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ECONOMY'S OPENNESS RESULTS IN A HIGH TRADE VOLUME SHARE IN TURKEY'S GDP

New momentum in Turkish economy

ANALYSIS

By İbrahim Öztürk

TODAY'S ZAMAN

The Turkish economy sustained three successive economic crises in the 1990s. The economic crisis in 2001, however, was the low point of this trend -- the economy contracted more than 5 percent. Since then, Turkey has implemented a comprehensive structural reform package coupled with sound monetary and fiscal policies to establish macroeconomic and financial stability and improve the business environment.

The reform agenda's critical milestones were the central bank's legal independence, the introduction of a free-floating exchange rate regime in 2001 and an inflation-targeting regime in 2002.

This program has helped Turkey succeed in a significant process of disinflation since 2001. Briefly summarizing some of these achievements aids in understanding the process from this point on.

First, the basic macroeconomic indicators improved notably. After 24 quarters of successive high growth (2002-2007), the real gross domestic product (GDP) grew almost 50 percent on a cumulative basis, bringing the average annual growth rate to 7 percent. Also, the GDP rose to $658.7 billion in 2007 (from $196.7 billion during the 2001 crisis), making Turkey home to the world's 17th-largest economy. Parallel to this, per capita GDP exceeded $9,000 (in terms of Purchasing Power Parity [PPP] $13,000) by the end of 2007.

Sources and characteristics of growth

Return of the private sector: The first striking characteristic of such speedy growth: It was powered by the private sector.

Returning to the age of productivity, the new growth process is supported by continuous productivity gains. In fact, the labor productivity index rose to 170 in 2007 from 100 in 2001 and total factor productivity rose to 45 percent between 2002 and 2005 from almost just 3.3 percent throughout the 1990s. It is therefore not surprising that Turkey recorded a significant decline in inflation while achieving high annual growth of average 7 percent between 2002 and 2007.

Openness, integration and convergence: Third, the Turkish economy's openness has resulted in a high trade volume share in GDP. For instance, exports, which stood at only $31.3 billion in 2001, increased by more than twofold in 2007, reaching $107 billion; imports increased to $160 billion from $41.4 billion. CONTINUED ON PAGE 08

PHOTO TARIK ÖZTÜRK

Economy Minister Mehmet Şimşek

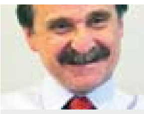
Şimşek: Turkey does not need new agreement with IMF

ABDULHAMİT YILDIZ / ERCAN BAYSAL, ANKARA

Turkey is entering a new era in terms of its relations with the International Monetary Fund (IMF) as the country's current stand-by agreement approaches its end in May. The government has accomplished two consecutive programs for the first time in Turkey's history and plans to sign a letter of intent with the IMF in the third week of May.

Turkish Economy Minister Mehmet Şimşek says the government is hoping to finalize the last IMF review this week and that Turkey does not need another stand-by agreement thanks to its current economic condition. "Turkey's financial figures are pretty strong. Turkey does not need any urgent financial input given its reserves, budget performance and privatization performance," Şimşek explains.

Minister Şimşek spoke to Today's Business last week and evaluated the recent transformation of the Turkish economy. Şimşek says Turkey has four alternatives regarding its relations with the IMF: The first option is to sign a new stand-by agreement to cover urgent financial needs. CONTINUED ON PAGE 11



Tahir Uysal

Reforms increase investor confidence, spur FDI

TAHİR UYSAL / YASED CHAIRMAN

High levels of investor confidence have been generated mainly by the political and macroeconomic stability achieved in the last five years owing to a commitment to structural reforms, efforts for the improvement of the investment environment and the start of accession talks in the European Union membership process.

On the global level, high levels of liquidity and a surge in merger and acquisition (M&A) activities have provided a favorable and supportive environment for an increasing trend of foreign direct investment (FDI) inflow to Turkey, with mega deals of record-high value taking place. Turkey climbed to 16th place among top FDI-attracting countries in 2006, up from 53rd place in 2003, 38th place in 2004 and 23rd place in 2005. CONTINUED ON PAGE 14

Islamic banking: After consolidation comes further growth

PAUL WOUTERS, İSTANBUL

Every economy faces the challenge of raising enough liquidity to finance and sustain sufficient growth. Money only flows in suitable streambeds, and that is what most governments try to regulate and supervise.

But even then it remains a big task to entice international finance to come to your particular country. The competition for available funds is indeed fierce. There is an additional need for the right equilibrium between market regulation and economic growth momentum. Turkish politics used the last six years to grow financial compliance and governance to international standards. CONTINUED ON PAGE 07

PHOTO ONUR ÇOBAN

Turkey has not been significantly affected by the subprime crisis, but it has started to feel the pressure of the credit squeeze and other side effects.

TURKEY WEATHERING CURRENT CRISIS ARMED WITH LESSONS FROM 2001

İBRAHİM TÜRKMEN, İSTANBUL

There is almost unanimity among analysts that thanks to the lessons Turkey learned from the big financial crisis in 2001 and the policies it adopted as a result, the financial and capital markets are much stronger now than they were seven years ago. Reşat Karabıyık, the general manager of Turkey's leading securities company, Bizim Menkul Degerler (BMD), says that if the level of turbulence currently being experienced in Turkey had hit the markets in 2001, the share of foreign ownership in the stock market would have fallen by more than 50 percent.

Karabıyık spoke to Today's Business last week and shared his opinions on the current conditions of the Turkish capital markets and the recent global and domestic developments affecting them.

He said the economic and political spheres in Turkey have always been intertwined, causing the economy to sneeze if the politics get cold. But there is a rapid process of normalization going on, he added: "Let's assume that there was a closure case against the governing party some 10 years ago while a terrible global crisis was hitting the capital markets everywhere in the world. CONTINUED ON PAGE 06

Turkish factoring industry set to grow with exports

MICHAEL KUSER İSTANBUL

Factoring in Turkey is a relatively new financial service industry dating back to the late 1980s. Factoring operations first began as departments within commercial banks, which then converted those operations into separate companies in the early 1990s.

Worldwide, the main trade associations are Factors Chain International (FCI) and the International Factors Group (IFG). Statistics from these organizations show that factoring volume increased last year by almost 15 percent, compared to almost 12 percent in 2006. The world total now stands at 1.3 trillion euros.

International factoring has grown even faster, in excess of 40 percent in 2007. FCI attributes last year's particularly high growth rate to the decision to include figures for export invoice discounting. "According to the definition of international factoring, export invoice discounting is not export 'factoring' as only one service element is provided, namely finance," the group said in its annual report. CONTINUED ON PAGE 10

VOB exec says global crisis changed how foreign investors see Turkey'

ALİ RIZA KARASU İZMİR

Exchanges trading in futures and options contracts are likely to offer investors and enterprises alike a more secure option than over-the-counter markets in times of global economic crisis, according to Çetin Dönmez, general manager of the İzmir-based Turkish Derivatives Exchange (VOB).

Noting that political stability is essential for market stability, Dönmez indicated that foreign investors retain a bright outlook in terms of Turkey's future. He argued that Turkey's financial structure is far better than in the past and that foreign investors are well aware of this reality. Even investors from developed countries, who always regarded Turkey as a risky country in the past, have come to realize that there are higher risks in their own countries than the perceived or estimated risk in Turkey.

Dönmez said the products processed at VOB will be diversified, noting that it has shown significant progress since it was established in 2005. VOB allows the online trade of futures and options contracts and is the first private exchange in Turkey. Its shareholders include the Turkish Union of Chambers and Commodity Exchanges (TOBB), İzmir Commercial Exchange (İTB), the İstanbul Stock Exchange (İMKB), the Association of Capital Market Intermediary Institutions (TSPAKB), Akbank, Garanti Bank, İş Yatırım Menkul Değerler, İMKB Clearing and Custodian Bank, Turkish Industry and Development Bank (TSKB), Yapı ve Kredi Bank and Vakıf Yatırım Menkul Değerler. VOB has four markets: shares, foreign exchange, interest and commodity.

The YTL/$ and YTL/euro rates are applied for foreign exchange futures contracts while DİBS 91, DİBS 365 indices and the benchmark DİBS indices are used for interest contracts. Under the index contracts are the İMKB-30 and İMKB-100 indices, while the commodity futures contracts have cotton, wheat and gold contracts.

Compared to worldwide practices, VOB's product diversity is considerably limited. However, it has exhibited outstanding performance. In its first year, VOB's transaction volume was about 1 percent of that of the İMKB. However, this rate rose to 10 percent by the end of 2006, and to about 60 percent by the end of 2007. Its total transaction volume, including position closures, was YTL 3 billion in its first year, rising to YTL 17 billion in 2006 and YTL 117 billion in 2007, indicating a six-and-a-half-fold increase.

Foreign investors' interest in VOB has also increased. In March 2008, local investors accounted for 76.26 percent of the total transaction volume, while foreign investors accounted for 23.74 percent of it.

Dönmez, who worked at the İMKB Department of Risk Management before joining VOB as general manager, pointed out that there is a worldwide trend for growth in futures markets. The latest economic fluctuations will boost interest in these markets, he noted, adding that this will accelerate the trend in the US and Europe favoring the development of unaudited and over-the-counter markets into exchanges. VOB will have its share of these, Dönmez forecast, saying he anticipated a twofold growth in VOB's transaction volume in 2008.

New products based on share, foreign exchange and interest-based futures and options contracts will be introduced, he noted, adding that they have given a time period of about two years for the opening of transactions of options contracts. The newly founded VOB has shown considerable growth compared to the İMKB because VOB is a private company, he observed. Stressing that VOB is a joint stock company, he noted that the executive board is "able to make quick and flexible decisions."

He suggested that the recent global economic crisis had added to the risks in financial markets and that, just like human beings, countries have memories: "In our country, the word 'crisis' brings a rise in interest rates and foreign exchange rates to mind. The US fears a worldwide economic crisis just like the one in 1929, while the Germans are afraid of high inflation. This is the main reason why the US Federal Reserve is pumping money into the markets. Since the ruling politicians and bureaucrats in the US are scared of the economic recession ingrained in the country's collective memory, they have taken such decisions, risking a rise in inflation."

Dönmez indicated that the current crisis will give birth to new measures that may include new arrangements for unaudited funds. For him, this crisis has changed the way foreign investors tend to regard Turkey, showing them that it is not as risky as it is generally perceived to be. "Those who treat Turkey as a country with high risks have come to realize that their own countries, too, are as risky as Turkey," he explained.

Stressing that Turkey has a bright future, Dönmez suggested that the country's financial structure is now much healthier than in the pre-2001 period: The country was lucky in that interest rates were higher when fluctuations started in the markets due to the strict interest rate policies of the Central Bank of Turkey. He argued that high interest rates have served to soften the impact of the fluctuations by halting the outflow of money from Turkey. A recent statement by the central bank, hinting that rates might be raised further, should be seen from this perspective, he noted.

"Just like any country around the globe, Turkey will be affected by this crisis," he said, citing Turkey's being surrounded by oil producing countries as an advantage.

Dönmez likened the risks in the financial markets to earthquakes and stated that the closure case brought against the ruling Justice and Development Party (AK Party) should be viewed from this perspective. Noting that political stability is one of the most important criteria for investors, he added: "Currently, the closure case is a risk, but in the future, there will be other risks. What is important is that you should take measures against these risks." A number of incentives will be introduced to boost interest in VOB, which offers important opportunities, particularly for the non-financial sector and small and medium-sized enterprises (SMEs), he revealed.

VOB investors currently benefit from a number of tax exemptions. There will be no withholding tax on income arising from value increases obtained from futures contracts until Dec. 31, 2008, Dönmez noted, citing tax exemption as a precondition for the development of the exchange. He also stressed the importance of incentives in terms of the banking insurance transaction tax (BSMV), arguing that there is a high possibility of outflow of money from Turkey due to rising costs attributable to the BSMV.

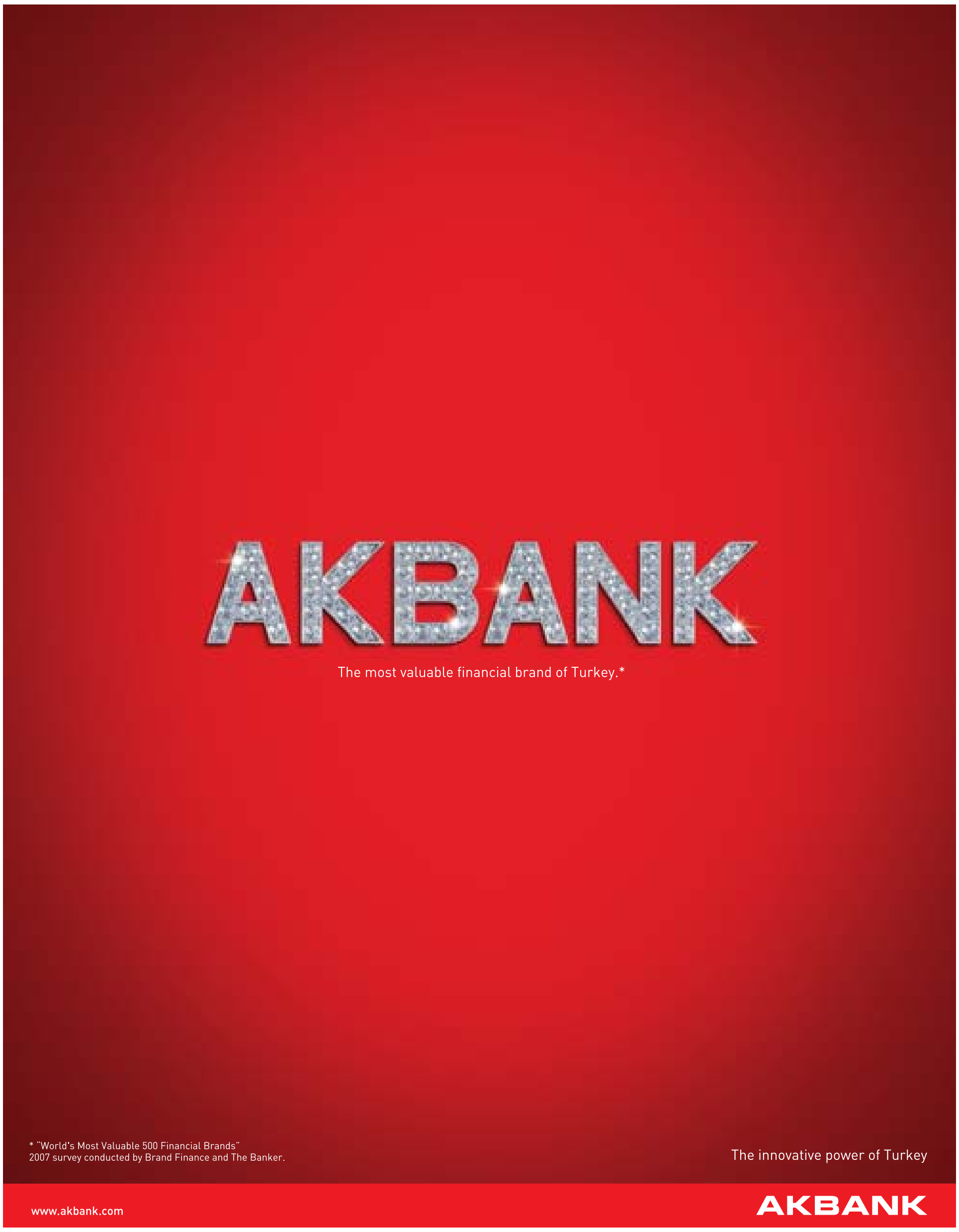


PHOTO TODAY'S ZAMAN

Turkish Airlines (THY) is among companies to benefit the IPOs most. Its Chairman Temel Kotil (L) enjoys looking at the details of new aircrafts THY has bought.

Running capital markets in favor of the corporate sector

ANALYSIS
Professor Çelik Kurtoğlu
TODAY'S ZAMAN

The İstanbul Stock Exchange (İMKB) was established in the mid-1980s; the number of companies represented on it today has exceeded 300. Considering its current level, the İMKB has the proper infrastructure legally and physically for further growth and for the ability to cope with modern problems. Legislation pertaining to capital markets in Turkey has developed in accordance with international standards, including governance-related issues initiated by a crisis following the Enron scandal in the US. Such issues include the corporate governance principles, which are fully in line with international practices, and the corporate governance index, which has recently become operational.

Few Turkish companies have made use of the entire set of capital market instruments. They have often resorted to more expensive bank financing, which has also limited their growth potential.

Principal reasons include the high rates of inflation and interest that discouraged bond issuances. They also caused many companies to be reluctant to improve their financial reporting standards and the low degree of floatation in the market.

Very few companies have agreed to offer more than 20 percent of their equity in the stock market. The major reasons behind this situation include family ownership and restriction to buy back shares to a treasury account. A draft commercial code offers major changes which will contribute to the quality of governance and enable companies to buy their own equity.

Political and economic instability, together with low floatation have limited foreign institutional investment in the İMKB. This has incurred another result whereby institutional investors lacked the urge to monitor their equity investment, hence the absence of a proxy mechanism did not help improve the İMKB's performance quality.

Finally, the corporate governance index has not yet delivered its expected results. The Brazilian and Italian experiences have shown that the index beats the principal index, which has not yet been the case at the İMKB. The weight of the financial institutions in the İMKB index is very high and they have not yet had their corporate governance quality rated.

Returning to observation as to the fundamentals of the İMKB, it would be fair to say that it is up to the Turkish companies to increase their transparency and the amount of float, and hence benefit from the advantages of the capital markets. We have reason to believe that this will happen as requirements of traditional bank financing become more stringent and companies recognize the advantage of capital markets. Increasing institutionalization in family-owned companies will of course make the more substantive contribution to this process.

Foreign investors in Turkey share domestic concerns about future

PHOTO TODAY'S ZAMAN

Ziya Akkurt

İBRAHİM TÜRKMEN İSTANBUL

There is no longer any difference between foreign and domestic interests in Turkey in terms of concerns about the country's problems, says Ak Securities General Manager Ziya Akkurt; both are connected to Turkey by billions of dollars.

He used a Turkish proverb, "They have put their hands under the rock," in reference to the fact that foreign companies all have responsibilities that cannot easily be given up solely because the economy has hit a rough patch. "We almost share the same sensitivities, and there is no longer a clear line delineating a foreign investor from a domestic investor," he said.

Akkurt was speaking to Today's Business last week about recent global and local developments. He mentioned the closure case against the Justice and Development Party (AK Party) filed by the chief public prosecutor of the Supreme Court of Appeals and criticized the action as "shooting oneself in the foot."

"There was no need to sink into such a bad crisis, particularly when the world is staggering under severe turbulence," he claimed. But the responsibility does not lie solely on the shoulders of one side; it is shared equally by both the prosecutor and the AK Party, who contributed to the tense atmosphere with their uncompromising attitude. "Everyone is to blame on this issue, as nobody has done their duty properly," he added.

The economy is being seriously tested both internally and externally, but has so far proven more durable and far stronger than in 2001, Akkurt asserted. He recalled that the financial crisis then had stemmed from a liquidity crisis, but soon started to impact the banking sector. There was a chain reaction that triggered problems in the Turkish Central Bank. Then the troubles spread to the non-financial sectors, marking the point at which the national economy fell prey to the destructive effects of the crisis.

Akkurt claimed that the 2001 crisis was a structural crisis; thus the structural reforms of the time helped the country recover. Akkurt underlined the role played by the industrious Kemal Derviş (now head of the United Nations Development Program, UNDP), appointed economy minister by the coalition government despite not being an elected member of Parliament.

The acceleration gained through the determined steps taken in this post-crisis period helped Turkey to move in step with the global economy, and the positive course it set out on then is still being followed, despite some slight deviation from the main route, Akkurt said.

For him, the main factor behind Turkey's successful recovery was the financial discipline enforced through an International Monetary Fund (IMF) stabilization program and Turkey's loyal commitment to a stand-by agreement deal with the IMF.

At this point, Akkurt opened a parenthesis to share his opinions on the new course of relations with the IMF following the completion of the current program in May. The program has so far helped Turkey find remedies for tenacious diseases. "Turkey's economy was integrated into the world economy thanks to this program. Political figures have been removed from the operation of the economy, since this program forced the privatization of state assets," Akkurt noted, citing a couple of examples of the diseases the Turkish economy had been suffering from.

He recalled the haggling of politicians over the sharing of the management of state-owned corporations. "This was at the root of many corrupt practices, such as bribery and malversation. Thus we could claim that the 2001 crisis was beneficial to the nation, as it caused such bad habits to be eradicated. It cost us a great deal, but in the end it was good," he said.

He noted that Turkey's economy is now strong enough to weather political unrest. This stability is being tested by the political tremors of the closure case filed against the Justice and the Development Party (AK Party) and is being rocked by the turbulence of the global crisis, but it is still enduring these shocks without much loss, Akkurt noted. "For example interest rates have hovered between 15 percent and 18 percent for a long time. If there had been the old structure, they would have already soared to over 40 percent. The exchange rates would have already skyrocketed," he added.

Akkurt also gave his opinion on the current turbulence in global markets, which began last year as a problem in the US mortgage market caused by subprime loans, but later took the whole world in its grip. "I believe what is going on is the starting point of a structural transformation in the global markets," he noted, clarifying that in this model new financial powerhouses are on the ascent. Wealth is no longer accumulating in certain locations like Western Europe and the US as it did traditionally; it is moving to other locations such as the Middle East and China.

Akkurt also touched on sovereign wealth funds (SWFs), which, with trillions of dollars of assets, have risen as important players during the recent crisis. He quoted the famous Turkish saying "History is made up of recurrences," noting that SWFs were resurrecting state capitalism again, long after its demise, since SWFs largely comprise state funds and central bank reserves. In the past, major European countries and the US purchased the economic assets of underdeveloped nations by exploiting their capital-based might; now the same is being done by the third-world countries of the past, he explained.

He also noted a difference between the crises of old and the current troubles: "In the past, crises were more local, but now they are happening on a global scale. The entire world is entering a crisis simultaneously, and it is exiting it more or less at the same time. It has happened this way thanks to the increased levels of interdependence and faster means of communication. There is the Internet now."

As a final remark on the international economy, Akkurt made a bold prediction that the next wave of crisis might stem from Africa, as this continent still needs to take a lot of major steps in order to catch up with the rest of the world.

FDI inflows surge in the context of Turkey's new competition law

ANALYSIS

By Alper Fevzi Kara*

TODAY'S ZAMAN

The introduction of competition law in Turkey is the result of the country's international obligations led by two overwhelming dynamics. The first dynamic has been a wave of globalization which resulted in a tendency toward the worldwide harmonization and adoption of competition law all over the world. One of the most obvious instances where this tendency took shape was in the World Trade Organization's (WTO) Uruguay round of negotiations: As the developed world agreed to gradually reduce customs duties for exports of developing countries, the latter, in return, pledged to incorporate intellectual and industrial property rights and competition law into their legislation for the sake of opening up to the league of free market economies in the true sense of the word.

Apart from this global effect, the second dynamic had a rather Turkey-specific imperative; namely, Turkey's quest for European Union membership. In fact, articles 32, 33 and 41 of the March 6, 1995 Association Council decision No. 1/95 provided Turkey competition rules to be applied for the proper functioning of the customs union agreement. These articles are actually identical to those which outline the framework of EU competition law, namely articles 81, 82 and 86 of the EC Treaty.

Accordingly, Turkey put into effect the Act on the Protection of Competition No. 4054 as of Dec. 7, 1994 and the executive body, the Turkish Competition Authority, started functioning on March 7, 1997.

Turkish competition law urges the Competition Authority to focus on three main areas of intervention:

■ Agreements, decisions and concerted practices of undertakings that cause the prevention, distortion or restriction of competition.

■ Abuse of a dominant position by big companies.

■ Mergers and acquisitions, which would give or strengthen the status of the dominant position of those involved in the market. The law requires that the parties to a particular merger or acquisition should report the transaction to the Competition Authority before it takes place if their combined market share exceeds 25 percent or their combined aggregate turnover amounts to more than YTL 10 billion.

FDI inflows in relation to competition law

According to numerous studies by the World Trade Organization (WTO) and the Organization for Economic Cooperation and Development (OECD), for which the 1998 OECD communiqué to the WTO can serve as a good example, there appears to be wide consensus that:

■ Foreign direct investment (FDI) is the most important channel through which advanced technology is transferred to developing countries and thus efficiency is enhanced.

■ FDI has the potential to rapidly restructure industries at a regional or global level and to transform the host economies into prodigious exporters of manufactured goods or services to world markets.

■ FDI can serve to integrate national markets into the world economy far more effectively than could have been achieved by traditional trade flows alone and thus help them respond to global economic opportunities.

Noting these benefits, the United Nations Conference on Trade and Development (UNCTAD) added in its 1997 World Investment Report that a liberal FDI regime must be complemented by rules on competition in order to have such benefits maximized. As that report suggests, macroeconomic stability and the implementation of a transparent competition law and policy have become the trademark of a functioning free market.

As a matter of fact, open policies toward FDI and properly functioning competition polices are mutually supportive. On the one hand, the overarching policy goal of competition law is not to protect domestic firms from foreign competition, but to ensure competitive domestic market structures and the efficient allocation of resources by prohibiting practices that restrain competition or create barriers to new entrants. Therefore, in the absence of a competition law, the most efficient foreign producers may not be able to penetrate a market due to discrimination in favor of domestic enterprises.

PHOTO ONUR COBAN

Saudi Oger owner Muhammad Hariri (L) hands a check to Finance Minister Kemal Unakıtan for Türk Telekom.

As liberal investment policies and an effective competition law in place make markets contestable, the entry of multinational companies (MNCs) might have the effect of breaking up a comfortable domestic oligopolistic market structure, reducing the likelihood of cartels and monopolies.

MNCs expect competition authorities to ensure a level playing field between domestic and foreign firms. However, when considering the prospect of investing abroad in a developing economy without a well-established competition law, foreign investors face the uncertainty of not knowing if and when competition legislation will be introduced and, perhaps more importantly, how it will be implemented. So, it is argued that an economy that has an effective competition law, especially one in which competition rules are consistent both in letter and application to those prevailing in major jurisdictions, most notably the EU and the US, is in a better position to attract FDI than one that has not.

In this respect, that Turkish competition law has been modeled after EU competition law can be considered an advantage for Turkey. This is so because a foreign investor may easily grasp the legal system in Turkey and find himself in a familiar legal environment. Indeed, that 66.2 percent of FDI inflow ($12.7 billion) to Turkey in 2007 came from EU countries speaks volumes about the already arising effects of this advantage.

In addition, the need for competition law is also evident once MNCs penetrate the market, as the impact of FDI is not always pro-competitive. This time around, competition law would have to fight against abuses of market power by MNCs which might result in monopoly profits, lower efficiency and entry barriers for potential competition. It is also often the case, where the affiliates of two separate MNCs compete with one another in a particular market. Subsequently, the parent companies overseas decide to merge. With the affiliates no longer independent of each other, competition in the host country may virtually disappear.

In the face of adverse consequences brought about by such mergers and acquisitions, competition law again proves to be the remedy.

FDI's current status in Turkey

Even in the recent past, such as at the turn of the new century, the interest of FDI to Turkey used to be at modest levels, between approximately $500 million and $900 million yearly. In 2000 Turkey could hardly attract one-thousandth of the whole of FDI spread around the world. However, from 2003 on, thanks to an ardent campaign of structural reforms, Turkey made impressive strides and rose to the upper league of countries that attract an FDI of $20-$30 billion on a yearly basis. The inflow of FDI entered the country through privatizations, mergers, acquisitions of private sector companies and banks, and real estate investments. In 2007 the net FDI hit a fresh record of $21.9 billion.

According to an UNCTAD report, Turkey now takes a nearly 2 percent share of the world's FDI. Just seven years ago, in the developing world, Turkey had a 4.5 per 1,000 share of FDI inflows. Now, this ratio has also expanded to nearly 5.5 percent.

There is no doubt that this outcome came about on the back of well-managed structural reforms among which the role of an effectively executed competition law should not be underestimated. As a matter of fact, the Competition Authority's activities and efforts are highlighted in a positive manner in EU progress reports on Turkey, published yearly. In these reports, the implementation of competition law stands out as one of the rare chapters where Turkey is ready and confident enough to engage in full integration with the EU.

* *Alper Fevzi Kara is an expert on competition law and policy.*

PHOTO KÜRŞAT BAYHAN

Hüseyin Erkan

İstanbul Stock Exchange at a glance

HÜSEYİN ERKAN*

The origin of an organized securities market in Turkey has its roots in the second half of the 19th century, when in 1866 the Ottoman Empire's first securities market was established, bearing the name the Dersaadet Securities Exchange.

However, Turkey had to wait until the early 1980s for the establishment of the stock exchange in its modern form. A government decree with the force of law foreseeing the establishment of securities exchanges in Turkey was issued in October 1983. One year later, in October 1984, the "regulations for the establishment and functions of securities exchanges" was published in the Official Gazette. Regulations concerning operational procedures were subsequently approved, and the İstanbul Stock Exchange (İMKB) was formally inaugurated at the end of 1985.

Stock trading on the İMKB started in its first, small building in January 1986. Stock exchange indices were calculated on a weekly basis at the time. The settlement and clearing center was established in July 1989, which in 1992 was transformed into an independent company. The bonds and bills market was established in 1991. In 1994 daily trading was extended to four hours, and in the same year trading was fully automated. In 1995 the bourse moved to its new building in İstanbul's İstinye district. The İMKB Web site was launched in late 1996.

In 1998 the İMKB started to disseminate market depth data, setting a milestone in terms of transparency. In 1999 the new computerized trading software for the bonds and bills market, which had been developed as part of a wide area network (WAN) project, was completed and put into operation.

In 2000 the İMKB started trading on a WAN through workstations located at intermediaries' headquarters. In 2004 the Exchange Traded Fund (ETF) market was established to provide an organized and transparent market for trading participation certificates of ETFs.

In addition to stocks, fixed income securities are traded on the İMKB. The bonds and bills market was opened in 1991 with outright purchases and sales. One year later, in 1992, corporate bonds and revenue-sharing certificates started to be traded in the bonds and bills market. In 1993, a repo/reverse repo market was founded. Today, the average daily trading volume on the İMKB bonds and bills market is over $10 billion, and it is the fifth largest market in the world in terms of trading volume.

Currently, 319 companies are traded on Turkey's stock market, with a market capitalization of $201 billion. The average daily trading volume on the stock market stands at $1.2 billion. The İMKB is the 29th largest market in terms of trading volume. Since its foundation the İMKB has provided funds totaling $37 billion to the Turkish economy.

The İMKB was recognized as a designated offshore securities market by the US Securities and Exchange Commission (SEC) in 1993 and as an appropriate foreign investment market by the Japan Securities Dealers Association (JSDA) in 1995. The İMKB is an active member of the main securities markets federation, the World Federation of Exchanges (WFE), and has other prominent alliances. The İMKB has protocols for cooperation with numerous exchanges, including those of Great Britain, South Korea, Kyrgyzstan and others. The İMKB is also a shareholder of the Kyrgyz and Azerbaijani stock exchanges. Back in 1995 the İMKB initiated the foundation of the Federation of Euro-Asian Stock Exchanges (FEAS), which currently has 32 stock exchange members from 29 countries and eight central securities depositories as affiliate members.

The İMKB's future prospects include establishing a technology center which will facilitate the efficient functioning of capital markets in Turkey, build a common electronic trading platform and secure an efficient margining and integrated risk management surveillance system. These will help develop an efficient network through which all capital market institutions will communicate with each other, increasing the İMKB's competitive strength and developing a structure that will ensure an immediate and sound reaction to external shocks as well as a decrease in overall transaction costs in the market. The İMKB aims to strengthen the supply side of the stock market by proactively promoting initial public offerings.

** Hüseyin Erkan is chairman and CEO of the İstanbul Stock Exchange.*

Markets await cues from Federal Reserve

What a difference six weeks makes. Right before the last Federal Reserve meeting, investors were worried about the global banking system imploding. Now, investors are betting the credit markets are on the mend and Wall Street is looking forward to an economic recovery. But the market wants to hear this week that the Fed is confident, too.

The central bank's policy makers meet today and tomorrow to decide whether to lower interest rates again, and to issue an updated assessment of the US economy and financial system. Most investors believe the Fed will lower rates by another quarter percentage point but will also suggest they are gearing up for a pause. "There's enough mixed signals out there that now's the time to put that forward," said Kurt Karl, chief US economist at Swiss Re, referring to mediocre-but-not-horrific readings on the economy and corporate profits that have helped bring some stability to the stock market.

Already, the central bank has incrementally reduced the key federal funds rate by 3 percentage points since last summer, to 2.25 percent from 5.25 percent. On top of rate cuts, the Fed has been lending more money to banks, while the government is preparing to send out tax rebates. "There's just an awful lot in the pipeline, and it takes time to work," Karl said. Rate cuts at the federal level typically take at least six months to start affecting the broader economy.

But while Wall Street finally appears ready to hear that rates might stay put, a halt to rate cuts would not be a completely positive sign. Sure, it would suggest that the Fed believes economic risks are easing, but it would also indicate the central bank is growing more worried about the threat of inflation.

It is not uncommon for inflation to flare up in the early part of a recession, and then pull back as the economy weakens further. But considering how high prices are for basics like wheat, rice, corn and gasoline, the market faces a situation where consumers' discretionary spending could be dampened until there's a significant shift in the commodities markets. Last week, crude oil surged to a record close to $120 a barrel.

So in addition to the Fed's meeting, Wall Street will continue to examine earnings from consumer-focused brands like Kellogg Co., Procter & Gamble Co., and Colgate-Palmolive Co., as well as economic data.

The government reports Thursday about personal spending and Friday about employment -- the biggest driver of spending. **New York** AP

Turkey weathering current crisis armed with lessons from 2001

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Let's assume again that the army was crossing the borders to fight terrorists camped out in the land of another country. The bourse would have already collapsed, and we would have gone bankrupt. These negativities are all on the stage now, but Turkey seems to be quite successful against this test of durability."

For Karabıyık, foreign investors are also sharing these positive observations, as they are still hanging on to 70 percent of the total holdings in the capital markets. "If they weren't confident that things would get better, this share would have already fallen to 35 percent. I don't accept the claims that they are staying in the market due to a lack of buyers at the current prices. The past experiences have so far shown that in hard times, foreign interests are simply selling off, leaving an emerging market in a hurry to hedge themselves from further losses. But they now trust that the current mess will be dispelled and that Turkey will successfully complete its integration in the global markets."

He further remarked that the capital markets in Turkey are quite young compared to those in the developed world, as their legal infrastructure was first introduced in Turkey in 1986, more than 100 years after the US, for example. They lack experience and are not well rooted, but they have the flexibility to adapt themselves to the most modern systems and the ability to absorb any bumps from outside. The Capital Markets Board (SPK) and the İstanbul Stock Exchange (İMKB) are managing these processes quite successfully, Karabıyık noted.

The massive influx of foreign interests into the markets that carried the share of the foreign investors to beyond 70 percent is a good indicator that Turkey is moving on the right path, Karabıyık underlined. But his answer to the question of whether the non-financial sectors are equally prepared was "no." "We still have a considerable number of deficiencies in this regard," he asserted, adding that only 35 percent of the companies on the top-500 list prepared by the İMKB -- or some 170 of companies -- are being traded on the İMKB.

From this perspective, Karabıyık is critical of the preparations conducted for the formation of a special stock market for small companies. He admits that any step toward the establishment of such a bourse would always be welcome, as previous examples in the rest of the world have proven how effective such stock exchanges can be for an economy. But improving the structures of small companies, enriching them with stronger financial capabilities and teaching them how to best assess the stock markets are more urgent needs, he said. "We are encouraging the companies that are planning to go public to prepare themselves for the initial public offering (IPO) for a year or more for restructuring," he pointed out, adding: "The small companies still do not know how to run in the stock markets, they are still integral actors of the unregistered economy. They still are not aware of the basic premises of corporate governance. They still don't have family-business constitutions despite most of them being family businesses. Only after overcoming these deficiencies can a stock market for small companies have a chance of running smoothly, and this takes around three to four years."

Karabıyık also maintains that establishing brand new bourses would not be rational, when instead they could be built as parts of existing bourses, which have already acquired a certain level of experience after overcoming a series of financial crises. He suggested that such a policy would cause great savings by cutting costs on importing know-how and employees while giving way to faster progress.

Only securities company serving all participation banks

Bizim Menkul Değerler (BMD) was founded in 2003 as a 50-50 partnership between Boydak Holding and Turkey's leading food conglomerate, Ülker, to provide intermediation services in the capital markets in addition to offering effective fund management services for its customers. It is the only intermediation company that serves interest-free participation banks. BMD General Manager Reşat Karabıyık believes this status is an extremely important part of BMD's mission.

He said capital markets are just a part of the financial sector but that they should never be evaluated separately from the non-financial sectors, as these two require each other to survive. "Looking at the foreign markets anywhere in the world, we see the same case: The capital markets improve in connection with and as a response to the needs of the non-financial sectors," he noted, adding that the capital markets are where long-term fund resources meet their demand.

As the most eye-catching difference of BMD from other securities companies, Karabıyık points to their experience with industrial activities. This experiences comes from the collective resources of BMD's partners, both of which have decades of experience in many businesses. This enriches BMD with the ability to understand the needs of non-financial companies better and to prepare suitable financial instruments accordingly. "BMD is in the first row among the intermediation companies in terms of making money out of consultancy services," he said.

BMD serves its customers with four basic investment funds. One of them is a normal fund based on shares, but the other three are unique, not only in Turkey but also in the world. One is the gold and energy fund, of which gold makes up of more than 35 percent while the remaining shares belong to energy companies. The construction industry fund is another option. What renders it unique is that it contains not just the shares of construction companies, but also of companies that are indirectly related to the construction business, such as cable manufacturing, cement, home appliances and iron production. Finally, they have the Islamic Market Fund, an exchanged-traded fund that they designed in collaboration with Dow Jones. BMD is currently serving three participation banks: Türkiye Finans, Kuveyt Türk and Albaraka. It has recently signed on with Bank Asya, as well, and the two will start working together after the SPK approves the deal.

PHOTO TURGUT ENGIN

BMD General Manager Reşat Karabıyık

Islamic banking in Turkey: After consolidation comes further growth

Turkish politics used the last six years to grow financial compliance and governance to international standards. As a result, international conventional market players have entered the scene with know-how and financial resources. The so-called Islamic finance niche, however, has undergone a far more structural change. That change was mostly market driven but was also moved forward by the intelligent planning of its members

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As a result, international conventional market players have entered the scene with know-how and financial resources.

The so-called Islamic finance niche, however, has undergone a far more structural change. That change was mostly market driven but was also moved forward by the intelligent planning of its members.

In 1983 the Özal government allowed the establishment of the so-called special finance houses to try to attract more investment from the Middle East. Back then, with Islamic finance still in its early stages, it was as a brave and apparently close to visionary move to use the liberalization phase at the World Bank and the IMF for this purpose.

The first foreign-funded special finance houses (Albaraka Türk, Faisal Finans, Kuveyt Türk) were soon followed by local players such as Family Finans and Asya Finans. Ever since those early days, the growth of the specific market has outperformed the conventional counterpart. The need for the products at offer and the value for the local economy are beyond doubt and are uncontested.

The 2001 crisis made clear that these finance institutions not only belonged under the umbrella of the Banking Regulation and Supervision Agency (BDDK), but also that the funds solicited from the public had to be protected by the Savings Deposit Insurance Fund (TMSF). As part of the general, post-crisis overhaul of banking regulations, the revaluation of special finance houses was completed in 2005 when they were recognized as full-blown participation banks.

The cost of that crisis to the Turkish banking sector is reported to have been $20 billion (for state-owned banks), with an additional exposure for commercial banks totaling some $43.9 billion. The Islamic finance sector weathered the crisis successfully and immediately prepared for further expansion. This was proof for the advantage of financing the non-financial economy and staying away from the exorbitant speculation on foreign currencies and in high-interest-paying government bonds.

There was a period of voluntary consolidation in the interest-free banking industry after 2005 as a result of strategic investments among the special finance houses. Bank Asya opened the most recent upgrading by its extremely successful IPO in 2006, and Albaraka Türk followed that move in 2007. National Commercial Bank (KSA) became a 60 percent shareholder in Türkiye Finans at the end of March 2008, while Kuveyt Türk at present waits for better market conditions to launch its own IPO.

Islamic finance worldwide is entering a first major innovative phase, and just now the Turkish market boasts the active presence of three first-tier Islamic banks. Indeed, NCB, the Albaraka Banking Group and Kuwait Finance House all rank in the top 20 Islamic banks worldwide asset-wise.

The also highly ranked Dubai Islamic Bank for the moment only has a representative office, but is reported to be interested in taking over a local bank. Just recently, Qatar Islamic Bank announced its application for a participation bank license, and last year there also was, among others, the entrance of Unicorn Investment Bank (Unicorn Capital Turkey) and Orion Overseas (Orion Investment Turkey). For some time now, Doha Bank, ABC Islamic Bank, National Bank of Kuwait Capital and Amlak Finance have also been part of the financial scene.

Numerous investment possibilities, however, are lost to the absence of sufficient compliant investment tools. The sector has awaited the regulatory creation of participation certificates, the so-called sukuk, for some time now. There are indeed substantial amounts of money available that cannot be used failing the existence of these financial instruments.

Propelled by their daring strategies, successful IPOs and the large resources of their underlying international shareholders, the Turkish participation banks are bound to become larger, middle-sized market players that are already making a positive contribution to the development of the real economy in Turkey and to the welfare of its population.

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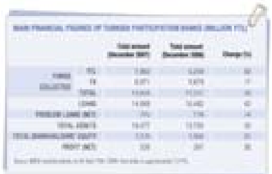

Turkey's new momentum

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Growth with a sound public sector fiscal structure: A fourth, more significant development is that this jump in national income is associated with sound improvement in public sector fiscal balances and a march toward achieving price stability. According to recently revised data, the ratio of net government debt to GDP has come down to 29 percent, whereas budget deficit to 1.7 percent.

Toward price stability: The consumer price index (CPI) came down from 68.5 percent in 2001 to 8.4 percent in 2007. Moreover, the list of countries that lowered inflation in 2007 was quite short due to global inflationary pressures in food and other commodities. However, unlike this historical success in reducing inflation from almost 70 percent in 2001 to 7 percent in 2005, there has been significant resistance on the inflationary front since 2006. In fact, the rate of inflation climbed to 9.6 in 2006 and then receded to 8.4 in 2007. As the targeted rate was 5 and 4 percent in 2006 and 2007, respectively, the inflation figures realized constituted a dramatic departure from the targets and therefore a significant erosion of credibility took place toward the central bank's policies.

In this success until mid-2006, the overall architecture of the implemented stabilization program, an appropriate external environment since 2002 and the strong leadership quality of the single-party government -- resulting in political and economic stability -- have been the major driving forces. Other than this general environment favorable to a process of disinflation, there are some other factors that describe Turkey's fight with inflation.

The first factor is overall aggregate demand factors. In fact until mid-2006, when significant signs of deterioration began in both the domestic and external environment, final consumption demand was favorable. However as the domestic demand-driven factors constituted a remarkable threat to consumer inflation and global liquidity risks rose, the central bank began implementing a tight monetary policy. Among many tools, high policy rates and liquidity management became focal points. With an expected time lag, the concrete results of this policy have been observed in the final private consumption figures in almost every category. For this reason, the lowest GDP growth figure since 2002, 4.5 percent, was recorded in 2007.

As underlined above, the second important element in inflation has been the major improvement in public sector fiscal balances. The budget deficit declined from almost 16.5 percent of GDP in 2001 to almost 0.7 percent in 2006 and 1.7 percent in 2007. Therefore, the public sector borrowing requirement declined almost to below zero, parallel to improvements in public sector accounts. Since the public deficit is about to be eliminated, contribution to disinflation from this sector is limited. However social security reform is the key component that could support both disinflation and fiscal balance.

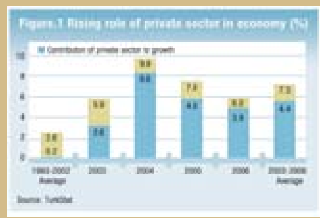
In addition, when cost and productivity figures since 2002 are considered, it is seen that productivity-driven positive factors outpaced those of cost-driven negative ones in fighting inflation until mid-2006. Despite the dramatic rise in the price of cost-push factors, including major commodities and food, triggered mainly by Asian high-growth economies and global warming, a positive surge in both labor and total factor productivity since 2002 neutralized the process in favor of disinflation. Unfortunately, what is observed as of today is that cost-driven factors began dominating the rise in productivity and therefore there is now a cost-driven inflationary inertia not only in Turkey, but also in the world economy.

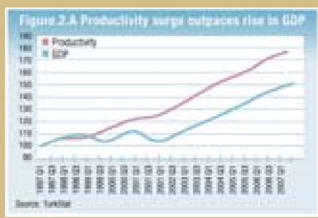
Finally, the successful management of expectations, as a major factor that fueled inflationary dynamics in the near past, has been quite efficacious in Turkey's process of disinflation. In fact, the central bank's high credibility between 2002 and 2005 played a crucial role in eliminating existing deviations from the inflation target. However as the credibility of the central bank has deteriorated for the last two years, this factor would also start negatively contributing consumer inflation as the labor class would start demanding retroactive compensation by the coming collective bargaining processes.

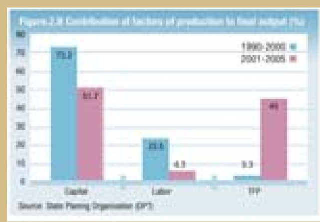
Under these conditions, for the next few years Turkey will witness a relatively slower growth path and inflation somewhere around 8-10 percent. However other than waiting for a fall in commodity prices parallel to the global slowdown in growth, the Turkish government must continue reforming the economy to establish a fertile ground for a production-oriented economy by minimizing costs and enhancing productivity and therefore profitability. Moreover, Turkey must be able to keep positive expectations alive toward the medium to longer-term targets so that private fixed capital investment will continue without any major interruptions, and therefore the rise in productivity will achieve a new and sustainable momentum. Obviously, political and economic stability constitutes the sine qua non condition of this longer perspective. This is inevitable, particularly in keeping stability in money markets, i.e., stability in the foreign exchange market so as to minimize FOREX's pass-through effect on inflation and interest rates as a major destabilizing factor in production costs.

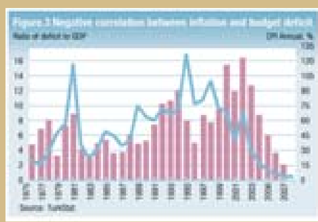
Table 2 Current Account Deficit (CAD) and Fragility Indicators

	2000	2001	2002	2003	2004	2005	2006	2007
Exports/Imports coverage	0.58	0.85	0.88	0.79	0.74	0.70	0.69	0.70
Export yields/Short term external debt	1.08	2.10	2.44	2.23	2.15	2.07	2.28	2.68
Export yields/External debt service	1.45	1.40	1.39	1.64	2.29	2.10	2.31	2.39
Tourism revenue/Foreign trade deficit	0.35	2.17	1.16	0.69	0.57	0.51	0.30	0.29
CB reserves/Short term external debt	0.82	1.21	1.71	1.53	1.18	1.18	1.37	1.61
CB reserves/CAD finance	1.64	-	20.02	11.36	11.36	2.61	1.96	1.68
CB reserves/CAD	2.26		18.49	4.36	4.30	2.61	1.97	2.21
CB reserves/Imports	0.44	0.52	0.39	0.54	0.54	0.41	0.47	0.48









Resilient economy: Considering the recently worsening global and domestic economic environments, it has emerged that the Turkish economy is quite resistant. In that regard, financial stability has critical importance, playing a key role in promoting and channeling savings to the productive sectors and therefore triggering economic growth.

The achievement on the inflation front has significantly improved the macroeconomic environment and eliminated vulnerabilities that burdened the financial system's proper functioning. The Banking Sector Restructuring Program and other measures taken following the 2001 crisis led to the formation of a strong and resilient financial system. The Banking Law enacted in 2005 is in line with the best international practices. The asset size of the Turkish banking sector has increased by more than threefold in the last six years and had reached $500 billion as of 2007. Still, there is vast unexplored potential in the sector, given the size of Turkey's young population and the low rate of credit utilization by households and private business.

Moreover, the banking sector's capital adequacy ratio (CAR) stood at 18.8 percent, well above the minimum legal requirement of 8 percent and the EU average, 12.1 percent. Short-term liquidity ratios comfortably meet the legal thresholds. Thanks to the sector's sound and resilient structure, foreign direct investment (FDI) to the Turkish banking system has surged since 2005, and the share of foreign investors in the total capital of the sector is now more than 40 percent. Rather than financing government deficits, the banking sector has returned to its core function of serving as an intermediary between borrowers and lenders. The rate of total loans to total deposits, a proxy for the banking sector's intermediation function, has increased almost twofold since 2001, reaching 80 percent as of 2007.

Another important vulnerability of the Turkish economy has been the current account deficit (CAD), which was 5.8 percent of GDP in 2007. However the elements of its finance are quite robust: almost 58 percent of CAD ($38 billion in 2007) has been financed with FDI and the remainder with long-term oriented credit. The share of short-term capital inflows in CAD is almost negative.

Moreover, as shown in Table 2, fragility indicators around the balance of payments deficit are at least not worse than those in 2000, prior to Turkey's 2001 crisis.

A nation of rising expectations: The Central Bank of Turkey defines four distinguishing characteristics of the nation that set it apart from other emerging market countries.

First, unlike the countries in Central and Eastern Europe, Turkey has a young population, a demographic gift that could accelerate economic growth. But of course having great potential does not guarantee success -- the Turkish economy is currently utilizing less than half its workforce. Improving the state of the labor market, removing rigid labor market regulations, reducing the tax burden on employment and, more importantly, enhancing human capital through educational reforms are essential to accelerating the economic growth rate on a sustainable basis.

Second, Turkey is a net commodity importer, in contrast to the Latin American countries and South Africa. We need to import an excess of $35 billion of oil and natural gas each year, almost 5 percent of our GDP. Looking at the composition of our foreign trade, it is clear that imports are mainly commodities and intermediate goods, whereas industrial goods account for more than 90 percent of total exports. Therefore promoting Turkey's competitiveness is the key to its future success.

Third, the domestic savings rate is well below 20 percent of GDP, requiring foreign savings to finance Turkey's recently rising investment, which is well above 20 percent of the GDP. As the savings-investment gap is around 5 percent of GDP, it is therefore not surprising to observe a strong and direct positive relationship between the growth rate and the current account deficit. Of course, the upward trend in energy prices has also contributed to the widening of the current account deficit, to 5.8 percent in 2007. The current account deficit is a structural problem and a source of vulnerability, but nonetheless Turkey had no difficulty in its financing in the past six years. In fact, the quality of foreign capital flows has improved sharply. The current account deficit can now be financed through FDI and long-term capital inflows. The FDI inflows were in excess of $20 billion in each of the last two years, putting Turkey among the top FDI recipient developing countries.

Fourth, Turkey is one of the few countries with a "convergence story." The negotiations with the European Union over full membership status provide a major stimulus to policy makers to bring Turkey's huge potential to life and complete the reform agenda. This agenda consists of next-generation policies and reforms that focus on removing structural bottlenecks and improving the economy's capacity for labor absorption, innovation and competitiveness.

Turkey has had a weighty structural reform agenda since 2001. However the continuation of such reforms is of vital importance to the sustainability of the economic gains achieved in recent years and for economic resilience to future shocks. The most important structural reform in the pipeline is the social security reform, expected to significantly improve Turkey's fiscal balances in the medium and long terms, and also expected to contribute to our domestic savings rate. Other prominent steps that should be taken include reducing the size of the unregistered economy and broadening the tax base; reforming the labor market to increase job creation and bring the business environment to a level on par with international competition; re-designing the education system to make it consistent with labor demand and raise the quality of the labor force; privatizing the energy market; and ensuring energy supply security.

These steps together with macroeconomic stability would obviously make Turkey a more competitive country in the international economic arena.

Looking ahead, the main goals are to achieve and sustain price stability and economic growth. The prerequisites are macroeconomic stability, structural reforms and adherence to the principles of good governance both in public and private institutions. Turkey has learned that economic growth at the expense of price stability is not sustainable. Together with the EU anchor in place, Turkey is moving decisively to becoming a big economy -- above $1 trillion.

PHOTO TURGUT ENGİN

'Turkey must continue to pursue privatization'

İBRAHİM TÜRKMEN İSTANBUL

The combined effect of the global credit crisis and ongoing internal political unrest has had a negative impact on the value of Turkey's state-owned assets, but this should not deter the government from achieving its privatization goals, according to Garanti Securities President and CEO Metin Ar.

Both the Finance Ministry and the Privatization Board (ÖİB) are still keen to proceed with the selling of state assets, he said, and underlined his belief that privatizations will form the strongest element of mergers and acquisitions (M&A) in Turkey in 2008. "Indeed, I predict this, and I hope it will be so," he added.

Ar spoke to Today's Business in an exclusive interview last week. Providing consultancy and technical assistance to companies interested in M&A and privatizations in Turkey, Garanti Securities is currently busy with preparations for national phone company Türk Telekom's initial public offering (IPO).

State-owned companies have lost almost one-third of their value due to the latest turbulence in the international and domestic markets, but this should not be viewed as wholly bad news, Ar suggested. "Actually the former prices were higher than normal, and they were a consequence of excessive global liquidity and the positive aspiration of Turkey's booming economy. Therefore the current lower prices are not bad," Ar claimed. While a private company is entitled to hold off on sales during unfavorable market conditions, a state should diligently continue to sell since such behavior constitutes the very essence of a free market economy, he noted. Furthermore the situation is more or less the same elsewhere. For example, he said, Deutsche Telekom lost 22 percent of its market capitalization in the last six months.

Postponing privatizations until market conditions improve should not be seen as a valid option, Ar opined. "If you believe that tomorrow will be better than today, waiting might be acceptable. However, markets are always shaped by the balance point of conflicting expectations about tomorrow," he noted, adding that the state may forgo selling an asset at, say, YTL 100 million with the expectation that prices will surge again in the near future, but in reality the price may fall to YTL 75 million after six months.

Indeed, Ar insisted, the onus is on the state to "get rid" of all its economic activities via privatization, since the private sector always deals with trade more efficiently. The privatized companies will probably run better and will earn more profit, allowing the state to obtain more corporate tax from them, he explained, and added that thus the state will be better able to focus on core responsibilities such as education, health and defense.

The world economy has hit a rough patch since May 2007 in the wake of the subprime mortgage crisis in the US and the subsequent domino effect in the global interdependent markets. Ar shared his analysis of this ongoing economic depression and its possible impact on the Turkish economy. The tremor began with subprime loans, but soon spread, he noted. Major investment funds revealed massive levels of writedowns and losses, inflicting serious damage on their capital structure. Thus they started to seek out healthy capital owners, such as sovereign wealth funds, to partner with in order to rid themselves of the deleterious effects of the worsening global crisis. In this way the positive climate had inverted by July 2007. There was excessive liquidity in the markets due to low interest rates, reflecting the worldwide search for good investment opportunities until June. Because of this, finding the necessary financial resources for any business activity from simple housing loans to major acquisitions was quite easy, Ar noted. Both individuals and companies could easily find funds for their consumption or investment, and were therefore ready to pay more for longer term installments than to pay less but at once and in cash. Ar claimed that such was the case in the sale of state petrochemicals manufacturer Petkim, which took place before July. The bidders offered more than Petkim was thought to be worth, with the confidence they could easily find the necessary funds, even beyond what they needed. "In almost all privatization deals, the same scenario played a role," Ar said.


Garanti Securities President and CEO Metin Ar

PHOTO ONUR COBAN

The conditions are no longer as good as they were a year ago, however, Ar claimed. "In the past, 20 banks were rushing to provide money for a project, but now only five banks are volunteering. Besides, they are selling money at higher rates with more guarantees. Moreover, they are willing to meet a smaller portion of the financial needs of a project," he added, and said these factors have slowed economic activity in the country. M&A has also shown a declining pattern for the same reasons, Ar said.

He also shared his thoughts about the closure case opened against the Justice and Development Party (AK Party). He said it was quite hard to make a mathematical estimate of how the case had contributed to the current situation in the markets. "We made an analysis a fortnight ago," Ar noted: "The global crisis started around the second week of July 2007, but didn't have a negative impact on Turkey until Oct. 15. This date was chosen because it was the day the benchmark index of the İstanbul Stock Exchange (İMKB), the İMKB-100, peaked in terms of dollars. From then on, the stock market has followed a declining pattern." During the four-month period between July and October, the developed Western markets were declining, while emerging countries like Turkey were on the ascendant, he emphasized. But after October Turkey also tasted the bitter flavor of the crisis.

The rate of decline in the İMKB-100 was 32 percent between Oct. 15 and the first week of April. However, the index has suffered only a 5 percent drop since the closure case was filed on March 14.

Asked whether there has been any change in the positive perceptions of foreign investors regarding the overall market appearance in Turkey, Ar said some companies were negatively affected, while others view the developments as "normal." He concluded by saying that the current situation is far better than in 2001, when investors simply closed shop in terms of Turkey: "Now they are saying that the markets have changed, so have the prices. They are reassessing the markets at new prices without giving up on Turkey."

Vulture subprime buyers ramp up purchases

NEWS ANALYSIS

By Jennifer Ablan and Al Yoon

TODAY'S BUSINESS

The allure of rotting mortgage bonds has grown so strong that Wall Street's vultures have begun picking over their carcasses -- a signal the credit crisis has entered a crucial stage in its vicious cycle.

In the past two months, these intrepid investors have begun betting billions of dollars on a hunch that mortgage security prices have fallen enough. It is a risk few have taken for a year or more as the credit crisis rooted in this very market wreaked havoc in financial markets around the world.

In early February, bid lists for bonds backed by middle-quality mortgages found no takers, even at what were then considered fire-sale prices, between 75 cents and 80 cents on the dollar. But the following month, though, Jeffrey Gundlach, chief investment officer at bond manager Trust Company of the West, began snapping up these same securities at 65 cents on the dollar during what he calls the darkest moments for the markets.

"You had a massive, massive supply-demand imbalance that had developed into a death spiral," Gundlach said of the systemic liquidity squeeze in early March. "Those securities were really cheap against the fundamentals, so we went in big and started buying."

Watch the vultures

The behavior of Gundlach and those like him is important because this brand of investor -- patient, value scavengers willing to stomach some initial loss in exchange for huge windfalls when a market turns -- frequently signals that a market is forming a bottom when they are active.

In early March, banks and hedge funds stripped of access to credit had to sell mortgage securities to raise cash for margin calls. That helped send already panicky US markets into a full-fledged credit freeze.

But the Federal Reserve stepped in and announced that it would lend up to $200 billion of US Treasury securities to banks for 28-day periods in return for debt, including a range of mortgage-backed securities. That broke a month-long sell-off, sending the mortgage securities rallying strongly.

That set in motion a number of major buyers into the mortgage market.

In recent months, a number of big players have bought battered mortgage securities, including Marathon Asset Management, an $11.5 billion hedge fund manager specializing in distressed assets; Trust Company of the West, with $160 billion with assets under management, and Metropolitan West Asset Management, with $27 billion in assets, as well as UK-based investment boutique, Thames River.

Prime time for subprime bonds

"We're not finding any problems finding opportunity," said Tad Rivelle, chief investment officer at Metropolitan West Asset Management in Los Angeles.

The Alt-A mortgage securities, as well as the ones purchased by Gundlach, which are loans whose quality rests in the vast space between subprime and prime, and subprime mortgage-backed securities "are as rich an opportunity set as the corporate market was back in 2002 when the bubble burst in telecom," Rivelle added.

Bruce Richards, chief executive officer of Marathon Asset Management in New York, told Reuters recently that his firm has purchased more than $1 billion par value in residential real estate loans. Richards also said that he expects Marathon to buy another $1 billion or more this year.

Thames River Capital fund manager Ken Kinsey-Quick has moved long into some battered subprime assets after shorting the sector last year.

Kinsey-Quick, who runs around $2.3 billion in funds of hedge funds, said he had invested in the securities at the start of April because he thinks they are cheap.

For his part, Rivelle of MetWest will be looking at the Alt-A market, but for now he's been a purchaser of the safest part of a subprime bond that typically gets paid off in full, even in foreclosure.

"Even if there was a substantial and rapid rise in foreclosures and delinquencies in these deals, the rub is the servicer sells the property and generates some amount of cash in the process," Rivelle said. This cash flow gets directed to these 'AAA' securities, causing them to be repaid at an accelerated rate, he added.

"As for those bonds that Gundlach bought at 65 cents on the dollar: They looked great at 65 and at 80, they look kind of fully priced against the fundamentals."

Waiting for the forced selling

Truth be told, risks to investing now rather than later persist. Downgrades of bonds backed by subprime loans by Moody's Investors Service, Standard &Poor's and Fitch Ratings continue apace as expectations of falling home prices have led rating companies to boost expectations on delinquencies. Subprime loan default rates have more than doubled to 25 percent this year, and will climb above 30 percent by December as a worsening job market adds stress to homeowners already faced with unaffordable mortgages, according to Friedman Billings Ramsey Inc. research.

Credit Suisse on Tuesday boosted its forecast of subprime foreclosures over the next two years to 1.39 million from its October estimate of 730,000.

"We're certainly looking (at distressed assets), though we think that a lot more downgrades are coming that will result in substantial supply from forced sellers," said Julian Mann, a manager of mortgage- and other asset-backed bonds at First Pacific Advisors in Los Angeles, California.

Gundlach doesn't doubt that, saying, "The fundamentals in housing are still terrible. You better believe there will be downgrades coming."

"At that point, he'll be looking to buy again, he said." **New York** Reuters

PHOTO MUSTAFA KIRAZLI

TURKISH FACTORING SET TO GROW WITH EXPORTS

Though factoring has its roots in commercial banking, the sector has suffered from misunderstanding by consumers and bankers alike

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"But even without the inclusion of export invoice discounting, the results illustrate that exporters and importers around the world are becoming more and more familiar with the advantages to be derived from a factoring arrangement: working capital, credit risk protection and collection service for the exporter, while the importer benefits from buying on open account terms without the need to open letters of credit or to accept other payment conditions with a similar restrictive character," the report concluded.

Currently, there are 97 registered factoring companies in Turkey, of which 41 are members of the Turkish Factoring Association (FD). Member companies account for over 90 percent of the country's total factoring turnover. FD Chairman Zafer Ataman estimates turnover will total nearly 20 billion euros in 2008.

Market structure

Ataman has worked in the factoring business since its inception in Turkey in 1990, was a co-founder of the FD and now manages Strateji Factoring and Yatırım Leasing, subsidiaries of the Turkish Electricity Trading and Contracting Company (TETAS).

The Banking Regulation and Supervision Agency (BDDK) regulates the factoring industry in Turkey and must approve the establishment of any new factoring company. The minimum capital requirement for new and existing companies is currently set at YTL 5 million, though this amount may change under a new draft law for the sector.

Though factoring has its roots in commercial banking, the sector has suffered from misunderstanding by consumers and bankers alike. Seen as lenders of last resort, factoring agents have been compared to loan sharks and usurers.

Of course no one forces a company to sign over its receivables to a third party, but the traditional high real interest rates in Turkey and the reluctance of commercial banks to lend to the manufacturing sector combined to make factoring one of the few viable options for desperate managers to get financing for their businesses.

Ataman hopes the misperceptions of factoring will fade with better market conditions and new structuring via BDDK regulation. "As you know, the new changes in the draft legislation mean that for the first time factoring will have a new law," said Ataman. "Regulations applied to the market mean improvement; they will clear up misunderstanding."

The importance of interest rates lies in the factoring practice of linking advance funding fees to the current interest rate. Factoring companies generally charge a commission on receivables, which also covers the credit risk protection implied in assuming control of collections.

"We don't have the final figures, but it looks as if growth in the first quarter this year was slow compared to 2007, but still increasing in turnover," said Ataman. "Factoring this year should grow along with increased demand for Turkish exports, but the extent of the growth depends on interest rates."

Analysts widely expect the Central Bank of Turkey to keep its benchmark policy rate unchanged at 15.25 percent through the rest of the year.

Big bank business

Commercial banks appreciate the value that factoring's slice of the market represents, which roughly translates into a quarter of total export volume.

"Indeed, the banks dominate the Turkish market, which in a way is oligopolistic," said Ataman. "The top nine factoring companies by volume are all bank subsidiaries."

Strateji Factoring, by comparison, is one of the largest private factoring companies in Turkey and recorded international turnover last year above $250 million.

Jeroen Kohnstamm, secretary-general of FCI, said slowing consumer demand in the US this year would likely hinder growth in the key export factoring market of China. His forecast pointed out the better situation of Turkey, which exports a much greater share, over half of total exports, to the more buoyant Eurozone.

ECONOMY MINISTER: TURKEY DOES NOT NEED NEW AGREEMENT WITH IMF

Mehmet Şimşek says the social security system in Turkey has become a catastrophe now due to the political populism of the past.

CONTINUED FROM PAGE 1

But considering Turkey's fiscal discipline, debt conversion and reserves, there is no need for this, according to the economy minister. The second option is to sign a precautionary stand-by agreement with the IMF. This course of action is usually preferred by countries that do not need financing but have some fragile points in their economies. The third alternative is after-program monitoring, which is available for countries that use 100 percent of their debt quota or below after their stand-by agreement has ended. Turkey's debt quota is SDR 1.191 billion at the IMF level, but Turkey's debt to the IMF is SDR 4.36 billion. Therefore, Turkey's debt to the IMF is beyond its quota. The last option is monitoring in the context of article four, which is the normal procedure as followed for the current program.

In order for Turkey to opt for the last option, it will have to forgo its right to withdraw $3.6 billion promised under its current stand-by agreement and pay back an additional $5.1 billion to the IMF. Şimşek says the precautionary stand-by agreement fits Turkey best, as it guarantees necessary financial elasticity and sends strong positive messages to investors. He adds that they are also studying the after-program monitoring option: "However, the renewal decision for the IMF program is not a technical decision, but a political decision, so our government will decide on this. Even though the program concerns me, I have refrained from making any kind of redirection on this issue."

'We have realized the necessary reforms, yet nobody seems interested'

Şimşek does not agree with the claim that reforms have slowed down: "We have taken a lot of steps in terms of reforms, but this does not interest some. I think this looks like a scene in which deaf people are trying to communicate with each other by speaking."

Şimşek says the social security system in Turkey has become a catastrophe now due to the political populism of the past, pointing out that in 1970 there was one retired person for every 24 workers, whereas now there are only four employees for each retiree. "In a country like Turkey, where the average age of the population is 28-29, the social security system must have reserves of trillions of dollars. Now, unfortunately, forget about saving money, we have to spend three to four times more than the sum allocated for investment in the budget. If they knew the situation, the people who protest the social security reform on the streets would protest the previous system, not the coming one."

The economy minister also responds to criticism over the raising of the retirement age. He argues that the retirement age is 60 and over in developed countries, adding that the minimum requirements in terms of days worked for retirement were raised by 2,046 for men and 2,048 for women. According to Şimşek, if the social security reform is not carried out Turkey will have to transfer $1.8 trillion to the social security system between 2008 and 2075. "If we had invested the funds that we transferred to the system since 1990 into education and infrastructure, today all of members of the social security system would be in better condition."

Speaking on the topic of what must be done for the Turkish economy to compete on the global scale, the economy minister points to the achievements of developed countries as examples for Turkey. The elasticity of the labor market and the energy industry, the financial markets with numerous instruments and the creation of companies with high added-value and profit margins are a few of these achievements, the minister noted. He further pointed out that reforms had also been made in the electricity sector to decrease costs. The access to cheaper energy resources is vital for industrialists to be able compete with their global rivals. As part of efforts to decrease Turkey's dependence on oil, natural gas and imported coal, studies for establishing geothermal, hydroelectric and nuclear power plants have started. "All these developments show that Turkey's energy market is rapidly being liberated," Şimşek said.

Another important step to be taken for the sake of global competition is the decreasing of burdens related to employment. For this reason, the financial burdens on employment will begin to decrease this year. Şimşek says minimum-wage earners will pay lower taxes, adding: "They still claim they are paying the highest tax on wages among all Organization for Economic Cooperation and Development [OECD] countries. This is not correct. Also, our government promised to introduce a 5 percent reduction on their burden. We will apply this within the year." The economy minister says they will create elasticity in the employment market and that there will be programs for meeting the needs of qualified employees. "It will be easier to benefit from the unemployment fund," he adds. Increasing the production of goods with high added value has the utmost importance for global competitiveness, according to the economy minister. Şimşek says his ministry prepared Turkey's industrial inventory, adding that Turkey needs to stop using so much muscle power and begin using more brain power. As such, he explains, the government promulgated one of the best laws in the world for research and development. Turkey will catch up with Europe by 2012 in terms of R&D, and the sector's portion in national income will increase to 2 percent.

New incentive system to be launched in 2009

Touching on regulations related to the incentive system to encourage investors to spend money in particular areas of the country, the economy minister says the current incentive law will be valid until the end of 2008 and that the regional and sector incentive law will be valid beginning from 2009. Pointing out that privatizations are not just sources of income, Şimşek adds, "Privatizations are necessary in Turkey in order to develop the competitive atmosphere and increase productivity. Look at all the companies we have privatized. All of them have increased their profitability, employment and tax payments." Asked whether the latest political and economic developments affect the decisions of the foreign investors that are planning to enter the energy generation business in Turkey, Şimşek says energy investors think in the long term, adding: "You present a 140 megawatt tender and 27 companies apply for this. Three to five of them may be affected by these factors, but no one who believes in the development of Turkey in the long run will abandon this tender."

Şimşek says the government will also complete the Southeastern Anatolia Project (GAP) and construct a new irrigation system for agriculture after completing its energy projects, thus creating new areas of employment.

The economy minister says Turkey's development rate was slightly lower than expected in 2007, but that Turkey has been developing for 24 quarters without any break. He explains that Turkey has developed at an average rate of 7 percent annually since 2002 despite external economic shocks and that last year's growth of 4.5 percent was higher than the Turkish Republic's average growth since its establishment in 1923. According to Şimşek, the rate of public debt stock compared to national income decreased to 29.1 percent at the end of 2007, but public debt stock decreased 39 percent compared to the national income. He adds that these numbers are far lower than the EU average of 60 percent and added that they were also meeting the EU's Maastricht criteria with the country's annual budget.

Turkey's inflation is 5 pct, not counting energy and food prices

Elaborating on the factors that cause inflation to go beyond the country's targets, Şimşek says energy, food and tobacco in 2007's inflation rate of 8.4 percent accounted for 70 percent of it. He adds, "We do not want our citizens to poison themselves," referring to the rise in tobacco prices.

However, he says, the global shocks in food and oil prices have an important influence on the climbing inflation rates. Oil was $25 per gallon in 2002, but today its price exceeds $100. The drought in Turkey and the increase in world food prices have resulted in increases in food prices for Turkey, too. Considering these factors, it is evident that 70 percent of Turkey's inflation is independent of Turkish monetary policies. Şimşek says the government maintains a cautious monetary policy to keep inflation in single digits in the medium term, adding: "When you look at core inflation and omit food and energy prices, Turkey's inflation is around 4.5-5 percent. If we avoid shocks in food and energy prices, inflation targets can be met in the medium term."

Currency is not the most important factor in global competition

The minister emphasizes that the foreign trade deficit has increased by 17 percent in the last eight years, at times when foreign currency was high against the Turkish lira as well as when foreign currency was low. "There has also been an increase in imports, but the amount paid for oil and natural gas last year was $34 billion. Turkey's foreign trade deficit is $38 billion," he says, adding that foreign currency is not an important factor in determining competitive power. "Imports have been on the rise because we have stepped up our investments and oil prices have skyrocketed. While there was natural gas in only seven cities in the past, now 50 cities have it. We should also admit that foreign currency negatively impacts some business areas, but the essence of the problem is still not the currency itself.

Could sovereign wealth funds be a new source of financial optimism for Turkey?

MEHMET ÖĞÜTÇÜ / ALASTAIR NEWTON*


PHOTO TODAY'S ZAMAN

If the data is anything to go by, Turkey has indeed become a major power in the world economy in terms of both total trade volume and inward foreign direct investment (FDI). In 2007, it boasted an impressive foreign trade volume of $277 billion (though with a huge trade deficit of $62.8 billion) and FDI inflows of $22 billion (from a meager $1.1 billion in 1995). The İstanbul Stock Exchange (İMKB) was the fifth best performing among emerging market countries. And Turkey's gross domestic product (GDP) growth rate was 4.5 percent -- one of the highest in the Organization of Economic Cooperation and Development (OECD) world if still lower than growth lasting the previous three years (2006: 6.9 percent, 2005: 8.4 percent, 2004: 9.4 percent). Yet, in common with other major economies Turkey's economic growth is widely expected to stutter this year thanks to a combination of internal factors -- both economic and political -- and the global slowdown.

For all the recent concern among the developed world's political classes and in the press, we believe that one potential reason for optimism at the global scale is the growing clout of so-called sovereign wealth funds (SWFs). The question we look to explore here is whether Turkey can attract more investment from these funds to help ensure its continued financial health through the current downturn and into the medium-term.

Grow, grow stronger

"SWF" as a term has only been around since 2005. But the first such fund dates back to 1953 -- the Kuwait Investment Board, now worth approximately $250 billion, set up to manage oil revenues even before Kuwait gained independence from the United Kingdom. For the 50 or so years which followed, these government funds were simply referred to as institutional investors or government institutions.

Since the turn of the century, such funds have proliferated thanks to a combination of surging energy prices and booming Asian exports, typically being created when a government has a budgetary surplus and little or no international debt. Simon Johnson, the International Monetary Fund's (IMF) chief economist, thinks SWFs will be worth $10 trillion by 2012. Stephen Jen, an economist at Morgan Stanley who follows 29 SWFs, estimates their current holdings at almost $3 trillion; he projects that -- thanks to the magic of compounding and the funds' new-found appreciation for equity investing -- SWFs will control up to $12 trillion by 2015.

Although SWFs -- combined with the closely related "diversified monetary authorities" (DMAs), e.g. the Saudi Arabian Monetary Agency -- currently make up no more than 3 percent of the world's $165 trillion-worth of traded securities, they have a lot of firepower: more equity than (unleveraged) private equity and more funds than hedge funds. And they are growing fast (about 20 percent annually) -- the Gulf's big funds could gain from oil and gas revenues another $300 billion to manage this year alone. Add to that the growth of other state-owned financial assets looking to invest -- pension funds (estimated at $22.7 trillion), mutual funds ($20.8 trillion), insurance assets ($20.5 trillion) -- and the marvels of compound interest, one soon gets to some very impressive numbers.

Who are the targets?

The funds' horizons in 2007 stretched into a range of sectors including consumer retail (10 percent of deals by value), communications and technology (4 percent) and industrials (4 percent), as they have also looked to diversify away from their traditional focus of government bonds into the full range of financial instruments. But it is in financial institutions where they really made a major impact last year with that sector accounting for a massive 63 percent of deals by value. We judge that such investments have been made primarily for the long-term value which they potentially offer; but, one way or the other, there does appear to have been an element of SWFs looking to play the "white knight" in an effort to soften concerns about them in some political circles in the OECD area.

That said, while SWFs may well continue to invest in financial institutions, such a disproportionate investment in one sector will, in our view, likely prove to be a product of the current times and, therefore, something of an anomaly. In that regard we find particularly interesting the fact that last year 11 percent of deals by value were in real estate with Dubai's flagship property company Emaar alone engaged in an estimated $65 billion-worth of foreign projects in economies ranging from India in the east to Morocco in the west via Turkey.

What are the motives of SWFs?

We entirely endorse the publicly stated view of European Commissioner Charlie McCreevy who noted in late February: "There is… no instance of sovereign wealth funds acting in any manner other than responsibly up until now." But it is difficult to counter categorically concerns that some SWFs may be motivated by factors other than straightforward return on investment. In addition to the sheer size of the funds, such concerns notably include: lack of transparency over both overall strategy and individual investments of SWFs and concern over the quality of governance and regulatory oversight in the funds' home countries as well as fears that investment decisions may be influenced by "political" factors. Whether or not there is any justification for these, their impact risks being compounded by what we see as a rising tide of protectionism across OECD economies, coupled with residual "economic nationalism" in some.

In principle, the vast majority of modern economies welcome foreign investment. But, in politics, appeals to fear often "sell" better than those to reason, and protectionism enjoys its own "logic." The hypocrisy of erecting barriers to foreign investors while demanding open access to developing markets is self-evident (even if the likely consequent long-term damage to one's own economy is less so). While every country therefore has legitimate concerns over national security and financial stability -- as is underlined by the existence in the US of the Committee on Foreign Investment in the United States (CFIUS) and in Europe by a substantial body of regulation on free movement of capital in the EC Treaty -- the case for additional regulation specifically aimed at SWFs is therefore far from clear-cut in our view.

Whatever their motives, SWFs look set to be around for the long-term and could be a significant influence on prices and markets. We expect them to continue to diversify the range of their investments in terms of instruments, currencies and sectors. As they do so, we believe they will usually be greeted with open arms -- arguably underlined by recent Chinese investment in both Total and BP. For, as with private equity and hedge funds, anxieties about SWFs owe less to the reality than to a mix of secrecy and suspicion.

SWFs and Turkey

Even putting the current downturn to one side, there are many reasons why we believe Turkey should proactively court SWFs into its economy. Notably, Turkey faces huge current account and trade deficits in a global environment, marked by signs of significant slowdown this year and in 2009 when it will be hard to continue attracting both direct and portfolio investments to finance these deficits. SWFs from Russia, the Gulf and Asia will therefore find a warm welcome awaiting them from Turks keen on bridging this gap. Equally, Turkey's improved business environment and enhanced economic and strategic ties to the Gulf, Russia and Asian surplus countries could well result in substantial SWFs inflow.

Two prominent Gulf SWFs are already active in Turkey -- the Kuwait Investment Authority (KIA) and Dubai Holding (DH). KIA owns the Cevahir shopping mall in Istanbul, for which it paid $750 million in 2006 through its London-based subsidiary St. Martin's Property. And, in addition to the Emaar development noted above, DH's international property development subsidiary, Sama Dubai, became involved in 2005 in a joint $5 billion investment venture with the Istanbul Metropolitan Municipality, the first project of which is the multi-use Dubai Towers Istanbul (though this project has hit some legal obstacles). Close government-to-government relations between Turkey and many SWF home countries should be instrumental in attracting more funds for property, infrastructure investments and the expected privatization of Halkbank and Vakıfbank, as well as in the energy-sector as minority partners.

All that being said, there is still a great deal of work to be done by both the authorities and the domestic business community to overcome the past perception of Turkey as an economy which has not been particularly welcoming to foreign investment. Though recent years have seen a significant improvement in that regard, for the Turkish economy to benefit significantly from SWF investment this improved image needs to be carefully nurtured or risk the funds turning to other opportunities in the region and more widely. So, the answer to the question of whether SWF's are indeed a new cause for financial optimism for Turkey rests largely, in our view, in Turkey's hands. For it is clear to us that the investment opportunities in Turkey mean that the SWFs will continue to come if they are made welcome and if inter-governmental relations are effectively leveraged.

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The basic statistics

- The global annual GDP is $50 trillion.
- The top seven sovereign wealth organizations control each in excess of $100 billion, with some as high as $700 billion.
- Pension funds globally control $20 trillion.
- Bank assets are estimated to be $60 trillion.
- Equity market capitalization around the world is $50 trillion.
- Sovereign and non-sovereign debt aggregates are in excess of $60 trillion.
- Private equity accounts for:
- $700 billion of investor capital globally
- 20 percent of global mergers and acquisitions activity
- 60 percent of initial public offerings in the US
- There are 181 private equity funds around the world with more than $1 billion under management, compared to five in 1989, and 4,000 buyout deals were completed by the private equity industry in 2006.

'Turkish economy like a woman in labor but unable to deliver'

The economy is harhsly being tested by a globally-oriented crisis currently but has proven succesful to persist against it so far, says Professor of Economics İbrahim Öztürk. He resembled the economy to a pregnant woman who has come to brink of delivering birth in great pains but still unable to reach the happy end. "As long as the stability is retained, there is nothing to fear," he claims.

MEHMET ŞAHİN ADANA

Turkey's economy is now able to weather crises, with the public sector witnessing financial stability and the banking sector, which had itself triggered crises in the past, currently enjoying a strong structure and foundation, said Associate Professor İbrahim Öztürk, a faculty member at Marmara University's department of economics.

Speaking at the Association for Anatolian Businessmen's (AGİD) regular monthly meeting, titled "Let Us Share the Experience with Successful Entrepreneurs," Öztürk noted that the country has come to the brink of crisis but that it is able to resist. He compared the economy to a woman in labor but unable to deliver, and underlined that this was the first time such a hurdle has been faced while the atmosphere was so positive. Recalling that financial stability has been maintained in the public and banking sectors, both of which have been major sources of economic crises in the past, Öztürk noted that the stability could remain despite economic upheaval.

Öztürk, who recalled that price stability had been maintained owing to a reduced rate of inflation, a growth in demand in Turkey, which is home to a large, young population, also made mention of efforts to improve income distribution and unemployment and on bringing the national income to EU standards. Noting that wealthy people live in very small houses in Japan, which enjoys a $40,000 per capita income and a $4 trillion gross domestic product (GDP), Öztürk said that in Turkey, people with low incomes, slightly higher than the minimum wage, reside in large houses. "This is our problem. It is hard to achieve greater levels of industrialization this way," Öztürk said and asked that action be taken in regard to this wealthy lifestyle, sustained on the basis of credit.

Recalling that Turkey had suffered from three serious financial crises between 1994 and 2001, Öztürk noted that growth, financial stability and price stability -- three eminent problems in the economy -- were questioned in 2001. Öztürk further noted that the economy, which collapsed in 2001, recovered owing to International Monetary Fund (IMF) support. He also said that the public sector has no problem vis-à-vis debt. Pointing out that Turkey has a current account deficit second only to the US, Öztürk stressed that the Turkish economy is approaching figures it saw in times of crisis, with an unemployment rate of 10.5 percent despite consecutive growth rates of the economy of 7 percent on average between 2002 and 2007.

In his speech Öztürk also listed reasons for the current deficit. "The country has a poor services sector which in the past included banking and retail business. Foreign capital filled this field in return for growing demand. There is a growing tendency in the world toward monopolization in the world's banking sector, but we are unable to sell our banks; naturally, they cannot find partners. For this reason, bankers that have sold their banks leave this field. You may be upset by this, but it was the right thing for them to do because they had no chance at competition. Those who sell their banks invest in the energy sector. A lack of capital and insufficient savings is the primary reason that has led to the current deficit."

AGİD Chairman Ahmet Coşkun, who also gave a speech during the same meeting, underlined that there are troubles as well as opportunities in the country's economy. Noting that a number of sectors have grown exponentially, Coşkun stressed that businessmen should make solid and reasonable assessments to determine how to benefit from these sectors. Recalling that they are acting in reliance on the slogan "We took a step for this country," Coşkun also noted that plans are being developed in these regular meetings to take the necessary steps. Coşkun further gave some brief information on AGİD's activities, noting that it was a member of the Turkish Confederation of Businessmen and Industrialists (TUSKON), which includes 154 associations and 15 federations.

The chairman noted that TUSKON, the fastest growing civil society organization over the last two years, has made a contribution in the amount of $5.5 billion to the Turkish economy during this period and said that total turnover amounting to $1.5-2 billion is expected in the second African trade meeting this year. Coşkun further said: "Yes, the country is struggling with some problems. We are all experiencing these troubles. But there are positive developments as well. We always recommend optimism. Two people talk about economic crises when they get together, but this sort of attitude does not generate any good. We will have high morale if we try to see the glass half full. This will bring about good results."

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Reforms increase investor confidence, spur foreign direct investment

CONTINUED FROM PAGE 1

Based on preliminary data for 2007, Turkey will again be among the top 20 countries to attract FDI.

After receiving an average level of $1 billion per year in the 1990s, FDI inflow to Turkey increased to $2.9 billion in 2004, $9.8 billion in 2005 and $20 billion in 2006. As of the end of 2007, inflow stood at $21.9 billion. The total amount of direct foreign investment in Turkey's 85-year history had reached nearly $140 billion as of the end of the third quarter of 2007. The FDI inflow/gross domestic product (GDP) ratio in Turkey increased from an average of 0.5 percent in the 1990s to 1 percent in 2004, 2.7 percent in 2005 and to 5 percent in 2006.

International investors have an already important and growing share in the Turkish economy. There are 140 companies with foreign capital among the 500 largest industrial concerns in Turkey. As of 2006 these companies have a 41 percent share in total sales, a 37 percent share in profits, a 46 percent share in exports and a 28 percent share in employment. International investors in the automotive sector are among the country's major industrial investors and are also its largest export companies. Chemicals, energy, high-turnover consumer goods, food and tobacco are some of the other main industrial sectors in which international investors have an important share. The services sector also has attracted the attention of international investors with a high interest in the financial sector -- particularly over the last three years.

Looking at the countries of origin for FDI inflow to Turkey, European countries are at the top of the list, accounting for 60 percent of inflow between 2003 and 2007. In the same period the Netherlands accounted for 25 percent of FDI inflow, the US for 11 percent and Greece and Belgium for 10 percent each.

A lighthouse for foreign investors

The International Investors Association (YASED), founded in 1980, is a non-profit business association whose members are international companies operating in Turkey. Being the most important representative of foreign direct investors in Turkey, YASED has more than 250 international companies among its members. YASED members share a common vision and work proactively to promote a better business environment in Turkey, matching the best global business practices. YASED is committed to developing better channels of communication and coordination with other organizations in the business community and to generating greater awareness among the general public of subjects related to FDI and improving the image of FDI in Turkey among all stakeholders. The most important part of YASED's mission is lobbying in support of initiatives to harmonize Turkish legislation and business practices with international norms and to be committed to improving the ethics and the principles of corporate governance.

For more information on the business environment and FDI in Turkey, visit YASED's Web site at www.yased.org.tr.

PHOTO TURGUT ENGIN

YASED Chairman Tahir Uysal

Turkey's strategic location makes it an important option as a regional base as well. Many international investors in Turkey, including BASF, Benetton, BP, BSH, Coca-Cola, General Electric, Imperial Tobacco, Microsoft, Pepsi, Procter&Gamble and Unilever, use Turkey as a regional base for their operations.

Efforts to improve investment environment and YASED's contributions

Between 2003-2007 close to $50 billion in FDI entered the country, making the new challenge sustaining this level and ensuring greenfield investments. To maintain the current level and sustain the upward trend Turkey has to continue with structural reforms and efforts toward the improvement of the investment environment. A new reform process was launched in 2002 where the Coordination Council for the Improvement of the Investment Environment (YOİKK) was formed in order to improve Turkey's competitiveness in attracting FDI, determine the necessary steps and generate policies to remove administrative barriers to both local and international investment. Major business associations are part of this platform, which forms a healthy environment for the dialogue between the public and the private sector.

Since the establishment of the YOİKK mechanism, many of the technical committees' recommendations have entered into force as new legislation, policies or legislative amendments. The new Foreign Direct Investment Law of Turkey, which entered into force in 2003, is one of the most significant examples of providing a better match with international standards and reaffirming the equal treatment of foreign investors. There have been simplifications in the establishment of companies and licensing and permit procedures, and improvements in intellectual property rights issues and in the employment of expatriates. A decrease in the corporate tax rate from 30 percent to 20 percent as of 2006 was a major step as were deregulation and restructuring efforts in certain sectors, which have proven successful. Another important outcome of YOİKK works was the establishment of Turkey's Investment Support and Promotion Agency in 2006. The promotion agency provides an extensive range of services to investors with a one-stop-shop approach.

The road ahead

Beside these positive developments, there is still a long way to go to ensure a satisfactory level of FDI in the coming years. Fluctuations in the global economy since the second half of 2007 and uncertainties for 2008 are expected to hinder the upward trend in FDI both globally and in Turkey. The extent of this slowdown is still unclear, but FDI inflow of $15-20 billion for Turkey is expected in 2008.

Issues that have been made a priority by the International Investors Association (YASED) for the term ahead are the unregistered economy, transparency, employment, education, taxes, incentives, intellectual and industrial property rights, R&D investments and promoting Turkey as an attractive destination for FDI -- especially greenfield. Finally we support the EU membership process as an anchor for progress on these issues. Efforts toward the transition to a fully registered economy and a better tax and incentive scheme are at the top of the agenda. Hence Turkey has come a long way but should progress on these issues to provide a more favorable investment environment for both existing and potential investors.

Economy Minister Mehmet Şimşek and Lorenzo Giorgianni, the IMF's mission chief in Turkey, pose together.

Turkey to decide on new roadmap with IMF in August

ERCAN BAYSAL İSTANBUL

Turkey is at a crossroads with the International Monetary Fund (IMF), which it has frequently turned to in times of economic crisis. After the IMF Executive Board assesses a letter of intent Turkey has prepared in connection with the last review of the program, the current stand-by arrangement will come to an end. After the conclusion of the stand-by arrangement, post program monitoring will automatically start and will be in force until the Turkish government pursues another option available to the country. The IMF is reportedly of the opinion that Turkey does not need another stand-by arrangement.

IMF officials conveyed the IMF's position to Minister for the Treasury Mehmet Şimşek during his US visit two weeks ago. Turkish officials said then that Turkey may need a precautionary stand-by arrangement, given the political uncertainty surrounding the closure case brought against the ruling Justice and Development Party (AK Party). Turkish officials in charge of the country's economy noted that the country must be prepared for the outcome of the closure case. The possibility of making a precautionary stand-by arrangement with the IMF was also reported to Prime Minister Recep Tayyip Erdoğan, who is not warm to the idea of signing another stand-by agreement with the IMF.

IMF officials, on the other hand, stressed that Turkey must do its homework, including drawing up a clear schedule for the privatization of public banks, restructuring the revenue administration and taking steps toward revising civil service salaries. A new roadmap is expected to be formulated in August after developments are assessed in July.

Şimşek stated after his return from the US that assessments are being made about a possible precautionary stand-by arrangement. "Whether this will be a precautionary one or not will be decided by our government. Even if we make this decision today, the process will take several weeks or months since the IMF will make certain performance assessments," he said.

Debt to the IMF down $7.6 bln

Loans Turkey has received from the IMF since 1958 amount to 30.6 billion Special Drawing Rights (SDR), a potential claim on the freely usable currencies of IMF members (today, 1 SDR = $ 1.55). A total of 92 percent of this loan (SDR 28 billion) was received under the last three arrangements. The highest loan amounted to SDR 11.9 billion under a stand-by arrangement signed after an economic crisis in 2001. For the last five years, Turkey paid back more than it borrowed. The country's total debts to the IMF fell from $23.5 billion in 2002 to $7.6 billion in October 2007. Despite frequently voiced criticisms about the IMF abusing Turkey, Turkey's quota has been raised in parallel to the increase in the country's gross national product (GNP), as has been the case with China, Mexico and Korea. Turkey's quota was increased from SDR 964 million to SDR 1,191.3 billion.

Urgent loan availability under precautionary stand-by agreement

If Turkey chooses to make a precautionary stand-by agreement with the IMF, planned reviews will take place, as in normal arrangements. While the country has not made any commitment about utilizing loans, Turkey will be able to make use of these loans when needed.

İMKB, TOBB to promote public offerings

ERCAN BAYSAL ANKARA

PHOTO TURGUT ENGIN

The İstanbul Stock Exchange (İMKB) has reached an agreement with the Turkish Union of Chambers and Commodity Exchanges (TOBB) on a project that will invite Turkish companies to go public. A protocol for the project will be signed between the İMKB, TOBB, the Association of Capital Market Intermediary Institutions of Turkey and the Capital Markets Board (SPK) in two months.

During the first stage of the project, the companies on the İstanbul Chamber of Industry's (İSO) annually prepared Top 500 and Second 500 lists that are not listed on the İMKB will be urged to offer some of their shares to the public. International consulting firms will provide consultation to these companies about adapting to capital markets. After the consultations, the companies will be tested under international criteria and those that pass the tests will be invited to the İMKB.

Speaking to Today's Zaman, İMKB President Hüseyin Erkan said they were going to push for more Anatolian firms to be listed on the İMKB. He noted that the number of companies listed in 2002 was 320 and that the number remained the same at the end of 2007 as new companies only replaced those that had left the stock exchange. "We need to increase this number," he said, adding that they hoped to increase the number of companies on the İMKB to 1,000.

Only 105 out of top 500 listed

Only 105 of Turkey's top-500 industrial companies' shares are traded on the İMKB. Erkan said they were going to focus on these companies first. He also emphasized that making companies open to the public was not their only aim. He said they wanted to set a model for bolstering the corporate culture among Turkey's companies in the long run. The Turkish economy is facing hard times amid fluctuations in the global financial markets and political uncertainty caused by a closure case against the ruling Justice and Development Party (AK Party). However, Erkan said foreign investors' long-term confidence in the Turkish economy still persisted.

Erkan said international investors preferred to leave high-profit markets slowly. "But there is no real outflow from the Turkish market," he said. According to Erkan, the investors leaving stocks were investing in Treasury bills that have interest rates of around 18-19 percent. "They would not prefer to invest in US Treasury bills, which have an interest rate of around 2.5 percent."Erkan said some fears that investors were leaving the market but that this was not really the case. He explained the decline in the value of stocks also had caused that the foreign share in the stock market was still at around 71 percent, but that the majority of one-day transactions are being made by domestic investors. He said 80 percent of these transactions are made by domestic investors.

Time for prudence among Turkish non-bank companies

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One channel through which the growing disturbance in the US and European financial markets could affect the Turkish economy and other emerging markets is an outright outflow of capital. However, that is not very likely with the current state of the problems abroad and the returns offered in Turkey in general.

Another channel could be a slowdown in the external demand for Turkish exports. That will show its effects in the relatively longer term, and a weaker lira (at the recent rates) will affect the market in the opposite direction.

Still another channel could emerge with the worsening of the credit crunch in the Western financial markets through a difficulty in rolling over existing loans or in obtaining import finance by the real sector players.

The banking sector in Turkey is currently much stronger compared to 2001 and compared to its peers in many other countries. Foreign exchange open positions are virtually zero. Risk management and internal control/audit functions are more developed and strict, and the Banking Regulation and Supervision Agency's (BDDK) supervision is quite tight.

With relatively low foreign borrowing by the banks compared to their balance sheet sizes, difficulty in rolling over their foreign debts does not at all seem to be an insurmountable problem. Nevertheless it is reasonable to expect that the Turkish banks will now be looking to geographically diversify their banking relationships.

Non-bank companies have to be more careful, though. They have accumulated a significant amount of foreign debt and need more financing for their imports. A difficulty in obtaining new import financing may lead to a costly adjustment in the external balances of the country. But at the same time that scenario could give momentum to local production that would otherwise be displaced by cheaper imports.

Turkish non-bank companies will also have to be careful not to be affected by the problems of their foreign bankers. Recently there was an insightful example of that possibility. Société Générale, one of the world's largest banks, sued a Turkish company, Goldaş. Société Générale's claims have been reflected in the Turkish press as the bank having sent the company 15 tons (i.e., 15,000 kilograms!) of gold and never hearing about that gold again in terms of payment or return.

A bank in this situation would not give much confidence to its depositors as it would mean a quite alarming lack of risk management and operational capacity. The exact reason for the claim, which comes after what appears to have been many years of cooperation between the bank and its client, is not clear. But the case hints that other Turkish companies may face similar unreasonable demands from their foreign bankers. It may thus be time for them to diversify their bankers.

Central bank profits down dramatically

The Turkish Central Bank has announced a net profit of YTL 261 million for 2007, which is less then a tenth of its profit in 2006, when the bank had a net profit of YTL 3.1 billion. This decline in profits stemmed from the bank's losses in Turkish currency transactions

A PRINCELY DAY OUT

Fortunately, cars are not allowed on the islands, so the first thing you appreciate is the relative silence after the continual roar of traffic through central İstanbul

ASHLEY PERKS İSTANBUL

At this time of year, there are some days when you just don't know what to do; either it's raining or it's trying to snow (Pffff! in Istanbul?!) or like today, the sun is shining in a clear, bright blue sky. So what should one do? I had been indoors for two days during Kurban Bayramı and as soon as I saw the sun and blue skies, I knew exactly what I wanted to do: go to the islands. I live in Bostanci so it is very easy to go down and catch a launch or steam ferry heading for the Princes' Islands. By the way, even if you don't have the privilege of living in Bostanci, if you check out İDO timetables, you should be able to find a ferry or sea bus going to the islands. And it is well worth it.

Fortunately, cars are not allowed on the islands, so the first thing you appreciate is the relative silence after the continual roar of traffic through central İstanbul. You can hear the rumble of steamers, the throaty roar of some boat driver, or the throbbing of a launch bringing residents and visitors to the islands of course, but in general you hear nothing but the whistle and bustle of birds in the trees and the sibilant sighing of the wind through the pine trees. However, you do have the rather piquant odor of the horses that pull the phaetons that serve as taxis on the islands to put up with.

Apart from the silence, there is the magnificent sight of the islands themselves as you approach, even from far off. On this bright blue day, there is an impressionistic image of gray shapes rising out of the wintry white sunlight, contrasting with the cobalt blue sky -- itself competing with the sparkling aquamarine of the sea, today as calm as a millpond. In short, a perfect day for sailing! Kınalıada, quite built up, is easily recognizable, resembling an aircraft carrier with its Mohican haircut created by the raft of telecommunication aerials.

Next comes the smallest of the inhabited islands, Burgazada. Personally, it is my favorite. Little visited, because it has nothing much to see but a very pretty Greek church, and generally inhabited by İstanbulites, but which also has a small expat community during the summer, it boasts, however, the highest point of the four Princes' Islands, crowned with a small copse of pine trees. Turning left and then taking the next right from the boat station, you can follow a long and winding road that leads up to the summit from which you have a magnificent view, not only of the other islands, but also, on a clear day, across the sea to the range of hills leading down to Yalova. There is a bizarre football pitch too, so if you go with friends you will be able to play soccer between the trees! Continuing clockwise round the island, you will pass a ruined church and then come upon a café with probably the best view in İstanbul.

The second largest of the islands is Heybeliada, which I love very much too. Famous for its historic Greek orphanage and Turkish naval college, it also has a wonderful picnic area up in the pine forest -- turning right from the boat station -- where you can sit, even on a cold winter's day, and admire the beauty of the view over to Burgazada and Kınalıada. West-facing, it guarantees you afternoon and evening sun if the weather is right, and the chance for a moment of calm before you return to the storm of mainland İstanbul.

The largest of the archipelago is, aptly named Büyükada, or Big Island. With the famous Hotel Splendide -- once the residence of Trotsky when he was in exile in Turkey -- it has all the hallmarks of a southern English seaside resort with a dash of Cote d'Azur. Hugely popular and overrun with domestic and foreign tourists during the summer, it is nevertheless a beautiful island, and, if you have the funds, a "grand tour" in a phaeton is well worth the expense. The maritime views are, of course, breathtaking, but you will also come across numerous very interesting buildings from the Ottoman Empire including, at its pinnacle, a Greek church.

What is so refreshing about any and all of these islands is the sense of life lived at a gentler pace than on the mainland. There is the absence of traffic, of course, but also the way people indigenous (or almost) to the island go about their business in such a relaxed and unhurried manner. My working life is frenetically busy, but just to spend one day on one of the islands is such a tonic; I feel almost as if I have had a holiday. The sea-air is so fresh and invigorating and the smell of grass and pine so refreshing that it is, quite literally, a breath-taking experience.

The day can start so well, with a cup of coffee at one of the water's-edge cafés and a read of the newspaper while watching the intricate ballet of ferries, sea-buses and launches coming and going from the Bostanci harbor. Seagulls swoop and squawk, crested grebes bob and bustle and cormorants sail majestically through the throng, diving now and then for the tiny fish that swim this close to shore. You can watch couples walking entwined in a romantic promenade or power walkers taking their daily constitutional. Nipping between both, a growing peloton of cyclists eat up the pink tarmac of the bicycle lanes. In fact, you don't have to leave Bostanci at all if you don't feel like it, because the view and the sights and sounds of the harbor are pleasure enough, but all the coming and going of boats and the very sight of those islands, sparkling by day and lit up at night like moored off-shore cruise liners, tempts you to get up and go and grab the first boat across.

If you want to buy or rent permanently on any of the islands, prices are well below those on the mainland. Even so, it is worth having a Turkish speaker with you as real estate agents will try and pump up the price when they deal with a foreigner. Ferry, sea-bus and launch connections to the mainland at Bostanci and Kadıköy as well as Eminönü on the European side are regular and good, but winter can present problems and you have to be very familiar with the last sailing hours of the day.

Whether you fancy living there, renting for the summer or just want to have a really relaxing and uplifting day out, taking the time to cruise around the Princes' Islands will, I can assure you, make your day and be as beneficial as any hyper-expensive break in the traditional resorts. If you are living and working in İstanbul, you have no excuse. Go on, have a princely day out!