

THE CBRT PRESS RELEASE

ON THE PROGRAMMED FOREIGN EXCHANGE BUYING AUCTIONS

Effective from 6 May 2003, the Central Bank of Turkey (CBRT) has decided to hold daily foreign exchange buying auctions under the framework of the following arrangements.

As is known, it has been made public in the various CBRT press releases that, in the cases where there is an excess foreign exchange supply resulting from the reverse currency substitution process and the strong balance of payments position, the CBRT might resume foreign exchange buying auctions with the aim of enhancing its foreign exchange reserves, without conflicting with the floating exchange rate regime, and without disrupting the long-term trend and the natural equilibrium level of the exchange rate.

In fact, the CBRT held foreign exchange buying auctions for this purpose between April and June 2002, and purchased USD 795 million in total. However, the programmed foreign exchange buying auctions were interrupted in July 2002 after observing somewhat artificial price formation in the foreign exchange market since reverse currency substitution slowed down and the volume of foreign exchange transactions was reduced due to political uncertainties experienced in June 2002. However, it was repeatedly stated that developments in balance of payments and reverse currency substitution process had been closely monitored by the CBRT and that foreign exchange buying auctions could be re-started by announcing in advance.

In evaluating the reverse currency substitution, the foreign exchange deposits, excluding interbank deposits, showed a constant upward trend along with domestic and international developments until December 2002 starting from July 2002 when the CBRT foreign exchange buying auctions were halted. It was observed that the foreign exchange deposits remained stable in the period of January-February 2003. Foreign exchange deposits started to decline in early March 2003 together with the depreciation of Turkish lira following the rejection of the motion allowing the deployment of foreign troops on Turkish soil by the Turkish Parliament and the

commencement of Iraqi war. The total foreign exchange deposits, which stood at USD 47,6 billion as of 28 February 2003, decreased to USD 45,5 billion (provisional data) as of 18 April 2003, decreasing by USD 2,1 billion.

From the standpoint of evaluating the reverse currency substitution process, it is important to examine whether the amounts withdrawn from foreign exchange deposits have gone out of the banking system or invested in Turkish lira instruments. It was observed that, a substantial part of the withdrawn foreign exchange deposits has switched to Turkish lira investment instruments due to developments between 28 February and 18 April 2003, while the amounts going out of the banking system have remained limited. In this period, the total amount of Turkish lira deposits, repos, mutual funds and Government Debt Securities (GDS) that are owned by individual and institutional investors and are held in the bank accounts have increased to TL 127,3 quadrillion from TL 119,3 quadrillion, showing a nominal increase of 6,7 percent.

Of the TL 8 quadrillion increase in the investment instruments, a sizeable amount of TL 6,3 quadrillion is accounted for the increase in GDS that are held and owned by individual and institutional investors. The total GDS held with the banks by individual and institutional investors have increased to TL 53,7 quadrillion as of 18 April 2003 from TL 47,4 quadrillion on 28 February 2003.

During the same period, as the decline in foreign exchange deposits mainly materialized in March 2003 when portfolio shifts took place to take advantage of rising exchange rates and interest rates, the developments in April 2003 should be evaluated separately. In April 2003, it is observed that the decline in foreign exchange deposits have stopped, and the total foreign exchange deposits have realized as USD 45,5 billion (provisional data) as of 18 April 2003, which was USD 45,1 billion as of 28 March 2003, increasing by USD 0,4 billion only. This increase has resulted from the fact that the foreign exchange banknotes held outside the banking system began to flow back to the system in late March 2003. According to the provisional data obtained from banks, during the period between 27 March and 30 April approximately USD 950 million foreign banknotes entered into the system. Accordingly, the foreign exchange deposits have increased to a limited extent, and the residents' demand for Turkish lira investment instruments has continued. The residents' total Turkish lira investments have increased to TL 127,3 quadrillion as of 18 April 2003, from TL 124,9 quadrillion on 28 March 2003.

In addition, the reinforced fiscal discipline by extra measures taken in 2003 budget, the completion of the fourth review with the IMF, the promising budget performance in recent months and the realizations of certain measures taken for

achieving fiscal discipline are all increasing the likelihood of the continuation of excess supply in foreign exchange, together with the favorable prospects in balance of payments in summer months.

In view of the above analysis, the CBRT has decided to resume foreign exchange buying auctions by considering that its strong reserve position will boost the market's confidence in the current program. As it was the case in 2002, the CBRT does not target any specific reserve level. The aim here is to enhance the CBRT's foreign exchange reserve position in a way the excess foreign exchange supply does not create an extra volatility in exchange rates and disturb the foreign exchange liquidity and foreign exchange positions of the banks, without targeting any exchange rate level.

As in 2002, the monthly programs of foreign exchange buying auctions will be announced in advance. However, The CBRT may, with a prior notice, suspend the auctions before the end of the period in the cases where the depth of foreign exchange market is lost; and excessive volatility is observed in exchange rates due to an external shock or unpredictable developments.

The foreign exchange buying auctions will be subject to the following rules.

Rules for Foreign Exchange Buying Auction:

1. The total amount of daily foreign exchange buying will be USD 20 million. However, auctions will not be held on the public holidays in the United States, even if they coincide with the working days in Turkey. Auctions will not also be held on half working days since there is no indicative exchange rate fixing on these days. Accordingly, in May 2003 there will be foreign exchange auctions on 17 working days except for 26 May 2003, which is holiday in the USA.
2. In the event that there is no bid at all, or the total of the bids are less than USD 20 million, the amount of daily auction can be increased up to USD 40 million by starting with the first subsequent tender in order to compensate the foreign exchange that is not purchased. In other words, even if the total amount of

foreign exchange which could not be bought surpasses USD 20 million, the amount to be added to daily amount of USD 20 million for compensation will be limited to USD 20 million. However, the amount of foreign exchange that has been programmed but could not be purchased in the previous month will not be compensated in the auctions to be held in the subsequent month.

3. Banks and special finance houses (institutions) authorized to operate in the Foreign Exchange and Banknotes Markets are allowed to participate in the auction.
4. Auctions are to be held under the multiple-price auction method.
5. The maximum bid price will be the arithmetic average of the first five observations obtained the same day in accordance with the “Rules for Fixing the Indicative Exchange Rates” made public by the CBRT press release dated 28 March 2002 No: 2002-25. The maximum price thus obtained and the total amount of the auction including the amount to be compensated will be posted on the CBRT’s Reuters page “CBTQ”.
6. Institutions may bid between 14.40 and 15.00.
7. Minimum amounts that can be bid for is USD 1 million and its multiples. The maximum amount that can be bid for is limited to the total amount stated in the auction.
8. Institutions cannot change their bid amounts and prices during the auction.

9. If there is more than one bid at the price the auction is cut, the distribution will be made on a pro-rata basis.
10. Institutions willing to participate in the auctions will send in their bids by stating their price and amounts through the telephone numbers 3091966-89 of the Foreign Exchange and Banknotes Markets Division.
11. Auction results showing the total bid amount, average, maximum and minimum prices will be posted on the CBRT's Reuters page of "CBTQ".
12. No transaction commission will be charged.
13. Institutions that do not fulfill their obligations arising from the auctions will be subject to the sanctions as specified in the Standing Order of the Foreign Exchange and Banknote Markets.