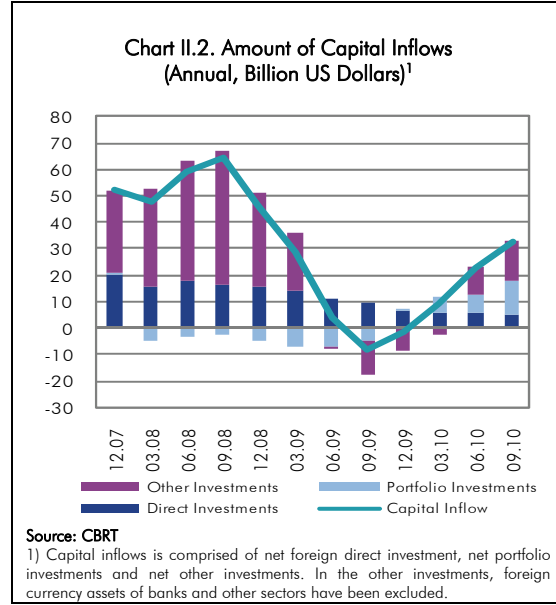
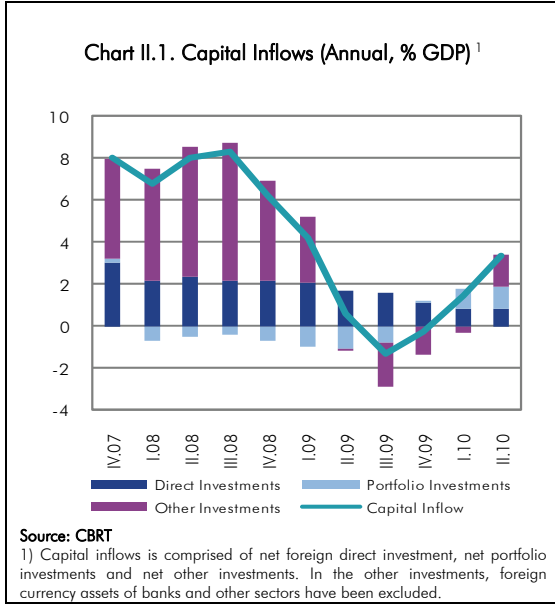


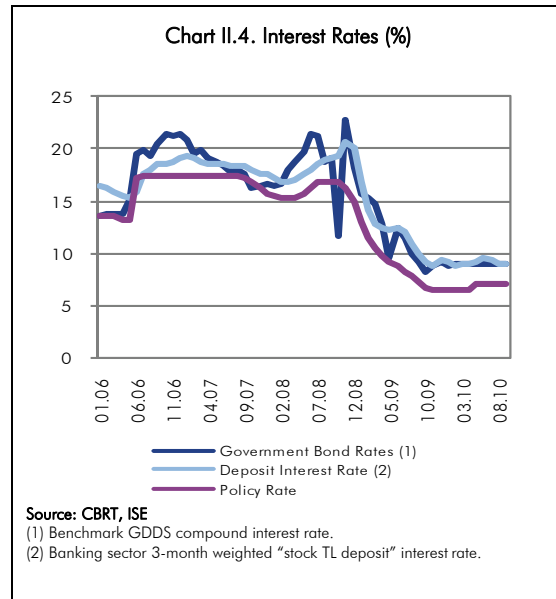
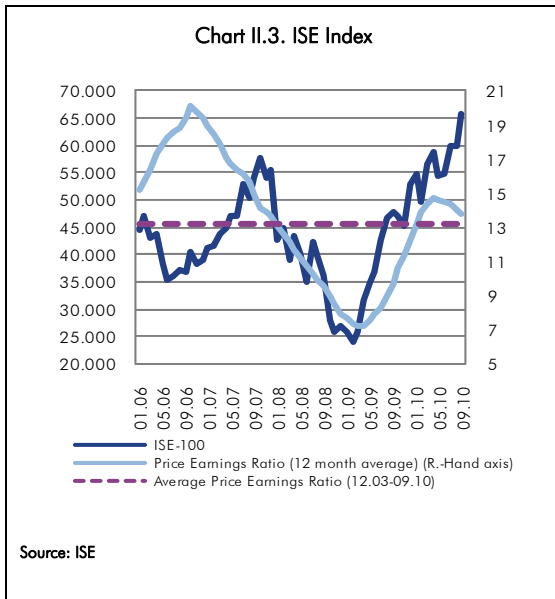
II. DOMESTIC ECONOMIC OUTLOOK

The faster than expected recovery in economic activity, the Medium-Term Program indicating that the financial discipline will continue, the stability in the financial system, the positive ratings of credit rating agencies and the risk premium indicators following a course even below pre-crisis levels, all suggest a positive outlook for the Turkish economy. As capital inflows accelerate along with these developments and the increase in the global risk appetite, market interest rates fall, asset prices escalate and the Turkish lira strengthens. In turn, these developments, trigger consumption and investment demand, increasing loans used both by households and firms, and contribute to growth of the economy on the back of domestic demand. Economic growth reflects positively on the labor market as well and despite the fact that unemployment rates are still above pre-crisis levels, they are in recess. Despite strong domestic demand, core inflation indicators display a positive outlook. However, the weak course of foreign demand, domestic demand-driven growth and the strengthening of the Turkish lira, negatively influence the foreign trade balance, leading to an expansion in the current account deficit. Consumption-driven tax revenues increasing parallel to economic recovery and public expenditures that are kept under control, affect public finance positively. In the upcoming period, besides the acceleration in short-term capital flows, loan growth with increased pace and widening of the current account deficit are important in terms of financial stability. In this framework, macroprudential measures will come to the forefront on Turkey's agenda as in other countries.

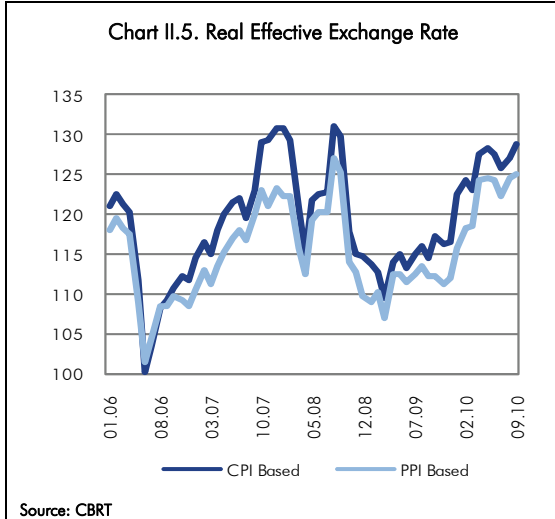
The increase in the global risk appetite, the high growth rate of the Turkish economy, discipline in public finance, a sound financial system and relatively high interest rates lead to capital inflows, which are primarily composed of banks' borrowings from abroad and portfolio investments. Net capital inflows, which reached 8.3 percent of the GDP during the third quarter of 2008, fell to 1.3 percent of GDP in the third quarter of 2009 on the back of the global crisis. This development was mainly attributable to the fact that the banks and other sectors were net external debt payers at that time. With the exit from the global crisis, capital inflows gained pace and reached 3.4 percent of the GDP by the second quarter of 2010 (Chart II.1). The increase in other liabilities, due to the surge in foreign borrowing of the banks, was particularly influential on the acceleration of capital inflows after the global crisis, and the weight of foreign direct investments on capital inflows gradually decreased. Of the capital inflows, reaching USD 32.6 billion dollars in annual terms as of September 2010, USD 14.6 billion was from other liabilities and USD 12.9 billion was from portfolio investments, but the share of foreign direct investments remained only USD 5.1 billion. A breakdown of the other liabilities indicates that while the net liabilities of the banks were on the rise, the other sectors were net external debt payers (Chart II.2). The main factor driving the non-financial institutions to be net external debt payers is the borrowing facility provided to firms with the amendment made to Decree No. 32 of the Law on Protection of the Value of the Turkish Lira; according to which firms were allowed to borrow in foreign currency from domestic branches under specified terms and conditions. Accordingly, it was observed that firms shifted their borrowing from abroad to domestic loans.



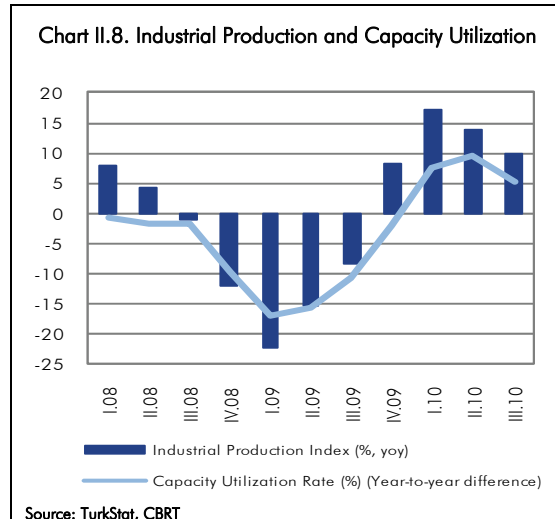
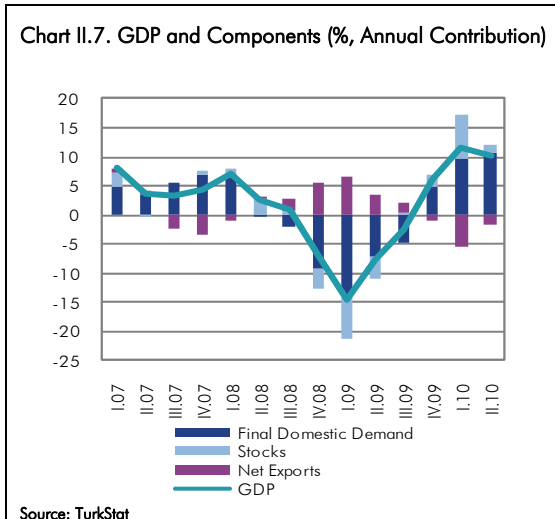
Capital inflows affect financial markets positively and support the surge in asset prices. Improvements in risk perceptions related to Turkey and the increase in global risk appetite both positively influence the stock and bond market. In 2010, the stock markets maintain their rising trend and the price-earnings ratios are close to historical averages (Chart II.3). Likewise, bond prices are also on the rise. Accordingly, GDDS interest rates are receding (Chart II.4).



Along with increasing capital inflows on the back of restored confidence in financial markets, liquidity conditions have improved and the Turkish lira has strengthened. Real effective foreign exchange indices point to a strengthening of the Turkish currency. As of September 2010, the Turkish Lira appreciated by 10.4 percent according to CPI based index and by 11.8 percent according to PPI based index, compared to end-2009 (Chart II.5). One of the best indicators in measuring the liquidity conditions is the spread between the bid and ask prices of financial assets (exchange rate and bond market). The market liquidity index which is formulated based on these indicators and which reflects the confidence in the market, increased after the peak of the global crisis, suggesting an improvement in market confidence; however, it is still behind pre-crisis levels (Chart II.6).

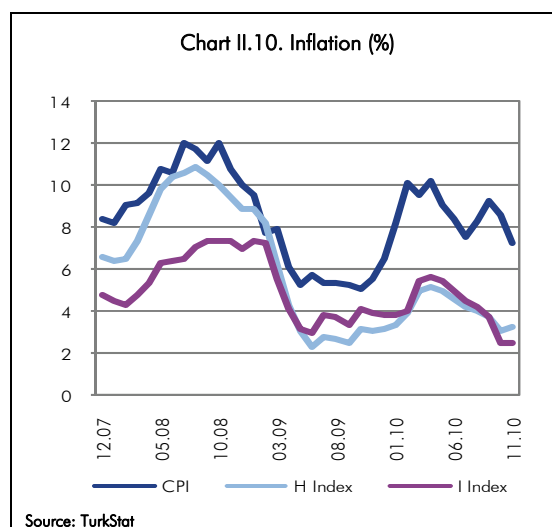
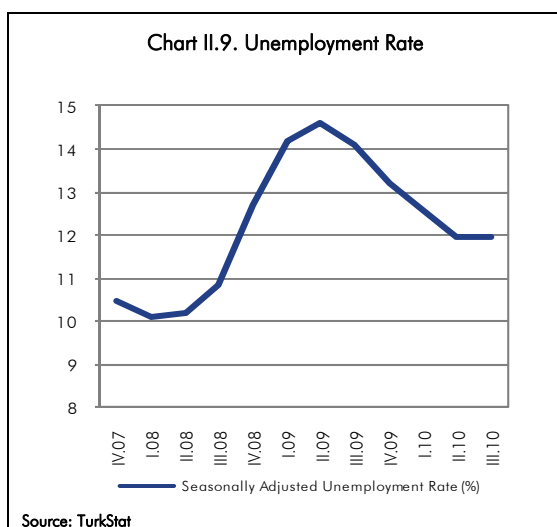


With the support of domestic demand, the economy is recovering fast. GDP increased by 11.7 percent year-on-year in the first quarter and by 10.3 percent in the second quarter of 2010. Consequently, GDP, which had shrunk by 11.1 percent in the first half of 2009, grew by 11 percent in the same period of 2010. The growth of the GDP was mainly driven by the final domestic demand. In the first half of 2010, the final domestic demand contributed to GDP growth by 10.3 points, with a breakdown of 5.4 points by private consumption expenditures, 4.6 points by investment expenditures and 0.3 points by public consumption (Chart II.7). The industrial production and capacity utilization data for the third quarter of 2010 demonstrate that economic growth continued in the third quarter as well. Although the rate of increase displays a downward trend, industrial production increased by 10 percent in the third quarter of 2010, whereas the capacity utilization rate increased by 5.4 points compared to the same period of the previous year and was realized as 74 percent (Chart II.8). It is anticipated that industrial production, which displayed a more moderate increase in the third quarter of the year compared to the first half, is to re-gain momentum in the last quarter based on increasing consumer confidence and strengthening propensity to invest owing to waning political uncertainty after the referendum.

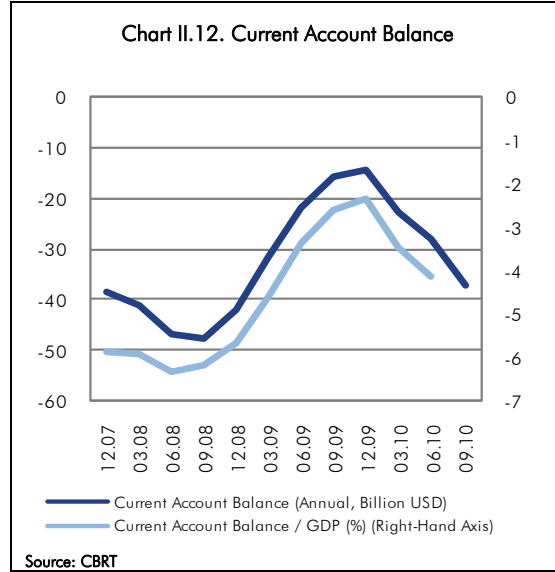
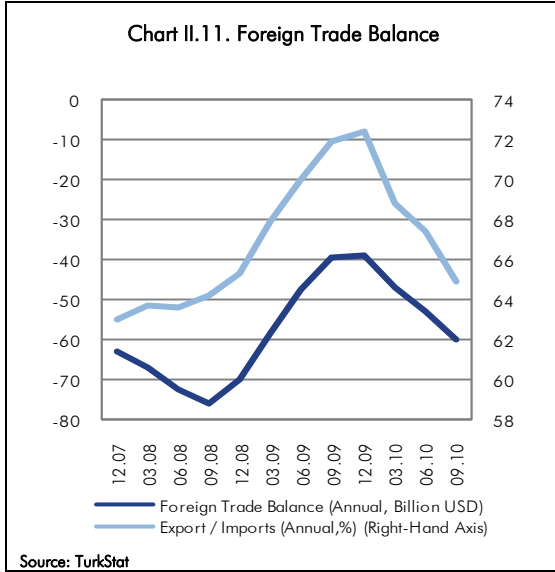


As unemployment rates are receding on the back of economic growth, the core inflation indicators are on a path consistent with the medium-term targets. The seasonally adjusted unemployment rate, which stood at 10 percent in April 2008, rose to 14.8 percent in April 2009 due to the global crisis and economic contraction. After this date, the unemployment rate decreased and

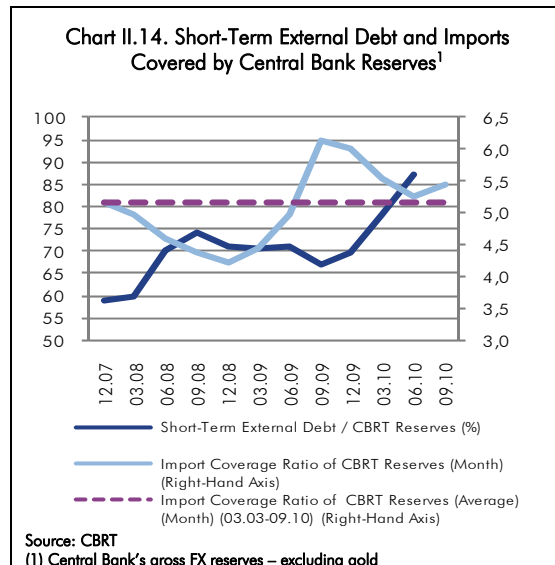
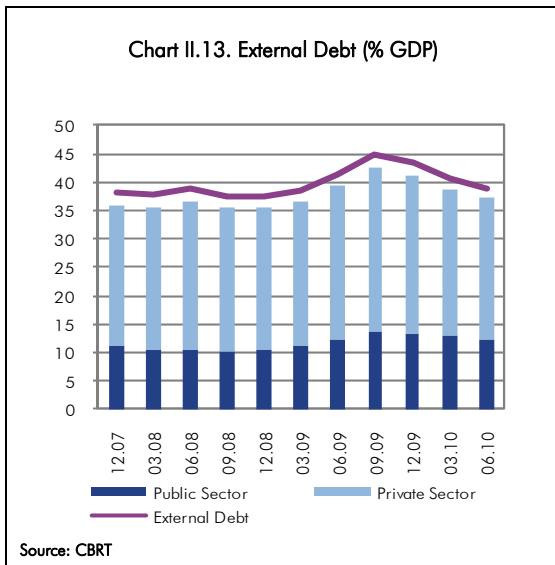
receded back to 12 percent by August 2010 (Chart II.9). Despite the improvement in employment conditions, unemployment rates are still at a high level. In this environment, the core inflation indicators have dropped to historic lows. While annual inflation was 7.3 percent in November 2010, core inflation indicators measured with H and I indices stand at 3.2 percent and 2.5 percent, respectively (Chart II.10). The fact that it took some time for capacity utilization rates to reach pre-crisis levels due to the weak course of foreign demand, the unemployment rate still preserves its high level despite the improvement in employment conditions and the strong position of the Turkish lira; all support the maintenance of low levels in core inflation indicators. In this framework, it is foreseen that annual inflation will be in a downward trend in the forthcoming period. The uncertainties in food prices continue to be the most fundamental risk regarding the short-term inflation outlook.



Domestic demand-based growth, appreciation of the Turkish lira, recovery in production, along with the need for imported intermediate goods and energy lead to an expansion in the current account deficit. Owing to the stagnation in economic activity due to the global crisis and the drop in commodity prices, the foreign trade deficit, which had been USD 75.8 billion annually in the third quarter of 2008, narrowed rapidly and fell to USD 38.8 billion as of the end of 2009. In response to the economic recovery, the foreign trade deficit started to rise again and reached USD 60 billion on an annual basis as of September 2010. As a result of these developments, the export/import coverage ratio, which stood at 72.5 percent at end-2009, decreased to 64.9 percent on an annual basis in September 2010 (Chart II.11). The differentiation in demand composition of economic growth, which is becoming more marked, affects the current account deficit negatively by increasing the foreign trade deficit. The current account deficit, reaching 6.3 percent of the GDP as of June 2008, declined to 2.3 percent of the GDP by the end of 2009 on the back of the global crisis and economic contraction. With the recovery in economic activity, the current account deficit started to rise again and reached to 4.1 percent of GDP in June 2010. Widening of the current account deficit continued in the third quarter of 2010 as well. The annual current account deficit, standing at USD 14.4 billion at end-2009, increased to USD 37.1 billion as of September 2010 (Chart II.12).

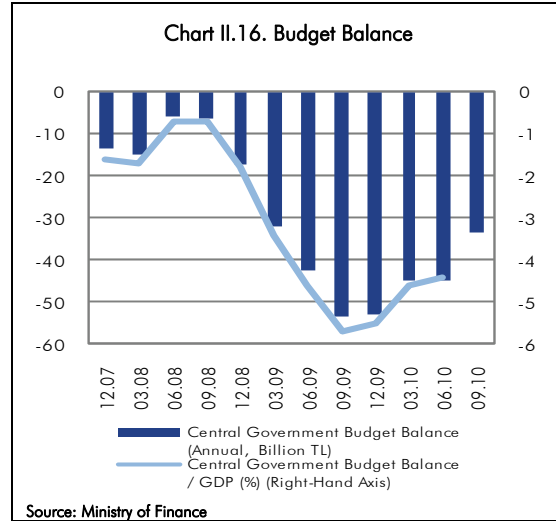
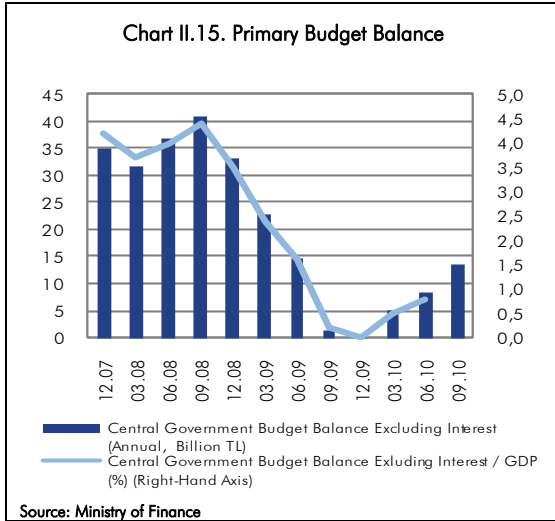


In spite of the rise in the current account deficit, the external debt service capacity indicators do not display a negative outlook. The ratio of external debt to GDP declined by 4.3 points and became 39 percent in the second quarter of 2010 compared to end-2009 (Chart II.13). The share of the short-term external debt within the total debt increased by 4.9 points to reach 23.3 percent compared to end-2009 figures. Although the ratio of short-term debt to Central Bank reserves is below 100 percent, it climbed to 87.3 percent in June 2010 from its level of 69.9 percent at the end of 2009. As of September 2010, the Central Bank reserves were able to meet the imports for a period of 5.5 months and, despite the recent decline, they are hovering around past averages (Chart II.14).

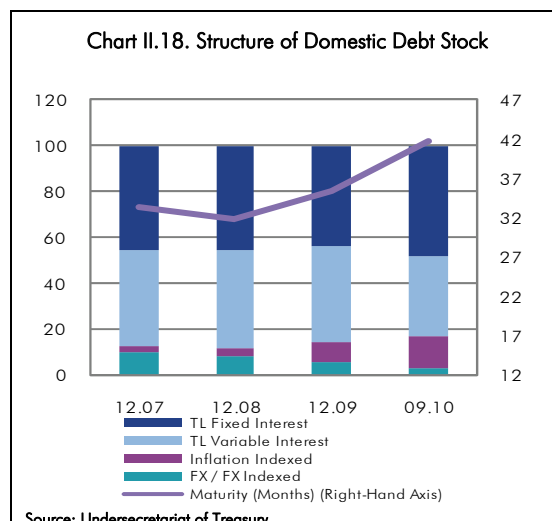
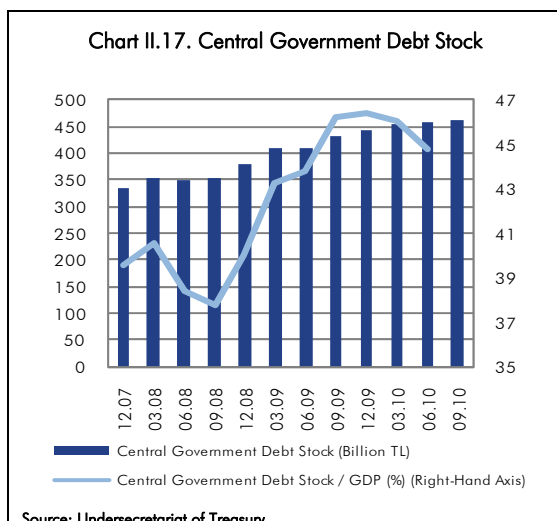


Increased tax revenues owing to the economic recovery and expenses that have been curbed have had a positive effect on public finance. Budget revenues based on indirect taxes surged due to the increase in domestic demand, interest expenses decreased on the back of falling interest rates and primary expenditures increased by a relatively small margin. In consequence, budget performance displays a positive outlook. The primary budget surplus, which had been TL 440 million in annual terms as of the end of 2009, increased to TL 13.7 billion year-on-year in September 2010. While the budget deficit stood at TL 52.8 billion in 2009, this figure receded to TL 33.2 billion year-on-year in September 2010. Thereby, the budget deficit, reaching 5.5 percent of GDP in 2009, when the economy shrank,

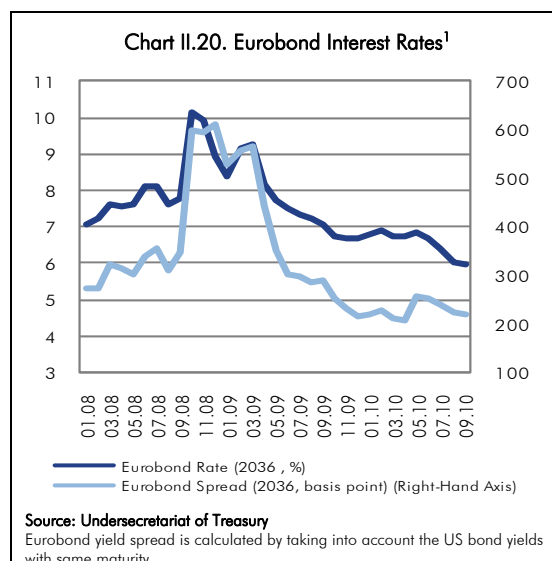
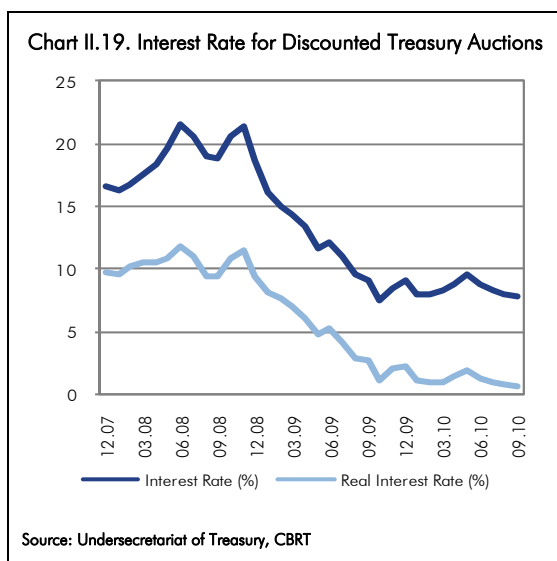
was down to 4.4 percent of GDP in the first half of 2010 (Chart II.15 and Chart II.16). In an environment of expanding current account deficit, it is considered essential for financial stability to contain public expenditures and not to slacken the discipline in public finance. In this framework, it is important to achieve the budget performance targets stipulated in the Medium Term Program (MTP) announced in October. As a matter of fact, the program targets anticipate a limited tightening in the fiscal policy in the upcoming period. The public finance indicators in the MTP indicate that the improvement that started to be observed in 2010 will continue with the contribution of an earlier and stronger than expected economic recovery.



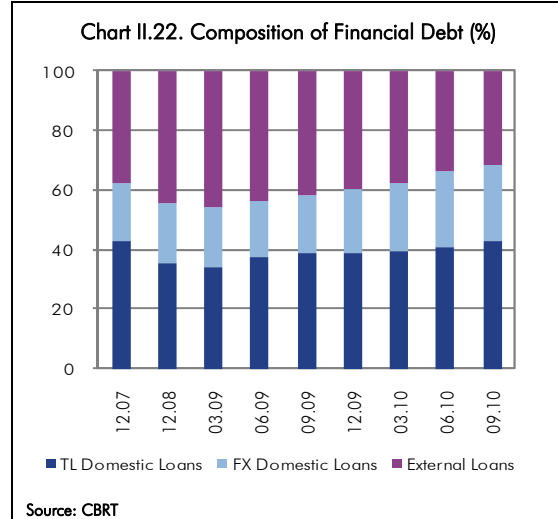
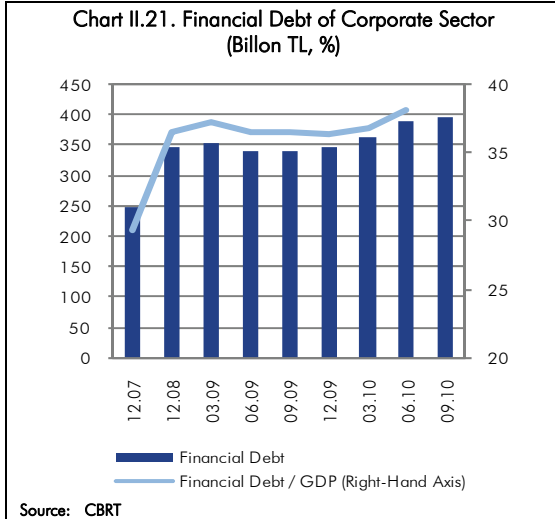
Public debt ratios and vulnerability indices of the debt stock are improving on the back of economic growth, positive budget performance and the drop in real interest rates. The rate of increase in central government debt stock, which had reached TL 441.5 billion in 2009 with an increase of 16.1 percent, slowed down in 2010. Central government debt stock displayed a limited increase by 4.3 percent in the first nine months of 2010, compared to end-2009 and was realized as TL 461 billion. The ratio of debt stock to GDP, which rose to 46.3 percent in 2009 with a 6.3-points increase, declined by 1.5 points in the second quarter of 2010 and fell to 44.8 percent (Chart II.17). 75.5 percent of the total debt stock of the central government is composed of domestic debt. The composition of the domestic debt stock reveals that the share of TL-denominated fixed rate debt and CPI-indexed debts are on the rise. In September 2010, the ratio of TL-denominated fixed rate debt to domestic debt stock increased by 4.2 points to reach 48.1 percent and those indexed to CPI increased by 5.5 points to become 14.5 percent, compared to end-2009. The maturity of domestic debt stock is also on the rise. The average maturity of domestic debt stock, which had been 32 months in 2009, increased to 42 months in September 2010 (Chart II.18). The decrease in the share of FX-denominated and FX-indexed stock is considered to be a favorable development in terms of the decrease in sensitivity to exchange rate risk, whereas, the increase in the share of fixed income securities and extension of maturity are considered positive in terms of decrease in sensitivity to interest rate hikes.



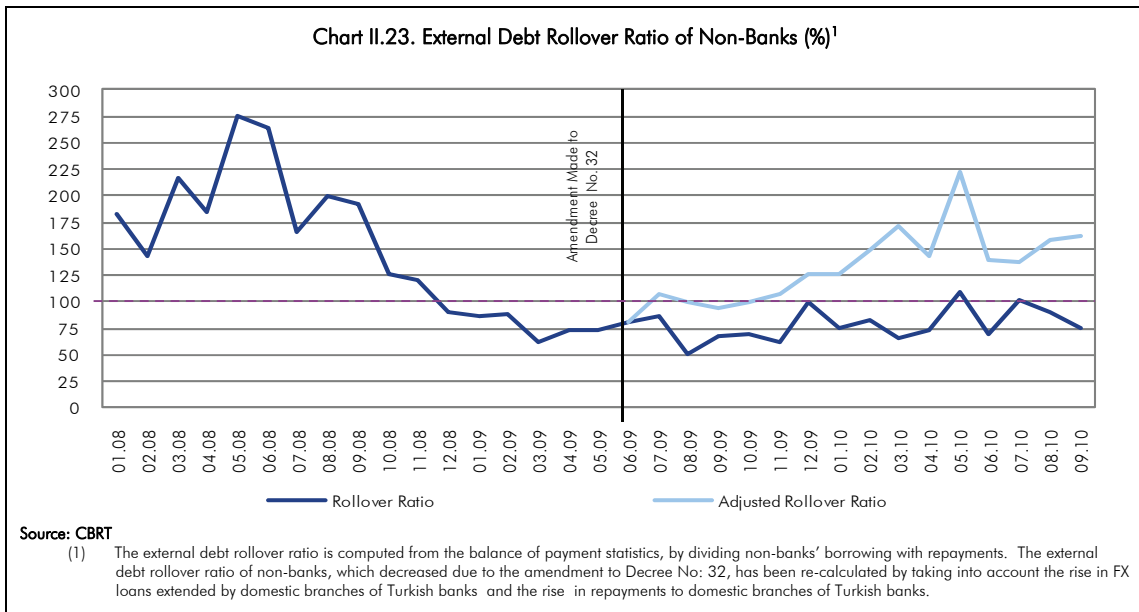
The narrowing of the budget deficit and improvement of public debt stock indicators underpin the decline in public borrowing costs. As a result of the increase in global risk appetite and positive developments in risk perceptions related to Turkey, the borrowing interest rate fell to 7.8 percent in discounted auctions as of September 2010. Adjusted for 12-month inflation expectations, it is observed that the real interest rate dropped to historic lows to stand at 0.6 percent (Chart II.19). As of September 2010, the Eurobond interest rate, which is to mature in 2036, was realized as 5.9 percent and the yield spread thereof declined to 218 basis points (Chart II.20).



On account of rapid economic recovery, fading uncertainties, the fall in interest rates and the improvement in lending conditions, corporate sector debt increased while the share of their foreign borrowing decreased. While no significant change was observed in firms' total financial debt in 2009, liabilities surged by 13.9 percent as of September 2010 compared to end-2009 and reached TL 395 billion. Consequently, the ratio of the corporate sector financial debt to GDP increased by 1.7 points in the second quarter of 2010, compared to end-2009 and reached 38 percent (Chart II.21). Although 57.4 percent of corporate sector debt is denominated in foreign currency, majority of this debt is long-term. As of September 2010, the share of foreign borrowing in total loans is 21.6 percent, whereas the share of FX loans extended to the corporate sector by domestic and foreign branches and affiliates of Turkish banks in total loans increased by 4.1 points compared to end-2009 and reached 78.4 percent (Chart II.22).



After the amendment to Decree No: 32 in June 2009, firms have shifted their credit utilization towards the domestic market and the external loans rollover ratio does not display any negative course. Between June 2009, when Decree No:32 was amended, and September 2010, the amount of loans extended to the corporate sector by foreign branches and affiliates of Turkish banks decreased by USD 7 billion, whereas the loans extended by foreign banks declined by USD 4.3 billion. On the other hand, FX loans extended by domestic branches of banks, increased by USD 27.8 billion. According to balance of payments data, the external debt rollover ratio of non-banks is 75 percent in September 2010; however, taking into consideration the increase in the volume of FX loans extended by domestic branches, the ratio is realized as 163 percent (Chart II.23).



Despite the rise in debt, corporate sector revenues from sales have increased and its profitability performance has remained strong. Total amount of sales revenues of manufacturing industry firms quoted on the Istanbul Stock Exchange (ISE) increased by 20.4 percent during the first nine months of 2010 compared to the same period of the previous year and their total net profits surged by 64.6 percent in the same period. Operating profits, which increased on the back of the rise in sales revenues, and the decrease in financial expenditures played pivotal role in firms' positive profitability performance (Chart II.24). As a result of these developments, the return on equity, which was 7.4

percent in the first nine-months of 2009, increased to 11 percent during the same period of 2010 (Table II.1). The increase in the profit margin was influential on the rise of return on equity of firms. The decrease in firms' financial expenditures, which are excluded from operating profits, affected their profit margin positively. As the net FX short position reaches 20.1 percent of own funds, appreciation of the Turkish lira puts downward pressure on exchange rate driven financial expenditures of firms and contributes to the rise in their profit margins.

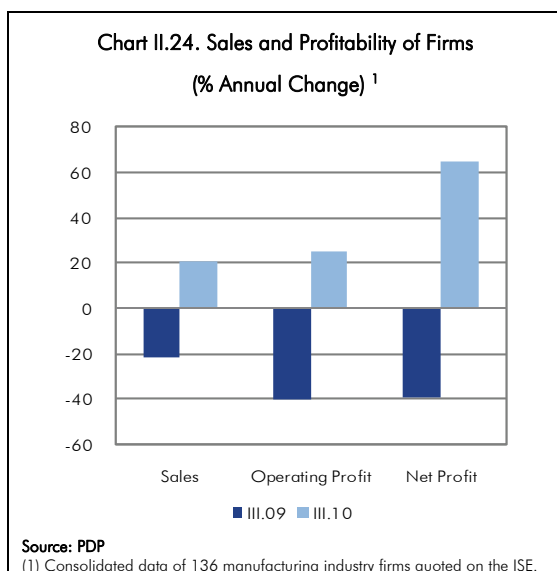
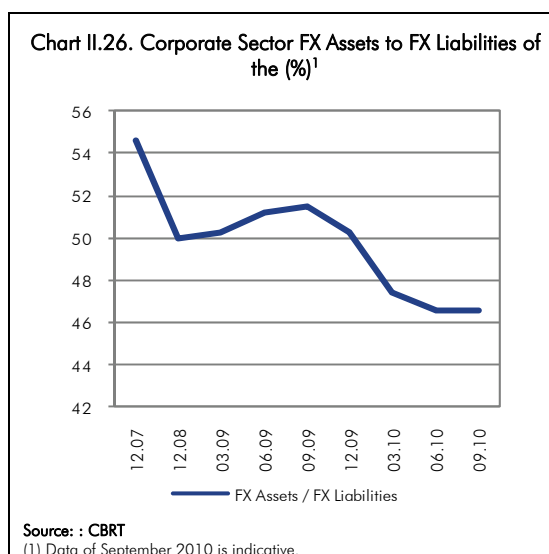
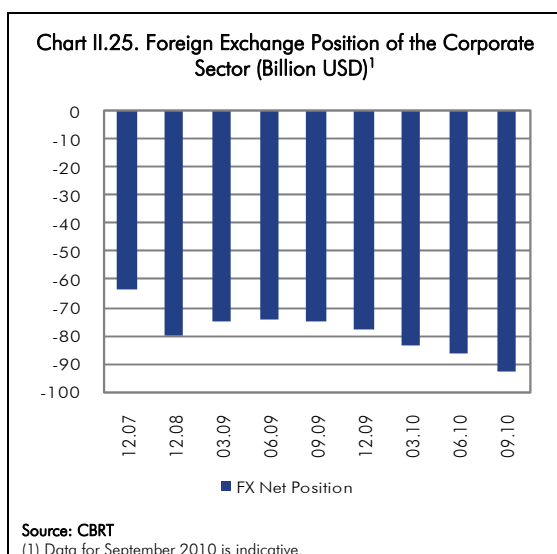


Table II.1. Return on Equity and Its Components¹

	09.08	09.09	09.10
Net Profit / Equity (%)	12.3	7.4	11.0
Assets / Equity	1.95	1.99	1.94
Net Profit / Assets (%)	6.3	3.7	5.7
Sales / Assets	1.00	0.77	0.85
Net Profit / Sales (%)	6.3	4.9	6.7
Operating Profit / Sales (%)	9.2	7.0	7.3

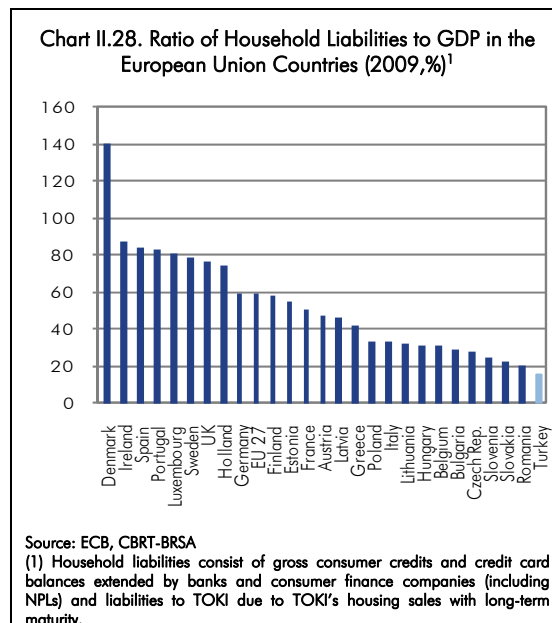
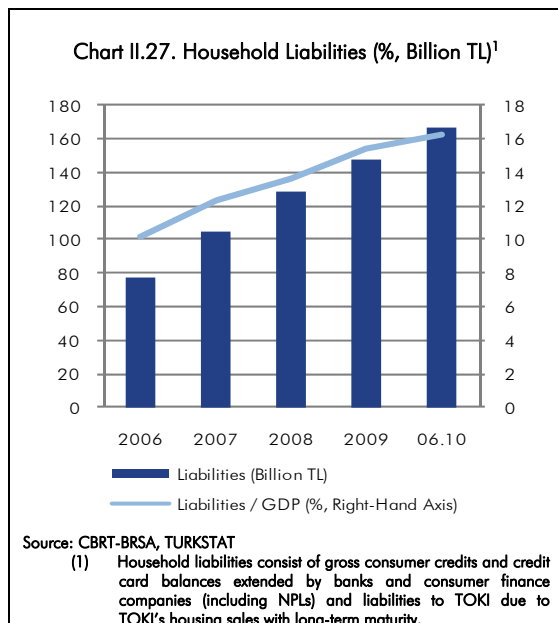
Source: PDP
(1) Consolidated data of 136 manufacturing industry firms quoted on the ISE.

The FX assets and liabilities of firms suggest that the FX net short position has increased and currency risk still remains important for them. The net short position of the corporate sector, which started to decrease after the global crisis, assumed an upward trend with the economic recovery. The FX short position that declined by 2.5 percent year-on-year in 2009 increased by 18.9 percent in September 2010 compared to end-2009 and reached USD 92.6 billion (Chart II.25). As of September 2010, the ratio of FX assets to FX liabilities went down by 3.7 points compared to end-2009 and declined to 46.6 percent (Chart II.26).



While household liabilities are on the rise, the debt service capacity does not display a negative outlook. On account of the improvement in consumer confidence owing to the decrease in interest rates and fading uncertainties, household indebtedness continued to rise. The ratio of household

liabilities to GDP, which was 15.4 percent in 2009, surged to 16.2 percent in the first half of 2010 (Chart II.27). However, when compared with selected EU countries, it is observed that the said ratio is low in Turkey (Chart II.28).



The fall in interest rates reduces the interest burden on households despite increased indebtedness. In response to the recovery in the labor market, the disposable income of households increased. Household borrowing costs declined on the back of the fall in interest rates on loans as a result of the decrease in policy rates and rising competition among banks. Thus, the ratio of household interest payments to disposable income, which had surged to 5.9 percent in 2009, declined to 4.8 percent in the first half of 2010 (Table II.2).

Table II.2. Household Disposable Income, Liabilities and Interest Payments^{1,2,3} (Million TL)

	2008	2009	09.10
Household Liabilities	128.966	147.083	177.314
Household Disposable Income	352.764	358.713	407.234
Household Interest Payments	19.653	21.114	19.697
Interest Payments / Household Disposable Income (%)	5,6	5,9	4,8
Liabilities/Household Disposable Income (%)	36,6	41,0	43,5

Source: BRSA-CBRT, TURKSTAT, SPO

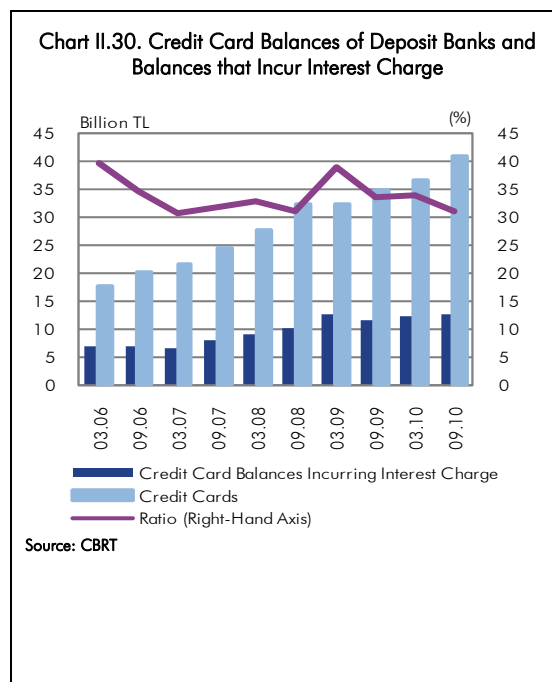
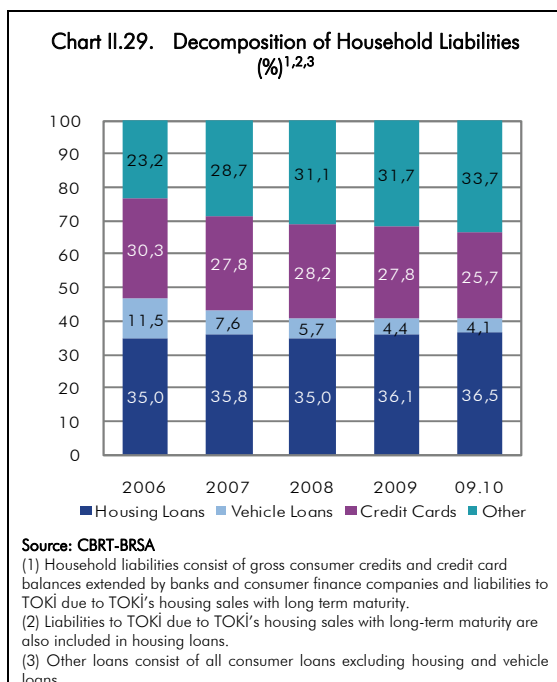
(1) Household liabilities consist of gross consumer credits and credit card balances extended by banks and consumer finance companies and liabilities to TOKI due to TOKI's housing sales with long-term maturity.

(2) As the repayments related to liabilities from TOKI's housing sales with long-term maturity are indexed to civil servant salaries, they are not included in interest payments.

(3) Household disposable income has been calculated by using the private sector disposable income estimation for 2009 and 2010 as mentioned in the 2011 Annual Program, assuming that the ratio of household disposable income for 2008, which was generated from the Income and Living Conditions Survey, to private sector disposable income has not changed. Since household disposable income generated from the Income and Living Conditions Survey has been utilized, the figures differ from those in the previous Financial Stability Reports.

While the share of housing and other loans within household liabilities has increased, that of vehicle loans and credit cards has decreased. When the development of household liabilities is analyzed by type, it is observed that other loans increased by 28.1 percent, housing loans went up by 21.7 percent, vehicle loans surged by 13.6 percent and credit card balances increased by 11.7 percent in September 2010 compared to end-2009 figures. As a result of these developments, while the shares of other consumer loans and housing loans within household liabilities increased, those of vehicle loans and credit cards decreased (Chart II.29). Although credit card balances continued to rise in 2010, the

ratio of credit card balances that incur interest charges to total credit card balances declined compared to end-2009 figures. (Chart II.30).



The number of consumer loan and credit card defaulters has decreased. According to the Central Bank Risk Center data, the number of consumer loan and credit card defaulters, which were 1,721,004 at end-2009, decreased to 1,688,567 by September 2010 (Table I.6).

Table II.3. Number of Credit Card and Consumer Loan Defaulters¹

	2008	2009	03.10	09.10
Banks	997.095	1.489.131	1.400.177	1.392.635
Asset Management Companies ²	139.862	330.156	430.197	443.866
Finance Companies	21.884	23.463	22.991	22.346
Total ³	1.093.47	1.721.004	1.690.726	1.688.567

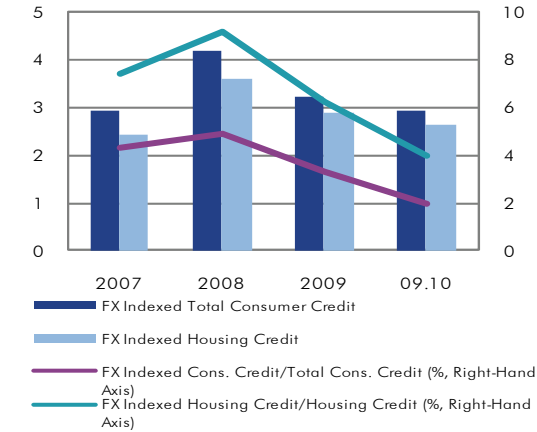
Source: CBRT

(1) Customers with more than one registry to a particular financial institution group are counted only once.

(2) Represents non-performing loans taken over by asset management companies from the SDIF and banks.

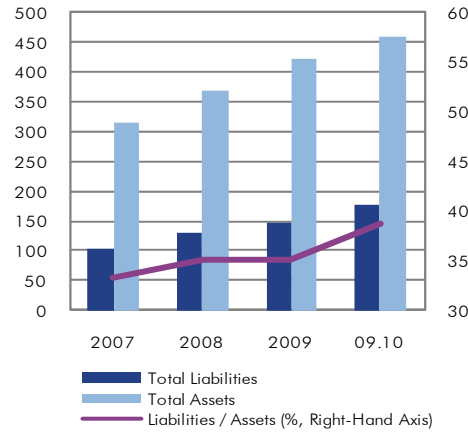
(3) As customers may have registry to more than one financial institution group, the sum of the three rows in the table and grand total are not equal.

Household liabilities do not bear interest rate and exchange rate risk. As opposed to many emerging market economies, primarily the Eastern Europe and Baltic countries, most of household liabilities in Turkey are denominated in local currency. Households in Turkey are not allowed to borrow in foreign currency and with the amendment to Decree No. 32 in June 2009; they are precluded from utilizing FX-indexed loans, as well. Thus, the ratio of FX-indexed consumer loans to total consumer loans, which was 4.9 percent in 2008, decreased to 3.3 percent at end-2009 and went down to 2 percent in September 2010 (Chart II. 31). Besides the low level of exchange rate risk they are exposed to, most of the loans granted to households do not bear interest rate risk, as they are fixed-rate loans.

Chart II.31. FX-Indexed Consumer Credits and FX-Indexed Housing Credits (Billion TL, %)¹

Source: BRSA-CBRT, SPK, CRA

(1) Consumer finance companies are not included.

Chart II.32. Household Financial Assets and Liabilities (Billion TL, %)¹

Source: BRSA-CBRT, CMB, CRA

(1) Household Assets = Savings Deposits + FX Deposits + Currency in Circulation + GDDS + Eurobonds + Stocks + Repos + Pension Funds + Mutual Funds (since December 2006). Household liabilities consist of gross consumer credits and credit card balances extended by banks and consumer finance companies and liabilities to TOKI due to TOKI's housing sales with long-term maturity.

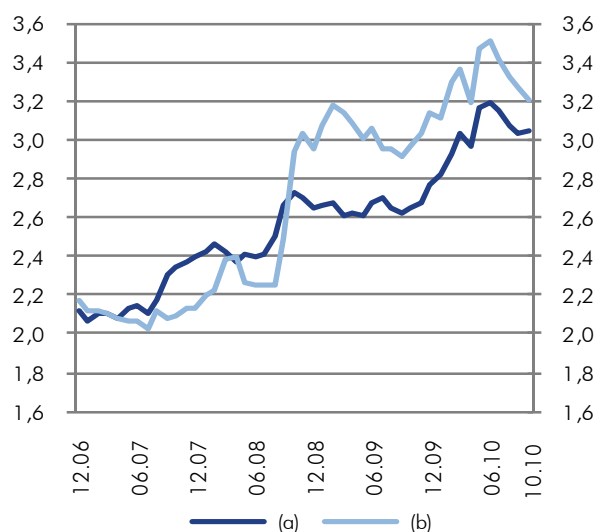
As household liabilities rose faster than assets, the ratio of liabilities to assets increased as well. The ratio of household liabilities to financial assets, which had declined slightly during the crisis, went up to reach 38.7 percent due to faster rising liabilities compared to assets in the first three quarters of 2010 (Chart II.32). The share of TL deposits, which constitutes the largest portion of household assets, went down in 2009, but resumed its 2008 levels in 2010. With the recent appreciation in Turkish lira against the US dollar and Euro, the share of FX deposit accounts in financial assets started to decline since 2008. Accordingly, the ratio of TL investment instruments to FX investment instruments increased compared to end-2009. Moreover, the share of government securities and Eurobonds decreased due to their low yields, while the share of equities and private pension funds increased (Table II.4 and Chart II.33). Particularly the increase in long-term pension funds is considered to be a positive development with regard to the financial system.

Table II.4. Composition of Household Financial Assets (Billion TL, %) ¹

	2008		2009		10.10	
	Billion TL	% Share	Billion TL	% Share	Billion TL	% Share
TL Deposits	188.1	51.3	209.6	49.9	236.5	51.1
FX Deposits	88.3	24.1	98.2	23.4	100.5	21.7
- FX Deposits (Billion USD)	58.6	-	65.2	-	70.3	-
Currency in Circulation	30.6	8.3	35.4	8.4	43.4	9.4
GDDS+Eurobond	19.7	5.4	14.1	3.3	10.1	2.2
Mutual Funds	20.8	5.7	26,1	6,2	27.2	5.9
Stocks	10.6	2.9	24.6	5.9	29.9	6.5
Private Pension Funds	6.3	1.7	9.0	2.1	11.5	2.5
Repos	2.2	0.6	2.3	0.5	3.1	0.7
Precious Metal Deposits	0.3	0.1	1.1	0.3	1.0	0.2
Total Assets	366.9	100.0	420.4	100.0	463.3	100.0

Source: BRSA-CBRT, CMB, CRA

(1) TL and FX deposits include participation funds.

Chart II. 33. Ratio of Household TL Investment Instruments to FX Investment Instruments ¹

Source BRSA-CBRT, CMB, CRA

(1) TL Instruments = Deposits + Repos + Gov.Dom.Debt.Sec. + Participation Funds (TL) + Stocks + Private Pension Funds + Mutual Funds (starting from April 2006); FX Instruments = FX Deposits + Gov.Dom.Debt.Sec. + Eurobond + Participation Funds (FX).
(a) Current TL value of FX deposits and Participation Funds (FX).
(b) For FX deposits and Participation Funds (FX), exchange rate prevailing on 29.12.2006 is used and the parity effect is eliminated.

It is much more important nowadays to ensure that financial services and tools that are becoming gradually more diverse and complicated are utilized according to their purpose, as well as to ensure that individuals are aware of their responsibilities and the risks that they take in this regard. In the aftermath of the financial crisis, work undertaken in the international arena in this field has gained pace. Within this context, it is of particular importance in terms of the CBRT's objective to support financial stability that priority is given to financial education for raising financial awareness, in cooperation with other related institutions and agencies. (Special Topic: IV.7).

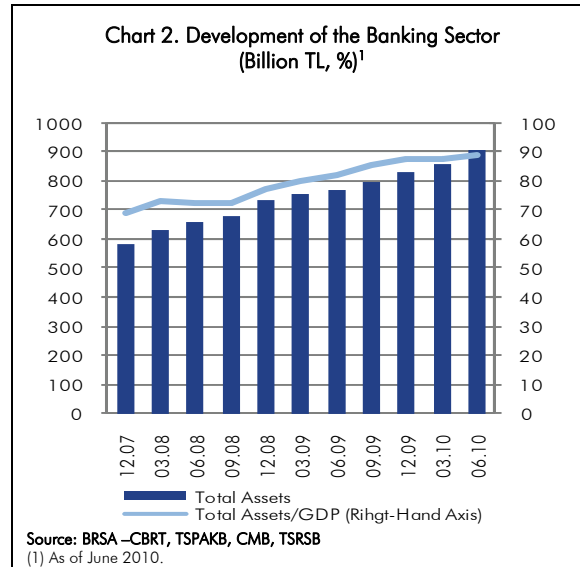
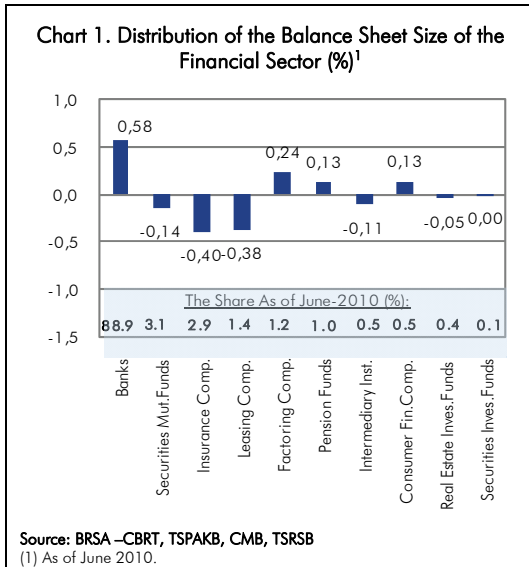
In the forthcoming period, continuing credit growth with increased pace on the back of strong capital inflows and the probable rise in the current account deficit stand as major threats to financial stability. Ample liquidity at global level stemming from expansionary monetary policies implemented by developed countries and relatively high yield lead to capital inflows to Turkey. The Turkish lira appreciates and market interest rates decline on the back of capital inflows, which, in turn, triggers the demand for consumption and investment. Additionally, differentiation in domestic and foreign demand becomes more apparent, the economy gains strength in response to domestic demand, household and corporate indebtedness increase and the current account deficit widens. Within this framework, the Central Bank will continue to use macroprudential policy instruments, primarily the required reserve ratios and liquidity management, effectively, in the upcoming period as well. On the other hand, strong public finance indicators, improvement in the profitability performance of firms, and the fact that the ratio of household liabilities to GDP is low compared to other countries and that they are Turkish lira-denominated increases the resilience of the Turkish economy against potential shocks.

Another risk factor is the deepening of public finance problems in developed countries particularly in EU countries and/or potential change in the tendency of capital inflows due to ceasing

the implementation of expansionary monetary policies by developed countries. Deepening of public finance problems in the EU –if it occurs- might directly affect the Turkish economy through credit and investment channels as well as through foreign trade channel since the EU is our most significant trade partner. A potential change in the trend of capital inflows will affect Turkey as well as other emerging economies.

GENERAL STRUCTURE OF THE FINANCIAL SYSTEM

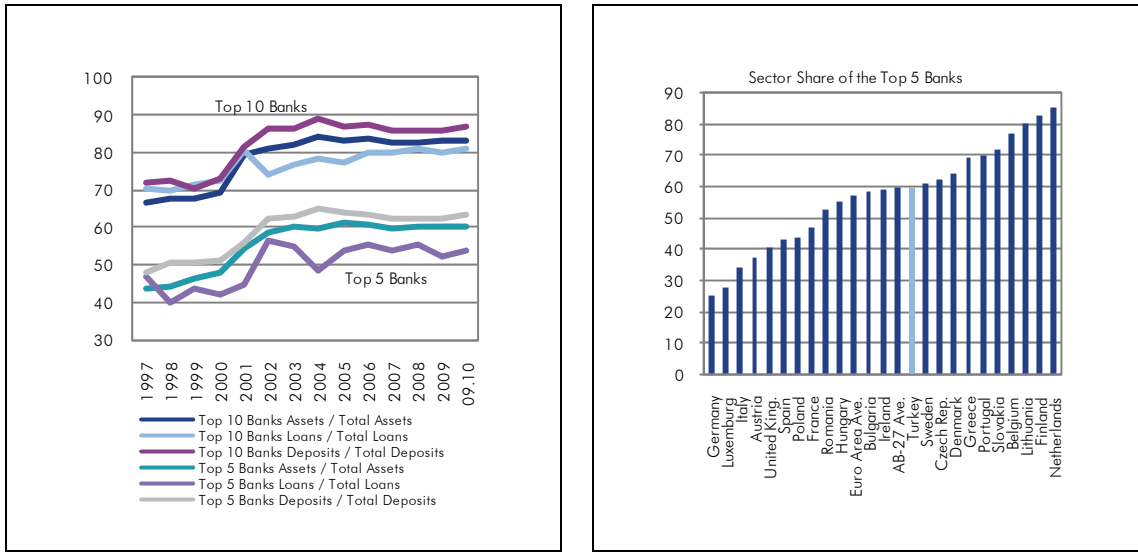
The Turkish financial sector, mostly composed of the banking sector, has followed a sound growth path. The balance sheet of our financial sector, which continued to grow in 2010 as well, grew by 17.3 percent annually to reach TL 1,022 billion in June 2010 and its ratio to GDP became 100 percent. The share of banks, which accounts for 88.8 percent of sector assets, rose by 0.7 percent, while the shares of factoring companies and pension funds increased by 0.2 percent and 0.1 percent, respectively, compared to the same period of the previous year (Chart 1). The total asset size of the banking sector, which weighs the most in the financial sector, rose by 11.2 percent in nominal terms and by 6.1 percent in real terms, to reach TL 927 billion in September 2010, compared to end-2009. Whereas, in terms of US dollar, it reached 642.5 billion with an increase of 14.6 percent. The ratio of the banking sector's total assets to GDP rose from 87.6 percent at end-2009 to 88.6 percent in the second quarter of 2010 (Chart 2).



Among the 49 banks operating in the Turkish banking sector as of September 2010, the share of the first 5 banks depending on asset size is 60.2 percent, while the share of the first 10 banks is 83.5 percent. While concentration is seen more on deposits, it is lower on credits.

In 2009, the level of concentration of the first 5 banks in Turkey was on a par with the EU average (EU-27), at 60 percent, and was also listed in the middle ranks among selected EU countries (Chart 3).

Chart 3. Concentration of the Turkish Banking Sector and a Comparison with Selected EU Countries (%)¹

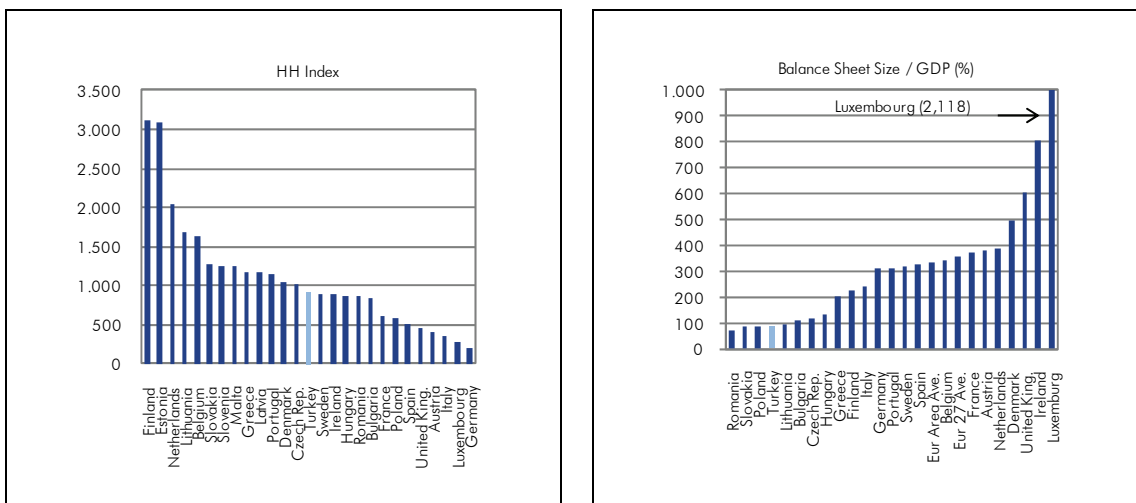


Source: BRSA, CBRT, ECB Report – 2010
(1) Data as of 2009.

The Turkish banking sector’s level of concentration displays a similar view in comparison with another concentration indicator, the Herfindahl-Hirschman Index (HHI)⁴. In fact, the concentration of the Turkish banking system ranks around the middle when compared to EU countries; outpaces that of developed countries and falls behind that of most of the emerging market economies (Chart 3). The said index, which stood at 632 for EU-27 and at 633 for the euro area average as of 2009, in Turkey rose from 886 in 2008 to 913 in 2009.

The share of the balance sheet size of the Turkish banking sector in GDP, which was 87.6 percent at end-2009, is larger than that of Poland, Slovakia and Romania, whereas smaller than that of other EU countries. This is an indicator of the high growth potential of the Turkish banking sector (Chart 4).

Chart 4. Comparison Between The Ratio of HHI Value and Balance Sheet Size of the Turkish Banking Sector to GDP with The Same Ratio in Selected EU Countries (%)¹



Source: TurkStat, BRSA, CBRT, ECB Report – 2010
(1) Data as of 2009.

⁴ HHI, is defined as the sum of the squares of the market shares of financial institutions operating in a market and used as a measure of the amount of competition in that market. A rise in the index shows an increase in concentration. An index ranging from 1000 to 1800 indicates that there is a moderate concentration in the sector, whereas a value above 1800 points to a high level of concentration.