is expected to be operational in 2020. At the end of 2016, our company started the construction of two office towers of 46 and 34-storey and 3 commercial blocks of 8-storey, which will be built within the scope of the IIFC project. As we are planning to lease the big block to our main shareholder Halkbank to be used as their Head Office, we also expect intense interest of national and international financial institutions for the other leasable areas in our project.

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MACROECONOMIC POLICY COORDINATION AND ECONOMIC OUTLOOK IN TURKEY

*Deputy Prime Minister*
*Mehmet Şimşek:*

# "THE WORST IS BEHIND US"

Overall, Turkey's policy response has largely achieved the desired macroeconomic objectives. The evident success of Turkey's recent experience with such macroeconomic policies hinges on several factors. First, and foremost, these policies represent the outcome of a coordinated and well-targeted policy design, implemented in a timely and selective manner when they are needed and would be the most effective.

Turkish economy has successfully weathered several major shocks in recent years, including geopolitical tensions, a number of terrorist attacks and a coup attempt. Despite numerous domestic and external shocks, the growth rate was comfortably above the emerging market average during the past decade. The growth was averaged to 6.7 percent during 2010-2016 period, which is likely to exceed 5 percent in 2017. So, what lies beneath Turkey's remarkable performance?

The answer, in my opinion, can be reduced to three key factors: **(i)** resilience of the Turkish economy built meticulously through structural reforms and fiscal prudence of the past 15 years, **(ii)** proactive policy response coordinated across all relevant policymaking institutions, and **(iii)** private sector dynamism and Turkey's stress-tested people.

Resilience is about accumulating buffers in good times; and proactive policymaking is about being ready to use this buffer when needed. Turkey had ample fiscal space when those shocks had hit the economy. Turkey's general government deficit was close to zero percent and debt to GDP ratio was 28 percent less than half of the Maastricht Criteria. Moreover, thanks to the macroprudential buffers accumulated in recent years, there was sufficient room to support the financial system. The government was able to provide the necessary stimulus on a timely, targeted, and coordinated basis.

The failed coup attempt in mid-2016 was by far the highest confidence shock to the Turkish economy over the past few decades. The Turkish economy in the absence of appropriate policy response could have easily entered a prolonged recession. Against this backdrop, starting from the last quarter of 2016, the government and other policymaking institutions have launched a set of supportive measures and incentives. We can classify these policies under five broad categories: **(i)** tax cuts and easing of macroprudential measures on consumer credit to boost consumption; **(ii)** new employment incentives to encourage hiring; **(iii)** sector-specific tax deferrals to help ease firms' cash flow constraints; **(iv)** Treasury-backed Credit Guarantee Fund (CGF) scheme to boost SME's access to finance; and **(v)** accelerating structural reforms. On the other hand, the Central Bank remained focused on price stability by undertaking a strong monetary tightening.

Mehmet Şimşek, Deputy Prime Minister

The economy's response to these coordinated measures has been strong, and recent data confirms that downside risks to economic activity have abated. The pace of economic recovery has gained strength as of the second quarter of 2017, with a wider sectoral spillover of the pickup in economic activity. With a more solid economic rebound ahead, we expect employment to rise further in the upcoming period, which will further support consumption expenditures, particularly on top of tax-cutled spending on durable goods.

In sum, we are confident that the worst is behind us. Turkey is returning to long term growth path. With the help of structural reforms Turkey is likely to join high income group in 5-7 years. Once the confidence of entrepreneurs and households has been restored, and uncertainties have waded, Turkey's strong fundamentals are now taking the lead to drive the economy on a solid and sustainable path.

An important pillar of the recent macro policies has been the support provided to the supply side of the economy. The most powerful measure was the new Credit Guarantee scheme. It was key to break the vicious cycle of weaken economic activity and credit crunch following two shocks in 2016. Together with other measures, the Treasury-backed credit guarantee mechanism has improved SME's access to credit and dampened the excessive procyclicality in bank lending.

Overall, Turkey's policy response has largely achieved the desired macroeconomic objectives. The evident success of Turkey's recent experience with such macroeconomic policies hinges on several factors. First, and foremost, these policies represent the

**All in all, we already have started to bear fruits of our policy mix, as Turkey's economic dynamics are returning to their natural course and converging recently to its underlying fundamentals-driven trend, having restored confidence and improved financial conditions rapidly.**

outcome of a coordinated and well-targeted policy design, implemented in a timely and selective manner when they are needed and would be the most effective. Second, both fiscal and macroprudential policies had ample policy space at the outset because of prudent and responsible implementation of past policies. Third, these policies were designed to provide a temporary stimulus, mainly as a jump-start device, without causing long term imbalances. Therefore, resorting to supportive countercyclical policies have been able to restore consumer and business sentiment without a major effect on government debt and the country's risk premium.

All in all, we already have started to bear fruits of our policy mix, as Turkey's economic dynamics are returning to their natural course and converging recently to its underlying fundamentals-driven trend, having restored confidence and improved financial conditions rapidly.

Recent indicators and official forecasts confirm that GDP growth in 2017 is very likely to surpass the Medium-Term Programme forecast of 4.4 percent. Moreover, there are signs that the economic recovery is spreading to an increasing number of sectors led particularly by exporting sectors, which indicates that the recovery in economic activity also proves durable rather than being one-off. The main drivers of growth in 2017 will be **(i)** the gradual improvement in tourism revenues, **(ii)** the strengthened confidence channel, **(iii)** the positive effect of the cumulative depreciation on net exports, and **(iv)** the normalization of commercial relations with Russia. We will also continue to see some impact from the measures and incentive packages to boost consumption and investment expenditures, as well as reduced uncertainty and improved financial conditions. Strong job creation on the back of the ongoing recovery will provide a basis for sustained growth. Investments are improving gradually as uncertainties wane and private sector confidence returns. In addition, we see investment expectations turning positive more significantly in non-exporting sectors, which is a clear indication of the domestic demand's spurring effect on investment expenditures.

Improvement in supply-side factors such as productivity, skilled labor force, innovation and investment environment are crucial to increase the growth potential of the country in the longer run. In order to foster inclusive growth in Turkey, the government has introduced effective solutions, including active labor market policies, tax breaks for new employment, and supporting SME's access to finance.

One of our priorities in the forthcoming period will be to achieve price stability i.e. reducing inflation from high single digits to low single

digits. While the Central Bank is operationally independent, we need to recognize that some of the drivers of inflation in the past decade have been largely structural. In this respect, we will lend support to Central Bank's efforts to achieve lasting price stability. Recently, we have been working jointly on three dimensions to pave the way for price stability. The first dimension is to enhance fiscal-monetary policy coordination. The second one is to contain the excessive volatility in food prices through a comprehensive plan which will support the productivity and efficiency in the agricultural sector. Third, a new project was initiated by the Financial Stability Committee to mitigate the risks emanating from corporates' FX borrowing. We plan to amend the existing regulations to discourage excessive FX risk taking by small firms and encourage the adoption of better risk management practices for all parties.

Now that the worst is behind us and the next elections are more than two years ahead, there is a window of opportunity to implement a comprehensive reform program. This is key to putting Turkey back on a high growth trajectory on a sustainable basis. The growth strategy in the program period is based on five main pillars: developing human capital, making labor markets more flexible, increasing capacity of technology and innovation development, strengthening physical infrastructure and improving institutional quality. To this end, main priorities of our Medium Term Programme are to increase domestic savings, to ensure private investment and export-driven growth, to accelerate structural transformation of various industries, and to become more competitive in the international markets by increasing technology and productivity level.

To sum up, Turkey's fundamentals are set to become even stronger. With a population of more than 80 million people and favorable demographics, per capita GDP of higher than 10,000 US dollars, and a dynamic private sector with a strong entrepreneurship culture, Turkey is on the path towards becoming a high-income economy. **EDT**

**Now that the worst is behind us and the next elections are more than two years ahead, there is a window of opportunity to implement a comprehensive reform program. This is key to putting Turkey back on a high growth trajectory on a sustainable basis.**

*Governor of the Central Bank of the Republic of Turkey*

*Murat Çetinkaya*

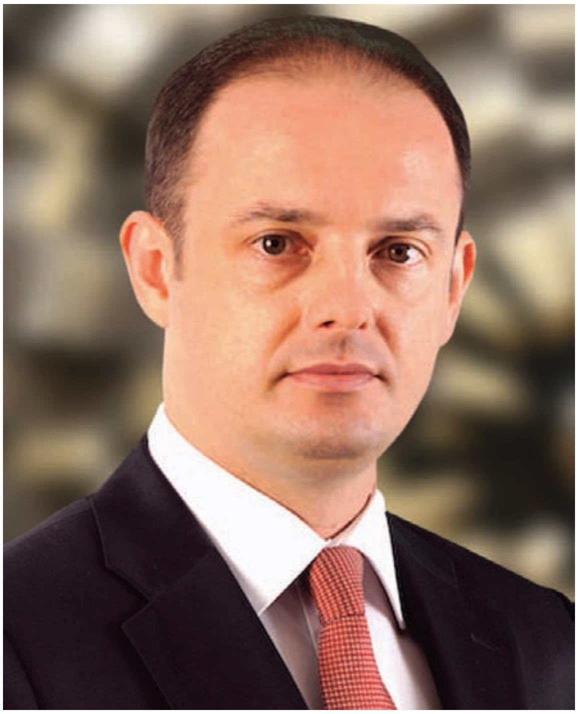
# The path to price stability: An integrated approach

The CBRT has taken an active role in helping formulate or initiate structural policy reforms that are related to price stability as well as financial stability. One major structural area has been food prices, which have played a major role in both the level and volatility of headline inflation in recent years.

Turkey has been implementing a price-stability-oriented monetary policy along with a floating exchange rate regime since 2001. This framework has been successful in bringing inflation down to single digits. It has also been helpful in coping with various shocks during the past decade. Although inflation was higher than those of peer emerging economies during that period, it has been relatively stable compared to previous decades, materializing at around eight percent.

Having consolidated the benefits of single digit inflation, time is ripe to bring inflation further down to our medium term target of five percent. To this end, Central Bank of the Republic of Turkey (CBRT) has formulated an integrated approach in 2016 to achieve and maintain a lower and more stable inflation. This approach preserves the price-stability-oriented monetary policy but also aims to complement this strategy by identifying the structural impediments to disinflation and promoting a coordinated effort among all relevant institutions.

The past year has been a demonstration of how coordinated policies can ease the trade-offs amid multiple shocks. In 2016, Turkish economy faced multiple adverse shocks, resulting in a large exchange rate depreciation and a slowdown in domestic economic activity. In response, policy authorities have taken coordinated and targeted steps to avoid a potential downward spiral resulting from adverse feedback loop between macro-financial stability and real economic activity. On the fiscal and macroprudential side, buffers that were built over the last decade allowed a counter cyclical policy response. Well-targeted tax incentives, macro-prudential easing, and credit support policies strengthened the confidence, supported credit and aggregate demand channels, and have helped reinvigorate real economic activity. On the monetary front, the CBRT has taken a series of decisive steps starting in late 2016 which include a significant tightening in policy rates and supportive foreign currency liquidity policy. Besides, monetary policy



*Murat Çetinkaya, Governor of the Central Bank of the Republic of Turkey*

framework was considerably simplified and serious efforts were put into addressing the structural aspects of inflation dynamics. Overall, with the help of these coordinated policies, fluctuations in financial markets have moderated, exchange rate has stabilized and the downside risks on economic activity have abated - with an expected growth rate that is well above the emerging markets average in 2017.

The main pillar of the monetary policy reaction has been the tightening in the policy rates, which has been particularly strong to curb the excessive volatility in the foreign exchange (FX) market in early 2017. It has also been effective in containing FX pass-through to domestic prices and spillovers to pricing behavior as well as inflation expectations.

The CBRT average funding rate has been raised by 370 basis points during the first half of 2017. Furthermore, with the aim of enhancing flexibility and instrument diversity of the Turkish lira (TL) and FX liquidity management, the CBRT launched a new swap facility where foreign currency is


*The Food and Agricultural Product Markets Monitoring and Evaluation Committee has stepped up its efforts during the past year, implementing a series of measures to monitor and improve the quality of Turkey's food supply chain, enhance market competition and production efficiency, and support stable supply and price formation for food products.*

provided to banks in return for TL deposits. This facility has been utilized extensively by market participants and proved instrumental in providing FX liquidity to the system without permanent reduction in central bank reserves, supporting tighter TL liquidity policy, and contributing to healthy price formation in over-the-counter swap markets by serving as a reference swap rate. As a result, implied FX volatility has significantly declined over this period.

Moreover, the CBRT has taken important steps towards simplifying the monetary policy framework. Compared to previous years, the composition of daily CBRT funding facilities has been stable and monetary policy stance has been clear with no surprise changes in the liquidity policy in between Monetary Policy Committee meetings.

We expect a steady downward trend in inflation starting from the end of the year. Key factors that contribute to the recent elevated levels have been the lagged effects of exchange rate depreciation, rising oil prices, administered price hikes, and unfavorable supply conditions in the agricultural sector. Some of these factors are expected to taper-off gradually in the forthcoming period, which should support the disinflation process. Moreover, unambiguously tight stance of monetary policy will help to anchor inflation expectations and support pricing behavior. Against this background, the CBRT has repeatedly emphasized that the tight stance in monetary policy will be maintained until the inflation outlook displays a significant improvement. Inflation expectations, pricing behavior and other factors affecting inflation will be closely monitored, and further monetary tightening will be delivered if needed. With the help of such policy stance, we expect a gradual convergence to the target inflation over the next few years.

The CBRT has also taken an active role in helping formulate or initiate structural policy reforms that are related to price stability as well as financial stability. One major structural area has been food prices, which have played a major role in both the level and volatility of headline inflation in recent years. A special committee titled "The Food and Agricultural Product Markets Monitoring and Evaluation Committee", was established in late 2014 under the coordination of the CBRT and the Ministry of Food, Agriculture and Livestock. The committee has stepped up its efforts during the past year, implementing a series of measures to monitor and improve the quality of Turkey's food supply chain, enhance market competition and production efficiency, and support stable supply and price formation for food products. We expect to harness the benefits of these measures over the medium term, which will support long-lasting price stability.

Lately, another major step on the semi-structural front has been the effort to contain risks emanating from FX borrowing of non-financial corporations. A widely noted concern regarding emerging markets is high FX indebtedness and potential risks associated with a strong reversal of accommodative global financial conditions. Turkey had already been well aware of such risks in early years and took actions accordingly, including restrictions on FX lending (June 2009). The CBRT has also implemented maturity-based FX reserve

**The CBRT not only maintains a tight monetary policy stance but also contributes to structural efforts for disinflation by identifying the source of the trade-offs, raising public awareness, and guiding relevant authorities to formulate targeted solutions.**

requirements (December 2014) to encourage banks to obtain foreign funds at longer maturities. These policies have been by and large effective in containing corporate sector leverage and FX related risks. Recently, the Financial Stability Committee has implemented a new initiative to construct a timely, standardized and detailed assessment on firms' FX exposures and the degree to which they are hedged against fluctuations in the exchange rates. As the next step, we plan to use these assessments to calibrate the necessary amendments to the existing regulations in order to encourage the adoption of better risk management practices for all parties.

To sum up, the coordinated policy actions have been largely successful in achieving the desired outcomes. Macro-financial risks have alleviated and output has recovered. Looking ahead, monetary policy is committed to achieving and maintaining price stability.

Accordingly, the CBRT not only maintains a tight monetary policy stance but also contributes to structural efforts for disinflation by identifying the source of the trade-offs, raising public awareness, and guiding relevant authorities to formulate targeted solutions. We believe that this approach will not only improve the policy tradeoffs but also safeguard a more sustainable disinflation process. **EDT**

## 5.1 PERCENT GROWTH IN FIRST HALF OF THE YEAR

# Turkey fourth fastest growing economy in Europe

Turkey leaves European Union, G20 and OECD nations behind with its performance in the first half of the year. Enjoying the best of times during the second quarter since the 2008 global crisis, EU posted a 2.4 per cent growth, while the Euro Zone and OECD posted 2.3 and 2.4 percent growth, respectively.

Having had a rough time in 2016 due to reasons such as a coup attempt, geopolitical risks and global uncertainties, Turkish economy entered 2017 in high gear, posting a 5.1 percent growth in the first half of the year. Year-end growth is expected to be around 5 percent in the light of a cascade of strong numbers announced.

With the growth rate achieved in the second quarter, Turkey comes in third place within the G20, closely following China and India. As for Europe, Turkey is the fourth fastest growing economy in the second quarter. Economists indicate growth in the third quarter may in fact exceed 7 percent, riding on the base effect. In case such an expectation becomes a reality, Turkey will assume the leader position in growth, leaving China behind.

Driven by government provided employment and tax incentive practices as well as the Credit Guarantee Fund providing relief for industrialists, this growth also enjoyed the positive impact brought on by a resurgence in domestic demand along with an increase in revenues in exports and tourism. Improved expectations and increased predictability in the economy have also contributed to the growth momentum.

**International Institutions revise expectations up**

Turkey leaves European Union, G20 and OECD nations behind with its performance in the first half of the year. Enjoying the best of times during the second quarter since the 2008 global crisis, EU posted a 2.4 percent growth, while the Euro Zone and OECD posted 2.3 and 2.4 percent growth, respectively.

While such strong growth is a testament to the resiliency of the economy, international institutions such as Moody's, Fitch, JP Morgan, Morgan Stanley, and Goldman Sachs have revised up their expectations regarding Turkey.

Numbers announced both in terms of consumption and production reveal the fact that this growth is healthy not just in a percentage value, but in composition, as well. Economists are predicting the 4.4 percent growth objective we have set out for 2017 will be achieved, and even exceeded at around 5 percent level, in an atmosphere of confidence and stability that has bolstered following measures taken by the stewards of economy and the April 16 referendum.

While Turkish economy posted a 2.9 percent growth in 2016, growth rate in the first quarter of 2017 was 5.2 percent.

**Activities constituting the gross domestic product**

Gross domestic product estimate by production increased by 16.3 percent in the second quarter with the current prices, and found to be 734.211 billion Turkish Liras. When activities that constitute the gross domestic product were examined, it was revealed, as a volume value chained in the second quarter of 2017 as per the same quarter of the previous year, that agriculture sector increased by 4.7 percent, the industrial sector increased by 6.3 percent, and the construction sector increased by 6.8 percent. The added value of the services sector, as the sum of trade, transportation, accommodation, and food service activities, increased by 5.7 percent.

**Exports, a driving force once again**

1.68 points of the growth in the second quarter of the year was due to the net export item. Thus, 1.98 percent of the 5.1 percent of the growth observed in the first half the year was due to net exports.

As per the most recent data announced by the Turkish Exporters Assembly, exports to the EU market continue with full speed despite the political circumstances. Exports in August increased by 11.9 percent compared to the same month of the previous year, reaching USD 12,439 million. While exports reached USD 102.5 billion with an increase of 10.7 percent as of the beginning of the year, exports figures for the last 12 months increased by 7.8 percent, reaching USD 151.8 billion.

Exports to EU countries in August were USD 5.9 billion. While the share of EU in exports was at 47 percent, exports to this market increased by 12 percent. Automotive again led exports in August with USD 1.8 billion. Exports in this sector increased by 9.4 percent. Automotive was followed by ready-made clothing and garment with USD 1.7 billion, and chemicals industry with USD 1.5 billion. The highest exports increase in August was the boat and yacht industry with 179.4 percent. And the olive and olive oil industry had the highest exports increase in agriculture with 70.5 percent increase.

**Industrial production exceeded expectations**

As per the Turkish Statistics Institute data, industrial production increased by 2.3 percent in July in comparison to the previous month. Industrial production increased by 14.5 percent compared to the same month of the previous year.

Industrial production in Turkey increased by 2.3 percent in July, and increased by 14.5 percent on a year on year basis, exceeding expectations. Whereas, the expectation was a monthly increase by 0.8 percent, and a yearly increase by 9.7 percent.

A seasonally adjusted and calendar-adjusted examination of industrial sub-sectors revealed that the mining and quarrying sector index decreased by 2.6 percent in July 2017 compared to the previous month, while the manufacturing industry sector index increased by 2.2 percent,

Comments on growth: **Mehmet Şimşek, *Deputy Prime Minister***

# An inclusive growth is absolute priority

With decreasing uncertainties on the heels of April 16 referendum, a distinct positive trend emerged in the financial markets. Meanwhile, both real sector and consumer confidence rallied. Treasury backed Credit Guarantee Fund surety system, the resources and effectiveness of which have been boosted, has been supporting the economic growth by means of commercial loans, as of the second quarter. Preliminary indicators for the third quarter of 2017 also reveal that this strong economic growth continues with increasing momentum.

While such strong growth that has been achieved is a positive development, that alone is not enough. An inclusive growth is our basic priority. As a result of the measures we have taken to increase employment as well as the momentum gained in economic growth, we have provided employment for around 600,000 more individuals during the second quarter of 2017, compared to year end numbers of the previous year. Thus, a gradual decrease was achieved in unemployment from the beginning of 2017.

Turkey has posted a strong average growth rate of 5.7 percent despite all adversity it has faced over the past 15 years, thanks to its strong economic foundations. We will be resolutely implementing our comprehensive reform agenda in the immediate future, in order to further increase this performance and accelerate the structural transformation of our economy. In these days where political uncertainties no longer exist, we are aiming to achieve high-income status with the contribution of structural reforms.

Comments on growth: **Nihat Zeybekci,** ***Minister of Economy***

## 5.5 percent level may be exceeded by year's end

With its second quarter growth performance, Turkey has forced IMF, which had predicted 2.5 percent growth, the World Bank, which had predicted 3.5 percent growth, and OECD, which similarly had predicted 3.5 percent growth for Turkey in 2017, to revise their growth expectations up by several points. The 3.5 percent growth as predicted in the Medium Term Program (MTP) for the second quarter was easily exceeded. The MTP goal that was set as 4.4 percent for the year shall be easily achieved. The 5.5 percent level may even be exceeded at the end of the year.

According to preliminary data and the Ministry of Economy analyses, third quarter growth shall be even stronger than that of the second quarter, going over the 7 percent mark. I believe we have a good chance of seeing a growth rate exceeding 7 percent, leaving even China behind. Our exports have increased by 10.8 percent in the first 8 month of the year, reaching 103.3 billion dollars. Such success is no coincidence; it is the fruit of reforms that have been implemented and hard work by our government. The fact that we are enjoying the fruits of such hard work on this day is extremely significant.


and the electricity, gas, steam and air conditioning production and distribution sector index by 4.8 percent.

A calendar-adjusted examination of industrial sub-sectors revealed that the mining and quarrying sector index increased by 0.8 percent in July 2017 compared to the same month of the previous year, while the manufacturing industry sector index increased by 16 percent, and the electricity, gas, steam and air conditioning production and distribution sector index by 11.7 percent

A seasonally adjusted and calendar-adjusted examination of main industrial groups revealed that the highest increase in July 2017 compared to the previous month was in energy with 3.7 percent.

A seasonally adjusted and calendar-adjusted examination of the production industry sub-sectors revealed that the highest increase was in the computer, electronic, and optics production with 17.3 percent. This increase was followed by tobacco production with 13.9 percent, and furniture manufacturing with 11.9 percent.

**Inflation down to single digit figures**

Yearly inflation rate decreased from 10.9 percent to 9.79 percent in July. Thus, the yearly CPI is down to single-digit figures again, after 6 months. The end-of-the-year inflation target of Central Bank is at 8 percent.

Consumer prices increased by 0.15 percent in July. A weakening was foreseen in inflation as of July this year on a yearly basis, due to the high increase in CPI last July. The monthly CPI change expectation in the market was in the 0.50 increase band with a decline of 0.56 percent.

Yearly inflation rate decreased from 10.9 percent to 9.79 percent in July. Thus, the yearly CPI is down to single-digit figures again, after 6 months. The expectation was to see an increase by 0.17 percent monthly, and 9.90 percent yearly. Core CPI increased from 9.20 percent to 9.60 percent. EDT

Comments on growth: **Naci Ağbal, *Minister of Finance***

## Preliminary indicators show strong growth continuation

Foreign demand, with increased global trade volume along with improved demand by our trade partners and recovery in tourism in the second quarter of 2017 has had positive impact in the form of 1.7 percentile points in growth. Preliminary economic indicators show strong growth continuation for the rest of the year, as well. Especially the recovery in tourism in the third quarter, favorable export conditions along with the base effect shall accelerate the growth. Unrelenting reforms we shall be implementing expediently, our measures, boosted confidence and positive developments in foreign conjuncture shall continue to support the resurgence in the economy.

**Exports in August increased by 11.9 percent compared to the same month of the previous year, reaching USD 12,439 million. While exports reached USD 102.5 billion with an increase of 10.7 percent as of the beginning of the year, exports figures for the last 12 months increased by 7.8 percent, reaching USD 151.8 billion.**

INVESTMENT

*Investment Support and Promotion Agency of Turkey (ISPAT)*

# YOU HAVE SOLID GROUNDS TO INVEST IN TURKEY

Turkey is a dynamic and growing G20 economy which uniquely links the East with the West. It is one of the world's fastest growing economies and geared to support international investors' growth through a modernizing and business friendly agenda, and access to large domestic and international markets.

### Robust Economy

Turkey's robust economy stands out as the 13th largest economy in the world with a track record of positive growth over the past decade, and most importantly with a bright future that will see it outperforming many rival economies. The average annual growth rate in 2003-2016 was 5.6 percent and GDP per capita tripled to USD 10,807 by 2016. Turkey's robust economic growth has been based on strong macroeconomic fundamentals with a successful management of public finance while controling inflation, thus providing market with predictability. Robust growth has generated significant economic activity, a vibrant domestic market, lucrative export opportunities, and an entrepreneurial spirit of the private sector.

### Strong Domestic Market

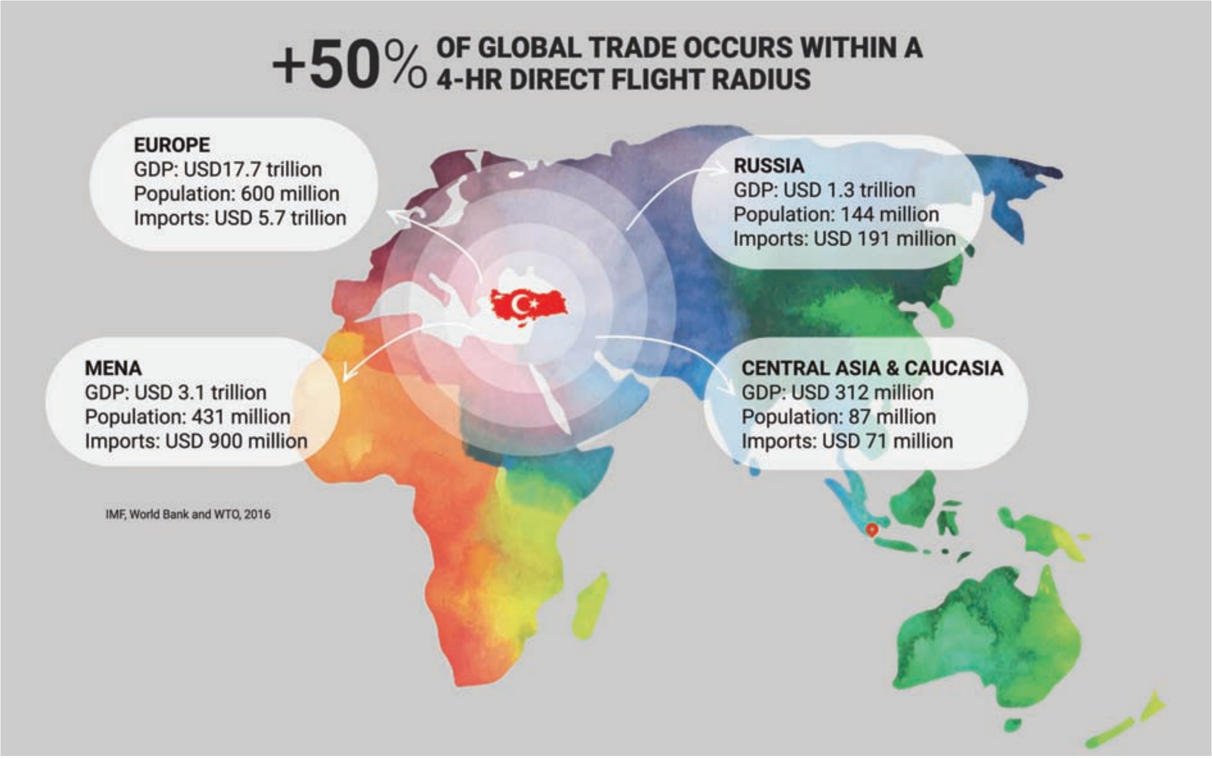
Turkey has a strong domestic market and its economic growth in the last decade has paved the way for the emergence of a sizeable middle-class with increasing purchasing power. The domestic market is further supported by emerging urban centers across Turkey. The country now has more than 20 urban centers with populations over 1 million.

### Geo-strategic Location

The domestic market in Turkey is connected with the key markets not only through customs union or free trade agreements, but also it is geographically and logistically well-connected with the rest of the world.

As such, Turkey's geo-strategic location provides investors easy access to lucrative regional markets. As a continuation of its historical role, Turkey is a prime location to host headquarters for many multinational companies thanks to its excellent connectivity, unique location, and strong bonds with its neighbors.

Also, an increasing number of companies from across the world, looking for expansion onto new markets, are finding a second home in Turkey to manufacture, as well as design and engineer, for a combined market of 1.6 billion people within a 4-hour flight radius.



**While having natural assets, such as a young population and a strategic geographic location, are important, without a business-friendly investment climate it would be impossible to attract international investments.**

### Favorable Demographic Structure

Further looking into the dynamics of the domestic market, Turkey's favorable demographic structure has also been a key driver of economic growth. With half of its population under the age of 30, Turkey stands out as the country with the largest youth population in Europe.

### Availability of Skilled Labor Force

The youth population translates into the availability of a skilled labor force with an industrious working culture and cost-competitive edge, which is yet another reason to invest in Turkey. The country has a number of successful world-class quality professionals and engineers, and coupled with competitive costs, such a qualified labor force has made Turkey more attractive to foreign investors.

### Reforms and Incentives

Turkey offers lucrative reforms and incentives that include manufacturing incentives as well as R&D and innovation support. Turkey is particularly aware of the importance of R&D investments in its efforts to move up the global value chain.

In 2016 and 2017, the Turkish government continued its long-standing policy of implementing comprehensive reforms in many areas and introducing new ones according to economic needs and changing conditions. These reforms have significantly improved Turkey's investment and business climate with solid results in key areas.

In February 2016, an R&D reform was implemented that included tax discounts for companies engaged in R&D, equal treatment of design centers and R&D centers in regard to incentives, and the establishment of technology development zones for strategic sectors such as ICT, healthcare, biotech, nanotech, defense, and aerospace.

In August 2016, Turkey passed a tax reform package that introduced tax exemptions for companies participating in the incentives schemes. Some of the exemptions covered stamp duty taxes, real-estate taxes, municipality fee taxes, and salary income taxes.

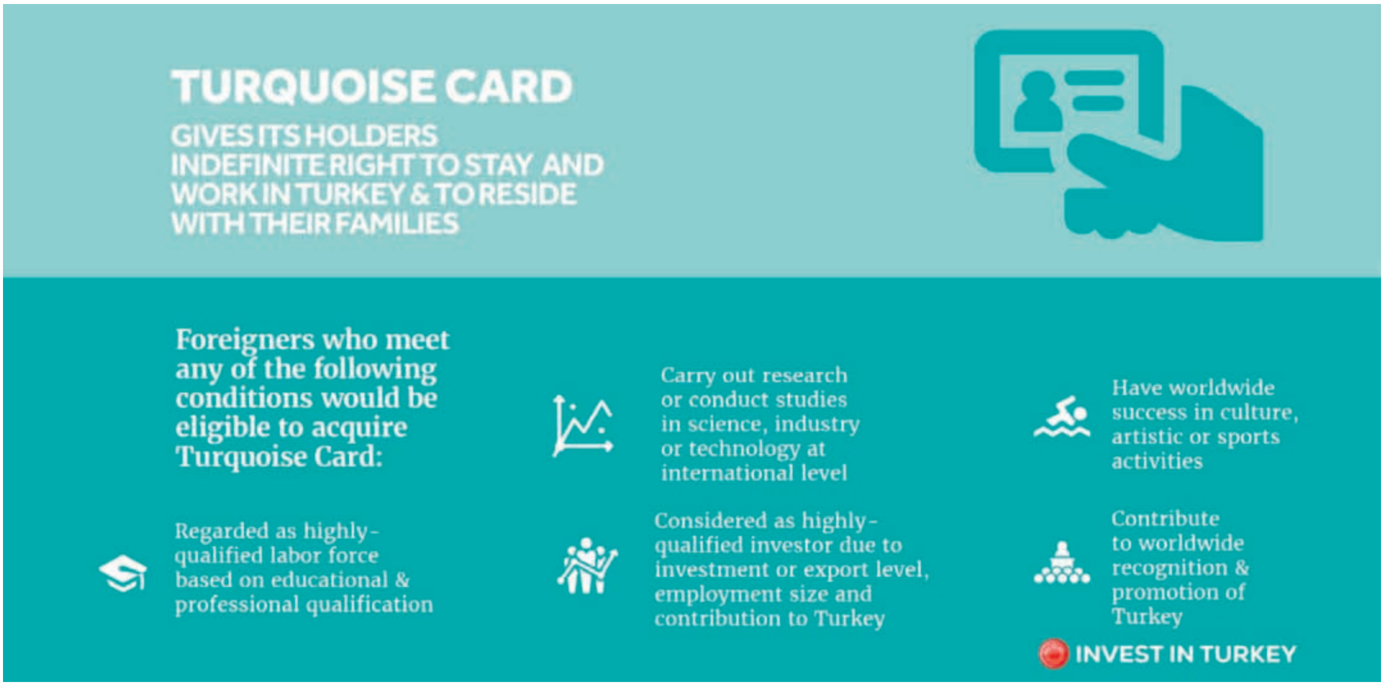
In September 2016, a project-based incentives system was introduced allowing up to 100 percent corporate tax exemption, free land allocation for 49 years, a state purchasing guarantee for manufactured products, interest waivers for loans utilized for fixed investments, and salary support for qualified employees.

Also in September, an incentive package for eastern Turkey was introduced. This package calls for TRY 140 billion incentives to be granted in 23 eastern and southeastern provinces of Turkey for investments in housing, factory, stadium, and irrigation projects. In line with this, the government will build 80 new factories each year and will lease them to investors. 1,200 initial applications worth a total of USD 5.2 billion had been made within this scheme, known as the "Attraction Centers Program".

In November, Turkey introduced a new private pension scheme. The private pension system is mandatory for all public and private company employees under the age of 45. Accordingly, the government provides 25 percent additional support and a TRY 1,000 one-time government support for participants.

In December 2016, the Economic Coordination Board announced 8 new support mechanisms for SMEs in Turkey. Support includes credit guarantee fund coverage of TRY 250 billion, TRY 50,000 loans for SMEs with three-year maturity and a grace period of one year, and the ability to postpone social security payments of SMEs.

In January 2017, Turkey eased citizenship criteria for foreigners with amendments made to the Citizenship Law. Now according to the law, foreigners who have made a minimum fixed capital investment of USD 2 million, have acquired an immovable property worth a minimum of USD 1 million, have created jobs for at least 100 people, have deposited at least USD 3 million in Turkish banks, or have bought at least USD 3 million worth of government bonds will be eligible to acquire Turkish citizenship.




Also in January 2017, the new industrial property law, including amendments in patents and trademarks, entered into force.

In February 2017, a regulation extending a 5 percent reduction to taxpayers who regularly pay income and corporate taxes passed in the Grand National Assembly of Turkey (TBMM). In the same month, new incentives for manufacturing were introduced and a regulation that introduced a VAT exemption to the first residence or workplace purchased in Turkey by foreigners or Turkish citizens living abroad was passed by TBMM.

February 2017 also saw the regulation on the Turquoise Card published in the Official Gazette and subsequently enter into force. The Turquoise Card gives its holders the indefinite right to work and stay in Turkey and to reside with their families.

In July 2017, a production reform package entered into force introducing exemption from certain taxes and fees in Organized Industrial Zones and Technology Development Zones. While having natural assets, such as a young population and a strategic geographic location, are important, without a business-friendly investment climate it would be impossible to attract international investments. Turkey has continually improved its investment climate through reforms that among other things offer protection and equal treatment to investors.

### Opportunities in a Variety of Sectors

Turkey offers abundant opportunities in a variety of sectors in which it has a competitive edge. Turkey's infrastructure investment need is a total of USD 700 billion between 2015 – 2023 and almost 30 percent of these investments are expected to be made through public-private partnership model mega projects. Grand Istanbul Tunnel, Canal Istanbul, and the Dardanelles Bridge are planned to be built in 2017.

In the energy sector, Turkey has ambitious targets to reach 34 GW of hydro, 20 GW of wind, 5 GW of solar, 1 GW of geothermal and 1 GW of biomass capacities by 2023. Within the scope of these targets, the tender for the construction of a 1GW solar power plant took place in Turkey in March 2017. Furthermore, the tender for a 1 GW wind power plant convened recently in Turkey and saw a Turkish-German consortium emerge as winners for the USD 1.5 billion project. **EDT**

*Chairman of Turkish Exporters Assembly*

*Mehmet Büyükekşi*

# EXPORTS: THE MAIN ENGINE OF GROWTH

Turkish economy grew by 5.1% in the second quarter, which was announced on September 11, after a growth of 5% in the first quarter of this year. Moreover, the first quarter data was revised to 5.2% from 5%. We have seen once again that we have made a very correct decision by declaring 2017 "Breakthrough Year" with net exports having positive contribution to growth.

With the recovery in global trade since the beginning of 2017, Turkey's exports also have accelerated with the contributions of the incentives and supports provided in the fields of export, production, investment and employment by the Turkish Government. We, as Turkish Exporters' Assembly (TIM), declared 2017 as the "Breakthrough Year in Exports" despite all the global, environmental and internal problems we faced last year. According to TİM, exports in August increased by 11.9% to 12.4 billion USD, while exports in the first eight months increased by 10.7% to 102.5 billion USD, and the exports in the last 12 month increased by 7.8% to 151.8 billion USD. Certainly, these positive developments in our exports also reflected in the growth rates.

Turkish economy grew by 5.1% in the second quarter, which was announced on September 11, after a growth of 5% in the first quarter of this year. Moreover, the first quarter data was revised to 5.2% from 5%. We have seen once again that we have made a very correct decision by declaring 2017 "Breakthrough Year" with net exports having positive contribution to growth. With the growth rate of 5.1%, Turkey is the fourth most growing economy among the countries whose data were announced in Europe. In the second quarter, Turkey's growth was higher than Germany, France, Italy and UK, as well as Euro Zone and EU averages, cementing its place among the successful economies of Europe.

Similar to the first quarter, net exports made a positive contribution to the growth in the second quarter, by 1.7 points. Thus, export growth has become the main engine of growth. In other words, the half of the growth in the first quarter and the one third in the second quarter was due to net exports.

The most powerful contribution to this high-quality growth comes from investments with 2.8 points, which is a source of happiness for Turkish economy. At this point, we can say that credit disbursements accelerated investment spending with the help of the Credit Guarantee Fund (KGF) since March.

Just as in the previous quarter, most financial institutions made upward revisions to their estimates regarding Turkey's growth. Goldman Sachs, Nomura, Morgan Stanley and J.P. Morgan have changed their growth forecasts for 2017 immediately.

We cannot deny the share of the steps taken by Turkish Government to stimulate the economy since the end of 2016. If we are to give some solid examples, our successful and continuous exporters can now receive special passports like government officials. Companies that want to open R&D and Design Centers are now receiving incentives from the Government. The state subsidies provided for exporters was increased three times, from 1 billion to 3 billion TL.

The structure of Turkish Eximbank has been changed in favor of exporters so that our companies can ease their financial difficulties. And, in order to integrate our exporters into the E-commerce system, the Ministry of Economy started an incentive program, covering a large part of the membership fees for E-commerce portals.

Briefly, the precaution, support and encouragement provided by Turkish Government has been effective in lifting our economy. We believe that by producing and exporting more, we will continue in this track, and reach higher numbers in the third quarter. Most economic indicators and the preliminary data, especially the industrial production index, support this expectation. In addition to these, exports will continue to contribute positively throughout the year.

As Turkish Exporters' Assembly, representing 67 thousand exporters who provide jobs for 3.1 million people, we would like to express our gratitude to the exporters who are the main actors behind the exports contribution to the growth with their hard work. Our year-end target is to exceed the target set by the Medium Term Program and to reach $155 billion and not to leave a single market where Turkey's products do not exist. **EDT**

*The Central Bank of the Republic of Turkey*

# TURKISH ECONOMY: FROM DUSK TO DAWN

Just a little more than a year after the coup attempt, Turkey is again one of the fastest growing emerging economies with a determined Central Bank to bring inflation back to its target and a decisive government to implement the necessary structural reforms for a sustainable future.

Turkish economy has gone through a very unique episode since 2016. Many domestic and external shocks like the coup attempt and US elections coincided in the second half of 2016, posing significant downside risks on economic activity coupled with a sharp depreciation in the domestic currency. Heightened uncertainty weakened the bank lending channel, while banks faced with rising borrowing costs due to credit rating downgrades and a sharp drop in global risk appetite. Rapidly depreciating currency also hit the economy through both exchange rate and confidence channels. Inflation edged up with the pass-through effect, exacerbated by rapidly rising food prices due to sharp base effects and supply shocks.

These concurrent adverse shocks have increased policy trade-offs, necessitating a coordinated policy response. Turkey was able to mobilize all its resources rapidly and decisively to withstand against these shocks and the economy has proven resilient against all kind of shocks thanks to its solid institutional base, well-functioning markets, strong banking sector as well as flexible and adaptive policy implementation power.

### The Key to Success: Coordination

In order to take the necessary steps to cope with multiple shocks, an unprecedented coordinated effort was initiated between the monetary, fiscal and regulatory authorities. The government assumed the role to stimulate the economy by fiscal policy through its fiscal space while the Central Bank of Turkey (CBRT) focused on its main objective of price stability by raising interest rates sharply, at the same time supporting financial market stability and FX liquidity by reserve requirements and other prudential measures.

Also, as an effort to stimulate bank lending activity in Turkey, the total amount of collateral guarantees for corporate loans provided by the Credit Guarantee Fund (CGF) was increased to 250 billion TL from 25 billion TL in the beginning of 2017. Moreover, the Financial Stability and Food Prices Committees have stepped up their efforts to overcome the structural and regulatory bottlenecks in the economy. As a result, economic activity and bank lending started to recover after the fourth quarter of 2017, external balance has improved, exchange rate has stabilized and both domestic and external confidence has recovered. Inflation rate is also expected to fall to single digits at the end of the year, after which it will maintain its downward path.

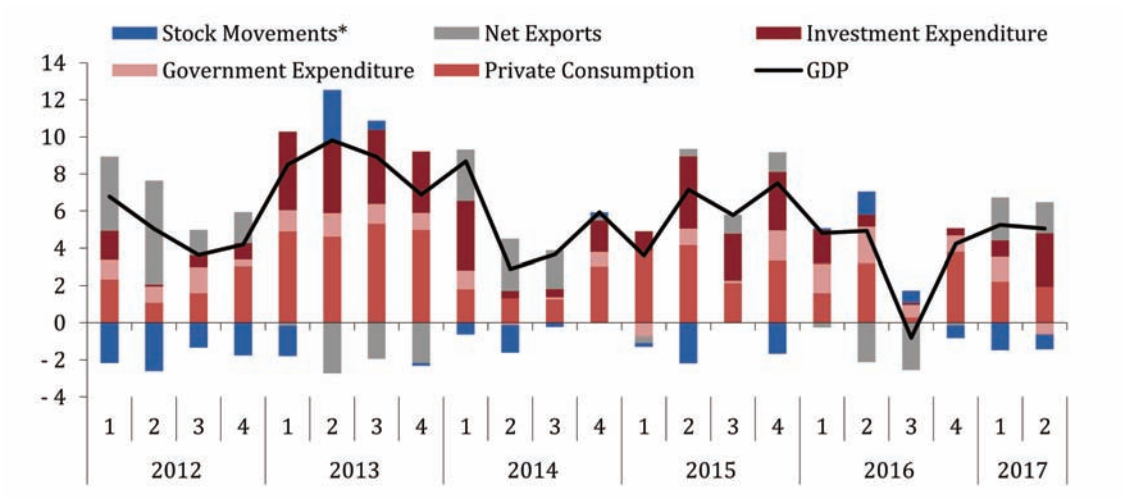

*CBRT Headquarter, Ankara.*

### Latest Developments

Second quarter growth rate was at 5.1 %, after a revised 5.2 % in the first quarter. Leading indicators suggest that strong economic activity continued in the third quarter as well and growth rate might be even higher due to a considerable base effect.

Main contributors to growth were investment and private consumption in the second quarter, as exports continued to be robust thanks mainly to strong external demand.

## Annual GDP Growth and Contributions (Percentage Points)




** Contains residual item*

**Source:** *TURKSTAT* **Last Observation:** *2017, Q2.*

Moreover, like in the first quarter, we observed a widespread recovery in activity among sectors, indicating a healthy growth performance. On the other hand, the increase in investment was mainly due to construction investment thanks to incentives, while machinery and equipment spending continued to falter. However, as capacity utilization rates in the economy increase further and thanks to increased predictability, machinery and equipment investment is expected to recover in the near future.

### Monetary Policy

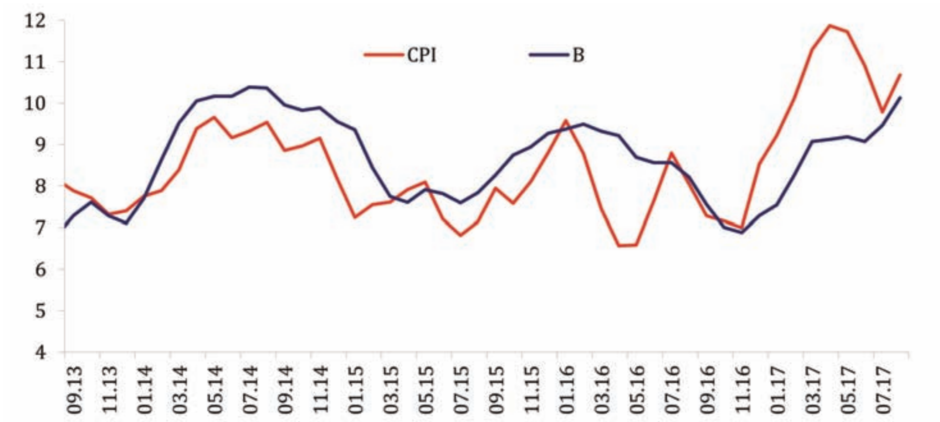
On the inflation front, headline CPI inflation has hovered at double digits throughout 2017, materializing at 10.68 % in August. Annual core inflation figures (B and C) were also elevated at 10.12 % and 10.16 % respectively.

Persistently high levels of inflation and developments in core inflation indicators pose risks on the pricing behavior, as a result of which the CBRT has maintained its tight policy stance since the beginning of the year. The monetary policy is unambiguously tight and the average cost of funding which is the main policy rate is very stable through time which has improved the predictability of the TL liquidity policy and enhanced the efficiency and predictability of the TL liquidity management.

The lagged impact of the monetary tightening will be seen in the final quarter of the year. Headline inflation is expected to come down starting from December 2017 and will follow the downward trend

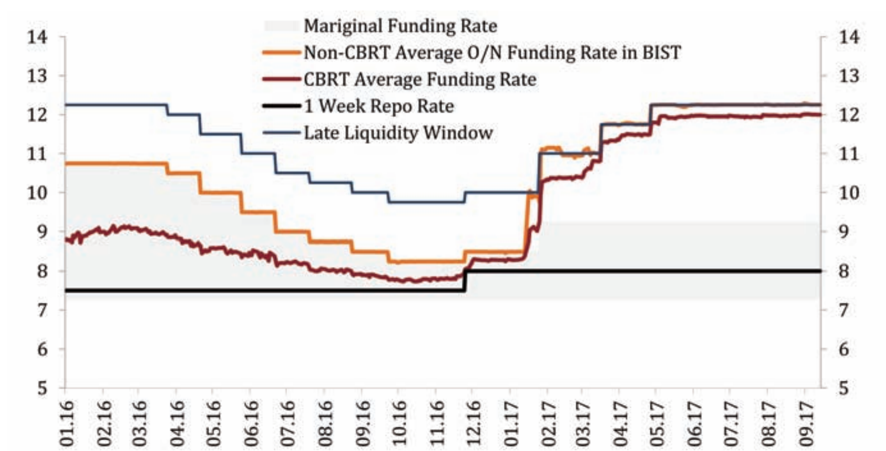
**The recent performance of the Turkish economy will be a solid base for a sustainable development phase in the coming future. The CBRT will maintain a cautious monetary policy stance and contribute to structural efforts for disinflation by identifying the source of the trade-offs, raising public awareness, and guiding relevant authorities to formulate targeted solutions.**

## CPI and Core Price Index (B)* (Annual Percentage Change)




**B index, among special indicators, which are newly released by the TURKSTAT, is the successor of the H index released before 2017.*
*B: CPI excluding unprocessed food, energy, alcoholic beverages tobacco and gold.*
**Source:** *TURKSTAT, CBRT* **Last Observation:** *August 2017.*

## CBRT Funding Rates (Percent)



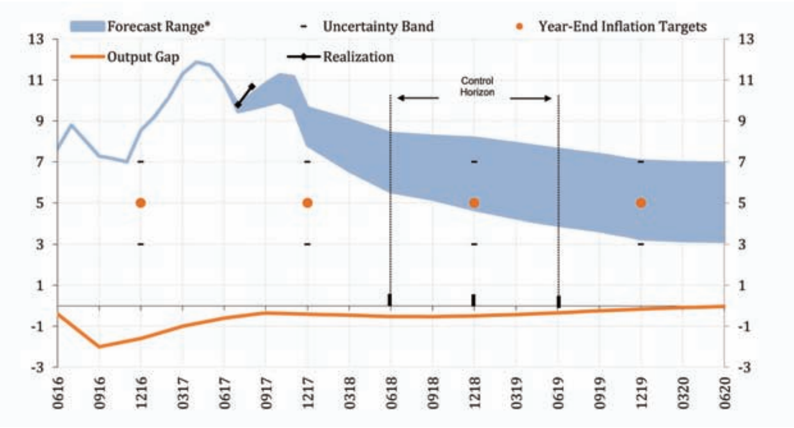

**Source:** *CBRT* **Last Observation:** *September 13, 2017* going into 2018. The monetary authority is determined to bring inflation down to the 5 % target. The tight policy stance will be maintained until there is considerable improvement in inflation dynamics, which means a bold and sustained improvement in the main trends in underlying inflation dynamics and inflation expectations.

**Financial Developments**

Loan growth recovered at a strong pace in the first half of 2017 amid macroprudential policies as well as other public measures and incentives. TL commercial loans have grown at a faster pace backed by the Credit Guarantee Fund since March. The annual growth rate of exchange rate adjusted total loans to the non-financial sector has reached 20 %. Having trended upward since the third quarter of 2016, the growth rate of total loans hovered above past years' averages on the back of commercial loans. Credit market is expected to converge to its natural rate of growth as the effect of temporary stimulus fades away after the third quarter.

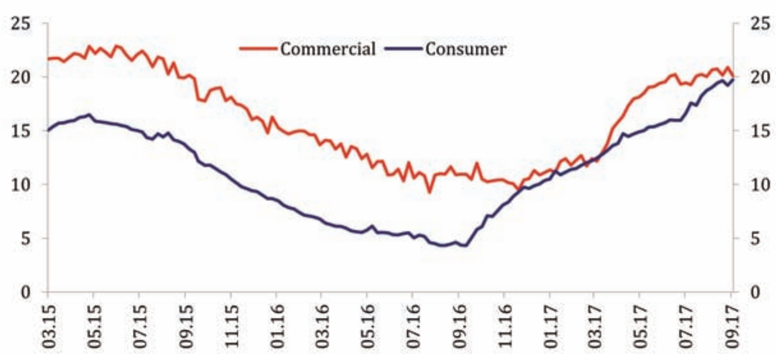
The balance sheets and capital adequacy ratios of the Turkish banking sector are still strong.

## July 2017 Inflation Report Forecasts



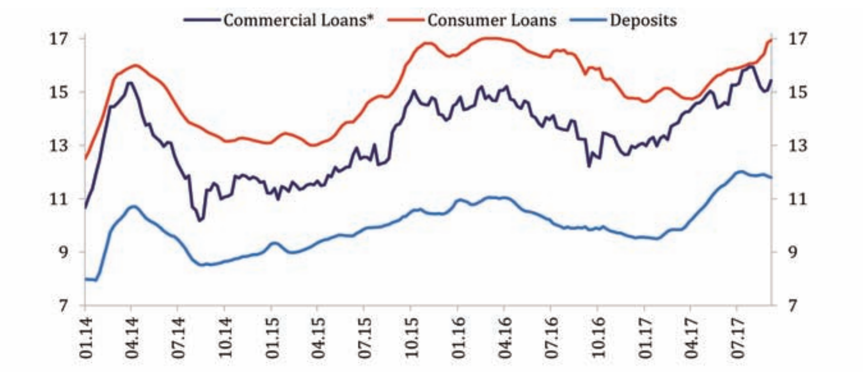

*Shaded region indicates the 70 percent confidence interval for the forecast.
**Source:** *July 2017 Inflation Report*

## Loan Growth Rates (Annual Percentage Change, Adjusted for Exchange Rate Effects)




**Source:** *CBRT* **Last Observation:** *September 8, 2017*

**TL Loan and Deposit Rates (Percent, 4 Week Moving Average)**




** Overdraft accounts and commercial credit card rates are excluded.*
**Source:** *CBRT* **Last Observation:** *September 8, 2017*

Overall non-performing loan ratio is at around 3% and we do not expect a major increase stemming from CGF loans thanks both to the design of the programme and to the health of the economy. Moreover, the CGF has contributed to the profitability of the sector, and capital adequacy ratios continue to increase. On the other hand, loan and deposit rates have responded to tightening, but we might see some retreat in the upcoming period with the expected slowdown in loan growth in the coming period.

### Fiscal Policy

Fiscal policy has been another important pillar in supporting economic growth through a number of new measures and incentives as well as public investment and spending, which are intended to generate funding for the real sector and to boost investment, employment and exports. As a result, the budget deficit widened in the first half of the year due to these measures as well as temporary allowances such as the postponement of the premium payments in the first quarter to the fourth quarter of 2017. However, with tax revenues poised for growth amid continued economic recovery and lifting of the temporary measures, budget balances are expected to improve. Going into 2018, maintaining fiscal discipline will be one of the main concerns of the government.


As a final word, today, just a little more than a year after the coup attempt, Turkey is again one of the fastest growing emerging economies with a determined Central Bank to bring inflation back to its target and a decisive government to implement the necessary structural reforms for a sustainable future. The recent performance of the Turkish economy will be a solid base for a sustainable development phase in the coming future. The CBRT will maintain a cautious monetary policy stance and contribute to structural efforts for disinflation by identifying the source of the trade-offs, raising public awareness, and guiding relevant authorities to formulate targeted solutions. We believe that this process will pave the way for a more sustainable disinflation process. **EDT**

INTERVIEW

*An interview with the General Manager of KGF*

*İsmet Gergerli*

# KGF IS A SIGNIFICANT STRUCTURAL REFORM

Credit Guarantee Fund PJSC (KGF) was established in 1991 as a non-profit joint-stock company according to its articles of association which does not distribute profit to its shareholders. With the institutionalization and growth of the Credit Guarantee Fund System, particularly SMEs, it is aimed to continue the strategic support for the growth and development of Turkey by facilitating access to financing for all enterprises.

**Are you working on new products? Could you give us an example?**

We have been working on it for a year. We have been working on developing an interest free system with the Islamic Development Bank its relative funds and also with other participation banks. We are in dialogue with the European Investment Fund and EBRD and hopefully we shall realize good results in the near future. With the help of foreign funds we are working on presenting new products to SMEs, especially to manufacturing and exporting companies.

**Expectations for KGF to support investment, employment and exports have started to increase. Were things different from today?**

Manufacturers, exporters, manufacturing industries, either service sector make use of this system in the already existing structure. When we analyze our existing guarantee system, about 30 percent are used by the manufacturing industry. When we look at the Turkish banking system, it seems that we have a guarantee system in line with the investment loans or manufacturing industry loans. For example, we issued around 4 billion 696 million TL guarantees for tourism sector, 20 billion 730 million guarantees for exporters.

**There is a public opinion that only working capital loans issued and they are not used for investment...**

Unfortunately, such a perception is created. We as KGF declared that working capital loans from 93%, investment loans from 3% of the total loans issued. However, this situation originates from technical definition particularly.

When we look at the implementation, we can see different results. While, the maturity within the definition of working capital loan is one year without any grace period in Turkish banking system, the loans that we issued as working capital loans have 5 years maturity and 1 year grace period.

In other words, a significant portion of the capital working loans that we issued function as investment loans.

*İsmet Gergerli, General Manager of KGF*

I have been in banking sector for almost 25 years. Talking as a person who is familiar with sector, one of the biggest gains that KGF provided is that Turkish banks extend loans to the companies with a maturity of 5 years and 1 year grace period. Thanks to ease and peace provided, many companies became able to look forward and accordingly make their plans. Therefore, economic growth started. Moreover, so long maturity is not common in investment loans directly extended by banks.

A report recently prepared by an analyst had an influence on me. In the report there is an expression that Turkish firms started to sell their manufactured goods more profitably. I interpret this statement as companies start to sell their products at a fair price due to the diminishing pressure on financing thus companies relieved now.

The economy management also wants the Turkish exporters to sell the goods more profitably providing the money that the producer deserves. KGF has also provided this.

**What is the situation in other countries? South Korea, e.g. We know that the KGF system has a role in increasing production.**

We have paid a visit to Korea Credit Guarantee Corporation (KODIT) with a technical team upon the invitation of KODIT, for 2 days.

KODIT is a 41 years old company that is entirely public. It has made crucial contributions to the industrialization and growth of the country. So if we are talking about South Korea miracle today, we can declare that KODIT has a big impact in it.

**How does the system operate?**

KODIT supports SMEs, but there are some differences in SME definition according to us. They have a different SME definition depending on each sector. For instance, total sales of companies operating in manufacturing industry should not exceed 136 million USD; total sales of technology companies should not exceed 55 million USD.

Only 3,000 companies in the country were excluded from the definition of SMEs. Nevertheless, when required, KODIT have undertaken a special task in loan access of companies such as Hyundai, LG, Samsung. KODIT works with 17 banks and has 2,300 staff, 109 branches and 9 regional coordination offices. KODIT is a very reputable supreme institution positioned on top of banks. In other words, the banks extend loans to companies, without any further need of examination which are approved by KODIT.

A country having a GDP per capita of more than 35 thousand USD and having exports of more than 500 billion USD and enjoying a current account

## The total guarantee volume has reached 214 billion TL

# WHO IS KGF? WHAT DOES KGF DO?

The Share Capital of KGF is in the value of 318.2 Million Turkish liras and with the General Assembly held on May 4, 2017, The Share Capital ceiling has been increased to 500 Million Turkish liras. Current shareholding structure; TOBB 29.1%, KOSGEB 29.1%, and 27 Banks 41.7%. 27 Banks / Participation Banks in the shareholding structure are private and public banks, and constitute 98% of the market size of the sector.

Since the beginning of 2016, the process of restructuring KGF has been initiated and its functioning and infrastructure has been shaped from scratch. The staff is professionalized and technological infrastructure has been renewed. Guarantee allocation system is structured in a way that works integrated with banks as in other world examples.

In addition, all business processes are defined in a synchronized manner by reconsidering and connected to the rules by the Regulations and Application Instructions; a transparent, accountable, auditable structure has been established.

Thus, in 2016, the KGF became an institution in compliance with International standards. The amount of guarantee given from our equity is maximum 3 million TL and our guarantee rate is 80%. For Treasury supported guarantees, maximum guarantee amount for an SME is 12 million TL while the guarantee rate is 90 %, for large scaled enterprises maximum guarantee amount for a company is 200 million TL while the guarantee rate is 85%. However, for exporters or businesses with foreign exchange earning activities, Treasury Supported Guarantee rate can be up to 100 %.

Treasury backed guarantee system commenced in 2009 and running up until 2015 a total of 1.8 billion TL was granted to 5,652 enterprises. With the cabinet decision dated 31.10.2016 to change the previous system and institutionalize the KGF, the total amount of guarantees granted to 19,483 enterprises reached roughly 5 billion TL at first stage, followed by the total amount granted increasing to 20 billion TL as of February 2017, meaning the total guarantee line supplied by the Treasury being fully utilized.

The guarantee volume being increased to 250 billion TL from 20 billion TL was recognized with the cabinet decision released on 10.03.2017 and accordingly with the protocol signed with the Treasury on 08.09.2017 the total guarantee volume has reached 214 billion TL with 330.771 enterprises being involved.

With the Treasury guarantee system's internal dynamics (7% cap on compensation) an autocontrol mechanism is in place causing banks to manage their portfolios accordingly with the willingness and trust gained in due course. This is a great accomplishment to be able to sustain the current system.

surplus of 100 billion USD each year contains a similar credit guarantee scheme for decades successfully. Moreover, KODIT plans to increase their presence even further.

**Is there a second credit guarantee institution in Korea?**

A subsidiary structure called KOTEC has been established to support only technology companies. The main income source of KODIT is commission. KODIT as a nonprofit organization gets commission ranging from 0.5% to 3% annually depending on companies rating. In addition, the banks pay a commission of 0.3% out of their total commercial loans each month. Last year KODIT earned 776 million USD from banks and the State also transferred 181 million USD from the budget.

When a company in South Korea applies to KODIT, the evaluation process takes 40 days. They became curious when we told that KGF evaluates 4,000 applications within one day.

While we have stated that we set up the technological infrastructure well, they asked that "Although, we are a technology advanced country, we are surprised at how did you manage it with such a few staff?"

As they were working with 2,300 people, we reached their double size with only 192 people.

**Can the KODIT model be adapted to TURKEY?**

KGF is not a business cycle but a tool that is used permanently. KGF is not a hammer, it's a rehabilitation center. A support mechanism is meaningful if it continues as a permanent structure. KGF can be a very important engine for economic growth in line with Turkey's 2023 vision. As a matter of fact, the work we have done since March is an example that allows us to say this. In this period, we issued around 192 billion 136 million guarantees for 330 thousand enterprises.

Today we have made a significant contribution to growth of economy, increase in employment and exports. In fact, International Credit Rating Agencies have revised their growth estimates for 2017 from 2.7 percent to 4.8 percent by referring to the KGF.

**So, do you consider KGF as a reform?**

Yes, I think KGF is a significant structural reform. The Banks experience a setback regarding risk management in that period due to capital adequacy ratio.

KGF is an initiative in terms of capital adequacy ratio. We achieved this with the support of the Government and Turkish Banking Regulation and Supervision Agency.

The KGF is a development for capital adequacy ratio. We eventually plan to become capable of stating credit ratings of individual companies to the banks. Actually, that is what KODIT accomplished. At the next stage, we plan to become able to reveal companies which are creditworthy to banks.

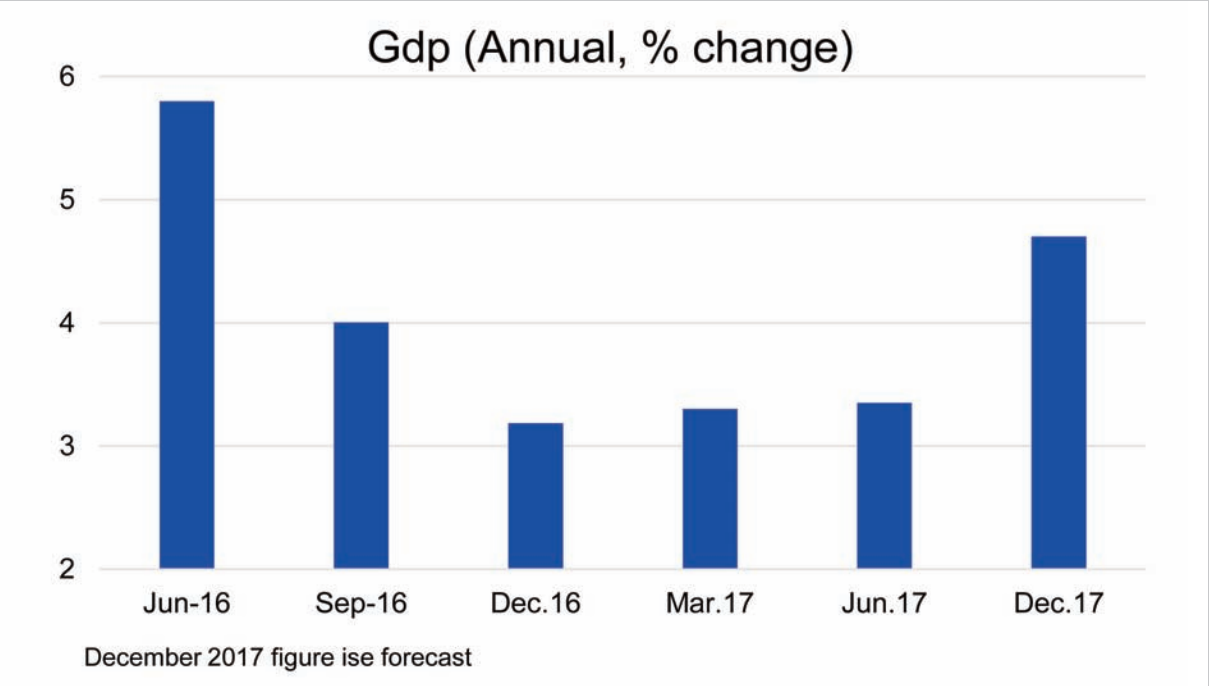
KGF is actually a tool that supports fiscal policies of economy administration and even it removes outdated collateral system. This is a contemporary financing technique that evaluates project risk to extend loans depending on project risk. **EDT**


*Grand Bazaar, İstanbul.*

*Chairman of the Board,*
*The Banks Association of Turkey*
*Hüseyin Aydın*

# Banking sector in Turkey

With the decision of the EU Commission dated 21 December 2016, Turkey has been declared as an 'equivalent country'. Through this decision, it has been confirmed that the banking sector in Turkey has equivalent regulation and practice with the EU.




## Turkish economy is expected to grow at about 5 percent in 2017.

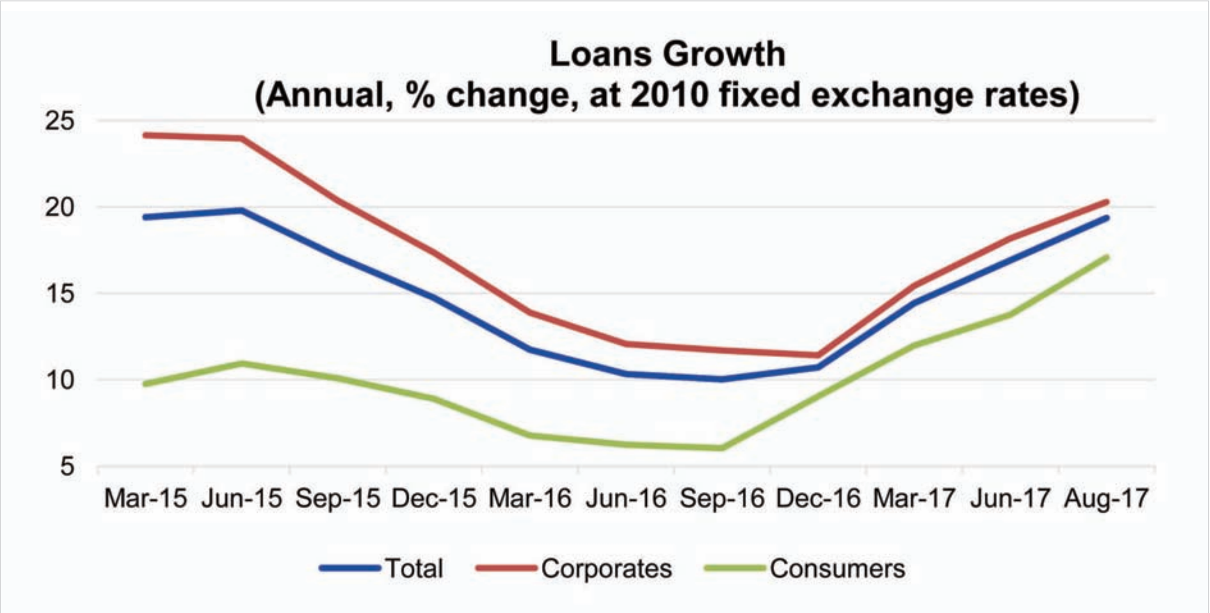
Turkish economy succeeded in dealing with the negative effects of 15 July treacherous coup attempt quickly in a short term period and began to recover strongly again from the last quarter of 2016. Thanks to the effective measures by the Government in both fiscal and banking sector policies to support growth.

Budget deficit to gdp ratio is about 2 percent with higher expenditures and had a slight impact on Government debt to gdp, rising to 32 percent in June 2017 up 0.4 percentage point from the end of 2016. Fiscal stimulus to combat unemployment has yielded intended results and unemployment rate has fallen to 10.4 percent as of May from 13 percent recorded in January. Current account deficit to gdp remains around 4 percent in the first half of 2017. Volatile gold imports hindered external balance from improving. Barring gold trade core goods and trade balance follows an improving trajectory. It has been observed that economy is in a trend not to heavily rely on current account deficit widening. Net capital inflows amounted to 29 billions, mainly in the form of portfolio flows, and direct investments. The Central Bank's international reserves increased by 2 billions to 108 billions.

Inflation is about 10 percent, rather above the target and expected to slow down below 9 percent at the end of this year. TL's value remained rather stable against major currencies encouraging investors demand for TL.

## The banking sector supported the growth.

Loans growth, gaining momentum in the last quarter of 2016 accelerated further in the first half of this year, thanks to vitality in the economic activities and Treasury's increased guarantees on loans extended by the Credit Guarantee Fund. Meanwhile, rather heavy legal prudential measures imposed by the authorities in 2014-2015 harmonized with the international standards during the last quarter of 2016 and the first half of 2017 and allowed banks to take additional risks.




Annual growth rate of loans at fixed exchange rate reached 19 percent in July, from 10 percent a year ago. Both commercial and consumer loan increased faster than last year.

Commercial loans accounted for 77 percent of total loans while loans to consumers took 23 percent of the total. SME's share in total loans was 24 percent.

Hüseyin Aydın, Chairman of the Board, the Banks Association of Turkey

**Selected Indicators (June 2017)**

| | USD billions | as % of Gdp |
|---|---|---|
| Liquid assets | 125 | 16 |
| Securities portfolio | 105 | 13 |
| Loans | 550 | 69 |
| Deposits | 449 | 56 |
| Non-deposit Funds | 230 | 29 |
| Shareholder's equity | 94 | 12 |
| Total assets | 845 | 106 |

Source: BRSA, CBRT

## High asset quality and capital adequacy contributed soundness

Financial soundness indicators have been rather strong; capital adequacy amounted to around 17 percent and remained above the regulatory level of 12 percent.

Non-performing loans before special provisions to loans ratio declined slightly to 3 percent. The ratio was around 2.9 percent in corporate loans and 4 percent in consumer loans. Provisions set aside for 77 percent of non-performing loans. It's been quite a good coverage ratio. Return on annual average shareholders' equity continued to increase to 14.3 percent in the first half of the year.

## EU Commission: "Turkey is an equivalent country"

With the decision of the EU Commission dated 21 December 2016, Turkey has been declared as an 'equivalent country'. Through this decision, it has been confirmed that the banking sector in Turkey has equivalent regulation and practice with the EU. The decision of the EU Commission means that the supervision and regulation framework of the banking sector in Turkey and its related activities are equivalent to EU regulations and practices.

## Turkish Banking sector grew faster than European Union

Turkish banking sector remained rather strong and continued to grow during the global crisis. There for many of the selected indicators moved up towards the EU average, albeit the gap remained high. **EDT**

**EU and Turkey, Comparison of Selected Indicators (as % of Gdp)**

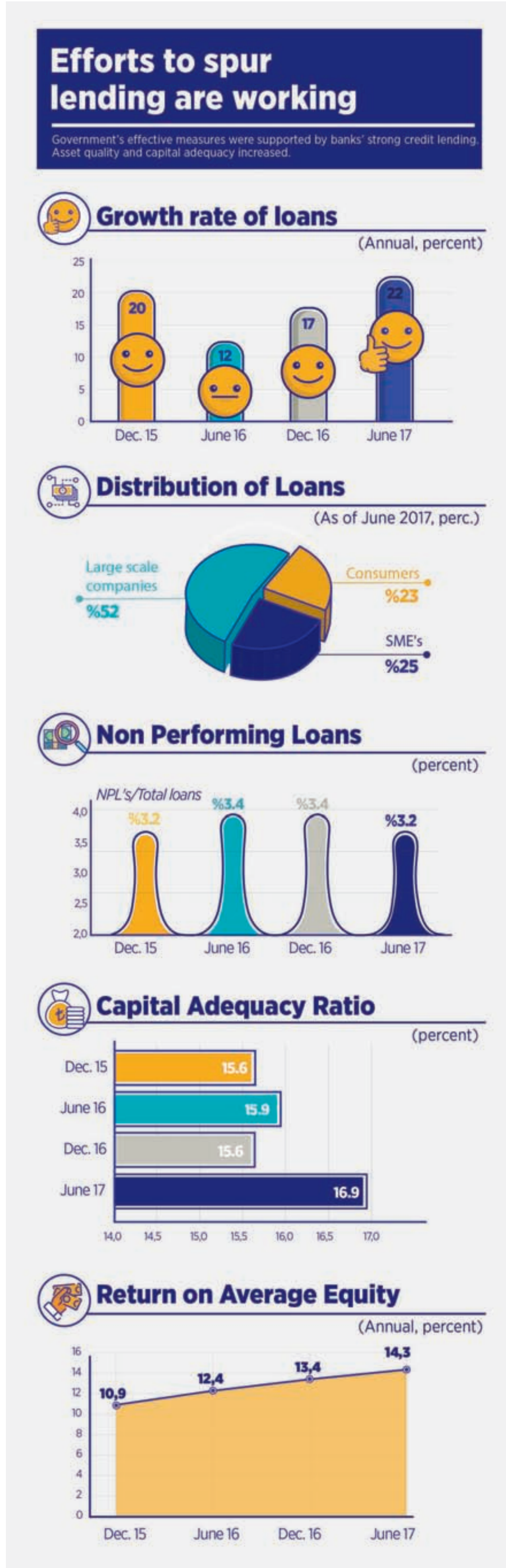
| | EU | | TR | |
|---|---|---|---|---|
| | 2008 | 2016 | 2008 | 2016 |
| **Assets** | 332 | 291 | 74 | 105 |
| **Loans** | 178 | 159 | 37 | 67 |
| **Deposits** | 162 | 149 | 46 | 56 |

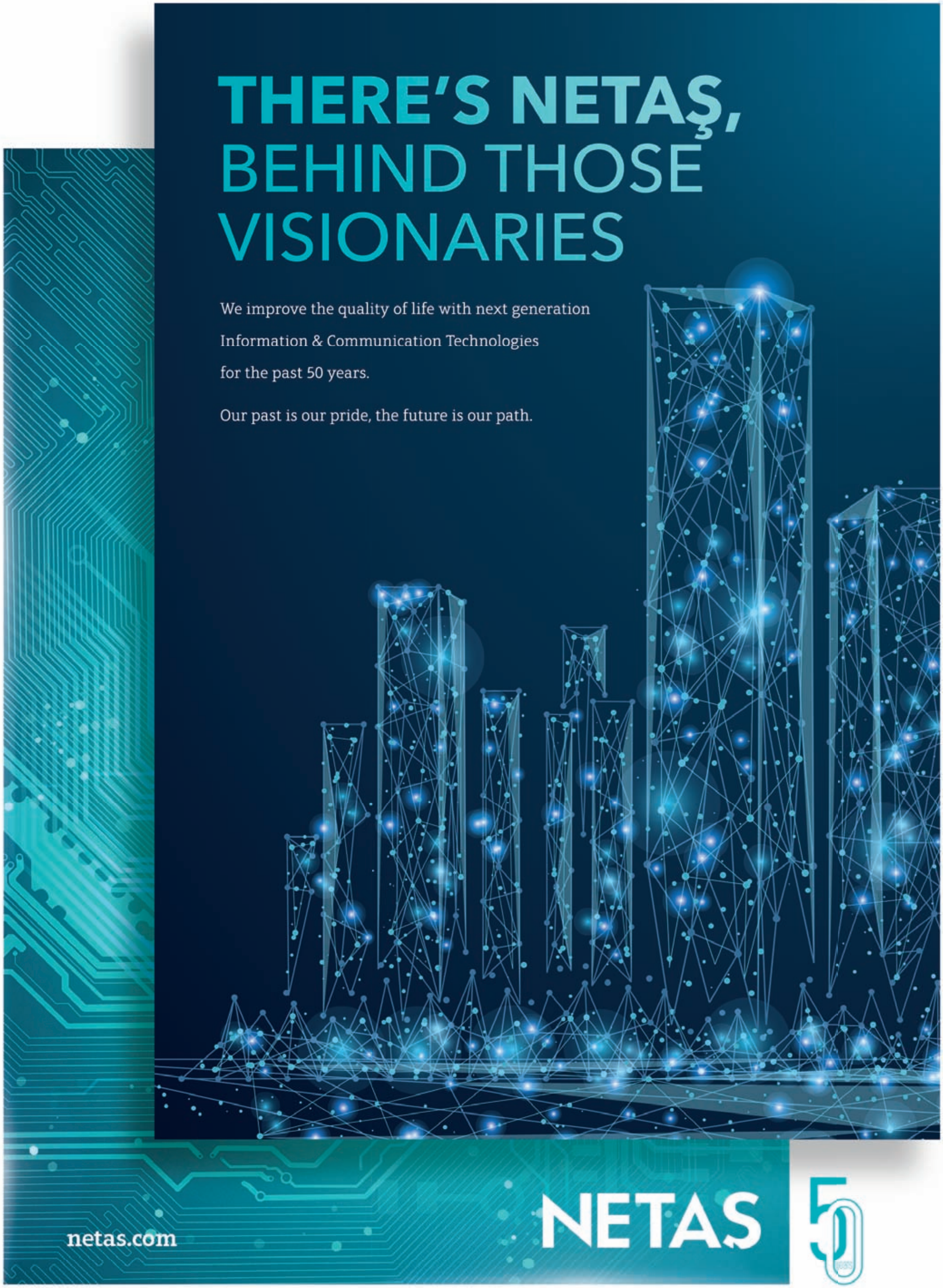
Source: ECB, Turkstat

### General information on the Banking System in Turkey

As of June 2017, number of operating banks was 51, of which 33 were deposit banks, 13 were development and investment banks and 5 were participation banks.

***For further information:***
*The Banks Association of Turkey, www.tbb.org.tr Information for Participation banks: The Participation Banks Association of Turkey (www.tkbb.org.tr).*

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BANKING

*Chairman, Participation Banks Association of Turkey*

*Melikşah Utku*

# The Participation Banking Ecosystem is Developing

It is inevitable that participation banking will have its own ecosystem which has different characteristics to conventional banking. This is led by the interest free banking standards. These standards are related to the regulation and supervision of banking operations, with its principles deemed compliant with the religion of Islam.

Participation banking is a banking model that has its own characteristics built on the principles of interest free banking. Starting with the ban on interest, it has basic features such as being based on the real economy and economic activity, it counters uncertainty, excessive risk and speculation, it adopts the principle of sharing the risk, and it refrains from offering banking services to business which would harm the good of the society. All of these things place participation banking in a sound and ethical banking position.

*Melikşah Utku, Chairman of Participation Banks Association of Turkey.*

Because such features constitute a robust banking model both in terms of assets and liabilities. The 2008 global crisis was a result of banking and financial transactions breaking away from the real economy, creating a huge bubble, bad risk management and default of 70% of variable rate housing loans, which would not be accepted by participation banking as they are also a form of uncertainty. If there had been a financial system with real economic loyalty, where a fixed-income credit system had been adopted which would have prevented the sale of receivables, the crisis would not have reached such a level and may have been overcome with less damage.

It is inevitable that participation banking has its own ecosystem with different characteristics to conventional banking. This is led by the interest free banking standards. These standards are related to the regulation and supervision of banking operations, provided its principles are deemed to be compatible with the religion of Islam.

These are a) the Gulf region (Bahrain) based AAOIFI (The Accounting and Auditing Organization for Islamic Financial Institutions) and b) Far East (Malaysia) based IFSB (The Islamic Financial Services Board).

Banks operating in Turkey have their own independent advisory boards which have the freedom to comment and notify their opinions according to the principles of Gulf and Far East standards. They benefit from these standards; however, the consultation committee within our association has also started to form Turkish standards. Meanwhile, the Participation Banks Association of Turkey (PBAT) has also started the translation of AAOIFI's Interest free Finance

**Department of Enforcement III within the Banking Regulation and Supervisory Authority (BRSA) responds to a critical need for interest free finance, and participation banking in particular. Recommended action steps are included in the Turkey Participation Banking Strategy Certificate in order to encourage other related public institutions to create similar units.**

Standards into Turkish, which are followed more closely in our country. Moreover, significant progress was also achieved towards the translation of Accounting, Supervision and Corporate Governance Standards.

Participation banking, which needs support from various public institutions due to its stated characteristics, has now found this support, even if it is a little late. For instance, the Department of Enforcement III within the Banking Regulation and Supervisory Authority (BRSA) responds to a critical need for interest free finance, and participation banking in particular. Recommended steps for action are included in the Turkey Participation Banking Strategy to encourage other related public institutions to create similar units. The General Directorate of Public Finance of Undersecretariat of the Treasury has exclusively issued 63% of the total Sukuk issuances, achieving significant success in Sukuk issuances, and also going a long way to bringing a solution to the liquidity problems faced by the sector. Another source of support has come at the level of deputy prime minister and from the ministries. A top level

**Undoubtedly, one of the major pillars of this ecosystem is the Priority Transformation Program held by Ministry of Development. With this program, the participation banking and interestfree finance development project was added as the 7th component to the Istanbul Finance Center Project, which is included in the 10th Development Plan.**

committee entitled "Interest free Finance Coordination Board" was established with the participation of the BRSA, the Treasury, the CMB, the PBAT, the CBRT, the BIST, the Ministry of Finance, the Ministry of Development and Participation Insurance at the level of president, undersecretary and general manager, headed by the deputy prime minister responsible for the Treasury. This committee has been tasked with developing participation banking and interest free financing and accelerating its development. The Board has held three meetings and these meetings have been directed towards taking direct actions as the Top Executive Committee. Undoubtedly, one of the major functions of this ecosystem is the Ministry of Development Priority Transformation Program. With this program, a participation banking and interest free finance development project was added as the 7th component to the Istanbul Finance Center Project, which is included in the Tenth Development Plan.

Apart from this public support, participation banking and the PBAT entered cooperation with important national and international institutions in 2016 and 2017. In March 2017, the "Innovative Products in Islamic Finance" Workshop was held in Istanbul with the cooperation of the BRSA, the PBAT and the Global Islamic Finance Development Center of the World Bank. National and international bankers and specialists offered presentations at the workshop, which proved useful for those attending. Meanwhile, the "Istanbul Talks" Workshop, where Islamic Finance was discussed, was again held at the British Consulate in March 2017. In 2016, PBAT participated in the World Halal Summit as a sponsor. Having participated in the World Gold Council and the Workshop on the Translation of Gold Standards into Turkish, the PBAT undertook an active and decisive task in this regard. In September 2016, the International Islamic Economy and Finance Conference was organized together with Sakarya University and İstanbul Sabahattin Zaim University.

We express our belief that together with our employees, customers and shareholders in the framework of the drawn ecosystem, we will achieve better results with our common beliefs and efforts and that we will be the regional leader of our sector, and I would like to express my sincere thanks to everyone who contributed to participation banking. **EDT**

*CEO, DenizBank Financial Services Group*

*Hakan Ateş*

# Turkey: Not Only Resilient in Crises But Also Agile in Policymaking

While structural strength is essential, also very crucial is the agility of the policymakers in providing the environment the structural forces can work effectively. Accordingly, when the failed coup skyrocketed uncertainty, the authorities quickly devised a system to relieve the ensuing bottleneck the economy, being well aware of the fact that such temporary liquidity strains must not prevent the real sector from honoring their obligations.

No country in the world has probably gone through as frequent and unfortunate economic and political events as Turkey did in her recent past. Following the economy's most destructive economic and financial crisis in 2001, uncertainty frequently hit the political scene. The military memoranda in 1997 and 2007, the two closing cases against the ruling party in 2002 and 2008, the Gezi Park protests and illegal probe against the Cabinet in 2013 were some of those events causing substantial volatility. Following them, the local, presidential, general elections and the presidential referendum from 2014 to 2016 only exacerbated the uncertainty. And the failed coup attempt in July 2016 took it to another level. Terrorism was around as another source of uncertainty. Terrorist strikes at the Railway Station and Kızılay Square in Ankara, the attack in Gaziantep, and several others in Istanbul such as those at the Atatürk Airport, the stadium at Dolmabahçe and the Reina club in Ortaköy (on the new year's eve) yielded hundreds of human casualties within the last three years causing a lot of grief all around the country. The bloody war in Syria was added to all these shoveling close to 4 million refugees to Turkey in the past 6 years. Though largely a result of a humanitarian response, the influx added to the fiscal burden and raised social integration issues and challenges ranging from terrorism to the education of the newborns in Turkey and the rise of unrecorded economy making it tougher to fight against the high unemployment in Turkey. The global economy was not without problems during this period, either. From the US mortgage crisis to the Greek debt problem and from the Bernanke Tapering to the Brexit, global economic uncertainty was high enough to add to Turkey's problems.

To the bewilderment of many, however, the economy remained resilient and the rising volatility did not turn to a full blown crisis during any of these turbulent periods. That was because after the devastating crisis in 2001 the economy had already achieved radical structural reforms and greatly improved its economic fundamentals. Fiscal discipline with a high primary surplus every year, a floating exchange rate system instead of fixed, an operationally independent central bank targeting inflation and several legal and institutional reforms had allowed a remarkable transition to a private sector driven economy from a state driven, investing $184 bn a year between 2002 and 2016 into the economy and growing it at 5.8% on average. An enviable performance, indeed, even among the fast growing emerging economies.

While structural strength is essential, also very crucial is the agility of the policymakers in providing the environment the structural forces can work effectively. Accordingly, when the failed coup skyrocketed uncertainty, the authorities quickly devised a system to relieve the ensuing bottleneck the economy, being well aware of the fact that such temporary liquidity strains must not prevent the real sector from honoring their obligations, e.g. paying debt back (to banks), their taxes (to governments) and wages/salaries (to the employees/households). And thanks to years of fiscal prudence (3% of GDP a year on average since 2003) and low public debt as a consequence (only at 9% of GDP in net terms), they had the structural strength to do so. As foreseen correctly, the economy contracted by 0.8% in the third quarter of 2016.

### A Timely, Innovative and Well Crafted Support for SMEs!..

The SMEs are of crucial importance to the Turkish economy, making up 99% of all business ventures, 78% of all employment and 36% of all business investment. But they get only 25% of bank loans and find it hard to reach financing during liquidity bottlenecks. Noting this once again during

*Hakan Ateş, CEO, DenizBank Financial Services Group.*

the last turmoil, which forced banks to become overcautious, the State's Credit Guarantee Fund (CGF) began to provide guarantees to banks in Turkey in lending those SMEs with annual sales less than TL40 mn and fewer than 250 employees using mostly Treasury resources with leverage (capped currently at TL250 bn or around 9% GDP). By using the guarantee banks comfortably deployed their liquidity to restructure or provide new loans for as long as five years duration (to be extended 3 more years) to the SME sector which would otherwise be locked out of the system simply because of greater uncertainty. The Treasury also compensates banks up to 7% of their non-performing CGF related loans.

Both the banks and the Treasury still remained comfortably above the internationally accepted risk criteria while providing this support. With its zero risk weight, the CGF based lending in fact improved banks' capital adequacy by around 150

> **Foreseeing its importance for the economy DenizBank took the lead role by partnering with the CGF as the only private bank in its pet project called "The Breath", a specially designed low cost fast track credit program for small caps.**

bps, which is currently 17% comfortably above the Basel III standard (including the capital buffer) and the 12% local regulation. Funding was also available as the banks were able to borrow around a net $8 bn (through mostly Eurobond issuance) from abroad and a further $10 bn of net capital flows (bond and equity) entered the markets since the beginning of the year. As for the Treasury, the budget deficit, including all subsidies, will likely remain below a well acceptable 2.5% of GDP by the year-end while still yielding primary surplus as of August. Also, the CGF related loans have performed remarkably well so far with only 1.7% of these loans non-performing and thus limiting the burden to the Treasury significantly.

The results were tremendous. The Fund quickly reached almost 500 thousand SMEs, or 50% of those using bank finance, within six months. Banks' NPLs remained low at 3.1% (bounced checks fell from 3.8% to 1.8% of the total since the beginning of the year), the government bolstered tax income (having risen by 15% in the first 7 months of the year), investment spending rose by 9.5% in real terms in the second quarter of 2017 and unemployment remained stable (at 10% as of May 17).

Overall, the economy accelerated its pace of growth to 5.1% in the second quarter and the CGF is estimated to raise GDP growth by 150 bps in 2017 keeping it above 5%. As DenizBank, we fully supported this timely and well crafted system for a segment that is the backbone our economy. In fact, foreseeing its importance for the economy we even took the lead role by partnering with the CGF as the only private bank in its pet project called "The Breath", a specially designed low cost fast track credit program for small caps, through which we have lent more than TL1 bn or 45% of the total lending.

As seen during many turbulent periods the Turkish economy has the structural shields to sail through strong winds. Agility and crisis know-how are equally important. The CGF support has been a clear example. **EDT**


*DenizBank Headquarter, İstanbul*

BANKING

*Şekerbank Chairman of the Board of Directors*

*Dr. Hasan Basri Göktan*

# Inclusive financing for sustainable growth

While the growth rates on a global scale have just recently been revised to an upward trend, Turkey, despite many unexpected events that took place in 2016 both locally and globally, has continued its economic resilience and presented a strong economic growth performance. The resilience and performance shown by the Turkish economy with the appropriate and cautious steps taken by the Government authorities after the July 15th coup attempt and other unexpected developments in its aftermath, that could have turned the markets upside down in any other country for a remarkable period of time, constitutes the greatest basis for our positive outlook for the future. This solid base that we have built with the steps taken to reinforce the economy in the last ten years will become even stronger with the decisive implementation of structural reforms and the emphasis that the banking sector is placing on inclusive financing.

**The path to achieving healthy and sustainable growth across the world economy is through being inclusive**

Ten years have gone by since the most severe crisis since the 1929 great depression to shake the world financial markets. Even though the inability to grow experienced after the 2008 crisis has been replaced with a relative optimism these days, the world still has not approached the pre-2008 growth rates. Despite the unconventional moves from central banks and the record breaking balance sheet sizes, speaking optimistically the global economy is expected to reach a growth of only 3.5 percent in 2017. If one remembers that the world economy had grown 5.7 percent in 2007 when the first signs of the crisis began appearing in the US, then we can clearly see the major change that happened in the world economy following the financial crisis.

Even though they remain drastically lower than the rates before the global crisis, the current predictions for global growth are being revised upwards. In this sense, a simultaneous recovery in the growth rate of developed and developing countries is being observed. The use of "Strong Recovery" as the title in the World Economic Outlook report updated by the IMF in July also shows that growth expectations are rising significantly.

However, what is important is to change the structure of the comparatively accelerated but noninclusive economic growth, which can lead to socio-political crises. The total of 34 million people, i.e 0.7 percent of the world's population, own 45.2 percent of the entire world's assets with their 113 trillion dollar presence. While people in the lowest income bracket comprise 71 percent of the world population, these same people have only a 3 percent share in the total assets with 7.4 trillion dollars. Therefore, the world economy can only achieve a healthier basis with structural reforms implemented by each country to decrease the income inequality and ensure an inclusive growth that will reflect positively on the wide masses.

*Dr. Hasan Basri Göktan, Şekerbank Chairman of the Board of Directors*

The recovery in the world economy in terms of growth supports the general predictions that central banks of developed countries will gradually decrease their support to the economy. However, the inflation rates remaining at low levels, is causing the global risk appetite to continue strongly as of the second quarter. The tapering effort of the major central banks to take the necessary steps by normalizing monetary policy over the medium term, especially the Federal Reserve (FED), also raises questions about the sustainability of developing countries' growth performance. It should be underlined that developing countries implementing strong structural reforms in these conditions will stand out among their peers.

**The power to recover quickly**

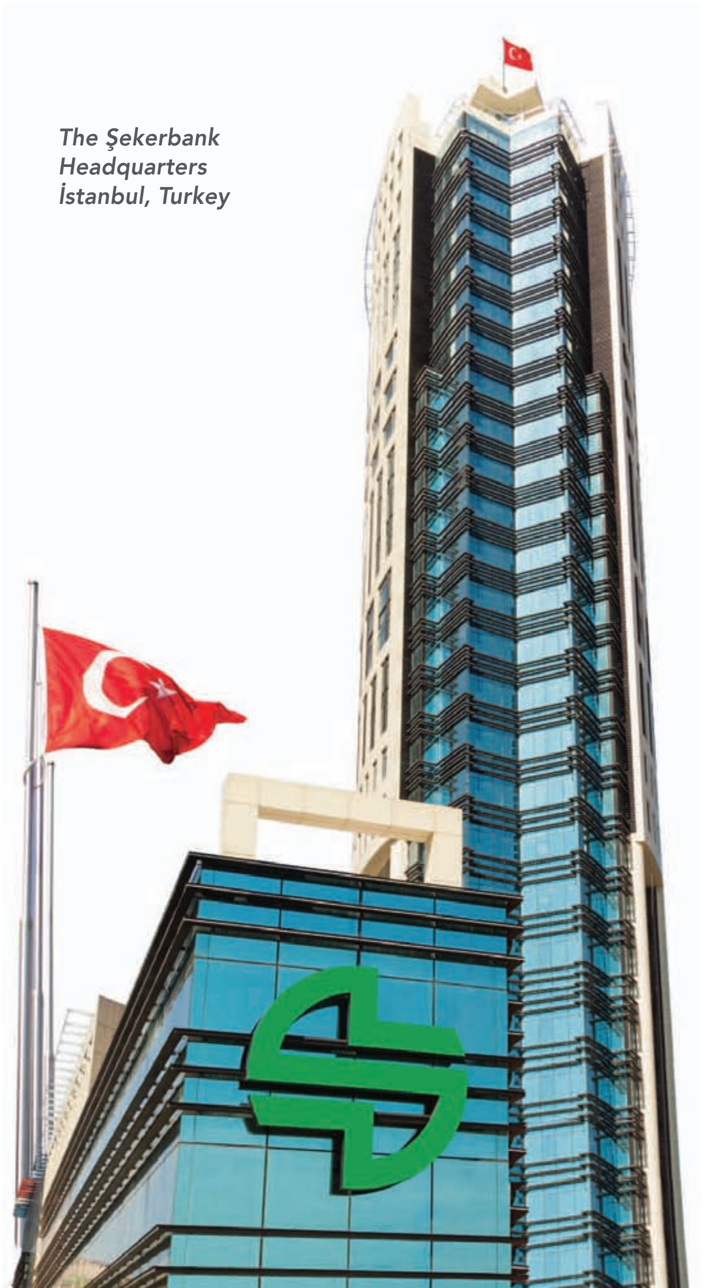
We believe that Turkey will be one of the countries to stand out positively in the coming period. In fact, Turkey has been able to maintain a fast and strong recovery despite the geopolitical risks in our region and unexpected developments such as the July 15th coup attempt. The proactive approach of the Government, as well as the Turkish Central Bank, The Banking Regulation and Supervision Agency, in addition to the uniting of the business world and society as a whole has resulted in this outstanding recovery performance. Even though the growth in 2016, a year in which many unexpected events occurred both locally and globally, was limited to 3.3 percent, Turkey has succeeded in closer to reaching its potential growth with the acceleration achieved in 2017. In other words, despite the number of problems the country has been exposed to, Turkey has managed to recover quickly and has presented a strong growth performance. After the events that could have turned the markets upside down for days in other countries, the resilience and performance shown by the Turkish economy has constituted the main basis for our positive outlook for the future.

**With the support of the Credit Guarantee Fund the banking sector became the locomotive of strong growth**

Turkey grew 5.2 percent in the first quarter of this year, displaying a performance that surpassed the IMF's 4.5 percent prediction for developing countries. The implementation of the Credit Guarantee Fund (CGF) with a considerable size of 250 billion TL as an important step to supporting production in line with the Government's strategy to maintain sustainable growth encouraged banks to accelerate the speed of loan growth. As a result, with an asset growth over 20 percent annually, the banking sector became the locomotive of GDP growth. Accordingly, FX adjusted commercial loans, increasing by 20 percent annually in the first half of the year stood out as the main factor of the total loan growth. We began to see the effect of the CGF on growth, a very important tool both in terms of supporting SMEs and large businesses and in terms of encouraging production, more clearly in the second quarter.

Thus, the Turkish economy consistently main tained a strong growth performance with 5.1 percent in the second quarter. While Turkey became the 5th fastest growing economy in the world with this performance, it also stands out as the 3rd fastest growing economy among the G-20.

Based on this performance, we see that international organizations and credit rating agencies are increasing Turkey's growth expectations for 2017 from the 2-2.5 percent band



*The Şekerbank Headquarters İstanbul, Turkey*


to the 4-4.5 percent band, while foreign banks are revising up their expectations to the 5-5.5% range. Most recently, Fitch revised the 2017 growth predictions for Turkey from 2.3 percent to 4.7 percent, a signal that these institutions have also noticed that Turkey has set a powerful growth potential into action.

### The importance of inclusive financing for sustainable growth

It has been observed that the revitalized domestic demand, as well as the recovery in international demand especially from Europe, has played an important role in the fast recuperation of the Turkish economy. In this respect it is observed that the contribution of net export to growth has increased. Meanwhile, leading indicators also show that the recovery in economic activity is gaining strength. For example the industrial production achieved its best performance of the past six years this July. It has also been observed that recovery in investment demand is continuing and consumer confidence is rising. The improving domestic and international conditions show that the Turkish economy will achieve a strong growth this year.

With its young population, natural resources, production capacity, and geopolitical positioning, which resultedly has its own risks and opportunities, Turkey has great potential in this era when the world's economic map is being reshaped. It is very important both for the economic authorities to decisively continue implementing structural reforms and for the financial sector to extending financial resources to the masses with a responsible banking approach to reveal this potential and to make the recent acceleration in economic growth sustainable. A banking approach that embraces all levels of society and enables groups that have insufficient access to financial resources to be included in production is indispensable for a healthy and sustainable growth that brings social welfare along with it. By decisively practicing strategic policies

**With the "EKOkredi" a loan we developed in 2009 as a first in Turkey to create awareness on energy efficiency and support the sustainability of natural resources, we continued to finance investments in energy efficiency with favorable conditions. We provided over 860 million TL to finance investments in the field of energy efficiency with "EKOkredi".**

that will make this goal attainable and while creating a continuous inclusive growth, Turkey will also become a center of attraction for investors.

### Şekerbank's leader role in inclusive financing

In this context the distinction of Şekerbank's founding mission, which is to support local development and production while growing hand in hand with society, is now more important than ever.

As a bank that has supported producers for 64 years since our foundation, we finance farmers, small and medium enterprises, and local production to make economic growth stronger and sustainable.

We have enabled our farmers, tradesmen and SMEs to use 70 percent of the loans that we have provided to the real sector within the scope of the CGF. In the first half of the year, we provided financing to nearly 8 thousand SMEs within the scope of the CGF. In line with our "Community Banking" mission stemming from the bank's foundation we will continue to undertake a leading role in financial inclusion. We will continue to support our farmers, tradesmen and SMEs not just in the big cities but in the provinces and districts of Anatolia and will continue to finance Turkey's production-based sustainable growth at all levels.

### We have provided financing to nearly 82 thousand farmer families...

Şekerbank is a bank that stands out in the sector with its way of doing business in community banking. "Family Farming Banking", started for the first time in Turkey and in the world with the main goal of preventing migration from rural areas to metropols, is the best example of this. With this project that aims to unite small-scale farmes in rural, increase productivity in agriculture and preserve the local culture we have reached about 82,000 farmers for over the past 2.5 years and provided approximately 5 billion TL.

### We introduced nearly 100 thousand people to energy efficiency

Meanwhile, with the "EKOkredi" a loan we developed in 2009 as a first in Turkey to create awareness on energy efficiency and support the sustainability of natural resources, we continued to finance investments in energy efficiency with favorable conditions. We provided over 860 million TL to finance investments in the field of energy efficiency with "EKOkredi". Thus, we have introduced energy efficiency to a total of over 96,000 people, including 88,199 individual and 8,053 SMEs and farmer customers. With the energy efficiency investments financed by EKOkredi, 27.6 billion kilowatt-hour in energy was conserved to date while a total of 5.9 million tons of $CO_2$ emissions were prevented. Also within the scope of EKOkredi, with which over 137,000 homes were insulated, 125 million cubic meters of natural gas was saved.

In the future, we will continue to support the farmers, tradesmen, SMEs and businesses that form one of the most important links of the production chain for the sustainable growth of the Turkish economy. We will also continue to play pioneering role in sustainable development banking to finance socially inclusive and environmentally sustainable growth. **EDT**

*TEB CEO*
*Ümit Leblebici*

# ‘Good Bank’ TEB continues to contribute to the Turkish economy

As it celebrates its 90th year in 2017, TEB continues to make an increasingly greater effort in order to provide multidimensional support that will nourish Turkey’s economic and social added-value growth in keeping with its ‘Good Bank’ vision. For nine decades TEB has been doing much more than just providing financial support in aid of creating an even stronger Turkey.

We at Türk Ekonomi Bankası (TEB) strive to create more value for all of our stakeholders by focusing on financial growth but on productivity as well. As we celebrate our 90th year in 2017, we continue our effort in line with our 'Good Bank' vision to be an institution which does more than accept deposits and make loans but which gives direction to the entire banking.

Looking back at this time, 2017 appears to be emerging as a good year overall. In line with this we have revised our lending growth targets upward. At midyear 2017, our bank's total assets stood at TRL 80.4 billion while its net profit amounted to TRL 589.7 million. During the first six months our lendings corresponded to 75% of our total assets. We extended nearly half of our TRL 60 billion in loans to the small- and medium-sized enterprises (SME) that are the engines of the Turkish economy. Our total deposits also increased by 4% during the same period and reached TRL 51.6 billion in value.

Besides our contributions as a bank in support of our country's added-value growth, we also initiate and carry out a wide variety of social responsibility projects ranging from innovation to sport, from financial literacy to entrepreneurship and from SME to women in business and angel investors.

### Supporting innovative ideas and contributing to the development of the entrepreneurial ecosystem

As our country advances towards the goals of its 2023 Vision, we believe firstly that it is necessary to change over to an economy that concentrates on technology and added-value creation and secondly that the way to do that is by strengthening an entrepreneurial ecosystem that is based on innovation. In line with our bank strives to contribute to efforts that enhance society's appreciation of culture and that see culture as one of the cornerstones of a new economic model. We support the entrepreneurs whose innovative ideas will be building the economy of the future and we contribute towards efforts to strengthen the entrepreneurial ecosystem. We encourage innovation and entrepreneurship among young people in particular and we have mobilized all of our resources in order to support their efforts in that direction. Having launched Turkey's most comprehensive startup business banking program in 2013, we continue to support efforts that transform entrepreneurs' business ideas into reality and economic value. At our TEB Startup House in Ataşehir in İstanbul and at the TEB Incubation Center, which is under the same roof, we provide entrepreneurs with guidance, promote their projects, and introduce them to investors without expecting anything in return.

The TEB Startup House is a concept that distinguishes our bank among its peers and has enabled us to firmly root ourselves in the entrepreneurial ecosystem. In 2015 we began working with the Turkish Exporters Assembly (TİM) to promote the startup business house concept around the country. Since them we've increased the number of TİM-TEB Startup Houses to nine. Under this program, entrepreneurs benefit from the gamut of financial and non-financial resources of TEB Startup Banking ranging from realizing business ideas to publicizing projects and from finding customers to making investor presentations while those whose projects have strong export potential can also take advantage of TİM's network and information assets. To date nearly 4,500 business ideas have been brought to the TEB Incubation Center and 438 of them have been

*TEB Headquarter, İstanbul.*

*Ümit Leblebici, CEO of TEB.*

accepted into the program while 53 entrepreneurs have received a total of TRL 63.7 million in investment. Besides, 198 entrepreneurs have benefitted from TRL 71 million in state support.

**TEB Private Banking Angel Investment Platform and Turkey's first bank authorized to issue angel investor licenses**

Just as entrepreneurs can get consultancy support at TEB Startup Houses, TEB customers who are interested in becoming angel investors can be awarded their certification through the TEB Private Angel Investment Platform. The TEB Private Angel Investment Platform received Treasury Under secretariat accreditation as a designated angel investor network in early 2015. With that accreditation our bank gained the distinction of being the first officially recognized owner of an angel investment platform in Turkey. Today the TEB Private Banking Angel Investment Platform licenses investors, monitors investment processes, and submits information and documents about investments carried out through the network to the Treasury.

Thanks to the knowledge and experience that we gained through the TEB Private Banking Angel Investment Platform, we launched the TEB Private Investors' Club, the first of its kind not just in Turkey but in the world. The TEB Private Investors' Club brings together serial investors from Turkey and around the world who have dedicated themselves to the concept of angel investment and who have achieved successful results especially in the area of technology-related investments.

**Helping entrepreneurs to achieve worldwide success through the TEB Fintech Future Four Program**

We at TEB believe that not just banks but also fintech (financial technology) companies are going to be playing active roles in the future of the banking and financial services industries as an outcome of the ongoing digital revolution. Our goal therefore is to be the player that is the most actively involved in shaping the course of this process. In line with this we last year launched TEB Fintech Future Four, a program specially designed for startups with fintech-related ideas and projects. The goal of this program is to provide startups with the consultancy support they need during the financial backing and commercialization stages so that they can germinate their ideas and in this way help them grow their own companies into global successes.

Students, professionals, in fact just about anyone with an idea can apply take part in this program. TEB Fintech Future Four's jury of experts consisting of professionals from our bank and the financial services industry so far have carefully examined 43 project submissions and giving priority to four of them.

Our goals here are not only to help these investments grow into world-class firms but also to make the program a win-win model for the Turkish banking industry as a whole. The ultimate aim of course is to make a big contribution to the growth of our country's economy and of its entrepreneurial ecosystem.

At this time we're continuing to support these four projects. At the outset we're doing this in France but we're on the lookout for ways to give the projects access to the global fintech startup ecosystem as well. Our aim is to lead the way in introducing Turkish fintech projects to the whole world.

### Consulting SMEs how to grow

Since 2005, TEB has been distinguishing itself in the Turkish banking industry by taking a "consultant bank" approach whose aim is to help the country's small- and medium-sized businesses achieve sustainable growth not just through the financial products and services that we provide but also through our non-financial services as well. Especially because of our latter offerings to such businesses, TEB is one of only three banks in the world to have been pointed out as models in the SME banking business line by the International Finance Corporation. TEB supplies SME with the knowledge and training they need directly through many of its firsts such as TEB SME TV, TEB SME Academy, and the TEB SME Consultants Program.

It's very important for Turkey to increase its foreign trade performance in order to achieve its 2023 Vision goals. In recognition of this, we launched a foreign trade campaign as an SME consultant bank by means of which we introduced them to new two services. One is tebledisticaret.com, a website where firms are just one click away from the most comprehensive information currently available; the other is our 'Foreign Trade Development Program', where SME can get specialized advice on how to use such information.


*Guidance for entrepreneurs at TEB Startup House.*

### Focusing on female business owners

The 'consultant bank' approach that we take in TEB SME banking also shows up in TEB Women's Banking, a business line in which we have developed special solutions that address the particular needs of women who go into business for themselves. Through TEB Women's Banking we support female business owners in such areas as finding the information they need to grow their business, entering new markets, and networking. We also give them access to specialized training, consultancy, and mentoring resources. TEB even received a prestigious European Business Award for its activities in this business line as the only bank in Turkey to receive a European Business Awards 'Ribbon of Honor' in the 'Customer Focus' category. Having launched TEB Women's Banking in order to engage women in economic activity not just as consumers but also as producers, we will continue to focus on our efforts in this business line in the period ahead as well.

### Two new services from CEPTETEB

While serving its customers through a network of more than 500 branches that reaches all over the country, TEB also continues to develop its productive business models by focusing its attentions on alternative delivery channels as well. In the early 2000s we were one of the first banks in Turkey to enter the realm of digital banking and to invest in it. With the steadily increasing demand for and use of online and mobile banking products and services, in 2015 we combined all of our digital banking business processes under our CEPTETEB brand and made that the focal point of our investments in this area.

As of the second quarter of 2017, we had 420 thousand CEPTETEB customers. In the case of online banking, some 40% of TEB customers are


*TEB branch in İstanbul.*

now making active use of it. CEPTETEB is Turkey's fastest-growing digital banking platform and we continue to add new products and services to it in order to make our customers' lives easier. Not long ago we introduced CEPTETEB Konut Kredisi, a home-finance product (the first of its kind in Turkey) that allows customers to complete all loan preliminaries in a digital environment without having to step inside a bank branch. At TEB we're also involving ourselves in ground-breaking projects in support of the financial services industry's wearable technologies transformation. We intend to continue our investments in the area of wearable technologies and to introduce new products that incorporate them.

### Financial literacy education for more than 225 thousand people

We believe that financial literacy is of the utmost importance to a country's sustainable growth. In line with this in 2012 we initiated the TEB Family Academy in order to promote financial literacy and to encourage thrift in keeping with our commitment to responsible banking. We are continuing those efforts today in order to help encourage saving habits among the public at large and to foster a more financially literate new generation. To date we have provided free-of-charge face-to-face financial literacy education to more than 225 children and adults.

In the case of the "I Can Manage My Budget" project that we are undertaking in collaboration with the Ministry of Education, our aim is to provide financial literacy education to five million people over a three-year period. We have also signed an agreement with the same ministry's General Directorate of Vocational and Technical Training in Ankara, under which financial-issue related content will be added to the banking and accounting curriculums of 1.2 million highschool students in order to increase their awareness of such matters.

### A European and Turkish "Great Place To Work" for the fourth year in a row

Top Employers Institute, an internationally-respected corporate research foundation that has been assessing companies' human resources policies and practices since 1991, recently cited TEB as one of the best employers in Europe and Turkey for the fourth time in as many years. Five years ago TEB launched a "Great Place To Work" program in-house in order to systematically achieve its goal of becoming a business that people want to work for. The 26 percentage-point rise in the number of employees who said they would recommend the bank as a top-notch employer is evidence that TEB is successfully on course as a great place to work. In last year's review by the Top Employers Institute, TEB remained the first and only Turkish bank to be included in the institute's Great Place To Work list.

### Continuing to contribute to society through our "Good Bank" vision

As it celebrates its 90th year in 2017, TEB continues to make an increasingly greater effort in order to provide multidimensional support that will nourish Turkey's economic and social added-value growth in keeping with its 'Good Bank' vision. For nine decades our bank has been doing much more than just providing financial support in aid of creating an even stronger Turkey. Besides contributing to the national economy, we shall also continue to contribute to the wellbeing of society through our 'Responsible Banking' approach. **EDT**

# THE HEART OF SILK ROAD WILL THROB AT THE İSTANBUL NEW AIRPORT

İstanbul New Airport, which is expected to be the largest airport in the world when fully completed in 2023, will serve as Turkey's primary airport and a hub for connecting flights between Europe and Asia.

Istanbul New Airport (INA) has the characteristic of being the largest infrastructure investment project that has been constructed as the single line with estimated 10.25 billion Euro investment cost throughout the history of Turkish Republic. INA plans to reach 150 million passenger capacity once it is completed and possibly expand this capacity to 200 million once all its phases are finished. The target is to take the INA into complete operation within four phases.

The airport is expected to provide opportunities for flights to more than 350 destinations for nearly 100 airline companies. 69 percent of passengers are expected to travel internationally while 31 percent are expected to travel on domestic routes.

The airport is being constructed on a 76.5 million square meters site located on an area on the north of European side of İstanbul with 35 km to the city center where urban development and expansion is relatively weak.

The number of employees working on the construction of Istanbul new airport reached 30,000, while 57 percent of the project, planned to open on October 29, 2018, is completed.

When the first phase of Istanbul's new airport is completed, it will have a capacity for 90 million passengers. Taking into consideration the fact that per capita expenditure in tourism the sector exceeds $700, the share of the expenditures by these passengers is expected to be above $7 billion, even if 10 percent of them visit Turkey as tourists.

İstanbul New Airport, which is to host the airlines companies that will come to Turkey for the first time, is getting ready to be the window display to showcase Turkey to the rest of the World. Istanbul New Airport, which will host around 100 airlines companies, is being designed to offer state-of-the-art practices of passenger experience, comfort and technology. As construction work proceeds at full speed at the İstanbul New Airport so as to prepare for the launch planned in 2018, commercial agreements are also being signed.

A natural transfer hub and an attractive destination in aviation, İstanbul New Airport will host important retail brands that had not been in the Turkish market before. With the largest duty free space of the world, Istanbul New Airport will be home to about 400 global brands.


Poised to become Turkey's showcase on a global scale, İstanbul New Airport will frequently receive mention for its unique passenger experience and international transportation. Amid construction works halfway towards completion, contracting continues for İstanbul New Airport. Following the signing of Duty Free Zone management agreement, the auction for eating and drinking facilities will be concluded in the first quarter of this year, and advertisement allocation areas will be auctioned in the coming days.

Looking to creating jobs and contributing to growth of markets in various business lines, Istanbul New Airport will also make Istanbul the new center of international transportation through its Cargo City located in the project area.

Within the scope of these 25-year contracts, MNG, PTT, Çelebi Ground Handling, HAVAŞ, Sistem Logistics and Bilin Logistics will build their

**İstanbul New Airport, set to be a game-changer in the global aviation sector, concluded area allocation contracts with six companies as regards the Cargo City and Ground Services Campus. The contracts, valid for the duration of the operation, will amount to an approximate EUR 250 million in total.**

own facilities at the "Cargo City and Ground Services Campus", from where they will serve İstanbul New Airport. Through the business volume to be created by the Cargo City, İstanbul New Airport, set to launch flights to 350 destinations, will support Turkey in reaching the targeted export figures, while increasing the e-commerce market.

### Cargo City equal to the size of 200 soccer fields!

A total of 150,000 square meters of space is allocated for ground services in the Istanbul New Airport. As for cargo, this figure will be 1.4 million square meters in total, including cargo aircraft parking areas and the Cargo City. This figure corresponds to the total size of 200 soccer fields of international standards. The Cargo City is constructed in a way to allow simultaneous operation of 35 wide-body cargo aircrafts.

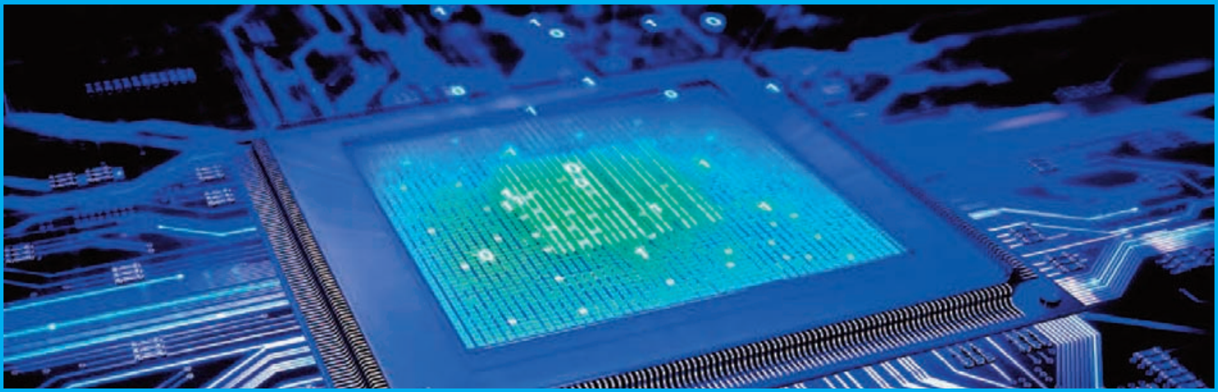
### Once all phases completed, it will even outrun that of Hong Kong

Currently, the airport with the largest global cargo movement is Hong Kong Airport with a volume slightly more than 4.5 million tons. Yet, the Istanbul New Airport will have a capacity of 5.5 million tons when its all phases are complete. MNG, PTT, Çelebi, HAVAŞ, Sistem Logistics and Bilin Logistics will operate on an area of around 200,000 square meters.

### Latest technologies in place for Cargo and Ground Services

As part of the Istanbul New Airport area allocation agreements for cargo and ground services, one of the largest contracts recently signed in the aviation sector, the companies will use the latest technologies to provide top-notch passenger experience.

İstanbul New Airport, which will recreate the Silk Road up in the sky, aims to give priority to passenger experience in terms of ground services, as well. To this end, services both in passenger terminals and aprons will consist of operations that extensively use technology, apply the most advanced techniques and make passengers feel privileged. **EDT**

*Chief Marketing Officer*

*Selcan Taşkıran*

# Netaş continues to deliver next generation technologies

One of the most important projects Netaş will focus in the coming period is the installation and 5 year operation of all wired and wireless networks at Istanbul's new Airport, which is expected to become the world's largest airport with an annual passenger capacity of 150 million once completed.

For the last five decades, Turkey's leading systems integrator Netaş continues to deliver next generation technologies and support Turkey's digital transformation through major projects.

One of the most important projects Netaş will focus in the coming period is the installation and 5 year operation of all wired and wireless networks at Istanbul's new Airport, which is expected to become the world's largest airport with an annual passenger capacity of 150 million once completed.

Netaş undertook the project in collaboration with Cisco, and under an agreement signed with İGA Havalimanı İşletmesi A.Ş. (İGA), the company will implement the fixed and mobile telecommunications infrastructure.

With its broad experience in ICT infrastructure and innovative approach due to the ownership of Turkey's first private telecoms R&D, Netaş will provide fixed and mobile telecommunication services like a telecom operator to all businesses within the airport, including airline companies, customs and security units, restaurants, parking lots and duty free stores over a single infrastructure.

**Fastest Internet access to 50,000 people with nearly 4,000 access points across the airport**

Within the scope of the project, Netaş will offer Wi-Fi coverage in terminal and parking areas via nearly 4,000 access points, providing c.50,000 visitors with simultaneous wireless network access. As such, the coverage capacity of the project makes it one of the world's largest of its kind. The infrastructure will be based on the latest and fastest Wi-Fi technology available, '802.11ac Wave 2', offering a wireless Internet access to visitors at speeds reaching up to 2.6 Gbps. The communication infrastructure to be built will also allow for indoor location services. In addition, Netaş will develop project-specific mobile applications, and various software & programs.

Prior to this project, Netaş had set up the telecommunications infrastructure of 45 smart stadiums all across Turkey. Nearly 50,000 visitors enjoy simultaneous uninterrupted Internet access at these stadiums, which further improved the visitors' entertainment experience while increasing the ability to take preventive measures against security risks. In addition to providing a high

A 3D plan of the Istanbul new airport.

**As a result of the efforts of Netaş R&D center, home to the best talents in Turkey; Netaş has published a total of 106 scientific papers on national and international platforms and applied for 220 patents over the past three years.**

bandwidth Wi-Fi infrastructure, the smart stadium concept includes a stadium system control room, game operation centers and security cameras. Furthermore, the e-ticket infrastructure, including a specific mobile application, was set up by Netaş.

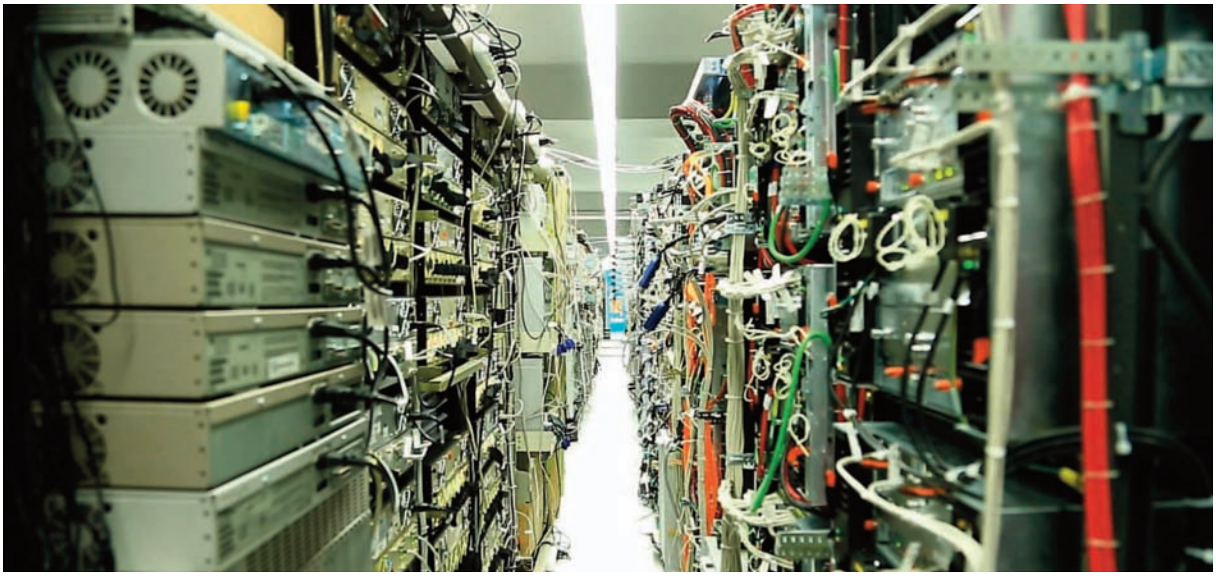
As a systems integrator and next generation technology developer, Netaş focuses on developing IoT architecture, mobile broadband solutions, including VoIP and Multimedia, VoLTE and VoWiFi, while providing its customers with solutions on networking, cyber security, unified communications, virtualization, cloud computing, broadband access, defense technologies, optical and carrier Ethernet, GSM-R, IT integration services and strategic outsourcing, as well as custom-tailored software solutions.

As a result of the efforts of Netaş R&D center, home to the best talents in Turkey; Netaş has published a total of 106 scientific papers on national and international platforms and applied for 220 patents over the past three years.

Operating as one of top 10 VoIP laboratories in the world, Netaş now exports next generation broadband, VoIP and multimedia software solutions thanks to its substantial R&D power, to more than 200 global operators across North America, Europe, and Asia. As a result, Netaş has been named as Turkey's top software exporter seven times over the past decade.

This is also reflected in the rise seen in the amount of orders Netaş has been receiving in the international market. The volume of overseas


Selcan Taşkıran, Chief Marketing Officer of NETAŞ



orders the company received in 2016 grew by 220% year-over-year.

The company's focus on the R&D and innovative end-to-end solutions has led Netaş to receive seven awards very recently in the IT 500 Turkey survey. In the year 2016, Netaş ranked in the first place in a total of seven categories, including "Systems Integration", "Systems Integration – Hardware", "Systems Integration – Software", "Network Hardware", "Sectoral Software" and "R&D Investment", as well as "Software Exports".

**Algeria: End-to-end solutions from GSM infrastructure to stadium IT infrastructure**

Among major international projects implemented by Netaş, those in Algeria and Bangladesh stand out with their extent and complexity. In 2014, Netaş signed a five-year contract with ATM Mobilis, Algerian GSM operator, for the improvement of the 2G and 3G transmission infrastructures and providing radio frequency (RF) optimization solutions.

Netaş also realized the next generation data center project, including the design and implementation of the software and hardware COE Phase III solution of Sonatrach, the world's 11th largest oil company and the largest one in Algeria and Africa. In addition, the company is currently setting up the IT infrastructure for the ongoing construction of a 50,000-spectator capacity stadium in Tizi Ouzou, Algeria.

**Bangladesh: A cooperation for almost two decades**

In Bangladesh, where the company has been operating since 1998, Netaş established a nationwide transmission network based on SDH and PDH technologies, followed by the setting up of the Nagar switchboard as a part of the 139K lines digital telephone switchboard project.

In 2014, Netaş signed an agreement with Bangladesh's national service provider BTCL (Bangladesh Telecommunications Company Ltd.) to increase the capacity of the national transmission backbone and modernize the equipment and software in the country, as the country's existing national bandwidth remained inadequate in meeting the continuously increasing demand. The Internet line, which was established in 2005 by Netaş, was upgraded to 240G (Gb/s) in 2008, without any interruption to the Internet service.

In addition, starting from 2013, Netaş included a new operator into its portfolio every year, and established the transmission networks of Mango Telecommunications in 2013, Fiber@Home in 2014 and BD Link in 2015. **EDT**

*Political Science in the Department of International Relations at Istanbul Bilgi University*

*Prof. İlter Turan*

# The Southeastern Anatolia Project Advances with the Construction of the Ilısu Dam

Ilısu Dam constitutes the latest dam to be built within the framework of the GAP project on the Tigris. Costing around 1 billion Euros, the hydro-electric plant will be the fourth largest producer of power in Turkey. It will offer limited irrigation; the dam is intended mainly for power generation, producing around 4.12 billion KwH energy annually. It is expected to contribute 412 million USD to the national economy each year.

## The GAP Project

As conflict has been raging in other parts of the Middle East, Turkey has been making unnoticed progress in the Southeastern Anatolia project, usually known by its acronym GAP. Those interested in water usage in the Middle East will remember that Turkey developed a grand project to benefit from the waters of the Tigris and Euphrates both for power generation and irrigation purposes by building a total of thirteen major dams on the two rivers. Starting in the 1960s with plans on the Euphrates and extending them to also cover the Tigris during the 1970s, the GAP project covers an area of 75,378 square kilometers which corresponds to roughly one eleventh of the territory of Turkey. When the entire project is completed, it is expected to irrigate 1,800,000 hectares of agricultural land (about 20 % of Turkey's irrigable land) and generate 27 billion KwH of power (more than 20 % of Turkey's hydroelectric potential) while expanding Turkey's employment by 3,800,000 persons.

Understandably, such a big project has stimulated great interest in the international arena for a variety of reasons. As the project got developed and moved to the implementation stage, downstream states, for example, grew apprehensive that Turkey would consume all the waters of the rivers and there would be little water left for them. They and their allies wanted assurances that a maximum amount of water would be made available to them, leading to a concerted effort to prevent the implementation of the dam projects. This strategy that was predicated on the

assumption that Turkey alone would not be able to construct the dams. While funding problems did cause delays, Turkey was able to proceed with dam construction, and, in the process, acquired the capability to build very large dams, an outcome which was not anticipated.

Today, Turkish companies rank highly among those that can build the world's largest dams. Not surprisingly, once it was seen that Turkey could build its own dams, the very countries that had joined those opposing the GAP project and withheld credit for the construction stage, began to offer credit for turbines and other equipment for power generation.

As Turkey proceeded with its dam construction, it also became evident that some of the fears regarding the use of water were not well founded. Only to make a point that ought to have been obvious from the beginning, if one of the purposes of building dams was to generate power, then water had to be allowed to run downstream. Furthermore, by holding water and regulating its flow, everyone, including those downstream, was assured of a reasonable flow even during months when the discharge of the rivers was extremely low. Dams that were built upstream in valleys with deep gorges lost less water through evaporation and evapo-transpiration, thereby actually helping increase the overall amount of water for human use than in earlier times. And finally, the technologies of irrigation Turkey employed were more oriented toward water conservation than those employed by the downstream users who often relied on no means other than natural flow.

Prof. İlter Turan, Istanbul Bilgi University

**Today, Turkish companies rank highly among those that can build the world's largest dams. Not surprisingly, once it was seen that Turkey could build its own dams, the very countries that had joined those opposing the GAP project and withheld credit for the construction stage, began to offer credit for turbines and other equipment for power generation.**

Much of the resistance to the GAP project derived from three factors. First, Turkey's departure from its historical dry-farming tradition and its decision to tap the waters of the Mesopotamian rivers introduced a need for adjustment in the pattern of water usage throughout the entire Tigris-Euphrates basin and therefore an element of unpredictability for the downstream countries that had been the traditional users of these waters. Second, downstream users assumed that they would retain the same patterns of water usage in the future and therefore assumed that their needs would constantly increase along with rapidly increasing populations.

If Turkey would use some of the waters, that would simply deprive them of more water in the future. This led them to the problematical tendency to conceptualize water needs only in quantitative terms and as a result, come up with exaggerated demands that could not be substantiated by their current consumption levels. Finally, rendering the question into a quantitative problem, led to a mindset that saw water usage as a zero-sum game, a predisposition that seriously undermined attempts to develop cooperative schemes regarding the use the two rivers' waters.

Over the years, it has become clear that the GAP project is going to go on but that it is not producing the multifarious outcomes the downstream countries feared. This is not to say that there are not problems, but the major problem is probably not a quantitative but a qualitative one, that of pollution. As the rivers flow South, they go through cities, towns and agricultural lands. Along the way, sewage is discharged into the rivers while irrigation water containing chemical fertilizers and pesticides slowly seep in. Turkish municipalities have been building sewage treatment plants along the rivers. In the area of agriculture, on the other hand, the employment of more sophisticated irrigation techniques, mainly intended to increase production, have reduced the chemical pollution. Nevertheless, a comprehensive, basin-wide project to reduce pollution with international backing would be a welcome way to improve water quality along the rivers. Unfortunately, such well-intentioned ideas will have to await the coming back of peace and stability to the region.

**The Ilısu Dam Project reflects the efforts of the Turkish government to blend the historical with the modern, the traditional with the new. At the same time, it demonstrates the determination of the successive Turkish governments to go on with the completion of the GAP project, irrespective of persistent efforts to impede its implementation.**

### The Ilısu Dam

Ilısu Dam constitutes the latest dam to be built within the framework of the GAP project on the Tigris. The initial history of the dam reflects all the patterns of behavior of both the downstream countries and their allies in the international community where a concerted effort to prevent the construction of the dam caused delays. But as had been already proven in the case of the Atatürk Dam on the Euphrates, the project was not cancelled. Costing around 1 billion Euros, the hydro-electric plant will be the fourth largest producer of power in Turkey.

It will offer limited irrigation; the dam is intended mainly for power generation, producing around 4.12 billion KwH energy annually. It is expected to contribute 412 million USD to the national economy each year.

As is the case with other major dams, the dam project is not only one of construction but one of major socio-economic transformation. During the implementation of the project, the lands and buildings of 107 villages and one town that will be submerged under the dam waters are being expropriated, new places are being prepared and/or built for resettlement, the farmers are being offered training and material assistance for raising more valuable cash crops, plans are being made for getting the residents to benefit from the potential the dam lake will offer in terms of aqua-culture, and new roads are being built in anticipation of increased economic activity. Since it is planned to have the holding of water commence at the end of 2017, there is intensifying activity to complete all the necessary jobs before the holding of water begins, although there will be time for the water to

reach most locations. There is a unique aspect to the Ilısu Dam, however, that has aroused greater interest in this particular project than in others. The historical town of Hasankeyf will also be submerged under the dam lake. This has aroused much controversy. While criticism that the historical town should not be allowed to be buried under the dam waters have not been accommodated since this, for all practical purposes, would reduce the benefits expected from the dam to inconsequential levels, they have been helpful in ensuring that major efforts are made to minimize the loss of historical value of the town.

For example, the lower part of the historical citadel to which visitors are banned because of falling rocks, is going to remain under the water, but the so called the middle gate which is the major historical piece constituting the entrance, is being moved to be reconstructed in a cultural park. The soft and eroding rock under the upper citadel, on the other hand, is being fortified so that the upper section of the citadel may be opened to the visitors. But the most significant feat so far, has been the relocation of the historical Tomb of Zeynel Bey, which has been restored and moved almost two kilometers to its new location. Some other monuments are in line to be moved to their new places.

Efforts are being made retain the historical character of Hasankeyf. An archeological museum is about to open in the new town that will display a collection of items that have been gathered from the various digs in the dam area. Some of these items are 12000 years old, they have been newly found and have not been displayed at other places. This promises to be a unique museum that is expected to attract visitors from around the world. Combined with the cultural park where many historical monuments will be moved and reconstructed, not all of Hasankeyf's history will be submerged. The historical nature of Hasankeyf will be complemented by the construction of homes that are designed as flat roofed one or two-story units whose architectural characteristics reflect those that prevail in the old town.

The Ilısu Dam Project reflects the efforts of the Turkish government to blend the historical with the modern, the traditional with the new. At the same time, it demonstrates the determination of the successive Turkish governments to go on with the completion of the GAP project, irrespective of persistent efforts to impede its implementation. Ilısu, like the rest of the dams in the GAP project, intends to diversify the energy sources of Turkey, improve its agricultural potential, create employment for a growing population. Developments so far have not justified the fear that Turkey's development of its transboundary water resources would inevitably inflict significant harm on its neighbors or create major problems for the international community. And Turkey looks forward to the day when tri-partite cooperation between the riparians of Tigris and Euphrates will become possible again, allowing all to enjoy the blessings these two rivers have given to them. **EDT**

INTERVIEW

*A Global Player*

*Ozan Özkural*

# "SUCCESS CANNOT BE MEASURED WITH MONEY ONLY"

Success is for a person is to find the inner strength to challenge all kinds of difficulties standing in front of their dreams; creating a vision ensuring that the people who trust in them and help them achieve these dreams also share the fruits of success along with themselves.

**How did you advance in your career? Could you please tell us about your road map briefly?**

At the age of 21, I began my career not as an investment banker but actually in the FMCG sector in Unilever UK's "management trainee" program. Unilever was a very good and major company but after a while I decided that it would be more appropriate for my character and life expectations to be in a sector that is fast moving like investment banking, in which right risks need to be taken and which can provide both material and spiritual satisfaction in exchange for these risks. For this reason, I started to work in the "principal investment & structured finance" department in Merrill Lynch London office, in 2004. At this department, I took part in economically and geopolitically important major transactions that ranges from Turkey to Italy, from Australia to America. After I started to manage these transactions, I also started to take on different tasks upon the emergence of the 2008 crisis.

At the beginning of 2008, our team of 62 people managing over an 8-billion USD balance sheet, started the year with only 4 people at the beginning of 2009, with its balance sheet reduced to 400 million USD. Having overcome this dramatic and challenging year meant that I took great responsibilities within a short duration. Towards the end of 2009, I started to work in global capital market - emerging markets department and I served as vice president at this department in 2010. At the beginning of 2012, I transferred to VTB Capital, Russia's second largest bank, as its responsible manager in charge of Turkey.

During my two years in VTB Capital, I managed an investment portfolio of approximately 2 billion USD and after I gained investment experience in both Turkey and the emerging markets in many areas and sectors, at the end of 2014, I founded with my Saudi Arabian partner our private equity fund named Tanto Capital Partners, of which I am the founder and CEO, and I still manage this fund.

*Ozan Özkural, Co-Founder and CEO of Tanto Capital Partners*

**What is success in your opinion? Could you please describe it?**

The success for a person is to find the inner strength to challenge all kinds of difficulties standing in the direction of his/her dreams and is to reach his/her desired goals with a vision ensuring that the people he/she trusts in realizing these dreams also climb up the stairs of success along with himself/herself. In doing so, it is important that they reach their dreams with modesty and by creating added value to essentially everyone around themselves. Also, these dreams do not necessarily have to be material or business related. The important thing is being successful in life, and it cannot be measured with money only.

**Being a player in international arena is a remarkable success. How does your cultural identity affect this position?**

The world is bigger than any country and in this "global village" we live, everyone is somewhat connected to each other. Therefore, in order to be a player in the international arena, it is necessary to be able to examine things really in the macro level and read well the cultural diversity of the several other players in the world, the changing interests, the anticipations, the political realities and more precisely, the global geopolitics.

Of course this does not mean that one will neglect their national identity. I am and proud to be Turkish. My childhood was also spent more in a multinational place like London and I think this enabled me to get on with and find common interest points with people from different cultures and countries faster and easier.

**What different cultures and countries contributed to you? Having this advantage, what would be your suggestions to executive candidates in Turkey and other foreign executives of international companies?**

Diversity is a good thing. As part of my job, for many years I have been to and still visit many places of the world and this have enabled and still enables me to perceive the culture of those countries and the differences among diverse cultures. If you can look at the differences without discriminating based on religion, language, race, sex, and basically without judging people, you can see that these differences make us so much stronger when combined correctly. The essential thing in business life is for the right people to come together. Therefore, my advice to the executives in Turkey is that they should travel the world as much as possible and become familiar with different cultures.

**The rate of senior female executives is low all over the world. What would be your recommendation for this rate to increase?**

First of all, it is absolutely essential that there is no income difference between a woman and a man who does the same job. In this matter, I think people, regardless of being a woman or a man, who will do the job best and have strong leadership qualities should be the senior executives. While this requires transformation in mentality, I am convinced that this issue will be at a better position and become more balanced and equitable with the new generation.

**If you were a person organizing an event for the cultural promotion of Turkey, what would you consider to be prominent in this event?**

The understanding and harmony among the different cultural identities in our country. Unfortunately, in recent times, the image of our country abroad has been a polarized nation to the extent we have never been before. We are a nation which, despite having a much more complex cultural structure than most of the countries in the world, has managed to turn this complexity into power rather than weakness, by harmoniously handling such mosaic structure.

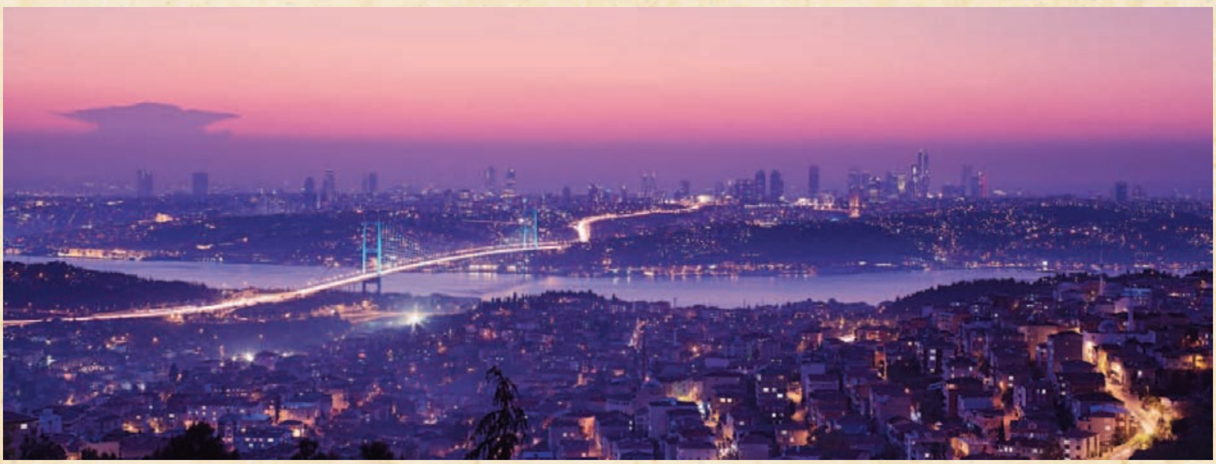
**What would be your Turkish movie and book suggestion to foreigners?**

As movie, My Father-My Son (Babam ve Oğlum). As book, Ataturk's The Great Speech (Nutuk). **EDT**

*EY Turkey*

*M&A Report 2016*

# Mergers & Acquisitions Activities in Turkey



In line with 2015, a vast number of deals in 2016 were small and medium sized transactions. We expect such transactions by both domestic and foreign investors to continue in the following years not only because of investors who aim to benefit from Turkey's mid-long term growth potential, but also their aim to operate within the region, using their Turkish operations as a hub.

In 2016, while many developed countries experienced a slowdown in their economic recovery, emerging countries overall recorded lower growth rates than in the previous year, some even reporting signs of recession. It was a year in which agendas were dominated by political, economic and security concerns. And in Turkey it was no different. Terror incidents, security issues, and economic issues resulted in Turkey underperforming its potential as well as a reduction in its growth rate. Compared to 2015, global mergers and acquisitions activity decreased in terms of volume although the number of transactions remained at similar levels. In Turkey, we experienced both a decrease in transaction volume as well as in the number of transactions in 2016.

There were many noteworthy developments in 2016; expectations for the FED to further raise its interest rates which accelerated the decline in growth rates of emerging countries, the US presidential election and the potential consequences thereof, and the mounting risk of the dissolution of the European Union following the UK's Brexit decision. Turkey was not immune to these events and recorded a growth rate below that of 2015. Furthermore, Turkey was (as were many EU countries) negatively impacted by political uncertainty in the Middle East, security problems and the worsening refugee crisis. Its relations with the EU also suffered. Terror incidents and an attempted coup in Turkey were among the other prominent factors affecting the domestic M&A activity. In the light of these developments, Turkey underperformed in terms of M&A activity.

In 2016, we witnessed the UK's decision to leave the EU, an important trade partner of Turkey, and increasing uncertainty about the EU's future. Turkey experienced an attempted coup, a subsequent state of emergency, a downgrading of its credit rating by S&P and Moody's which created pressure on its economic outlook. On the positive side, Turkey's relations with Russia improved in the second half of 2016, following the jet crisis at the end of 2015, which in turn positively affected trade and tourism activities.

Emerging countries, including Turkey, were also adversely impacted by expectations of radical foreign policy and economical changes in the US under the new administration, as well as by anticipation of additional interest-rate hikes by the FED following the end of its decade-long low interest policy. In Turkey, this manifested itself in the form of increased domestic interest rates, pressure on the Turkish Lira, and caused M&A activity to retract.

As a result of these, we observed declined investor appetite in Turkey. Based on sources available to us, the number of mergers and acquisitions in Turkey in 2016 was 243. This number is lower than in the previous year and transaction volumes also shrank considerably, mainly as a result of a fewer large ticket transactions. To put this into perspective, we note that global M&A activity also retracted in terms of total volume, although the number of transactions remained comparable.

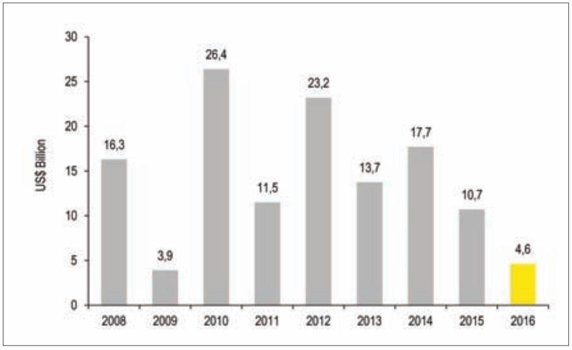
## Key Findings in 2016 M&A Activity

**Both the number of transactions and total transaction volume significantly decreased in 2016**

In 2016, there was a total of 101 deals with disclosed values totalling US$4.6 billion. None of these deals exceeded one billion US dollars. While high value transactions slightly increased the total transaction volume, the fact that there were only 17 deals over US$100 million highlights investors' continued interest in SMEs, as was the case in

previous years. On the other hand, of the deals with undisclosed values, we know that some were realized with deal values greater than US$100 million. Including our estimates for the deals with undisclosed values, we anticipate that the total transaction volume in 2016 was US$7 billion.

## HISTORICAL DEAL VALUES




**Source:** *EY Turkey M&A Report 2016*

234 private sector deals were realized in 2016 generating a total of US$3.5 billion or 77% of the total volume of all disclosed transactions. In addition, nine public sector deals generated a total transaction volume of US$1.1 billion. Since there were no public sector deals greater than one billion US dollars, private sector deals dominated the total transaction volume. Furthermore, the share of total transaction volume was dominated by foreign investors. In terms of investor origin, foreign investors formed 54% of the total transaction volume, and domestic investors 46% thanks to their presence in the privatization tenders. Due to negative developments in the region, global economic uncertainty and the events following the attempted coup in Turkey, foreign investors' interest in Turkey diminished in 2016. In our 2015 report, we noted that the total transaction volume of M&A transactions for 2016 was expected to be between US$10 billion and US$15 billion based on our survey of prominent members of the Turkish business community. Actual results for 2016 considerably fell below these expectations due to political and economic

uncertainties as well as the security issues in the neighbouring region. We believe that it may take a while for the political and economic uncertainties and security issues to subside. Therefore, we expect 2017 to be completed as a slow year for M&A activity, albeit relatively more positive than in 2016.

### Major deals in 2016

In 2016, no transactions exceeded one billion US dollars and the total volume of the top 10 deals was US$2.9 billion. Three of the top 10 deals were in the public sector and the remainder in the private sector. Public sector deals accounted for 28% of the total value of the top 10 deals: The Transfer of Operating Rights tender of Menzelet and Kılavuzlu HPPs won by Akfen Holding for US$400.9 million, the Transfer of Operating Rights tender of Almus and Köklüce HPPs won by Gül Energy for US$250.2 million and the privatization tender of TP Petroleum Distribution won by Zülfikarlar Holding for US$159 million. Private sector deals accounted for 72% of the total value of the top 10 deals. Major private sector deals in the top 10 were the acquisition of Mars Entertainment Group by CJ CGV for US$689.2 billion and the acquisition of 23.6% stake in Odeabank by International Finance Corporation (IFC), European Bank of Reconstruction and Development (EBRD) and private investors for US$265 million.


## TOP 10 DEALS WITH DISCLOSED VALUES

| Target | Sector | Acquirer | Country of Acquirer | Stake | Deal Value (US$ million) |
|---|---|---|---|---|---|
| Mars Entertainment Group | Entertainment | CJ CGV | South Korea | 100.00% | 689.2 |
| Menzelet HPP, Kılavuzlu HPP | Energy | Akfen Holding | Turkey | N/A | 400.9 |
| Odeabank | Financial Services | International Finance Corporation (IFC), European Bank of Reconstruction and Development (EBRD), Private Investors | USA, UK, UAE, Lebanon | 23.58% | 265.0 |
| Aksa Energy WPP Portfolio | Energy | Güriş Construction | Turkey | 100.00% | 259.0 |
| Borajet | Transportation | SBK Holding | Turkey | 100.00% | 258.0 |
| Almus HPP, Köklüce HPP | Energy | Gül Energy | Turkey | N/A | 250.2 |
| Alternatifbank | Financial Services | Commercial Bank of Qatar | Qatar | 25.00% | 224.9 |
| Rönesans Holding | Real Estate | International Finance Corporation (IFC) | US | 5.25% | 215.0 |
| TP Petroleum Distribution | Energy | Zülfikarlar Holding | Turkey | 100.00% | 159.0 |
| TAB Food Investments | Food and Beverage | Goldman Sachs, Credit Suisse, European Bank of Reconstruction and Development (EBRD) | USA, Switzerland, UK | Not Disclosed | 150.0 |

**Source:** *EY Turkey M&A Report 2016*

In 2016, the top 10 deals accounted for 62%. The average size of the top 10 deals was US$287 million, while the average size of all transactions with disclosed values was US$46 million. The average size of public sector deals was US$135 million and the average deal size for private sector was US$38 million. Of the private sector transactions with disclosed values, only 13 transactions exceeded US$100 million. The remaining 80 deals averaged just US$11 million. Thus, in line with 2015, a vast number of deals in 2016 were small and medium sized transactions.

We expect such transactions by both domestic and foreign investors to continue in the following years not only because of investors who aim to benefit from Turkey's mid-long term growth potential, but also their aim to operate within the region, using their Turkish operations as a hub.

### Profile of investors

Foreign investors constituted 54% of the total transaction volume. Foreign investors maintained their position ahead of domestic investors in terms of transaction volume.

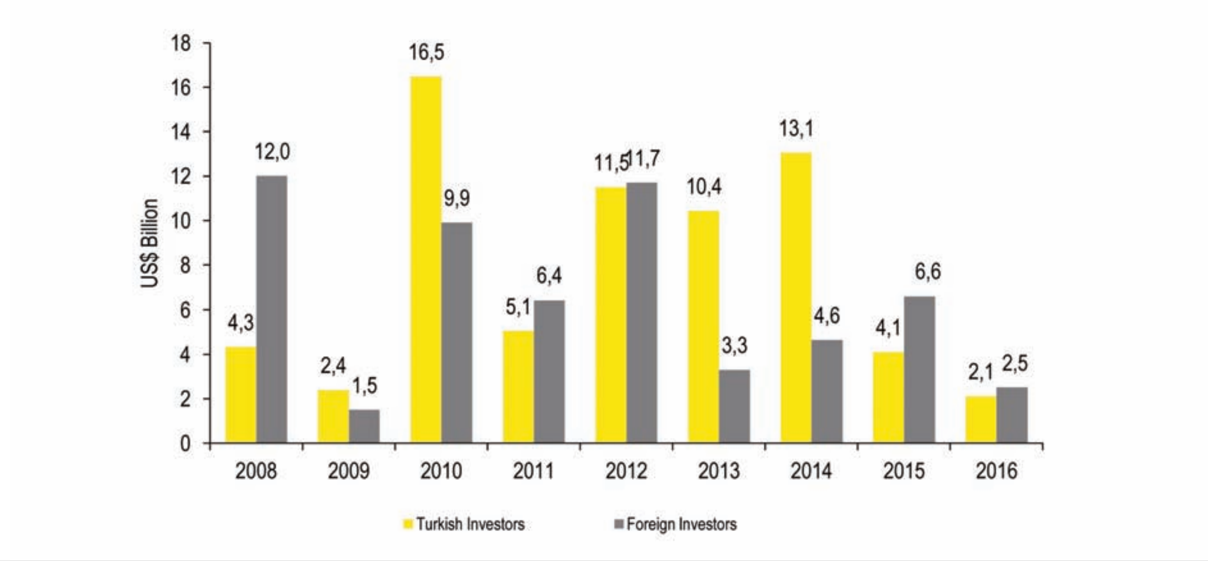
In 2016, while developed economies generally experienced a slowdown in economic recovery, emerging economies recorded lower growth rates and even showed signs of recession. In Turkey, this was also reflected in a decline in the number and volume of M&A transactions compared to previous year. In 2016, we observed a significant decrease in both transaction volume and in the number of transactions. In terms of investors' origin, as they did in 2015, foreign investors outperformed domestic investors and created a transaction volume of US$2.5 billion versus US$2.1 billion. In terms of the number of transactions, domestic investors preserved their comparatively stronger position against foreign investors in recent years with 150 transactions compared to 93 transactions by foreign investors in 2016.

In 2016, although foreign investors' share of total transaction volume decreased again, it still accounted for 54% of the total volume of transactions and still outperformed the domestic investors.

In terms of the number of transactions, foreign investors showed a similar performance to the last seven years, recording a smaller number of transactions compared to domestic investors. in 2016, the total transaction volume recorded by foreign investors accounted for US$2.5 billion.

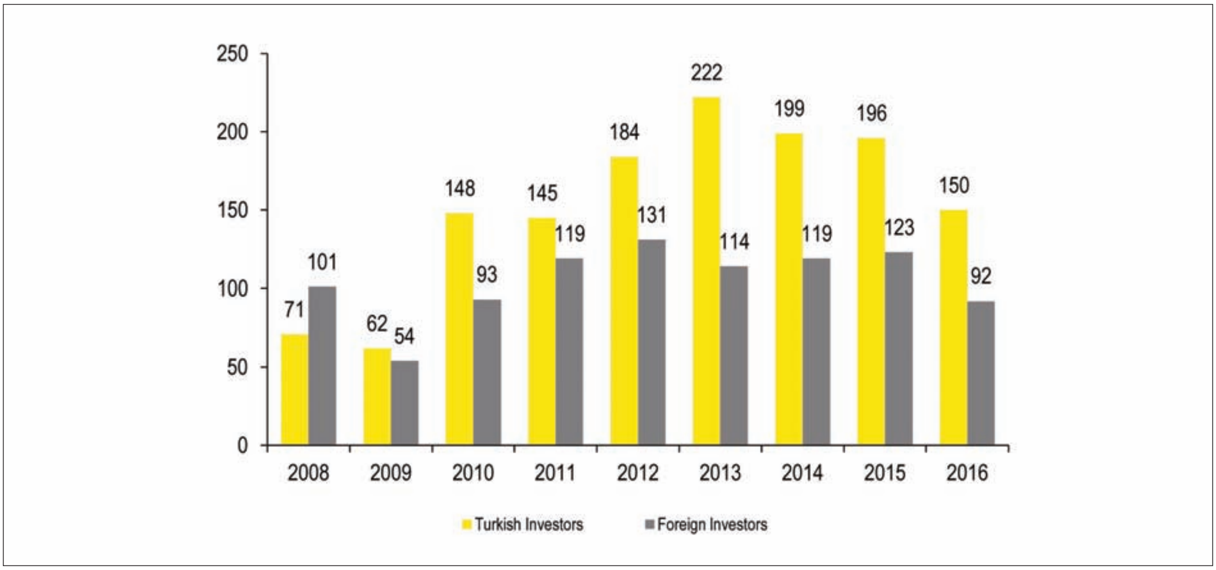
In terms of the number of transactions, in 2016, we observed that it fell to the lowest level in the last five years. Based on transaction volume, domestic investors recorded their lowest performance since 2003.


## BREAKDOWN OF TRANSACTION VOLUME BY DOMESTIC AND FOREIGN INVESTORS




**Source:** *EY Turkey M&A Report 2016*

## BREAKDOWN OF THE NUMBER OF TRANSACTIONS BY DOMESTIC AND FOREIGN INVESTORS



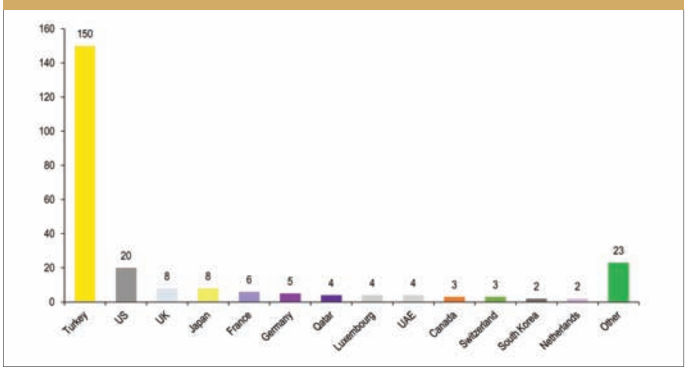

**Source:** *EY Turkey M&A Report 2016*

Based on disclosed transaction values, the average investment size by foreign investors in 2016 was approximately US$68 million (2015: US$179 million). The largest transactions realized by foreign investors were namely; the Mars Entertainment Group-CJ CGV and Odeabank-International Finance Corporation (IFC), European Bank for Reconstruction and Development (EBRD) and private investors. Excluding these two transactions, the average investment size by foreign investors was US$44 million compared to US$68 million in 2015. Hence, we conclude that foreign investors invested in companies that are smaller in size than the previous year.

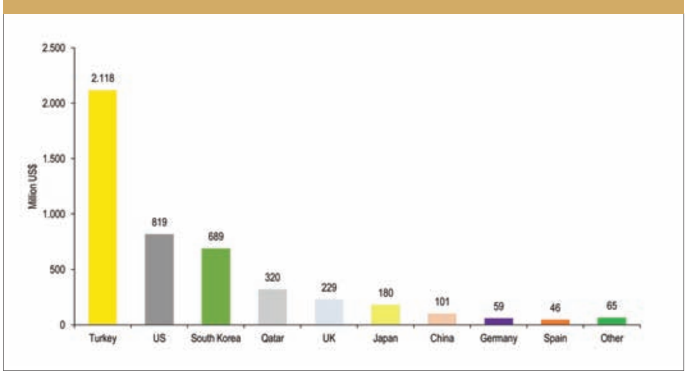
In 2016, the US led the way in terms of transaction volume. In terms of number of transactions US, the UK and Japan stood out among foreign investors.

As in the past, based on the number of deals, investors from the EU and the US dominated foreign investor transactions in 2016. EU countries and the US were followed by Japan, UAE, Qatar, Canada

## BREAKDOWN OF THE TOTAL NUMBER OF DEALS COMPLETED BY ORIGIN OF INVESTORS




## BREAKDOWN OF TOTAL TRANSACTION VOLUME BY ORIGIN OF INVESTORS



and Switzerland. In 2016, the US headed the list in terms of the number of transactions with 20 deals, followed by the UK with 9 deals and Japan with 8 deals. In terms of transaction volume, the US ranked first in 2016 with US$819 million, followed by South Korea with US$689 million. Other than the UK and Germany, other EU countries were not prominent in 2016, similar to 2015. Other countries worth highlighting were Qatar, Japan and China.

### Private Equity investments in Turkey

In 2016, interest in Turkey by private equity funds increased in number but decreased in volume

Private equity interest in Turkey which had risen in earlier years slowed down in 2014, increased in 2015 and again in 2016, with the number of transactions involving private equity funds increasing to 70 (2015: 57 transactions) and the share in the total transactions accounting for 29% (2015: 18%).

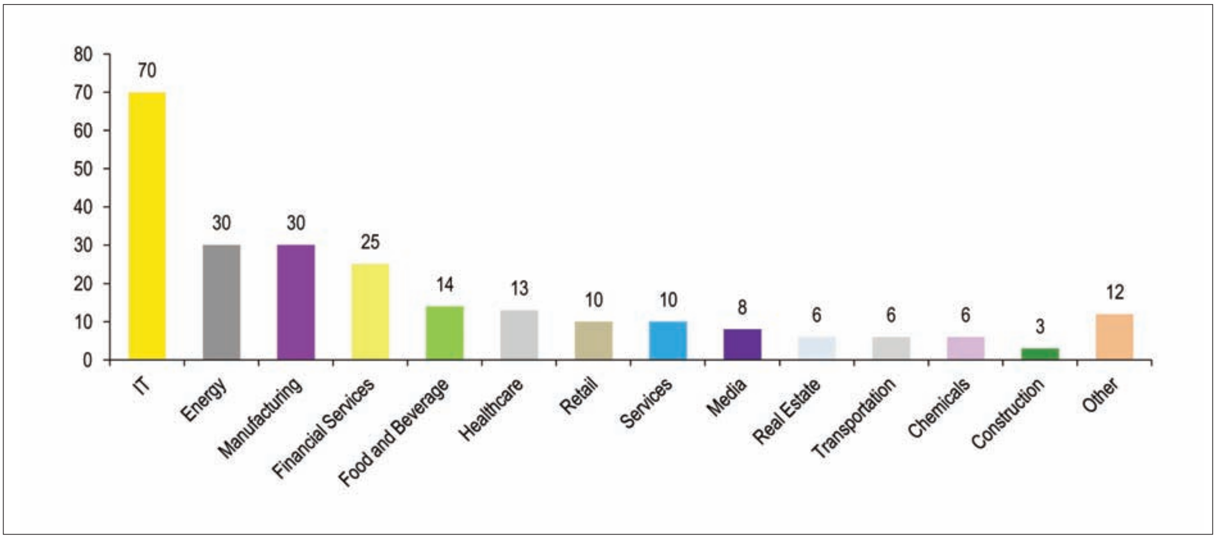
The volume of private equity transactions and the share in the total disclosed transaction volume decreased. Private equity funds executed deals with a total disclosed value of US$331 million in 2016 compared to US$1.6 billion in 2015. Amongst the disclosed transactions by private equity funds in 2016, the transaction with the highest deal value was the acquisition of Peyman by Bridgepoint. Another notable deal amongst transactions with disclosed values was the acquisition of TAB Food Investments by Goldman Sachs and Credit Suisse. Although the deal values were not disclosed, The Abraaj Group's acquisition of 9.95% shares of Fibabanka, Venture Capital Bank's investment in Mado, and Goldman Sachs' investment in Jolly Tour and Gordion Technology were the other significant transactions realized by private equity funds.

### Sectors that receives the most interest by investors

In 2016, as was the case in 2015, the energy sector ranked first in terms of transaction volume and the IT sector ranked first in terms of number of transactions.

Large volume transactions in the private sector, as well as continuing (albeit at a declining rate) privatizations, were the main reasons for the energy sector to rank first in terms of transaction volume this year. Three of the top 10 transactions

## SECTORAL BREAKDOWN OF TARGET COMPANIES IN TERMS OF THE NUMBER OF TRANSACTION




**Source:** *EY Turkey M&A Report 2016*

in 2016 were public sector transactions within the energy sector. In addition, a significant number of private sector energy transactions were realized in line with Turkey's growing energy needs. In 2017, we expect to see privatization of additional energy generation assets as well as intense M&A activity in the private sector.

As a result, we anticipate that the energy sector will continue to attract interest from investors as was the case in the recent years.

Entertainment and financial services were also among the leading sectors in terms of transaction volume in 2016. Manufacturing and the food and beverage sectors both stood out in terms of their transaction volumes and number of transactions, while healthcare and retail sectors were notable in terms of number of transactions alone.

## Overview of Public Sector's M&A Activity in 2016

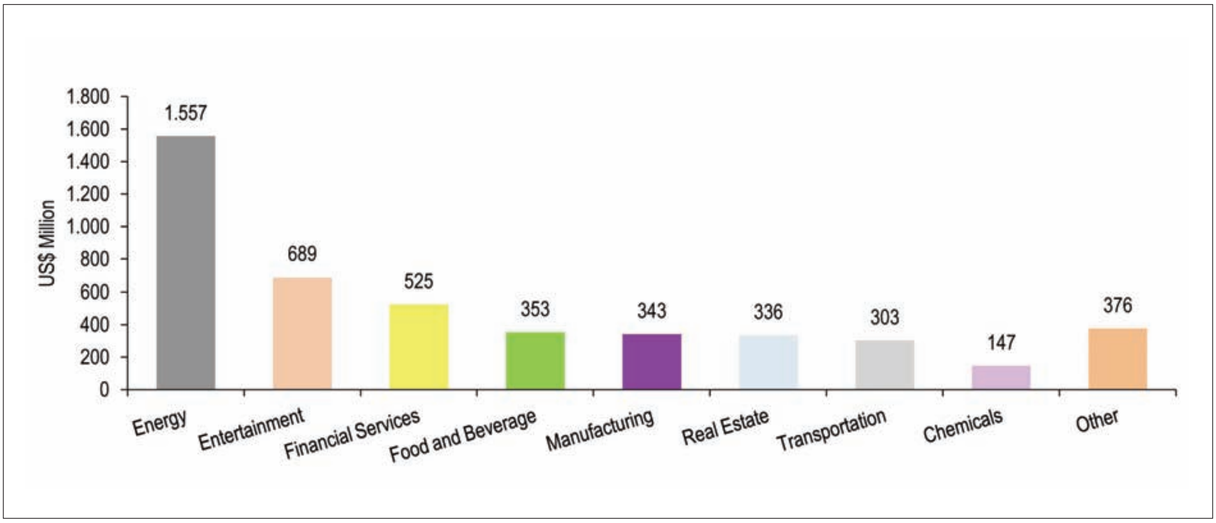
### In 2016, public sector deals constituted 23% of the total M&A volume

Public sector deals totalled US$1.9 billion in 2015, or 18% of the total transaction volume. In 2016, the total transaction volume of public sector transactions decreased to US$1.1 billion, constituting 23% of total transaction volume. The decrease in volume was a result of the failure to execute planned privatizations and tenders for the Transfer of Operating Rights due to security concerns and economic issues in Turkey. In 2016, 83% of public sector transactions were Transfer of Operating Rights, 15% were privatizations and 2% were Savings Deposit Insurance Fund (SDIF) transactions.

In 2016, the most noteworthy public sector deals were; the privatization of the Menzelet and Kılavuzlu HPPs via a Transfer of Operating Rights (won by Akfen Holding for US$400.9 million), the privatization of the Almus and Köklüce HPPs via a Transfer of Operating Rights (won by Gül Energy for US$250.2 million), the privatization of TP Petroleum Distribution won by Zülfikarlar Holding for US$159 million, and the privatization of the Adıgüzel and Kemer HPPs via a Transfer of Operating Rights (won by Bereket Energy for US$115 million). Together these four public sector deals constituted 85% of the total public sector transaction volume.

It is notable that, as in previous years, domestic investors were the main participants and winners of the privatization tenders in 2016. **EDT**

## SECTORAL BREAKDOWN OF TARGET COMPANIES IN TERMS OF TRANSACTION VALUE




**Source:** *EY Turkey M&A Report 2016*

The Headless Gods of

# *Mount Nemrut*

At the junction of the East and West civilizations, Nemrut Dağı (Mount Nemrut) is one of the most astounding sites in Turkey: A collection of colossal statues on a remote mountain 2150m high, adorning the temple and tomb of King Antiochus. Unknown until 1881 when an Ottoman geologist discovered these 10 meter-high stone heads, archaeological work began in 1953 to uncover their history.

Nemrut Dağı has been designated a World Cultural Heritage site by UNESCO, and is one of the most important National Parks in the country. In addition to the statues, the entire site includes art from the Commagene civilization, the Eskikale (Old Castle), Yenikale (New Castle), Karakuş Hill and Cendere Bridge. Most people use the nearby towns of Malatya, Kahta or Adıyaman as a base, and the road to the summit is only open from mid-April to mid-October because of heavy snow the rest of the year.

**The history**

Lying between the Seleucid and the Parthian Empires from 250 BC, this area has had a strategic location, and has benefited from a rich and fertile land, and a succession of independent thinking rulers. Breaking away from the Seleucid Empire, Mithridates I Callinicus founded the independent Commagene Kingdom in 109 BC, and set up his capital in Arsameia. He was the son of a prince, and claims ancestry with Alexander the Great and Darius the Great, King of Persia.

The Commagene Kingdom was a powerful one, priding itself on having religions, culture and traditions of the Greek and Persian cultures blended

into one. He died in 64 BC, and was succeeded by his son Antiochus I Epiphanes, who showed his ability early on as a statesman by declaring a non-aggression treaty with the Romans.

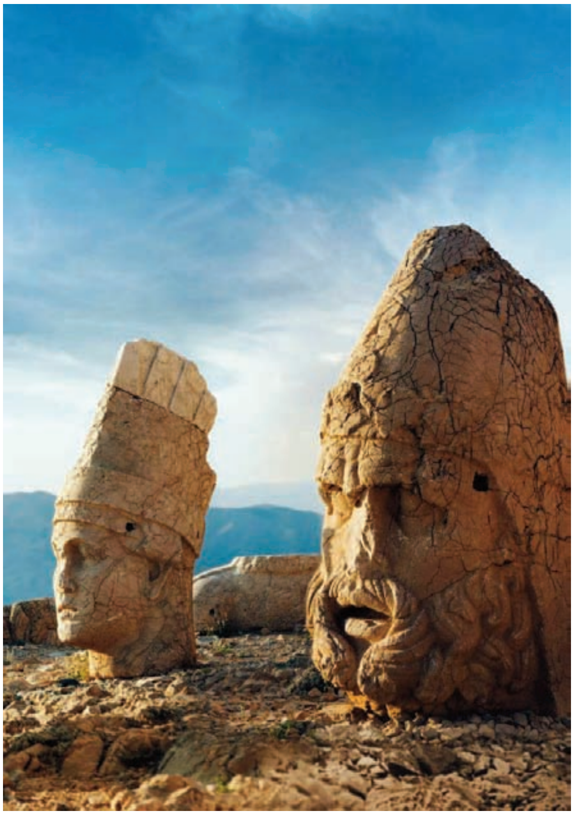
After a financially and politically successful start to his rule, Antiochus deemed himself worthy of god-like status, and ordered the building of a temple and funerary mound in his honor. Its size and location was a reflection of his ego and thoughts of his immortality, and he declared that when he died his spirit would join the god Zeus in heaven.

But the huge statues of Antiochus and the gods are all that remain of his reign, as his short-lived rule ended in 38 BC after he sided with the Parthians and fell out with the Romans, who later deposed him. The Commagene Kingdom was then taken over by the Romans.

Antiochus and his statues were all but forgotten for centuries until Karl Puchstein, a German engineer, stumbled across them whilst surveying the site in 1881. Two years later he returned with Karl Humann for a closer inspection, but it was not until 1953 that a team of American archaeologists returned and did a thorough survey. Since then, the site has been one of the most popular attractions in Turkey, despite its remote location.

### Karakuş Tumulus (Women Monument)

This 35m high monument was constructed by Mithridates II, as a memorial to his mother Isas. Situated 10km north of Kahta at the entrance to Nemrut Dağı, it was created to hold the royal ladies of Commagene. Four columns surround the site, each around 10m high, and surmounted by the large figures of an eagle and a lion.



### Climate

For visitors hiking to the top of Nemrut Dağı, the top of the mountain gets very cold at sunrise and sunset, even in summer. The higher land is snow covered for nearly half the year. Otherwise, the summer daytime temperature of the plains is extremely hot and dry reaching over 30 degrees, with winter's cold and wet and plummeting well below freezing point.

### How to get?

By Road: Because of its remote location, there are many private bus tours operating from the nearby towns of Malatya (100km), Adıyaman (80km) and Kahta (43km), all of which are well connected with the rest of Turkey. The road approaching the summit is very steep and rough and not easy to drive, so most people prefer to take an organized bus tour which will visit the site in a day trip, or perhaps an overnight to see the ruins at sunset/sunrise.

**By Air:** The nearest domestic airports to the site are at Adıyaman, Malatya and Şanlıurfa, from where buses can be arranged. **EDT**

# A COUNTRY OF VAST POTENTIAL AND RESOURCES

For 64 years now, investing in Turkey's potential has been at the core of our strategy for community banking, a mission stemming from our foundation. We have been working continuously to support local production and investments, expand financial inclusion, create awareness of energy efficiency and ensure access to financial resources for all farmers and SMEs.

**We will continue to trust and invest in Turkey's promising future; with its entrepreneurial spirit, youthful population, vast geography and production capacity.**

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