Turkish Economy and Turkish Banking System in 2004

1. General Evaluation

1.1. Economic Performance

The program revised with International Monetary Fund was completed.

Turkey and International Monetary Fund (IMF) had signed a stand-by agreement in 1999 for a period of 3 years. This stand-by agreement failed to be completed due to the financial crisis emerged in Turkey in 2001. However, it was revised with the IMF in 2001 by securing additional financing and extended until the early months of 2005.

The purpose of the economic program was defined as achieving a sustainable and steady economic growth environment by eliminating the macroeconomic imbalances. New monetary policy aiming to lower the high inflation rate and maintain price stability was initiated to achieve this goal. In order to support the monetary policy, a tight fiscal policy setting forth a primary surplus of 5 percent of GNP in the consolidated budget and aiming to lower the public sector deficit was envisaged. Another important target of the program was restructuring of the financial sector, and particularly the banking system. Accordingly, banks with weak financial structures were left out of the banking system, and the effectiveness of banking supervision has increased, and banking rules and regulations have been harmonized considerably with the international standards.

Developments in the Turkish economy and the banking system in 2002-2004 period took place in accordance with the targets of the economic program. Economic performance of Turkey improved considerably in terms of basic economic indicators. An important outcome of this improvement was that international rating agencies increased Turkey’s credit rating.

Improvement in economic performance continued in 2004; growth accelerated while inflation decreased.

Improvement in economic performance gained momentum in 2004. Monetary policy aiming at price stability under free floating exchange rate regime, and the fiscal policy implementations aiming to achieve balance in public finance in the long term, continued in parallel with the targets of the economic program. In addition to the policies aiming to establish sound macroeconomic balances and sustain stability in the financial markets, the process of economic recovery was supported by the positive developments in global economy.

Inflation declined further while growth accelerated. The economic growth rate of 9.9 percent in 2004 was considerably above both the program target and the long term average growth rate of Turkey. Per capita income increased above USD 4,000 for the first time in Turkey. Inflation in consumer prices decreased to a single digit after a long time. Fiscal discipline in public sector was strictly maintained. The ratios of both the public sector deficit and outstanding public debt to GNP declined. Real interest rates decreased considerably, while the maturity of public sector borrowing was extended.

In order to achieve the primary surplus target, which was one of the main indicators of the economic program, cost-lowering and revenue-raising measures were taken simultaneously. The implementation on the collection of a fund share equal to 10 percent of income tax was abandoned; however, the rate of corporation tax was increased to 33 percent and some of withholding rates in income tax were also increased to compensate the loss in public revenues. In order to curb domestic demand, the current rate for Resource Utilization Support Fund deducting from consumer loans, and the private consumption tax rate for automobiles were increased in the second half of the year. Special communication tax became permanent and its scope was broadened. The implementation of inflation accounting started in 2004 for the first time in Turkey.

Public sector savings deficit and private sector savings surplus narrowed.

The decrease in the public sector savings deficit (savings - investments) continued in 2004 due to the improvement in fiscal performance. On the contrary, savings surplus decreased considerably in private sector where the investment drive experienced a quick revival as a result of the improvement in expectations, relative decrease of the public sector pressure on resources, and also the improvement of Turkey’s borrowing capability in international markets. As a consequence of this trend, general domestic savings deficit increased. Consumption demand in private sector also accelerated.

Contrary to the expectations, rapid growth of the economic activity failed to contribute to the efforts to decrease the unemployment rate. The increase in unemployment rate halted, however the rise in employment was very slow. The data indicated that labor productivity increased in Turkey in 2004. Real (inflation-adjusted) wages in both public and private sectors increased slightly.

Foreign currency supply increased faster than foreign currency demand.

Banks as well as non-financial institutions in private sector increased their borrowing from abroad. At the same time, interest of the foreign investors for Turkish capital market instruments gained momentum. Despite the high-level current account deficit, foreign currency supply was higher than foreign currency demand. In order to ease the pressure of the foreign currency surplus on the financial markets, the Central Bank created foreign currency demand via its purchases from the market within the framework of auctions held in accordance with the pre-announced rules, as well as by direct buying interventions to the market occasionally. The Central Bank’s foreign currency reserves increased to USD 36 billion and its net foreign exchange position increased to USD 3 billion.

The Central Bank decreased its short term borrowing rate by 7 percentage points to 19 percent in parallel to the inflation expectations and realizations. Interest rate on government securities decreased by 5 percentage points to 23 percent.

Demand for TL investment instruments increased faster.

Demand for TL denominated investment instruments continued to increase as the demand for TL deposits and government securities grew in real terms. Foreign currency substitution remained rather sluggish. The ratio of M2RF (demand for money in all TL denominated investment instruments) to GNP increased by 3 percentage points to 30 percent, while the ratio of M2YRF (demand for money including also foreign exchange deposits) to GNP increased by 1 percentage point to 47 percent.

The ratio of loans both to deposits and GNP continued to increase. The ratio of total loans extended by commercial banks (performing loans + non-performing loans after provisioning) to total deposits + repos increased by 13 percentage points to 47 percent, and the ratio of total loans to GNP increased by 3 percentage points to 19 percent. The increase in loan supply mainly resulted from the rise in consumer loans.

Individual investors’ demand for government securities continued due to tax advantages of the government securities compared with deposits. However, the ratio of TL deposits to

GNP increased by 2 percentage points to 23 percent, while the ratio of total deposits to GNP remained the same at 41 percent. The ratio of government securities portfolio of individual investors to GNP was 23 percent. The increase in the ratio of investment funds to GNP by 2 percentage points to 6 percent was one of the significant developments in the recent period. There was no major change in the maturity structure of TL and Fx deposits, despite the ongoing application of lower withholding tax in favour of longer maturity deposits, and the average maturity remained the same at 3-month.

İstanbul Stock Exchange (ISE) Index and trading volume posted an increase of 38 percent and 47 percent in dollar terms, respectively, in 2004. Market capitalization of the companies traded in the ISE increased from USD 69 billion to USD 98 billion, while that of banks traded in ISE increased by 55 percent.

Foreign trade volume grew, current account deficit increased.

The economic growth that realized higher than expected led to an acceleration in the increase of imports. At the same time, increase in exports also continued. Foreign trade volume grew by 37 percent to USD 160 billion, and its ratio to GNP was 53 percent. Foreign trade deficit increased by 57 percent to USD 34 billion. In addition to high economic growth, other factors that had an effect on foreign trade were as follows; the continued increase in production and trade volume globally, continued liquidity supply in international markets, increase in oil prices, and the appreciation of TL against major foreign currencies.

Current account deficit increased by 92 percent and reached USD 15 billion in 2004. The ratio of current account deficit to GNP increased by 3 percentage points to 5.1 percent. Capital inflows gained momentum due to external borrowing of the banking system and other non-bank institutions in the private sector. Non-foreign exchange debt creating capital inflows continued to increase at a higher rate due to the rise in the demand of foreign investors for government securities and the shares of the companies traded in ISE.

Outstanding external debt reached USD 162 billion by an increase of about USD 16 billion. The ratio of external debt stock to GNP decreased from 61 percent to 54 percent.

Political developments and international economic relations;

The most significant internal political event in 2004 was the municipality elections held in March. The Ruling Justice and Development Party (AK Parti) maintained the public support that it held in general elections.

The relations with the European Union (EU) further improved as harmonization with the political and social regulations of the EU was completed to a great extent. Following the positive opinions of the EU decision organs, the heads of state or governments of the EU member countries resolved in the Summit held in 17 December 2004 that negotiations with Turkey for its full membership to the EU should start on 3 October 2005.

The IMF reviews on the assessment of the economic program were completed successfully. The Turkish government and the IMF declared that they agreed in principle for signing a new IMF-backed stand-by agreement at the end of 2004. The principle agreement sets forth a restructuring of Turkey's outstanding debt to the IMF. All these developments affected the forward-looking expectations positively.

1.2. Developments in the Turkish Banking Sector

Banking sector's performance also continued to improve in 2004.

Sustained economic performance also had a positive effect on the financial sector leading to further improvement in the performance of the banking system. Confidence in the financial sector and banking system increased, international credit worthiness of Turkish banks increased.

Financial institutions operated in a healthier environment as a result of the stability maintained in the money markets, the growth in economical activity, the recovery in competitive conditions of the operating banks due to the suspension of the activities of the financially weak banks, and the efforts of banks to strengthen their financial structure and shareholders' equity. The growth in demand for TL denominated financial instruments continued. Some of the basic risks were pulled down to more manageable levels due to the fall in inflation and interest rates as well as the improvement in foreign currency positions.

Demand for both corporate and consumer loans rose notably due to the fact that the pressure from public sector on financial markets decreased relatively. As a result of better expectations, demand for loans from both corporates and customers continued. Interest rates on deposits and loans decreased substantially due to ongoing intensive competition in the banking system

Insurance coverage on saving deposits was limited.

One of the most important developments in 2004 concerning the banking system was the removal of full insurance on saving deposits; the insurance coverage on saving deposits was limited to YTL 50. The transition to limited deposit insurance was realized smoothly in the markets due to the planing of this transition one year in advance by the BRSA, healthy relations among banks, positive approach of especially state-owned banks which lowered deposits rather below the market average, higher liquidity position of banks, and recovery in economic performance. Bank deposits continued to rise further following the limitation of deposit insurance.

There were intensive works in 2004 on the draft law amending the Banks Act No. 4389. The amendments mainly aim to harmonize the legal framework for regulation and supervision of banks with international standards. These efforts were considerably successful in harmonizing with best international practices regarding the regulations directly related with banks. Among the major amendments, important ones were the determination and definition of the banks' activities; definition of the private finance institutions as participating banks; and re-arrangement of the issues such as bank ownership, the risk relationship between banks and their partners, the structures of Banking Regulation and Supervision Agency (BRSA) and Savings Deposit Insurance Fund (SDIF).

Positive steps taken for the reduction of intermediary costs.

Some positive steps were taken for the reduction of the burdens increasing the costs of intermediary activities of banks. Stamp tax and duties on loans, and transactions yielding foreign exchange income were removed. The Resource Utilization Support Fund deduction rate of 3 percent as applied to commercial and corporate loans was lowered to zero from August. With an amendment made in December withholding tax on consumer loans was raised from 10 percent to 15 percent.

Risk management is getting more important.

In 2004, the banking system made serious efforts to develop risk management, reduce its operational costs, and increase the quality of the financial services within the framework of the prudential regulations and banking principles. Regulations concerning Basel II (New Basel Capital Accord) were monitored closely, and the effects of the regulations both on banking system and on the economy have been analysed.

Other important developments;

Pamukbank TAŞ, previously transferred to Savings Deposit Insurance Fund by a special law, was merged with state-owned T. Halk Bankası AŞ.

With an amendment in Banks Act in December 2003, special provisions were introduced in order to speed up the collection of the receivables stemming from the banks whose banking licenses were revoked or who were closed. The administration of the Savings Deposit Insurance Fund and the management of the non-performing assets were transferred to the newly established Savings Deposit Insurance Fund.

Registry pardon under the Law no. 5033 ruled that the debt records with negative content as kept in the Central Bank would be erased providing that such debts were paid within 3 months at the latest following the effective date of the referred Law, and that such erased records could not be taken into consideration in the banking transactions with banks and private finance institutions.

The General Assembly of Administrative Law Chambers of the Council of State dismissed the objection against its previous judgment that the verdict for the transfer of Demirbank and Kentbank to the Savings Deposit Insurance Fund was in contradiction with the laws. In other words, the Council of State regarded the transfer of Demirbank and Kentbank to the Fund unlawful.

PTT was allowed to use the word 'bank' in its title on condition that it would not collect deposits from the public.

Per capita bank assets were USD 3,212.

Total assets of the banking system grew by 23 percent on TL terms and 28 percent on dollar terms in 2004. Total assets of the banking system reached USD 229 billion, while its ratio to GNP remained the same at 71 percent as compared to the previous year. Per capita bank assets amounted to USD 3,212.

The number of commercial banks (depository banks) and non-depository banks operating in Turkey was 48 by the end of 2004. The number of banks was 33 less than in 1999, and 2 less than in 2003. Of the commercial banks 3 were state-owned, 18 were privately owned, and 13 were foreign banks.

Foreign investor interest boosts.

The share of commercial banks in total assets of the banking system was 96 percent. The state-owned banks had a share of 35 percent, while private banks' share was 57 percent in total assets. Foreign banks had 3 percent share in total assets. There was an increasing interest from foreign investors towards the Turkish banking system in the recent term. Following UniCredito Italiano SPA's purchase of 50 percent of the shares of Koç Finansal Hizmetler (Koç Financial Services), BNP Bank purchased 50 percent of TEB Mali Hizmetler AŞ (TEB Financial Services).There was a change in the status of

Deutsche Bank, whereby Deutsche Bank, previously in non-depository bank category, was granted the authority to collect deposits from the public. Citibank AŞ also switched to the category of banks established in Turkey, from its previous status as a foreign bank branch.

The number of branches and employees in the banking system began to rise in 2004, notably in privately owned banks. The number of bank branches increased by 140 to 6,106, while the number of employees increased by 3,914 to 127,163.

Improvement in balance-sheet structure continued.

Improvement in the balance sheet structure of the banking system continued in 2004. The share of TL assets in total assets increased to 64 percent in 2004 by an increase of 2 percentage points as compared to 2003, meanwhile the share of TL denominated liabilities in total liabilities also increased to 60 percent by an increase of 3 percentage points.

The share of loans in total assets rose by 6 percentage points to 34 percent. The ratio of loans to total assets was 21 percent for state-owned banks, 40 percent for privately owned banks, and 46 percent for foreign banks. Provisions were allocated for 89 percent of non-performing loans. The ratio of non-performing loans to total loans before provisioning was 6.2 percent, while the same ratio after provisioning was 0.7 percent. The share of securities in total assets was 40 percent. Securities account in the balance sheet formed 58 percent of the total assets in state-owned banks, while this ratio was 32 percent in privately owned banks. The share of permanent assets which were comprised of fixed assets, subsidiaries and non-performing loans decreased to 7 percent.

In liabilities side; the shares of TL deposits and foreign exchange deposits in total liabilities were 36 percent and 29 percent, respectively. Non-deposit liabilities in which funds borrowed from foreign banks and institutions constituted the principal part, had 15 percent share in total liabilities.

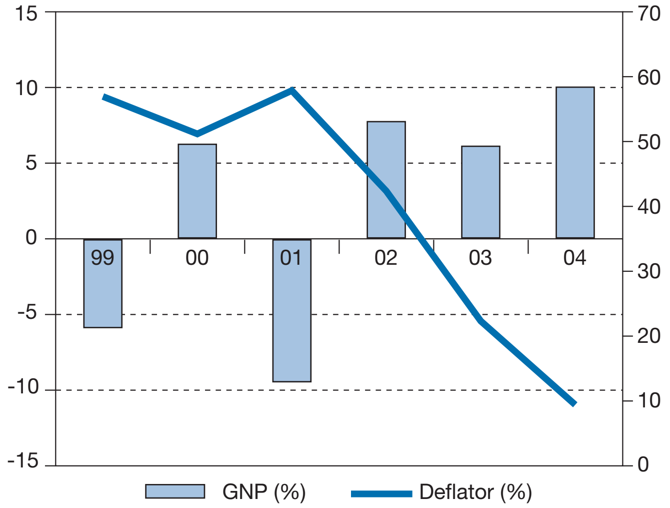
Shareholders' equity and working capital continued to increase.

Shareholders' equity increased by 35 percent and reached USD 34.4 billion in 2004. The ratio of shareholders' equity to total assets was 15 percent. The amount of losses from previous years was the main reason behind the increase in shareholders' equity. Working capital defined as shareholders' equity after deduction of permanent assets recorded an increase of 59 percent and reached USD 17.4 billion, amounting to 7.6 percent of the total assets.

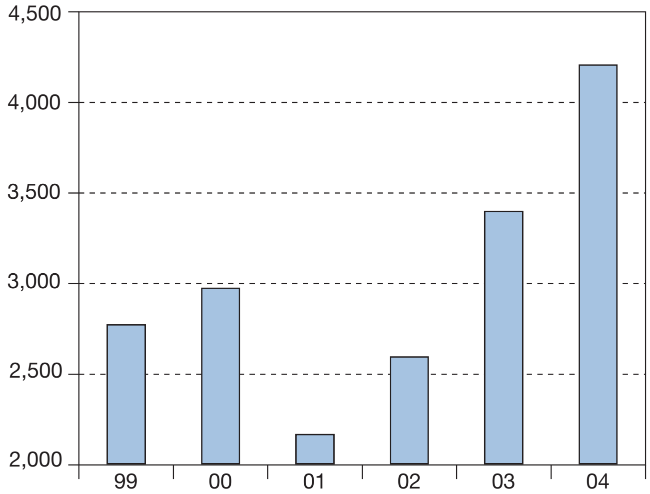
Profit margin grew by 15 percent in the banking sector. Profits of the state-owned banks increased by 50 percent, while that of private banks decreased by 3 percent. Return on equity was 14 percent in the sector; while it was 26.6 percent in state-owned banks, and 10.3 percent in privately owned banks.

The major contribution to the profits was the rapid increase in net interest margin. The ratio of net interest margin to total assets was 5.8 percent, while the contribution of trading account securities decreased significantly. Banks continued their efforts to reduce their operating costs, while on the other hand they concentrated on increasing the income from fees and commissions. There were initiatives to assume joint action by all banks for the purpose of reducing operational coasts. Banking system continues to focus on technological investments in order to increase the quality of the financial services, to generalize these services and benefit from economies of scale.

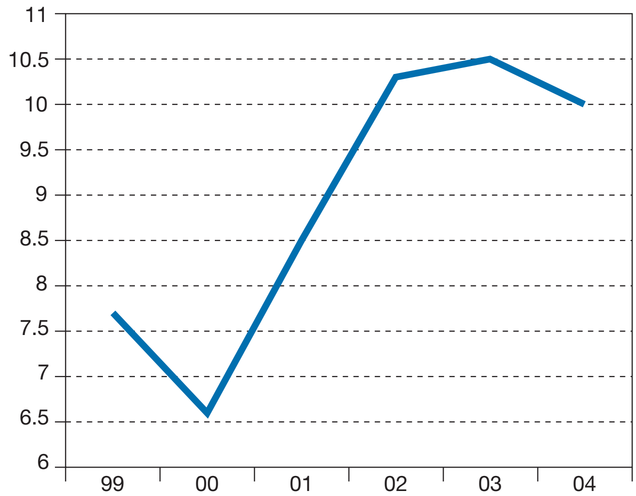
Inflation continued to decrease while growth accelarated



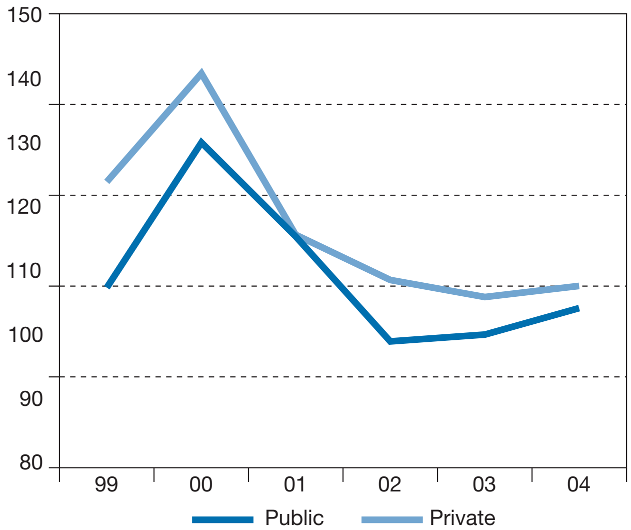
Per capital income reached the historicaly highest level



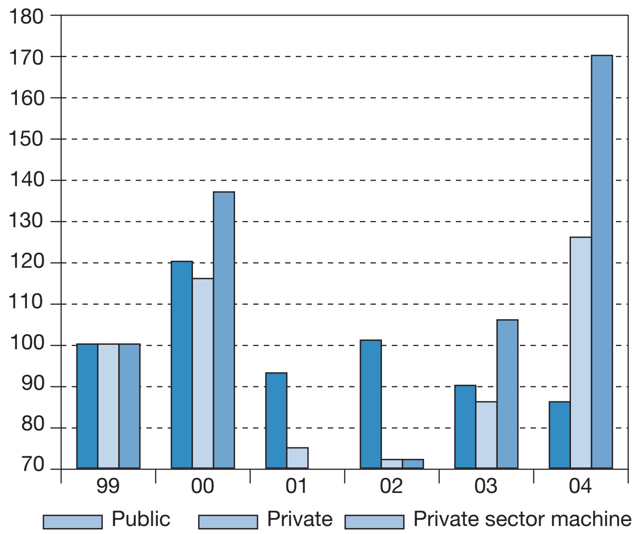
Unemployment rate decreased slowly in 2004



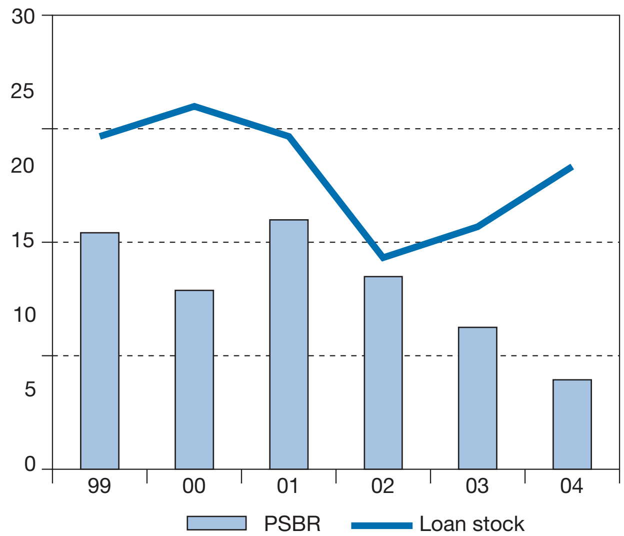
Real wages and salaries increased slowly in 2004.



Machine investments in private sector increased rapidly.



Loans began to climb while puplic sector borrowing requirement declined. (As percentage of GNP)



2. Developments in the Turkish Economy in 2004

2.1. Growth

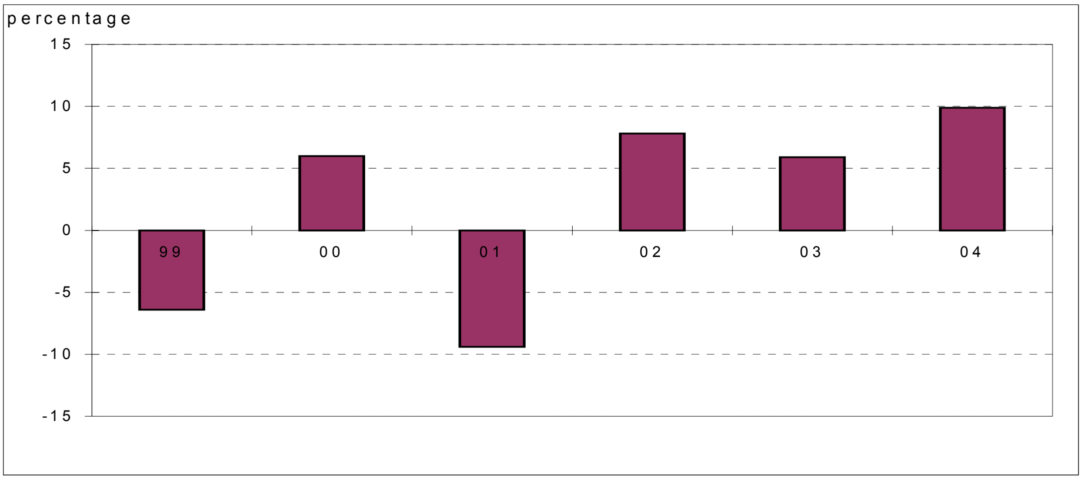
Recovery in the growth performance which began in 2002, accelerated further in 2004 leading to economy growth faster than predictions. According to the data of State Institute of Statistics, GNP increased by 9.9 percent, and GDP increased by 8.9 percent in 2004 in constant prices. GNP reached TL 428,932 trillion in 2004 with an increase of 20.3 percent in current prices. GNP deflator decreased from 22.5 percent to 9.4 percent.

Gross National Product

	1999	2000	2001	2002	2003	2004
Growth rate (percent)						
In current prices	46.3	60.4	40.5	55.8	29.7	20.3
In constant prices	-6.1	6.3	-9.5	7.9	5.9	9.9
Deflator (percent)	57.0	51.7	56.3	43.8	22.5	9.4
GNP						
(1987 prices, TL billion)	112,044	119,145	107,783	116,166	123,165	135,308
TL trillion	78,283	125,596	176,484	275,032	356,681	428,932
USD billion	185	201	148	180	239	300
Income per capita (USD)	2,879	2,965	2,146	2,598	3,383	4,172

GNP increased by 25.2 percent in dollar terms and reached USD 300 billion. Income per capita grew by 18.5 percent in dollar terms and 23.3 percent in current prices, and reached USD 4,172.

Growth of GNP (percentage change in constant prices)



There was a rapid growth in all main sectors of the economy except the agriculture. Agricultural sector, industrial sector and service sector grew by 2 percent, 9.4 percent, and 11.7 percent, respectively. In service sector, growth rate was relatively high, particularly in sub-sectors of trade, and business and personnel services. A slow recovery started in construction sector. Growth in financial institutions, government services and ownership of dwelling was rather moderate. In current prices the share of agricultural sector in GDP decreased by 1 percentage point to 12 percent in current prices; while that of service sector increased by 1 percentage point to 58 percent. The share of industrial sector in GDP remained the same at 30 percent.

Sectoral Growth Rates and Breakdown

	Percentage change (in constant prices)				Percentage shares in GDP (in current prices)			
	2001	**2002**	**2003**	**2004**	**2001**	**2002**	**2003**	**2004**
Agriculture	-6.5	6.9	-2.5	2.0	14	14	13	12
Industry	-7.5	9.4	7.8	9.4	29	29	30	30
Services	-11.2	7.5	6.7	11.7	57	57	57	58

Source: State Institute of Statistics

Industrial sector and the service sector, which posted a growth rate of 11.7 percent in 2004, continued to be the driving force behind the economic vitality. The growth rate in manufacturing industry, the most significant sub-sector of industry, was 10 percent. As for the sub-sectors of the manufacturing industry; the growth rate in sub-sectors such as leather, wood, chemical materials, plastics and rubber products, production in press and publications, and more pronouncedly in manufacturing of motor vehicles, medical instruments, communication devices, computing and office accounting machinery, major metals industry was higher than the growth rate of the manufacturing industry as a whole. Production in energy sector increased by 6.8 percent. Average capacity utilization ratio increased by 4 percentage points to 82 percent. This ratio was 86 percent in public sector, and 80 percent in private sector.

On the expenditures side, consumption grew by 9 percent while investments grew by 33 percent. Considerable portion of the rise in aggregate demand resulted from the private sector. Accordingly, consumption expenditures in constant prices grew by 10 percent in private sector, and by 1 percent in public sector. Private sector investments grew by 46 percent, while public sector investments contracted further by 12 percent. Growth in private sector fixed capital investments resulted from machinery and equipment investments which grew by 60 percent. Building construction started to grow from the second half of the year, and it increased by 15.3 percent as compared to the previous year.

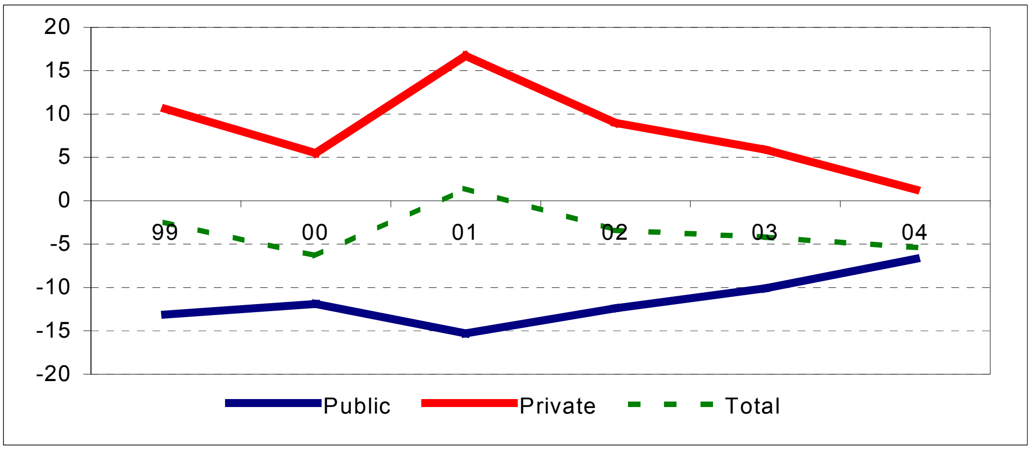
The shares of private consumption expenditures and investment expenditures in GDP were 64.1 percent and 19.4 percent, respectively. The share of public consumption expenditures in GDP was 7.1 percent while that of public investment expenditures in GDP was 4.7 percent. The major factor affecting the consumption expenditures of the public sector was decline in interest expenditures.

Net contribution of foreign trade account on growth was negative as the imports increased faster than the exports in 2004. Positive contribution of stock changes which was the most important contribution to the growth in previous years continued in 2004, as well. Stock changes increased by 15 percent in current prices.

The value added by financial institutions increased by 1.1 percent in 2004. This increase was mainly resulted from the increase in the number of employees in the banking sector and also slight increase in the real wages of the employees. The share of the financial institutions in GDP was 1.7 percent.

As for the general savings balance; domestic savings ratio increased by 3 percentage points to 22.1 percent according to the estimations of the State Planning Organization. The private sector savings decreased slowly while the public sector savings gap narrowed further.

Balance of Savings (As percentage of GNP)



Savings-investments gap continued to increase despite the rise in savings ratio. Gross savings-investments balance reached 5.4 percent of the GNP in 2004 from 4.2 percent in 2003. Public savings gap decreased to 6.7 percent from 10.1 percent in the previous year, while private savings surplus decreased to 1.3 percent from 5.9 percent.

Domestic Savings and Balance of Savings (As percentage of GNP, percentage)

	1999	2000	2001	2002	2003	2004
Domestic savings	19.8	18.1	17.4	19.0	19.3	22.1
Public	-6.4	-5.2	-9.9	-6.2	-5.3	-1.9
Private	26.2	23.3	27.3	25.3	24.6	24.0
Savings balance	-2.8	-6.5	1.3	-2.6	-4.2	-5.4
Public	-12.6	-12.1	-15.3	-12.5	-10.1	-6.7
Private	9.8	5.7	16.7	9.9	5.9	1.3
External funds	2.8	6.5	-1.3	2.6	4.2	5.4

Source: State Planning Organisation

2.2. Employment, Productivity and Wages

Real wages increased in 2004; however, the rise in employment was limited despite the fast growth in economy. Upward trend in partial productivity of the manufacturing industry considerably slowed down starting from the second half of the year.

Real Labor Cost Index (94=100)

	2000	2001	2002	2003	2004
Total					
Public	130	116	100	101	105
Private	141	116	109	106	109
Employee	130	117	120	122	128
Minimum wage	156	128	133	154	171

Source: State Planning Organisation, TİSK (Turkish Trade Union Confederation)

According to the estimations of the State Planning Organization, both real labour costs of public workers and real wage costs and the minimum wages of employees increased in real terms.

Increase in labour productivity slowed down to 2.2 percent in 2004 from 11.9 percent in 2003.

Productivity Index (Annual percentage change)

	2003	2004/I	2004/II	2004/III	2004/IV
Per worker	11.9	10.9	14.2	6.4	2.2
Per hour	11.4	8.5	13.6	6.4	1.6

Source: State Institute of Statistics

Collective bargaining contracts covering a total of 325,189 workers from 7,913 workplaces were concluded in 2004. In 2003, a total of 329,240 workers from 7,806 workplaces were covered by collective bargaining contracts. While a total of 144,772 workday losses were suffered in 23 strikes in 2003; the number of workday losses decreased to 93,161 in 30 strikes in 2004. A total of 20,826 workday losses were suffered in 1 lockout application in 2004, against 110,415 workday losses suffered in 2 lockout applications in 2003.

Contribution of the economic growth to the employment was limited. There was no significant change in the unemployment rate. According to the data of the State Institute of Statistics, total labour supply was 24.3 million people and the total employment was 21.8 million people. The number of unemployed people reached 2.5 million people, increasing approximately by five thousand compared to the previous year.

Unemployment Rate (Percentage)

	1999	2000	2001	2002	2003	2004
Unemployment rate						
Overall	6.4	6.3	8.4	10.3	10.5	10.3
Urban	9.4	8.2	11.6	14.2	13.8	13.6
Educated youth	...	...	25.5	29.1	27.8	30.0
Underemployment rate						
Overall	5.6	6.0	6.1	5.4	4.8	4.1
Urban	6.5	5.9	6.5	3.4	5.2	3.8
Educated youth	...	...	6.0	6.0	6.5	...

Source: State Institute of Statistics

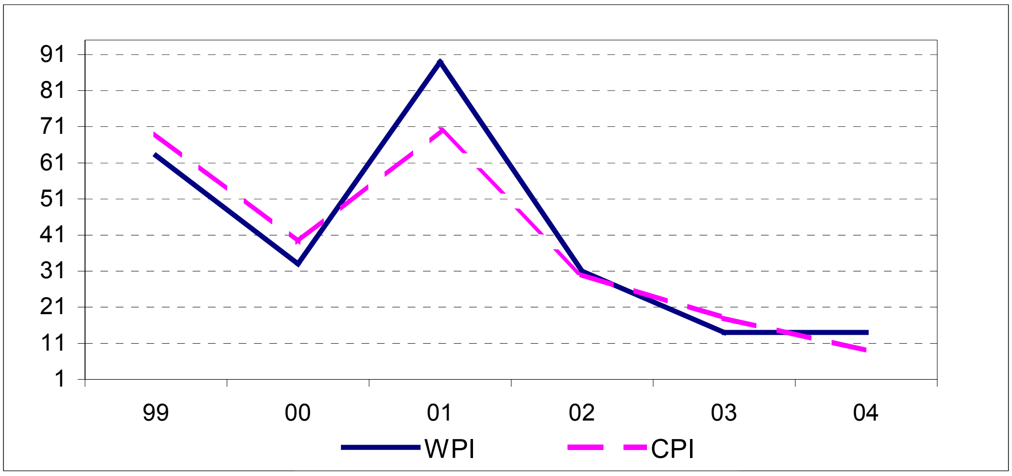
Accordingly, the unemployment rate was 10.3 percent by the end of 2004, as compared to that of 10.5 percent in 2003. Urban unemployment rate decreased by 0.2 percentage points to 13.6 percent in 2004. Unemployment rate was 14.4 percent, when underemployment was also included. Out of the total employment; 43 percent were employed in services, 34 percent in agriculture, and 18 percent in industry sectors.

2.3. Inflation

Keeping its downward trend started in 2001, inflation fell to single-digit level in 2004, which was the lowest level since Turkey's transition to the market economy in 1980. 12-month wholesale price index (WPI) decreased to 13.8 percent, and consumer price index (CPI) decreased to 9.3 percent. Increase in CPI was below the 12 percent target for 2004. Average annual price increases were 11.1 percent in WPI, and 10.6 percent in CPI.

Expectations and behaviours of economic agents were positively affected by the favourable approach and tight fiscal policy of the government, and by the adherence of the Central Bank to the implementation of monetary policies targeting price stability.

Inflation (12-month, percentage change)



Rising oil prices and the upward tendency in US interest rates didn't have a negative effect on expectations in the short term.

Imports became favourable depending on the real appreciation of TL against major foreign currencies. Decrease in real interest rates was limited despite the rapid fall in nominal interest rates.

Inflation (percentage)

	2001	2002	2003	2004
Annual average				
Wholesale	62	50	26	11
Public	71	49	25	11
Private	58	51	26	11
Consumer	54	45	25	11
12-month				
Wholesale	89	31	14	14
Public	100	32	11	20
Private	85	30	15	12
Consumer	69	30	18	9

Source: State Institute of Statistics

These two factors limited the price increases in turn. However, because of low-level of prices, the prices in public sector increased well above the average price increase in 12-month of 2004. Wholesale price index increased by 19.5 percent in public sector, and 11.7 percent in private sector as compared to the previous year. As for the manufacturing industry where prices increased by 14.8 percent in general; the increase in prices of the public sector was 24.3 percent, and 10.6 percent in private sector. Prices increased by 14.1 percent in agricultural sector, while there was a fall of 0.6 percent in energy sector prices.

2.4. Public Sector

According to the estimations of the State Planning Organization, total public revenues with 21 percent, grew above the GNP deflator. Total public expenditures increased by 10 percent. As a result public sector deficit narrowed by 26 percent. The ratio of total public revenues to GNP increased by about 0.4 percentage points to 30.8 percent, while the ratio of public expenditures to GNP fell by 3.1 percentage points to 36.7 percent. Due to the tight fiscal policy, the ratio of public sector deficit to GNP decreased to 5.9 percent in 2004 as compared to that of 9.4 percent in 2003.

Primary balance which was monitored closely as the most important indicator under the economic program regarding the maintenance of the fiscal discipline and the sustainability of the domestic debt dynamics continued to give surplus in 2004. Primary surplus was estimated as 8.4 percent in 2004, which was 7.7 percent in 2003. Consequently, the ratio of the consolidated budget primary surplus to GNP, was realized as 6.1 percent according to the definition under stand-by agreement signed with the IMF.

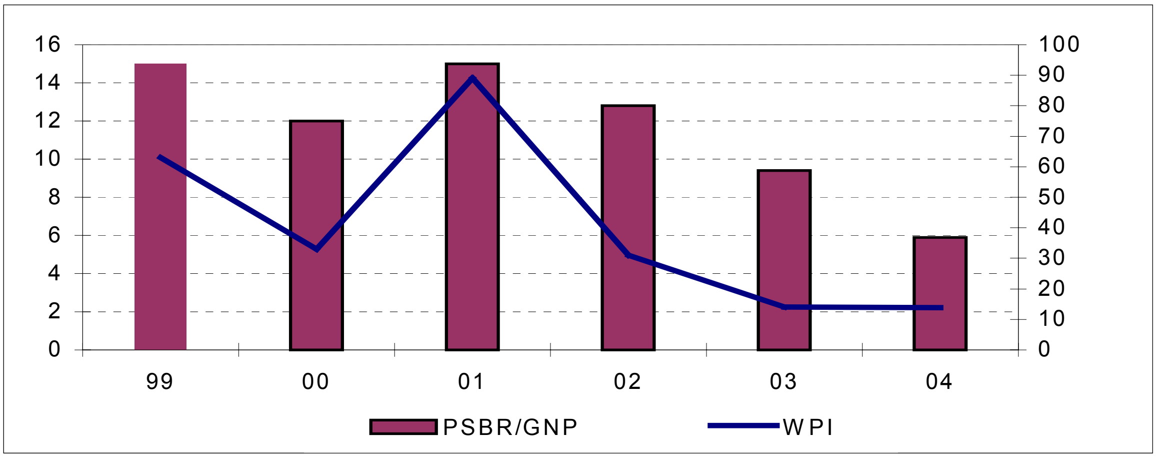
Public Sector Borrowing Requirement (As percentage of GNP)

	2000	2001	2002	2003	2004
Consolidated budget	10.9	17.4	14.9	11.3	8.0
SEE's*	2.1	0.4	-1.0	-0.7	-0.4
Local administrations	0.4	0.3	0.1	0.5	0.0
Funds	-1.2	-0.5	0.0	-0.1	-0.4
Other	0.5	-0.9	-3.0	-1.4	-1.4
Public sector deficit	11.8	16.4	12.8	9.4	5.9
Public sector primary balance	-5.7	-8.1	-7.0	-7.7	-8.4

Source: State Planning Organisation
* State-owned banks are excluded.

The share of tax revenues in total public revenues was 84 percent. 69 percent of the tax revenues were consisted of indirect taxes. Of the expenditures, 54 percent were transfer expenditures, and 33 percent were current expenditures. The interest expenditures which were the most significant item in transfer expenditures formed 40 percent of the total expenditures. This ratio was 42 percent in 2003.

Public Sector Borrowing Requirement/GNP and Inflation (Percentage)



The main developments affecting the public sector balance positively in 2004 were; revenue increasing arrangements, applications requiring discipline in expenditures, rapid growth in economy, subsisting positive effect of state economic enterprises to the public balance, rising value added tax collection from imports in line with the growth in imports, continued fall in interest rates in public borrowing, extension of the borrowing maturities, and the diminishing effect of the TL's appreciation against the major currencies on interest rates of foreign currency denominated and/or foreign currency indexed domestic and foreign borrowing. The rising deficits of the social security institutions and realization of privatization proceeds well behind the targets restricted the recovery in the public sector deficit.

A favourable performance supporting the accomplishment of the inflation target, and enabling a smooth roll-over of the public debt was achieved in the consolidated budget which constituted the most important part of public income and expenditures. Expenditures contracted in real terms due to the decrease in interest expenditures in line with the falling interest rates, and on the other hand budget revenues increased in real terms. The rate of the private consumption tax levied on tobacco products and alcoholic beverages was raised, and the imposition of special transaction and communication tax, introduced as temporary in 1999, became permanent.

While budget revenues increased by 10 percent, a rate close to the GNP deflator, expenditures remained almost the same. The reason behind the steady expenditures was the decrease in interest expenditures, which declined by 4 percent, while non-interest expenditures increased by 23 percent. Budget deficit narrowed by 25 percent in current prices, and primary surplus grew by 42 percent. The ratio of budget revenues to GNP fell to 26 percent from 28 percent; and the ratio of expenditures to GNP decreased to 33 percent by a fall of 6 percentage points. The ratio of interest expenditures to GNP fell to 13 percent from 16 percent. The ratio of budget deficit to GNP decreased to 7 percent, by a fall of 4 percentage points as compared to the previous year. The ratio of primary surplus to GNP in the consolidated budget was 6.1 percent. This ratio of primary surplus to GNP was 5 percent according to the definition provided in the stand-by agreement signed with the IMF.

Consolidated Budget (TL trillion)

	2003	Per. share	2004*	Per. share	Per. change	As per. of GNP 2004
Revenues	100,250	100	109,887	100	10	26
Tax revenues	84,316	84	90,093	82	7	21
Non-tax revenues	10,223	16	17,065	18	24	5
Expenditures	140,455	100	140,200	100	0	33
Transfer	94,761	67	84,147	60	-11	20
Interest expend.	58,609	42	56,488	40	-4	13
Domestic borrowing	52,719	38	50,053	36	-5	12
External borrowing	5,890	4	6,435	5	9	2
Non-interest	45,694	33	56,053	40	23	13
Personnel	30,209	22	28,948	21	-4	7
Current	8,305	6	19,133	14	130	4
Investment	7,180	5	7,972	6	11	2
Budget balance	-40,204		-30,313		-25	-7
Primary balance	18,405		26,175		42	6

Source: The Ministry of Finance, * Provisional

Direct taxes amounted to 35 percent of the total tax revenues while indirect taxes had a share of 65 percent. The main component of the budget expenditures was interest expenditures, which accounted for 40 percent of the total budget expenditures. The second largest item was personnel expenditures with 21 percent. Other transfer expenditures had a share of 20 percent, current expenditures 14 percent, and investments 6 percent. Efforts to finance the budget deficit concentrated more on domestic borrowing due to the positive factors such as decrease in interest rates, increased demand form the non-bank segment of investors for government securities, and the extension of maturity.

Almost all of the financing requirement of public sector was met through domestic borrowing. Net external borrowing was TL 2,200 trillion (7 percent). There was an increase of TL 944 trillion in the Treasury's cash/bank account.

Financing of the Consolidated Budget

	TL trillion			As percentage of GNP		
	2002	**2003**	**2004**	**2002**	**2003**	**2004**
Financing	31,910	33,795	29,791	12	9	7
External borrowing (net)	15,550	793	2,200	6	1	1
Domestic borrowing	17,953	34,606	28,535	7	10	7
Other	-1,595	-1,604	-944	-1	0	0

A total of TL 129,709 trillion of debt repayment was made in 2004. Found with the addition of the budget deficit figure of TL 29,791 trillion to this figure, the total financing needs was TL 159,500 trillion in 2004. TL 11,135 trillion of this financing need was met by foreign borrowing, while the remaining TL 148,365 trillion was met through domestic borrowing.

The average maturity of the domestic TL borrowing increased to 406 days from 344 days. On the other hand, annual compound interest rate of the average borrowing in TL decreased from 28 percent to 23 percent.

Outstanding domestic debt increased by 15 percent to TL 224,483 trillion. The share of non-cash outstanding domestic debt in the total debt stock decreased by 5 percentage points to 18 percent. The most significant portion of the non-cash domestic debt stock was consisted of securities given to the state-owned banks and to the banks transferred to the management of the Savings Deposit Insurance Fund by Banking Regulation and Supervision Agency for their receivables from the Treasury.

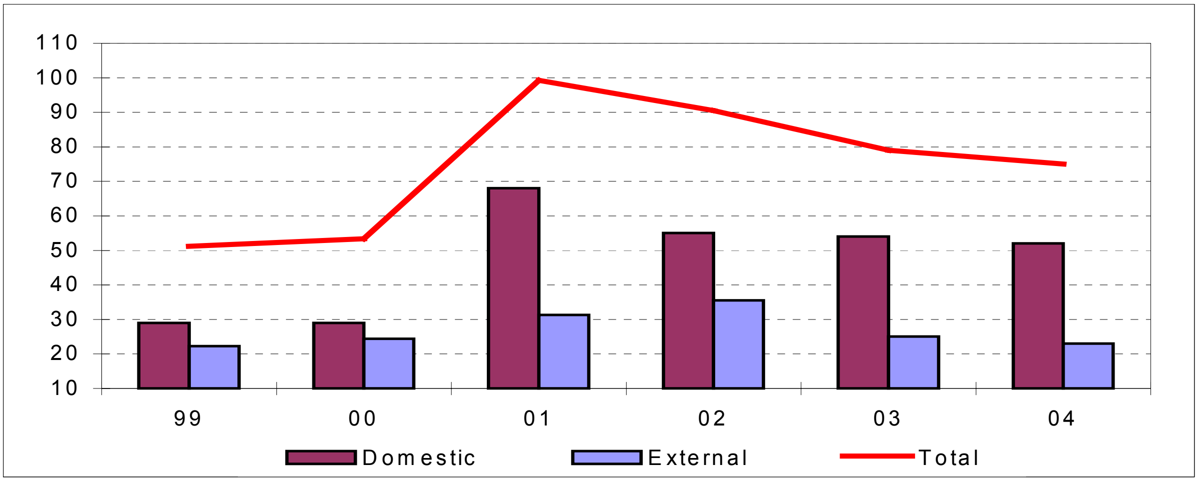
Non-cash Outstanding Government Securities

	TL trillion	**USD million**	**Euro million**
State-owned banks	24,539	771	350
Saving Deposit Insurance Fund	10,816	1,298	920
Central Bank	18,427	-	-
Total	53,781	2,069	1,270

A 37 percent of the outstanding domestic debt in the consolidated budget was owed to state-owned institutions, while the remaining 63 percent was indebted to the market. These ratios were 48 percent and 52 percent, respectively by the end of 2003. Deposit returns of T. İmar Bankası AŞ, and merger of T. Halk Bankası AŞ and Pamukbank AŞ, had a negative effect at around 2 percentage points in the ratio of outstanding domestic debt to GNP.

The share of securities with fixed interest rates in the outstanding domestic debt increased to 42 percent from 35 percent, and the share of exchange-rate sensitive securities decreased from 22 percent to 18 percent. The share of interest-rate sensitive securities decreased to 40 percent in 2004 from 43 percent in 2003.

Outstanding Public Debt (As percentage of GNP)



Outstanding domestic debt increased higher than the inflation. This was mainly due to borrowing of almost all financing requirement of the public sector through domestic borrowing on account of the favourable domestic borrowing conditions, and the repayments to deposits on T. İmar Bankası AŞ. On the other hand, the public sector fund demand from the financial sector continued in parallel to the growth of the financial system. The ratio of the outstanding domestic debt to GNP decreased from 54 percent to 52 percent. Total consolidated budget outstanding debt increased by 14 percent to TL 321,899 trillion (USD 226.3 billion) as of December 2004. Consequently, the ratio of the consolidated budget outstanding debt to GNP decreased from 79 percent to 75 percent.

Outstanding Public Debt

	TL trillion	(As percentage of GNP)			
	2004	2001	2002	2003	2004
Gov. securities	224,483	68	55	54	52
Cash	165,579	32	33	37	39
Non-cash	58,904	36	22	18	14
Bonds	194,211	58	41	48	45
Cash	135,307	22	19	30	32
Non-cash	58,904	36	22	18	14
Treasury bills	30,272	10	14	7	7
Cash	30,272	10	14	7	7
Non-cash	0	-	-	-	0
Central bank adv.	0	-	-	-	0
Domestic debt	224,483	68	55	54	52
External debt	97,416	27	34	25	23
Total	321,899	95	89	79	75

According to the data of the Central Bank, 54 percent of the government securities were held by banks. Total amount of government securities held by banks reached 68 percent of total deposits. Total amount of government securities held by non-bank sectors grew by 36 percent to TL 97,649 trillion. Of which, 36 percent (TL 34,707 trillion) were held by individual investors. Government securities held by non-bank sectors constituted 45 percent of the outstanding domestic debt, and 50 percent of the money demand (M2RYF).

Capital inflows had a major positive role in financing of the domestic debt in 2004. The amount of shares held by foreign investors increased by 80 percent to USD 16.1 billion as compared to 2003 year-end. According to the data of İstanbul Stock Exchange Settlement and Custody Bank Inc. (Takasbank), 55 percent of the market value of the shares in İstanbul Stock Exchange was held by foreign investors.

2.5. Monetary Aggregates

2.5.1. Monetary policy

Monetary policy primarily focused on maintaining the price stability. The Central Bank continued its implicit inflation targeting under the free floating foreign exchange regime. In order to reach the CPI inflation target of 12 percent, the Bank determined the level of the short term interest rates in accordance with realizations and expectations in inflation, by also taking into consideration the developments in monetary figures, and thus influenced the expectations in turn. On the other hand, the Bank created additional demand for foreign currencies through directly buying and/or holding auctions for buying the increased foreign currency surplus in the market due to change in portfolio preferences and increased capital inflows. The Bank announced that one of the purposes of its foreign currency purchases was to strengthen its foreign currency reserves.

The Central Bank's total foreign currency buying, which was USD 5.4 billion in 2004, reached USD 15 billion during 2002-2004 period. On the other hand, the Central Bank absorbed the additional TL liquidity created by these foreign currency purchases through open market operations or holding TL deposit buying auctions.

Interest Rates (end of period), Exchange Rates and Inflation (12-month, percent)

	2003	2004			
	Dec.	March	June	Sept.	Dec.
Interest rate (annual, comp.)*					
O/n	26	24	24	22	19
Government securities	28	25	28	25	23
Exchange rates					
TL/(USD)	-15	-23	5	8	-4
TL/Euro	2	-13	12	15	4
Inflation (WPI)	14	19.2	13.7	11.2	11.1

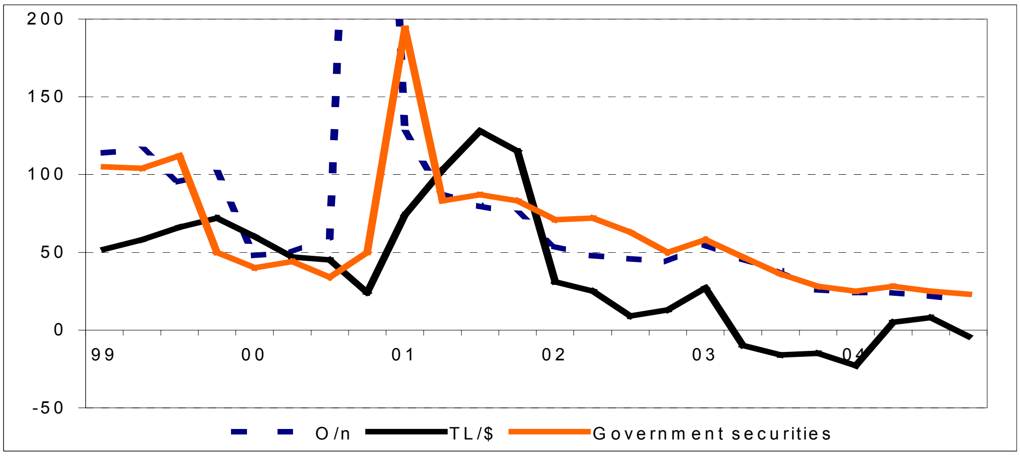
* Average

Short term interest rates fell by 2 percentage points to 24 percent annually in the first quarter of 2004. The Bank did not change in its short term interest rates in the second quarter of the year due to changing market expectations in line with the international markets. However, starting from the second half of the year, the Bank pulled the short term interest rates down to 22 percent in September and 19 percent by the end of the year. In addition to the downward trend in inflation and positive developments in international markets, other developments which effected the interest rates were; the reduction in the public sector borrowing requirements, change in the portfolio preferences in favour of TL investment instruments, and the continuing increase in foreign currency supply in excess of demand due to capital movements and positive accounts in net errors and omissions.

TL continued to appreciate against the major foreign currencies in real terms despite the descending trend in TL interest rates, the Central Bank's demand in the market, and the commercial banks' reserve accumulation. As of the end of March, TL's annual appreciation was 23 percent against USD, and 13 percent against euro in nominal terms.

However, TL depreciated against both currencies in the second and third quarters of the year. By the end of September, TL depreciated by 8 percent against USD, and 15 percent against euro. As of year-end figures, TL appreciated by 4 percent against USD while it depreciated by 4 percent against euro. TL appreciated against both USD and euro in real terms.

Foreign Exchange, Interest Rates on Government Securities and O/n Interest Rate (Percentage)



Strong foreign currency supply had also effect on the balance sheet of the Central Bank. There was no significant change in the size of the balance sheet; it just contracted by 2 percent compared to the end of 2003. The ratio of the Central Bank balance sheet to GNP decreased from 23 percent to 20 percent. On the other hand, positive changes in the structure of the balance sheet also continued.

Balance Sheet of the Central Bank, Selected Items (TL trillion)

	2003	2004			
	Dec.	March	June	Sept.	Dec.
Net foreign assets	17,262	17,194	21,110	24,549	23,048
Net domestic assets	23,585	24,041	22,265	21,297	21,071
Monetary base	15,010	17,101	19,009	20,114	20,328
Open market operations	8,260	7,898	4,653	4,514	3,622
Central Bank money	24,134	26,781	27,760	26,413	24,743
Fx deposits	6,517	5,568	6,920	7,477	6,099
TL liabilities	30,651	32,349	34,680	33,890	30,842
Banks' Fx deposits	10,196	9,077	10,342	11,955	13,276
Total domestic liabilities	40,847	41,426	45,022	45,845	44,118

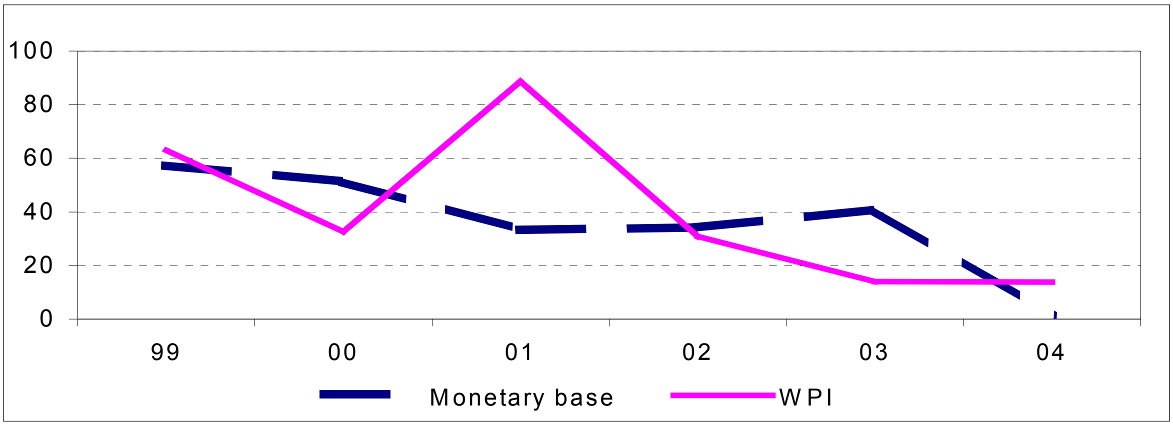
Source: Central Bank of the Republic of Turkey

The share of foreign assets in total assets continued to increase, while the share of domestic assets decreased due to the redemptions of the Treasury to the Bank. The share of foreign liabilities in total liabilities decreased. However, domestic foreign exchange liabilities increased as a result of the growth of the Treasury's foreign exchange assets. The liquidity injected to the market increased due to the growth of the economic activity and demand for TL instruments as well as the decrease in the domestic assets. Accordingly, the amount of money absorbed from the market through open market operations decreased, and the monetary base widened. Monetary base expanded in 12-

mount term by 27 percent by the end of September and 35 percent by the end of December, respectively. The markets preferred remaining liquid along the year.

The expansion in the monetary base was mainly due to the increase in net foreign assets. On year-to-year basis; net foreign assets, which showed no significant change in the first quarter, increased by 22 percent by the end of the first half and 34 percent by the end of the year, respectively. Net domestic assets slightly increased, in the first quarter, and decreased in the subsequent periods.

Monetary Base and Wholesale Inflation (Annual change, percentage)



The Central Bank's foreign exchange reserves increased by about USD 2.5 billion in 2004, and reached USD 36 billion. This increase almost entirely resulted from the foreign exchange buying auctions in the second half of the year. Net foreign exchange position of the Central Bank increased from USD 0.4 billion to USD 2.7 billion. Thus the increase in net foreign exchange position of the Central Bank accounted for above USD 12 billion in the last three years.

Central Bank's Fx Reserves and Net Fx Position (USD billion)

	2003	2004			
	Dec.	March	June	Sept.	Dec.
Fx reserves	33.6	32.6	32.4	34.2	36.0
Net reserve position	0.4	1.9	2.6	3.4	2.7

Interest rates paid for reserve requirements by the Central Bank were also reduced gradually in parallel to the decrease in short-term interest rates. The base interest rate of the Central Bank which was 16 percent at the end of 2003, was reduced to 12.5 percent at the end of 2004.

2.5.2. Money demand

The ratio of financial assets to GNP increased by 5 percentage points to 130 percent in 2004. Demand for TL instruments increased faster than the demand for foreign currencies.

The ratio of money and quasi-money instruments to GNP was 44 and that of capital market instruments to GNP was 86 percent by the end of 2004. There was no bond issuance from the private sector due to the heavy tax burden imposed on them, and the high returns of government securities. Despite this fact, the ratio of the government securities to GNP with 52 percent, was higher than the ratio of money and quasi-money instruments.

Financial Assets (As percentage of GNP)

	2001	2002	2003	2004
Money and quasi-money	**61**	**51**	**44**	**44**
Cash	3	3	3	3
Deposits	56	47	40	41
- TL	25	21	21	23
- FX	32	26	19	18
Repurchase agreements	2	1	1	0
Capital Market	**106**	**76**	**82**	**86**
Shares (market value)	38	21	27	30
Bonds and bills	68	55	54	52
-Public	68	54	54	52
-Private	0	0	0	0
Investment funds	3	3	5	6
Total	**167**	**127**	**126**	**130**

Source: Central Bank of the Republic of Turkey, Capital Market Board

Money demand for TL denominated investment instruments increased also above the inflation rate in 2004. Money demand consisting of TL deposits, repos and investment funds (M2RF) grew by 31 percent in current prices, and 15 percent in constant prices. TL deposits, which grew by 37 percent in 2004, had a major effect on the increase in demand for TL instruments.

Monetary Aggregates (2004)

	TL trillion	USD million	Percentage change TL	Percentage change USD
M2RF	127,403	95,340	30.6	36
Money in circulation	12,446	9,314	22.9	28
TL demand deposits	17,023	12,739	48.9	55
Repo	1,528	1,143	-50.4	-48
Investment funds	16,531	12,371	21.8	27
TL time deposits	79,875	59,773	34.6	40
M2YRF	200,929	150,362	20.7	26
Fx deposits	73,526	55,022	6.7	11

Source: Central Bank of the Republic of Turkey

TL equivalent of foreign exchange deposits increased by 7 percent while USD equivalent of foreign exchange deposits increased by 11 percent. This difference was caused by the appreciation of TL against USD and euro, as well as the depreciation of USD against euro. Accordingly, money demand including also foreign exchange deposits (M2YRF) increased by 21 percent in current prices, and 6 percent in constant prices. The share of foreign exchange deposits in money demand (M2YRF) decreased by 4 percentage points to 37 percent.

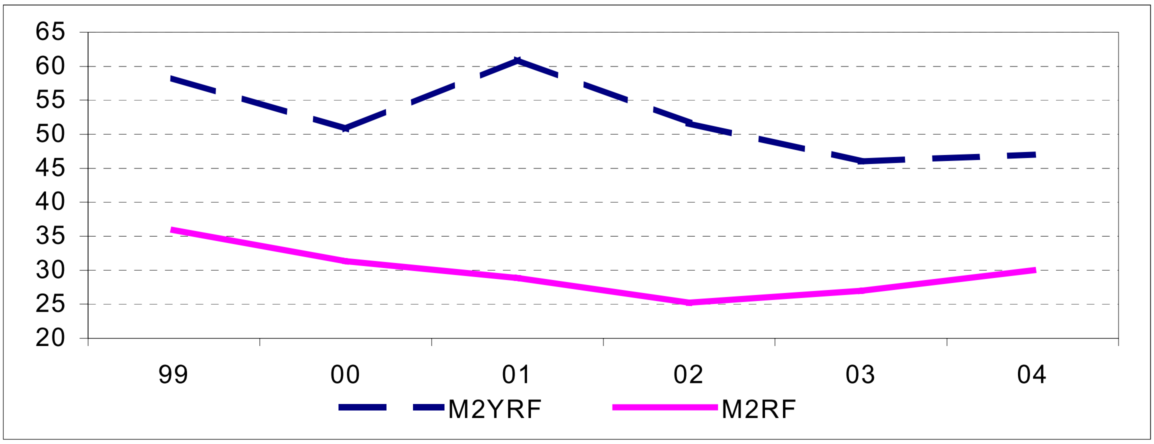
Breakdown of Monetary Aggregates (Percentage)

	2000	2001	2002	2003	2004
Money in circulation	5	4	5	6	6
TL demand deposits	8	5	5	7	8
Repo	9	3	2	2	1
Investment funds	1	2	3	7	8
TL time deposits	39	33	33	36	40
Fx deposits	38	53	51	42	37
M2RYF	100	100	100	100	100

Source: Central Bank of the Republic of Turkey

The ratio of money demand for TL instruments (M2RF) to GNP increased by 3 percentage points to 30 percent. The ratio of money demand including foreign exchange deposits (M2YRF) to GNP increased by 1 percentage point and reached 47 percent.

Money Demand (As percentage of GNP)



The factors positively affecting the preferences in favour of TL instruments were; a notable decline in inflation, high positive returns on TL instruments as TL appreciated against major foreign currencies, and sustained growth in economic activity. On the other hand, individual investors' preference for government securities against deposits continued due to tax advantages of government securities and investment funds, after being corrected according to inflation, were exempted from tax. Thus, government securities portfolios of non-bank investors grew considerably in recent years as well; in 2004 by 36 percent in current prices and 20 percent in constant prices. The ratio of government securities held by non-bank investors to GNP increased by 4 percentage points to 23 percent. Government securities held by commercial banks increased by 17 percent. The ratios of these government securities and total deposits to GNP were 27 percent, and 69 percent, respectively.

According to the data of the Central Bank, total deposits of the commercial banks increased by 22 percent in current prices, and 7 percent in constant prices. Similarly, TL deposits increased by 37 percent in current prices, and 20 percent in constant prices. However, TL equivalent of foreign exchange deposits increased by 7 percent in current prices, while it decreased by 6 percent in constant prices. The amount of total foreign exchange deposits increased from USD 49 billion as of December 2003 to USD 55 billion as of December 2004. The share of TL equivalent of foreign exchange deposits in total deposits decreased by 6 percentage points to 43 percent. The ratio of TL deposits to GNP increased from 21 percent to 23 percent, while the ratio of total deposits including foreign exchange deposits to GNP remained the same at 41 percent.

Deposit interest rates fell in line with the inflation rate. Interest rates (compound) for 1-month deposits decreased from 32 percent in December 2003 to 24 percent at the end of 2004, and interest rates for 3-month deposits decreased from 31 percent to 25 percent in the same period. The maturity structure of TL deposits improved slightly while that of foreign exchange deposits remained almost the same. Average maturity for the total deposits remained almost the same with 3-month.

State-owned-banks had 42 percent share in total deposits while the share of privately owned banks' in total deposits was 55 percent. As compared to the previous year, this development indicated an increase of 2 percentage points in the share of state-owned banks. This increase was due to the fact that state-owned banks had a lower share in foreign exchange deposits as well as the transfer of the deposits on T. İmar Bankası AŞ to TC Ziraat Bankası AŞ. The share of foreign banks in total deposits was 2 percent.

One of the major arrangements in 2004 for banking system was the limitation of deposit insurance on savings deposits with TL 50 billion. The transition to limited deposit insurance from the unlimited was rather smooth due to the planing of this transition one year in advance by the BRSA, healthy relations among banks and positive approach of especially state-owned banks, prudent liquidity policies of banks, and recovery in economic performance. Increase in the deposits of the banking system even accelerated after the introduction of the limitation to the deposit insurance.

Maturity Structure of Total Deposits (Percentage)

	2000	2001	2002	2003	2004
Total	100	100	100	100	100
Demand	19	17	19	20	21
1-month	29	34	30	26	25
3-month	38	38	38	38	38
6-month	9	6	8	10	8
12- month+	6	6	6	6	9
Average (month)	2.8	2.7	2.8	2.7	2.8

Source: Central Bank of the Republic of Turkey

State-owned-banks had a share of 56 percent in TL deposits, and 26 percent in foreign currency deposits. However, privately owned banks had a higher share in foreign currency deposits; 70 percent of foreign exchange deposits and 43 percent of TL deposits were held by these banks.

The ratio of loans to deposits increased. The ratio of total loans (performing loans + non-performing loans after provisioning) extended by commercial banks from their branches in Turkey to total deposits + repos increased from 34 percent to 47 percent.

Total loans extended by commercial banks in Turkey, excluding the loans extended by the branches abroad, increased by 52 percent in current prices and 34 percent in constant prices, respectively. Performing loans grew by 55 percent while non-performing loans after provisioning decreased by 31 percent. This was mainly due to the fact that the non-performing loans were rescheduled within the framework of the financial restructuring program was reported in the list of performing loans according to the regulations, as well as strong economic activity. Accordingly, the ratio of non-performing loans before provisioning to total loans decreased from 16 percent to 7 percent, and the ratio of non-performing loans after provisioning to total loans decreased from 3 percent to 1 percent.

Total loans, which were restructured within the framework of the financial restructuring program, amounted to USD 5.7 billion.

Total loans* (TL trillion)

	2000	2001	2002	2003	2004
Total loans**	29,602	38,812	39,413	56,144	85,601
Performing loans***	28,366	35,910	36,762	54,600	84,785
Non-performing loans (net)****	1,236	2,902	2,651	1,544	816
Non-performing loans *****	3,121	6,421	10,122	8,750	6,081
Total loans /GNP (percentage)	24	22	14	16	20

* Loans are extended by domestic branches of the banking system.
** Performing loans + non-performing loans (net)
*** Total loans of the banking system (loans to financial system are excluded)
**** Loans under follow-up after provisioning (net, banking system)
***** Loans under follow-up before provisioning (gross, banking system)
Source: Central Bank of the Republic of Turkey

A 94 percent of total loans was extended by commercial banks. Privately owned banks had a share of 69 percent in total loans while state-owned banks had 21 percent. Loans extended by commercial banks increased by 56 percent in current prices, and 37 percent in constant prices. The rise in performing loans was 55 percent in current prices, and 35 percent in constant prices. The main reason for the increase in total loans was the rapid growth in consumer loans and loans extended via credit cards.

Deposits and Loans (TL trillion)

	2000	2001	2002	2003	2004
Total deposits	56,293	103,767	131,018	147,351	170,424
- TL deposits	30,918	45,035	56,481	75,979	96,898
- Fx deposits	25,375	58,732	74,537	71,372	73,526
Total deposits+repo	62,317	106,560	133,973	150,418	171,952
Commercial banks' loans	27,146	34,480	34,860	51,398	80,289
- Performing loans	25,942	31,671	32,277	49,878	79,649
- Non-performing loans (net)	1,204	2,808	2,583	1,521	640
- Non-performing loans (gross)	3,068	6,271	9,972	8,567	5,905
Consumer loans and credit cards loans	6,695	4,768	7,001	15,212	26,678
- Consumer loans	4,619	2,323	2,902	8,634	12,925
- Credit cards loans	2,076	2,445	4,099	6,578	13,753
Selected ratios (As percentage of GNP)					
Total deposits+repo	49.6	60.4	48.7	41.8	40.1
Total loans	47.6	36.4	29.4	37.3	49.9
Commercial banks' loans	21.6	19.5	12.7	14.3	18.7
Consumer loans	3.7	1.3	1.1	2.4	3.0

Source: Central Bank of the Republic of Turkey

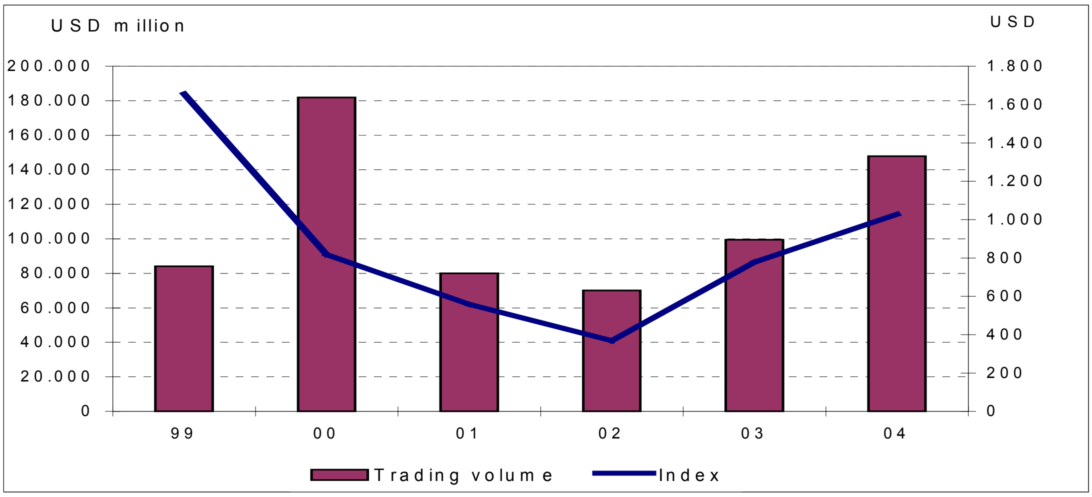
Thus, consumer loans increased by 50 percent in current prices and 31 percent in constant prices, while loans extended via credit cards increased by 109 percent in current prices and 84 percent in constant prices. The ratio of consumer loans and loans extended via credit cards to performing loans increased by 3 percentage points to 33 percent.

Total loans extended by commercial banks via their branches abroad amounted to TL 20,978 trillion. When such kind of loans were included, total loans (performing and non-performing after provisioning) of the banking system reached TL 101,267 trillion.

2.6. Developments in İstanbul Stock Exchange

İstanbul Stock Exchange Index (ISE) continued to increase in both dollar terms and TL terms. ISE index increased by 38 percent in dollar terms and reached 1,075 points, and in TL terms it increased by 30 percent to 24,972 points. Total trade volume expanded by 47 percent to USD 147 billion.

ISE Index (In dollar terms) and Trading Volume (USD million)



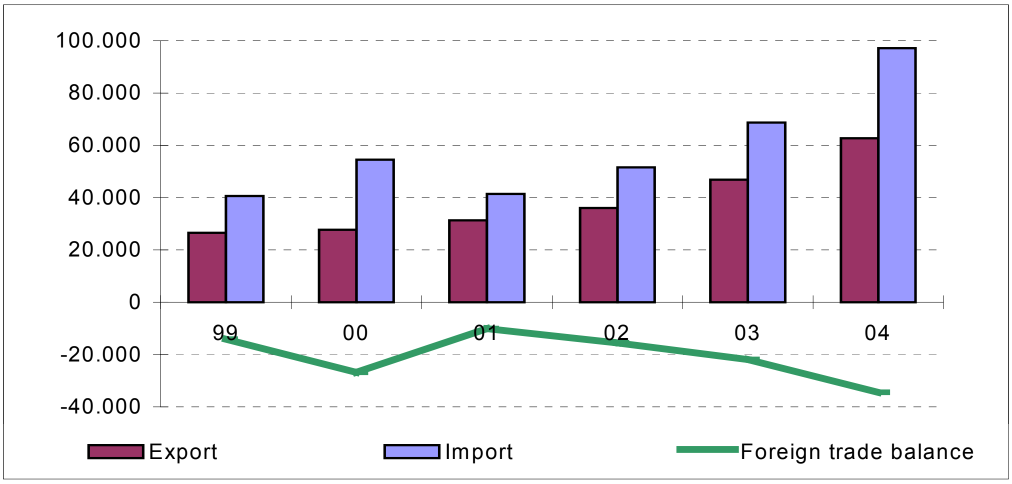
The positive factors behind the performance of the stock exchange were; acceleration of the economic growth, increase in industrial production and exports, downtrend in inflation, substantial increase in demand from foreign investors.

Market value of the companies traded in ISE increased from USD 69 billion in previous year to USD 98.1 billion in 2004. The ratio of the total market value to GNP increased from 27 percent to 31 percent. The number of companies traded in ISE increased to 297 from 285. While 13 new companies joined the stock exchange in 2004, 1 company left. By the end of 2004, the market value of 13 banks trading in ISE increased by 55 percent to TL 37,375 trillion. The market value of banks trading in the stock exchange constituted 28 percent of the total market value.

2.7. Balance of Foreign Trade

Upward trend in both exports and imports was maintained in 2004 as foreign trade volume expanded by 37 percent and reached USD 160 billion. Turkey's foreign trade was positively affected by the cross currency rates where euro appreciated against dollar due to the fact that exports were mainly in euro while imports in USD. On the other hand, exports growth was supported by the fact that TL's appreciation against major foreign currencies reduced the costs of raw materials and intermediary inputs while the export prices increased.

Balance of Foreign Trade (USD million)



On the other hand, imports also continued to grow at a high rate depending on the strong economic growth, the increases in domestic demand and particularly in private sector fixed capital investments, and the rise in exports.

Exports grew by 33 percent and reached USD 62.8 billion, while imports expanded by 40 percent and amounted to USD 97.2 billion. The coverage ratio of exports to imports decreased by 3 percentage points to 65 percent. The ratio of exports to GNP increased by 1 percentage point to 21 percent, while the ratio of imports to GNP increased by 3 percentage points to 32 percent. The ratio of the foreign trade volume to GNP was 53 percent. Foreign trade deficit increased by 57 percent and reached USD 34.4 billion. The ratio of the foreign trade deficit to GNP was 11.5 percent.

Foreign Trade (USD billion)

	2000	2001	2002	2003	2004
Exports	27.8	31.3	36.1	47.3	62.8
Imports	54.5	41.4	51.6	69.3	97.2
Foreign trade deficit	26.7	10.1	15.5	22.1	34.4
Foreign trade volume	82.3	72.7	87.6	116.6	160.0
Foreign trade deficit/GNP	13.3	6.3	8.7	9.2	11.5
Export/Import	51	76	70	68	65
Price Index * (94=100)					
Exports	88	86	84	92	107
Imports	95	95	94	101	114
Quantity index* (94=100)					
Exports	167	204	236	288	331
Imports	265	199	240	320	405

Source: State Institute of Statistics, * Average

Based on 12-month average, export quantity index and imports quantity index increased by 16 percent and 27 percent, respectively, while export price index and import price index increased by 16 percent and 13 percent, respectively.

Foreign Trade by Commodity Groups, 2004

	Exports			Imports		
	USD million	Per. change	Per. share	USD million	Per. change	Per. share
Capital goods	6,518	50	11	17,350	53	18
Intermediate goods	25,286	36	40	65,391	31	67
Consumer goods	30,783	28	49	13,927	85	14
Other	186	-36	0	493	6	1
Total	62,774	33	100	97,161	40	100

Imports of capital goods, intermediate goods, consumption goods increased by 53 percent, 31 percent, and 85 percent, respectively. The imports of intermediate goods constituted 67 percent of total imports. By sectors, the share of manufacturing industry in total imports was 82 percent. Machinery, vehicles, iron and steel, and chemistry were the most important sub-sectors of the manufacturing industry. Oil imports increased by 28 percent to USD 6.1 billion.

In exports; the shares of consumption goods, intermediate goods and capital goods were 49 percent, 40 percent, and 11 percent, respectively. By sectors, manufacturing industry constituted 94 percent of total exports, while agriculture had a share of 5 percent in total exports. Textile, vehicles, iron and steel, machinery were the most significant sub-sectors of the manufacturing industry.

OECD countries had a share of 64 percent in foreign trade volume. The share of EU countries was 51 percent. Foreign trade balance with EU countries which changed against Turkey following the signing of the EU Customs Union, gave a deficit of USD 11.1 billion in 2004, compared with USD 7.1 billion in 2003. EU countries had a share of 47 percent in the total imports, and 55 percent in the total exports.

Foreign Trade by Country Groups, 2004

	Exports			Imports			Exports-Imports
	USD million	Per. change	Per. share	USD million	Per. change	Per. share	USD million
EU	34,310	32	55	45,373	35	47	-11,063
Free zone	2,529	31	4	809	37	1	1,720
Other	25,935	34	41	50,979	45	52	-25,044
Europe	6,572	35	10	18,297	53	19	-11,725
Africa	2,952	39	5	4,779	43	5	-1,827
America	5,692	33	9	4,779	-3	5	913
Middle East	7,238	41	12	5,122	18	5	2,116
Other Asia	3,133	11	5	15,884	58	16	-12,751
Other	348	60	1	362	-42	0	-14
Total	62,774	33	100	97,161	40	100	-34,387

Germany ranked first with 14 percent share in Turkey's foreign trade. Germany was followed by United Kingdom and United States with 7 percent, and Russia and France with 6 percent. Exports to Germany constituted 14 percent of Turkey's total exports, while imports from this country constituted 13 percent of the total imports.

2.8. Balance of Payments

Current account deficit increased by 92 percent as compared to the previous year, and reached USD 15.4 billion. Thus Turkey's current account deficit in the last three years totalled USD 24.9 billion. The ratio of the current account deficit to GNP in 2004 increased by 2.2 percentage points to 5.1 percent.

The main contributing factor to the increase in the current account deficit was the growth in merchandise trade deficit, which was widened by 70 percent including the shuttle trade and reached USD 23.8 billion. Shuttle trade decreased from USD 4 billion in 2003 to USD 3.9 billion in 2004. Meanwhile, gold imports increased by 35 percent to USD 3.4 billion in 2004.

Current Account Balance (USD million)

	2001	2002	2003	2004
Current account balance	3,390	-1,522	-8,037	-15,410
-General merchandise	-4,543	-8,337	-14,010	-23,792
-Exports	34,373	40,124	51,206	66,864
-Imports	-38,916	-48,461	-65,216	87,249
-Services (net)	9,130	7,879	10,505	12,773
-Tourism (net)	8,090	6,599	11,090	13,364
-Income(net)	-5,000	-4,554	-5,559	-5,518
-Direct investments	52	-86	-400	-672
-Portfolio investments	-694	-835	-1,207	-1,195
-Other investments	-4,358	-3,633	-3,952	-3,651
-Interest expenditures	-5,497	-4,417	-4,586	-4,348
-Current transfers	3,803	3,490	1,027	1,127
-Workers remittances	2,786	1,936	729	804

The growth in the surplus of the service sector balance limited the current account deficit, which increased by 22 percent and reached USD 12.8 billion. Net tourism income increased by 21 percent to USD 13.4 billion, and thus became the most important contributor in the increase in the surplus of the service sector balance. Current transfers were slightly changed as compared to 2003, and continued to have a positive contribution of USD 1.1 billion to the current account. On the other hand, the investment income deficit was USD 5.6 billion. Interest expenditures which were the major item in the investment income balance decreased from USD 4.6 billion to USD 4.3 billion.

Current account deficit was financed by foreign borrowing based on capital inflows which continued to flow to developing countries like Turkey in high volumes due to the lower interest rates globally. Unclassified inflows under net errors and omissions account decreased; however, this item was still important.

Rapid growth in current accounts deficit, payment to the IMF, and the increase in reserves were predominantly financed by the increase in private sector borrowing and the referred unclassified inflows under net errors and omissions account. Capital inflows, which were USD 7.1 billion by the end of 2003, increased to USD 16.8 billion in 2004. Net errors and omissions account, which was USD 5 billion in 2003, decreased to USD 3 billion in 2004. A net amount of USD 3.5 billion was paid to the IMF.

According to calculations made with consideration of the transactions not recorded to the register of foreign debt, a resource inflow of USD 22.3 billion was realized in 2004.

Following the financing of the current account deficit, official reserves and bank reserves increased by USD 0.8 billion and USD 5.9 billion, respectively.

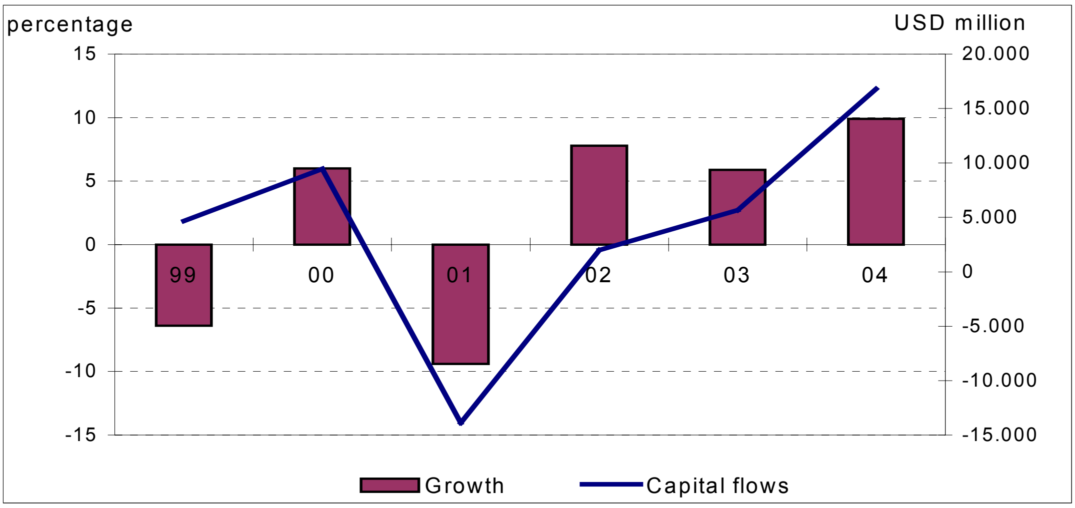
The increase in private sector borrowing was notable. Thus, transactions resulting liability for the private sector of USD 5.7 billion in 2003 increased to USD 12.6 billion in 2004. Such kind of transactions of banks and other sectors increased in 2004.

Capital and Financial Account (USD million)

	2001	2002	2003	2004
Capital and financial account	-14,643	1,161	7,091	16,965
-Capital account (net)	0	0	0	0
-Financial account (net)	-14,643	1,161	7,091	16,965
-Direct investments abroad (net)	2,769	863	1,195	1,709
-Portfolio investments (net)	-4,515	-593	2,569	8,023
-Other investments (net)	-12,897	891	3,327	7,233
-Net errors and omissions	-1,671	149	5,043	2,787
General balance	-12,924	-212	4,097	4,342
-IMF accounts	10,230	6,365	-50	-3,518
-Official reserves	2,694	-6,153	-4,047	-824

On the other hand, net direct foreign capital inflows increased from USD 1.2 billion in 2003 to USD 1.7 billion in 2004. Real estate purchases by foreigners, which increased to USD 1.3 billion in 2004 from USD 1 billion in the previous year, played an important role in this increase.

Capital Flows and Growth in GNP

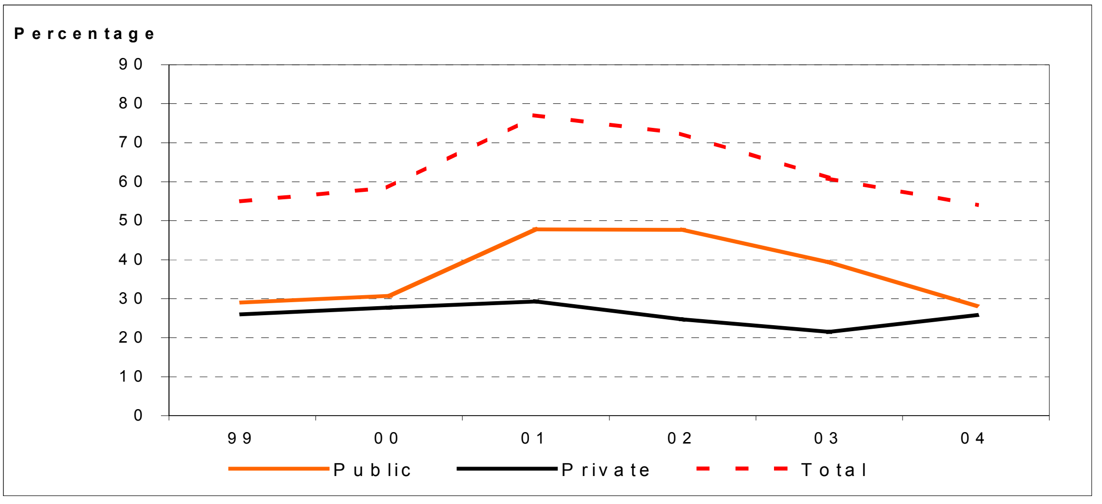


Balance of payments gave a surplus of USD 4.3 billion due to the effect of foreign borrowing and net errors and omissions account; thus official reserves continued to rise. Official reserves increased by USD 0.8 billion after repayments made to the IMF.

2.9. Outstanding External Debt

Outstanding external debt increased by approximately USD 16.3 billion and reached USD 162 billion as compared to 2003. Middle and long term outstanding external debt increased by USD 7.5 billion, while short term outstanding external debt increased by USD 8.9 billion. The share of public debt (excluding the debt of the Central Bank) in the total outstanding external debt increased by USD 4.4 billion and reached USD 73.8 billion. Outstanding external debt of private sector also increased by USD 6.7 billion in 2004.

External Debt Stock (As percentage of GNP)



Despite the 11 percent increase in the outstanding external debt in 2004, the ratio of outstanding external debt to GNP decreased by 7 percentage points to 54 percent due to the higher growth of GNP in dollar terms. The ratio of medium and long term external debt to GNP decreased by 8 percentage points to 43 percent, while the share of short term external debt increased by 1 percentage point to 11 percent.

The shares of public sector and the Central Bank in outstanding external debt were 48 percent and 13 percent, respectively. The share of the banking system in outstanding external debt was 10 percent, whereas that of non-bank sectors was 31 percent. The ratio of the public sector's debt (excluding the Central Bank) to GNP decreased from 20 percent to 19 percent.

Outstanding External Debt (USD billion)

	2000	2001	2002	2003	2004
Medium and long term	90.3	97.7	113.8	122.3	129.8
Public	47.7	46.3	63.7	69.6	73.8
Central bank	13.4	23.8	20.3	21.5	18.1
Private	29.2	27.7	29.7	31.2	37.9
Banks	4.6	3.2	3	3.1	2.3
Non-banks	24.6	24.5	26.7	28.1	35.6
Short term	28.3	16.4	16.4	23.0	31.9
Central bank	0.7	0.6	1.7	2.9	3.3
Banks	16.9	8.0	6.3	9.7	13.8
Non-banks	9.7	7.6	8.4	10.5	14.8
Total	118.6	113.9	130.2	145.4	161.7

Source: Undersecretariat of the Treasury *Provisional

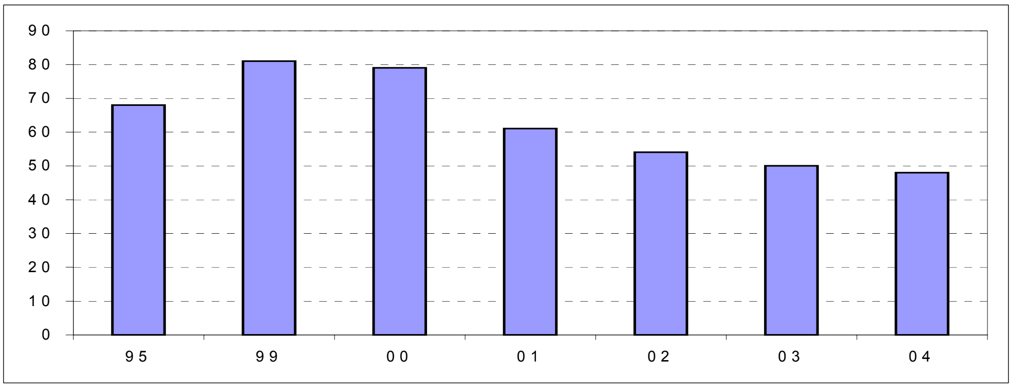
Of the medium and long term outstanding external debt, USD 40.9 billion was provided by official creditors, and USD 89 billion was granted by private creditors. The highest share in official creditors was held by international institutions, which also included the IMF, with USD 32 billion. Of the debt to private creditors, USD 33.4 billion was provided by commercial banks, and USD 30 billion was obtained through bond issues.

3. Turkish Banking System in 2004

3.1. The number of banks and branches

The number of banks operating in Turkey declined from 50 in 2003 to 48 in 2004. This development resulted from the transfer of Credit Lyonnaise SA, previously in the group of foreign banks, to Credit Agricole Indosuez Türk Bank AŞ, and the transfer of Pamukbank TAŞ to Türkiye Halk Bankası AŞ. Besides Deutsche Bank AŞ became a depositor bank, therefore it was transferred from the group of non-depository banks to foreign banks founded in Turkey.

Number of Banks (1995-2004)



Of the banks operating in Turkey, 35 were commercial banks (depository), and 13 were non-depository banks. Of the commercial banks, 3 were state-owned banks, and 18 were privately owned banks. There was one bank under the management of the Savings Deposit Insurance Fund, namely Bayındırbank AŞ. The number of non-depository banks was 13. Of which, 3 were state-owned banks, 8 privately owned banks, and 2 foreign banks.

Number of Banks and Branches*

	2002		2003		2004	
	Bank	Branch	Bank	Branch	Bank	Branch
Commercial banks	40	6,087	36	5,949	35	6,088
State-owned banks	3	2,019	3	1,971	3	2,149
Privately owned banks	20	3,659	18	3,594	18	3,729
Banks in the Fund	2	203	2	175	1	1
Foreign banks	15	206	13	209	13	209
Non-depository banks	14	19	14	17	13	18
State-owned banks	3	4	3	4	3	4
Privately owned banks	8	12	8	10	8	12
Foreign banks	3	3	3	3	2	2
Total	54	6,106	50	5,966	48	6,106

* Including branches in the Turkish Republic of Northern Cyprus and branches abroad.

The number of branches increased by 140 to 6,106 in 2004. By banking groups, the number of branches increased by 139 in commercial banks, and by one in non-depository banks. The number of branches in state-owned banks increased by 178 due to the transfer of Pamukbank TAŞ to T. Halk Bankası AŞ, and that of privately owned commercial banks increased by 135. The number of branches in foreign banks remained the same.

3.2. Number of employees

The number of employees in the banking sector increased in 2004, after the steep fall by 50,739 in 2000-2003 period. In 2004, the number of employees recorded an increase in all commercial bank groups, except in the banks in the Fund. The number of employees increased by 1,473 in the state-owned commercial banks, 6,266 in privately owned commercial banks, and 399 in foreign banks. However, the number of employees decreased by 109 in non-depository banks, and 4,115 in the banks in the Fund.

Number of Employees

	2002	2003	2004
Commercial banks	118,329	118,607	122,630
State-owned banks	40,158	37,994	39,467
Privately owned banks	66,869	70,614	76,880
Banks in the Fund	5,886	4,518	403
Foreign banks	5,416	5,481	5,880
Non-depository banks	4,942	4,642	4,533
State-owned banks	4,174	3,882	3,800
Privately owned banks	691	683	681
Foreign banks	77	77	52
Total	123,271	123,249	127,163

A 96 percent of total bank employees was employed by commercial banks; of which 31 percent were employed by state-owned banks, 61 percent by privately owned banks. On the other hand 4 percent of total bank employees were employed by non-depository banks;

Number of Branches and Employees Per Bank

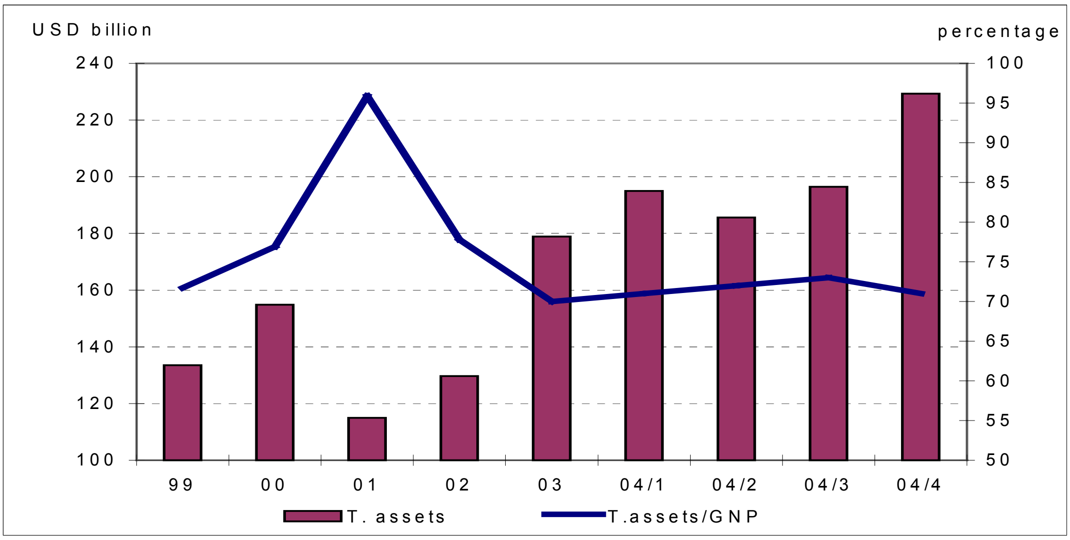
	Branch			Employee		
	2002	2003	2004	2002	2003	2004
Commercial banks	152	165	174	2,958	3,295	3,504
State-owned banks	673	657	716	13,386	12,665	13,156
Privately owned banks	183	200	207	3,343	3,923	4,271
Banks in the Fund	102	88	1	2,943	2,259	403
Foreign banks	14	16	16	361	422	452
Non-depository banks	1	1	1	353	332	349
State-owned banks	1	1	1	1,391	1,294	1,267
Privately owned banks	2	1	2	86	85	85
Foreign banks	1	1	1	26	26	26
Total	113	119	127	2,283	2,465	2,649

The factors in the steep fall in the number of bank employees and branches in 2000-2003 period were transferring of the financially weakened banks to the Savings Deposit Insurance Fund and/or closure of such banks within the framework of the restructuring program introduced in 1999, implementation of the restructuring program in the state-owned banks, and bank mergers, as well as banks' own efforts to reduce their operating costs.

3.3. Balance Sheet Items

As of December 2004, total assets of the banking sector increased by 23 percent to TL 306,542 trillion (USD 229 billion) as compared to 2003. The ratio of banks' total assets to GNP increased by 3 percentage points to 71 percent by the end of 2004.

Total Assets and Total Assets/GNP (1999-2004)



Main reasons for this growth in banks' balance sheet were; continued positive expectations towards economic activity and market stability, rapid growth in TL deposits, improvement in foreign borrowing opportunities, and the rise in shareholders' equity. This increase in banks' resources led to a rapid growth in banks' assets particularly in loans extended by banks.

Total Assets by Groups, December 2004

	TL trillion	USD million	Per. change (TL)	Per. change (USD)
Commercial banks	295,125	220,852	23	28
State-owned banks	106,903	79,999	29	34
Privately owned banks	175,937	131,656	24	29
Banks in the Fund	1,938	1,451	-73	-72
Foreign banks	10,347	7,743	49	55
Non-depository banks	11,327	8,476	10	15
Total	306,452	229,328	23	28

In commercial banks group, state-owned banks, privately owned banks and foreign banks grew by 29 percent, 24 percent, and 49 percent, respectively, while banks in the Fund contracted by 73 percent. On the other hand non-depository banks grew by 10 percent.

3.4. Market Shares

The distribution of the total assets in commercial banks and non-depository banks remained the same. Accordingly, the share of commercial banks was 96 percent. On the contrary, the share of state-owned banks in total assets increased from 33 percent to 35 percent, while that of banks in the Fund decreased from 3 percent to 1 percent. The shares of foreign banks and privately owned banks remained the same.

Market Shares of Groups (Percentage)

	T. assets		T. deposits		T. loans	
	2003	2004	2003	2004	2003	2004
Commercial banks	96	96	100	100	91	93
State-owned banks	33	35	38	42	18	21
Privately owned banks	57	57	57	55	67	67
Banks in the Fund	3	1	3	0	1	0
Foreign banks	3	3	2	3	4	5
Non-depository banks	4	4	0	0	9	7

The share of privately owned banks in total deposits decreased by 2 percentage point to 55 percent, while the share of the banks in the Fund decreased by 3 percentage points to 0,1 percent. However, the share of state-owned banks in total deposits increased by 4 percentage points to 42 percent. The share of foreign banks in total deposits remained the same at 2 percent. The rise in state-owned commercial banks' share in total assets and deposits was mainly due to the facts that transactions related with the depositors of T. İmar Bankası TAŞ were carried out over TC Ziraat Bankası AŞ, that Pamukbank TAŞ was transferred to T. Halk Bankası AŞ, and that the share of TL deposits in total deposits was higher in state-owned banks.

The share of state-owned banks and foreign banks in total loans increased by 3 percentage points to 21 percent and by 1 percentage points to 5 percent, respectively. The shares of privately owned banks remained the same at 67 percent. On the other hand, the share of non-depository banks decreased by 2 percentage points to 7 percent.

3.5. Concentration

The shares of the largest five and ten banks in the Turkish banking system increased considerably in the last five years. Consequently, the share of the largest five banks in total assets increased from 44 percent in 1998 to 60 percent in 2004. The share of the largest ten banks in total assets increased from 68 percent to 84 percent in the same period.

Concentration in the Banking Sector* (Percentage)

	1999	2000	2001	2002	2003	2004
Largest five						
T. assets	46	48	56	58	60	60
T. deposits	50	51	55	61	62	64
T. loans	42	42	49	55	54	48
Largest five						
T. assets	68	69	80	81	82	84
T. deposits	69	72	81	86	86	88
T. loans	73	71	80	74	75	77

* As of total assets

As of total loans, the share of largest five and ten banks were 48 percent and 77 percent, respectively. In terms of total deposits, the same shares were 64 percent and 88 percent, respectively.

In terms of total assets size, there were 2 state-owned banks and 3 privately owned banks among the largest five banks, while the largest ten banks included 3 state-owned banks and 7 privately owned banks, as of 2004. There were 4 banks with asset size of USD 10 to 20 billion (2 state-owned and 2 privately owned), 2 privately owned banks with asset size of USD 20 to 30 billion, and 1 state-owned bank with asset size of above USD 30 billion.

The Number of Banks by Asset Size

USD billion →	**+0-1**		**1-2**		**2-5**		**5-10**		**10-20**		**20-40**		**40+**
	99	**04**	**99**	**04**	**99**	**04**	**99**	**04**	**99**	**04**	**99**	**04**	**04**
Number													
Commercial	37	16	10	4	7	4	6	4	4	4	1	2	1
State-owned					1		1		1	2	1		1
Privately-owned	15	5	6	2	5	3	5	4	3	2		2	
In the Fund	17	11	1	1	1	1							
Foreign	5		3	1	1								
Non-depository	17	10	1	1	1	2							
Total	54	26	11	5	8	6	6	4	4	4	1	2	1

3.6. Currency Structure of Balance-Sheet and "Fx Assets and Fx Liabilities"

By the end of 2004 TL assets and Fx assets of the banking system grew by 28 percent and 15 percent, respectively, as compared to the end of 2003. On the other side, TL liabilities and Fx liabilities grew by 29 percent and 14 percent in the same period. The share of Fx assets decreased from 39 percent to 37 percent in the balance-sheet, and the share of Fx liabilities decreased from 43 percent to 40 percent.

Fx Position by Groups(*) (Percentage)

	Per. share Fx assets		**Per. share Fx liabilities**		**USD billion Fx assets-Fx liabilities**	
	2003	**2004**	**2003**	**2004**	**2003**	**2004**
Commercial banks	39	37	43	40	-7.5	-7.9
State-owned banks	26	24	27	26	-0.6	-1.6
Privately owned banks	48	45	53	49	-5.1	-5.7
Banks in the Fund	11	9	39	14	-1.4	-0.1
Foreign banks	44	36	50	43	-0.3	-0.5
Non-depository banks	46	41	42	38	0.3	0.3
Sector	39	37	43	40	-7.2	-7.7

(*)The definition of Fx position used in the table means the difference between Fx assets and Fx liabilities in balance-sheet. This definition differs from that of 'Net General Position' in the regulation on standard ratio for Fx Net General Position/Capital Base issued by the Central Bank and BRSA. Hence, Fx denominated loans in the balance-sheet, Fx assets and Fx liabilities in the off-balance sheet are not included in the former definition.

Assets and liabilities indexed to foreign exchange are not included in the definition of "TL assets-Fx liabilities". The difference between Fx assets and Fx liabilities in balance-sheet increased from USD 7.2 billion at the end of 2003 to USD 7.7 billion at the end of 2004.

According to the calculations made by Banking Regulation and Supervision Agency including also Fx-indexed assets and liabilities, foreign exchange position in the balance-sheet of the banking sector indicated a deficit of USD 1.9 billion as of 2004.

Banking Sector's Foreign Exchange Position in Balance Sheet

USD million	2002	2003	2004
Commercial banks	-585	-88	-1,969*
State-owned banks	194	319	506
Privately owned banks	-454	-519	-2,340
Banks in the Fund	-367	-3	…
Foreign banks	42	115	-135
Non-depository banks	34	54	113
Sector	-551	-34	-1,856

Source: BRSA Weekly Bulletin
* Banks in the Fund excluded.

3.7. Structure of Assets

Strong TL demand led the share of TL items in total assets to increase. The share of loans in total assets increased by 6 percent to 34 percent due to the rapid growth in economic activity and the high increase in the demand for consumer loans. Loans/deposits ratio including the loans extended by branches abroad increased by 8 percentage points to 52 percent. However, the share of liquid assets in total assets decreased by 1 percentage point to 14 percent. The share of securities in total assets decreased by 3 percentage points to 40 percent due to the increase in non-bank sectors' demand for government securities.

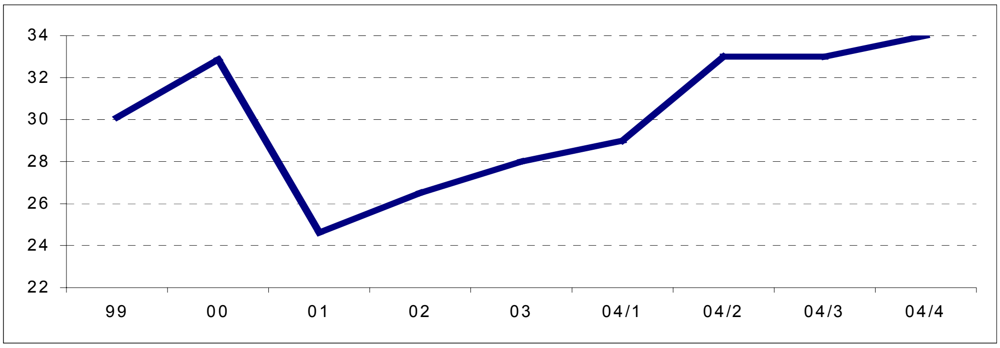
The Structure and Development of Assets

	TL trillion	USD million	Per. change (TL)	Per. share 2003	Per. share 2004
Liquid assets	43,020	32,193	19	15	14
Securities	123,680	92,554	16	43	40
Trading securities	19,086	14,283	-36	12	6
Invest. sec. available for sale	52,576	39,345	71	12	17
Invest. sec. held to maturity	52,018	38,927	13	19	17
Loans	103,241	77,259	48	28	34
Non-performing loans	6,356	4,756	-26	3	2
(-) Specific provisions	5,596	4,188	-27	3	2
Permanent assets	21,954	16,429	14	8	7
Investments and associates	3,733	2,793	56	1	1
Subsidiaries	7,449	5,575	19	3	2
Property and equipment	10,379	7,776	2	4	3
Intangible assets	393	294	-3	0	0
Other assets	14,557	10,893	-16	7	5
Total assets	306,452	229,328	23	100	100

There was a notable change in the structure of securities. The shares of trading securities and securities held to maturity decreased by 6 percent and 2 percent, respectively, while the share of securities available for sale increased by 5 percent.

Loans extended by banks' domestic branches and branches abroad grew by 48 percent and reached TL 103,241 trillion. Of loans 64 percent were TL denominated, and 36 percent were Fx denominated. According to the data of the Central Bank showing sectors' shares in total loans; individual loans had 16 percent, wholesale and retail trade sector had 12 percent, textile sector had 9 percent, each of food and finance sectors had 6 percent, and construction sector had 5 percent share in total loans. Other sectors' share was below 5 percent.

Loans/Total Assets (Percentage)



Both non-performing loans (before provisioning) and spesific provisions decreased by 26 percent and by 27 percent, respectively. As a result of these developments non-performing loans (after provisioning) decreased by 23 percent, and the share of non-performing loans (after provisioning) in total assets decreased from 0.4 percent to 0.2 percent.

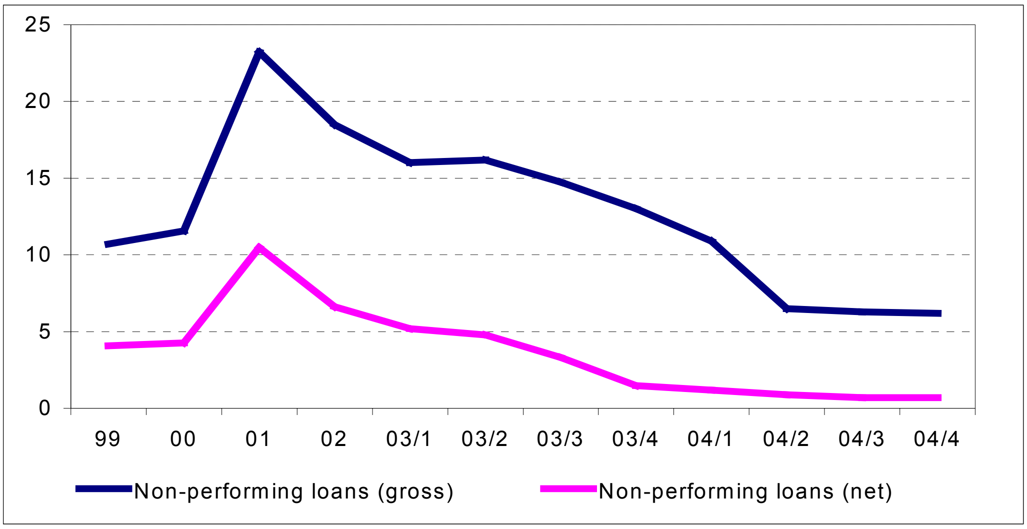
Non-performing Loans* and Specific Provisions (Percentage)

	Non-performing loans/ Total loans		Specific provisions/ Non-performing loans	
	2004	**2003**	**2004**	**2003**
Commercial banks	6	13	88	89
State-owned banks	11	34	96	98
Privately owned banks	5	7	84	80
Banks in the Fund	458	90	87	75
Foreign banks	3	4	75	79
Non-depository banks	3	3	87	90
Sector	6	12	88	89

The increase in non-performing loans was limited due to the growth in economic activity, the fall in inflation and interest rates, as well as the revaluation of financial assets. Thus, the ratio of non-performing loans (before provisioning) to total loans decreased from 12 percent to 6 percent; while 88 percent of such loans were allocated provisions.

Permanent assets increased by 14 percent to TL 21,954 trillion, while its share in total assets decreased by 1 percentage point to 7 percent. This was mainly supported by the fall in inflation as well as the sale of subsidiaries, investments and associations.

Non-performing Loans to Total Loans (Percentage)



Based on the remaining maturities; the share of demand assets in total assets was 14 percent, that of assets with 1-12 months maturity was 46 percent, and the remaining 40 percent of total assets had longer than one year maturity. On the contrary, the share of demand liabilities in total liabilities was 28 percent, that of liabilities with 1-12 months maturity was 64 percent, and the rest of the liabilities had longer than one year maturity.

2.8. Structure of Liabilities

Total deposits increased by 23 percent; however their share in total liabilities remained the same with 64 percent. Fx deposits increased by 12 percent, and their share in total liabilities decreased by 3 percentage points to 29 percent. TL deposits increased by 33 percent and their share in total liabilities increased by 3 percentage points to 36 percent. Consequently, TL deposits formed 55 percent of the total deposits, which increased to TL 197,394 trillion, while the remaining 45 percent were Fx deposits.

The Structure and Development of Liabilities

	TL trillion	USD million	Per. change (TL)	Per. share 2003	Per. share 2004
Deposits	197,394	147,717	23	64	64
TL	108,892	81,487	33	33	36
Fx	88,502	66,229	12	32	29
Non-deposit funds	45,261	33,870	16	16	15
Shareholders' equity	45,963	34,395	29	14	15
Paid-in capital	14,824	11,093	10	5	5
Supplementary capital	22,835	17,088	0	9	7
Reserves	23,460	17,556	11	8	8
Profit/loss	-15,156	-11,342	-31	-9	-5
Previous year	-21,612	-16,173	-21	-11	-7
Current year	6,456	4,831	15	2	2
Other liabilities	17,834	13,346	25	6	6
Total	306,452	229,328	23	100	100

Non-deposit funds having a share of 15 percent in total liabilities, increased by 16 percent in 2004 and reached TL 45,261 trillion. 54 percent of the non-deposit funds were formed by funds borrowed from foreign banks and institutions constituted

3.9. Shareholders' Equity

Total shareholders' equity of the banking system increased by 29 percent to TL 45,963 trillion (USD 34.4 billion). The ratio of shareholders' equity to total assets increased to 15 percent from 14.2 percent. The major contributors to the improvement in the shareholders' equity were the increases in reserves and paid-in capitals, and the decrease in previous years' losses. Redemption of some of the government securities injected to a state-owned bank as equity limited the increase in the shareholders' equity of state-owned banks.

Shareholders' equity

	TL trillion	USD million	Per. change (TL)	As per. of T. assets
Commercial banks	40,823	30,549	30	13.8
State-owned banks	10,068	7,534	5	9.4
Privately owned banks	27,399	20,504	31	15.6
Banks in the Fund	1,273	952	-250	65.7
Foreign banks	2,083	1,559	25	20.1
Non-depository banks	5,140	3,846	23	45.4
Sector	45,963	34,395	29	15.0

Real growth of shareholders' equity as well as the slower growth of permanent assets as compared to total assets caused the increase in working capital to continue. Working capital (shareholders' equity-fixed assets-non-performing loans after provisioning) increased to TL 23,249 trillion from TL 15,308 trillion. The ratio of working capital to total assets increased from 6.1 percent to 7.6 percent.

Working Capital

	TL trillion		As per. of T. assets	
	2004	2003	2004	2003
Commercial banks	18,542	11,515	6.3	4.8
State-owned banks	6,535	6,451	6.1	7.8
Privately owned banks	9,273	5,181	5.3	3.6
Banks in the Fund	1,149	-1,331	59.3	-18.6
Foreign banks	1,585	1,213	15.3	17.5
Non-depository banks	4,707	3,793	41.6	37.0
Sector	23,249	15,308	7.6	6.1

*Shareholders' equity-permanent assets-loans under follow-up after specific provisions

Net profit of the banking sector increased by 15 percent to TL 6,456 trillion. The increase rate of net profit was 50 percent in state-owned banks, 41 percent in the banks in the Fund and 33 percent in foreign banks. Net profit decreased by 3 percent in privately owned banks, and 29 percent in non-depository banks. Net return on assets decreased from 2.3 to 2.1 percent in the banking sector, while the return on equity decreased from 16 percent to 14 percent.

Net Profit-Loss, 2004

	Net Profit-Loss TL trillion	USD million	Per. change (TL)	Return on assets (percentage)	Return on equity (percentage)
Commercial banks	6,141	4,595	19	2.1	15.0
State-owned banks	2,682	2,007	50	2.5	26.6
Privately owned banks	2,825	2,114	-3	1.6	10.3
Banks in the Fund	386	289	41	19.9	30.4
Foreign banks	247	185	33	2.4	11.9
Non-depository banks	315	236	-29	2.8	6.1
Sector	6,456	4,831	15	2.1	14.0
Sector (excluding banks in the Fund)	6,070	4,542	14	2.0	13.6

3.10. Income-Expenditure

Net interest income of the banking sector increased by 57 percent before provisions. In an environment of falling interest rates, the increase in net interest income was mainly due to longer maturity of the assets as compared to the liabilities and the increase in total loans volume.

Income-Expenditure, December 2004

	TL trillion	USD million	Per. change
Interest income	40,409	30,240	4
Interest expense	22,731	17,011	-18
Net interest income	17,678	13,229	57
Net fees and commission income	3,966	2,968	48
Dividends	22	16	63
Net trading income	2,302	1,723	-65
Profit/loss on trad. account sec.	1,814	1,358	-64
Foreign exchange income/losses	488	365	-70
Other operating income	2,340	1,751	-16
Total operating income	26,308	19,687	12
Net operating income	11,620	8,695	25
Income before taxes	9,086	6,800	13
Provisions for taxes on income	2,647	1,981	9
Net profit/loss	6,456	4,831	15

Despite this positive development in net interest income and net fees and commission income; general improvement in the net profit of the banking system was restricted by the rapid decrease in net profit from trading account securities and in the net profit from foreign exchange transactions. Meanwhile, limited increase in operating costs of the banks as a whole also had a positive effect on the profit performance of banks. In 2004, income before taxes and net profit of the banking sector grew by 13 percent and 15 percent respectively.

3.11. Off-Balance Sheet Items

Guaranties and warranties increased by 19 percent, while commitments increased by 59 percent, in 2004. This increase in commitments was mainly caused by an increase in the irrevocable commitments item. The major sub-item in the irrevocable commitments item was credit card limits. Besides, derivative financial instruments and custody and pledge securities increased by 14 percent and 54 percent, respectively. Hence, the increase rate in off-balance sheet items amounted to 46 percent.

Off-Balance Sheet Items, December 2004

	TL trillion	USD million	Per. change
Guaranties and warranties	55,712	41,691	19
Commitments	85,040	63,639	59
Derivative financial instruments	38,974	29,165	14
Custody and pledge securities	333,506	249,574	54
- Accepted independent guar. and war.	11,849	8,867	-
Total	513,232	384,096	46