

# **CENTRAL BANK OF THE REPUBLIC OF TURKEY**

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## **BALANCE OF PAYMENTS REPORT**

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**2006 -II**

## SUMMARY

From the second half of 2005 onwards, export growth slowed down, whereas import growth gained pace. The said tendency continued in the first half of 2006 as well. During this period, annual increases in exports and imports were realized as 10.1 percent and 17.8 percent, respectively. Hence, the foreign trade deficit, which was USD 14.7 billion in period January-June 2005, reached USD 20.1 billion within the framework of the balance of payments definition in the same period of 2006. The decline in tourism revenues during the said period had an increasing effect on the current account deficit.

Exports of the textile and clothing sector, which constitute the largest share in overall exports, had displayed low performance since the last quarter of 2005, but boosted in May and June. However, export growth of these sectors remained below overall export growth. In the first half of the year, the largest contribution to overall exports came from exports of motor vehicles, which increased by 14.5 percent, displaying growth above the overall export performance. Exports of coking coal, refined petroleum products and nuclear fuels rose by 43.8 percent owing to high prices in the first half of the year. In the meantime, exports of machinery-equipment, which had significantly increased in 2005, maintained its growth during the January-June 2006 period, thus the rise in exports of the sector became 18.1 percent.

Imports of capital and consumption goods, which sustained their high-rated increases as of August 2005, rose by 13.0 percent and 31.1 percent, respectively, in the first half of 2006. On the other hand, imports of intermediate goods grew by 17.9 percent in the January-June period. Intermediate goods including crude oil and natural gas made the highest contribution to overall import growth owing to price increases.

Starting from the last quarter of 2005, the contribution of export prices to nominal exports lost pace. The exports unit value index, which declined by 0.9 percent in the first quarter of 2006, increased by 3.7 percent in the second quarter of the year. Meanwhile, import prices rose by 5.1 percent in the first half of 2006. The increase in import prices mainly resulted from the 37.5 percent rise in prices of the mining and quarrying sector that includes crude oil and natural gas. Moreover, import prices in the manufacturing industry, which declined in the first quarter of the year, rose by 4.1 percent during the April-June period. Adjusted for price effects, annual increases in imports and exports during the January-June period realized as 5.3 percent and 10.2 percent, respectively.

Excluding IMF loans and changes in official reserves (CBT + banks), capital inflows became USD 28.3 billion in the first half of 2006. In this period, direct investments and long-term credits and trade credits used by the private sector and banks became the primary determinants of the financing structure. Also in the said period, net long-term and short-term capital inflows, excluding portfolio, direct investments and IMF loans, were realized as USD 16 and USD 0.9 billion, respectively. In addition, net errors and omissions was positive, amounting to USD 0.2 billion.

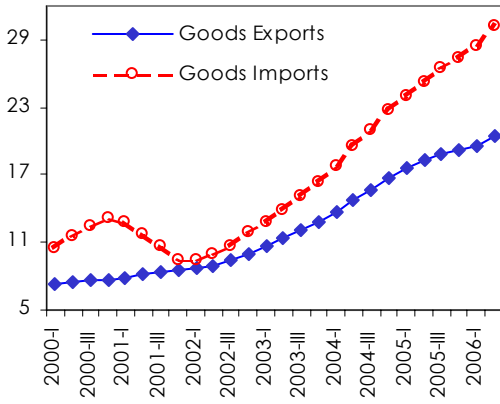
As a result of these developments, Central Bank reserves and banks' reserves increased by USD 4.1 billion and USD 2.2 billion, respectively, in the first half of 2006.

**Balance of Payments**  
(billion, USD)

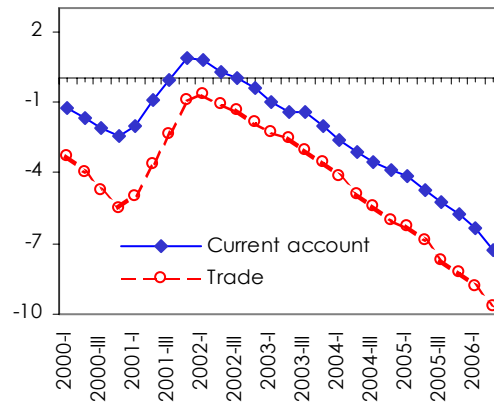
	Jan-Jun			Jan-Jun (12-month)		
	2005	2006	% change	2005	2006	% change
Current Account	-13.2	-18.7	..	-18.1	-28.6	..
Goods	-14.8	-19.9	..	-25.4	-38.1	..
Exports	37.0	41.8	13.0	67.3	81.8	21.5
Exports (fob)	35.4	39.5	11.5	63.9	77.6	21.4
Shuttle trade	1.7	2.4	43.9	3.4	4.2	24.7
Imports	-51.8	-61.8	19.2	-92.7	-119.8	29.3
Imports (cif)	-55.1	-65.2	18.3	-98.6	-126.9	28.7
Coverage adjustment	3.3	3.4	..	5.9	7.0	..
Services	4.0	3.6	..	11.5	13.6	..
Tourism (net)	4.4	4.4	-0.4	12.1	15.3	25.9
Credit	5.8	5.7	-1.0	14.5	18.1	24.7
Debit	-1.4	-1.3	-3.1	-2.4	-2.8	18.8
Other services revenues (net)	-0.4	-0.8	..	-0.7	-1.6	..
Income	-3.0	-3.0	..	-5.3	-5.6	..
Direct investment income (net)	-0.5	-0.5	..	-0.8	-0.7	..
Portfolio investment income (net)	-0.5	-0.4	..	-0.8	-0.8	..
Other investment income (net)	-1.9	-2.1	..	-3.8	-4.1	..
Interest income	0.4	0.6	61.4	0.7	1.2	74.8
Interest expenditure	-2.3	-2.7	15.8	-4.5	-5.4	20.5
Current transfers	0.6	0.7	..	1.1	1.5	..
Workers remittances	0.4	0.5	43.2	0.7	1.0	40.9
Capital and financial account	10.0	18.4	..	12.9	29.4	..
Financial account (excl. reserve assets)	16.6	22.5	..	20.8	44.7	..
Direct investment (net)	0.8	8.8	..	1.4	16.8	..
Abroad	-0.4	0.0	..	-0.8	-0.7	..
In Turkey	1.2	8.8	..	2.2	17.4	..
Portfolio investment (net)	6.9	-1.0	..	10.9	5.6	..
Assets	-1.0	-0.4	..	-2.6	-0.6	..
Liabilities	7.9	-0.5	..	13.5	6.2	..
Equity securities	2.8	1.0	..	3.7	3.8	..
Debt securities	5.1	-1.5	..	9.8	2.4	..
Non-residents' buyings in Turkey	3.4	-3.2	..	6.5	-0.7	..
Eurobond issues of Treasury	2.0	1.7	..	3.7	3.1	..
Borrowing	4.5	2.4	..	6.8	4.3	..
Repayment	-2.6	-0.7	..	-3.1	-1.2	..
Other investments (net)	9.0	14.7	..	8.5	22.3	..
Assets	1.6	-3.0	..	-3.1	-4.3	..
Trade credits	1.0	-0.4	..	0.6	-1.1	..
Credits	-0.1	-0.4	..	0.0	-0.1	..
Banks FX assets (- increase)	0.7	-2.2	..	-3.6	-3.2	..
Liabilities	7.4	17.7	..	11.6	26.7	..
Trade credits	2.0	2.4	..	3.4	3.9	..
Credits	4.7	13.4	..	7.3	20.7	..
Central Bank	-2.0	0.0	..	-4.0	-0.9	..
General Government	-1.6	-4.0	..	-1.9	-7.1	..
IMF	-0.6	-3.6	..	0.0	-5.5	..
Long-term	-1.0	-0.4	..	-1.9	-1.5	..
Banks	4.8	5.4	..	8.3	9.9	..
Long-term	3.9	4.6	..	5.6	7.2	..
Short-term	0.9	0.9	..	2.7	2.7	..
Other sectors	3.4	12.0	..	4.9	18.9	..
Long-term	3.1	11.8	..	4.5	18.6	..
Short-term	0.3	0.2	..	0.4	0.3	..
Deposits of non-residents	0.6	1.8	..	0.7	1.7	..
In CBT	-0.3	-0.5	..	-0.5	-1.0	..
In banks	0.9	2.3	..	1.2	2.7	..
Change in official reserves (- increase)	-6.7	-4.1	..	-7.9	-15.3	..
Net errors and omissions	3.2	0.2	..	5.2	-0.8	..

Source: CBT.

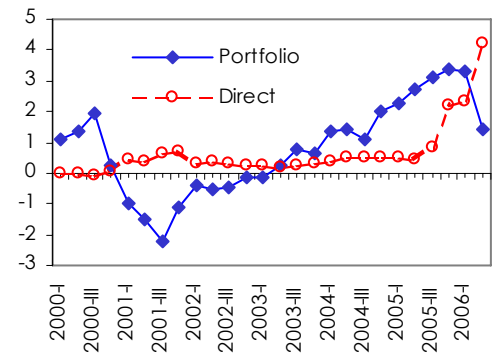
**Goods Exports and Imports**  
(12-month ave., billion US dollars)



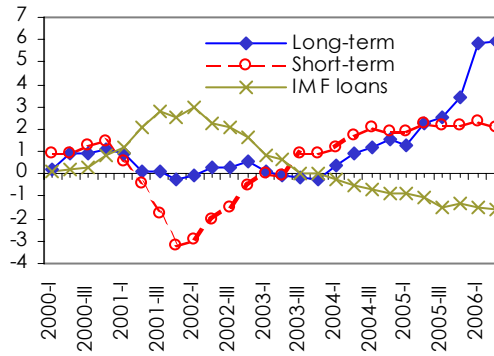
**Trade and Current Account**  
(12-month ave., billion US dollars)



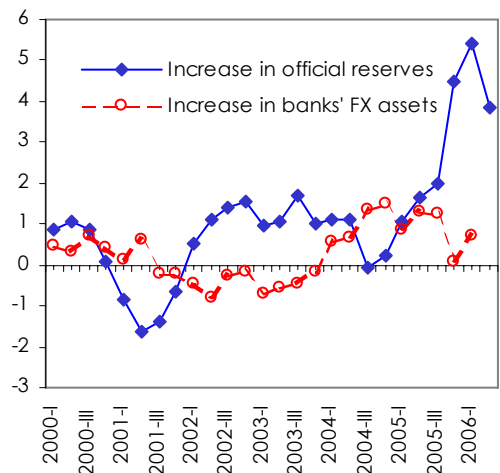
**Direct and Portfolio Investments**  
(12-month ave., billion US dollars)



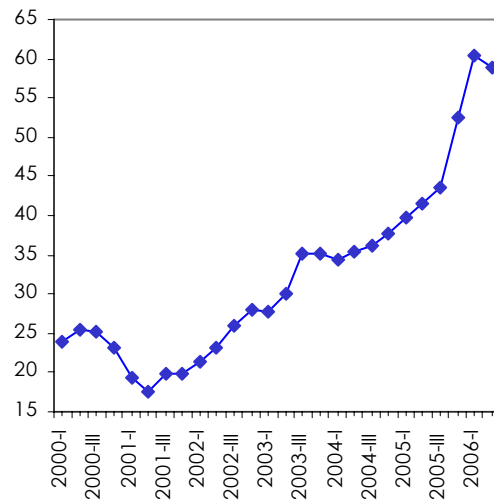
**Term Structure of Capital Flows**  
(12-month ave., billion US dollars)



**Reserves**  
(12-month ave., billion US dollars)



**CBT International Reserves**  
(billion US dollars)



Source: CBT, TURKSTAT.

## I. EXTERNAL ECONOMIC DEVELOPMENTS

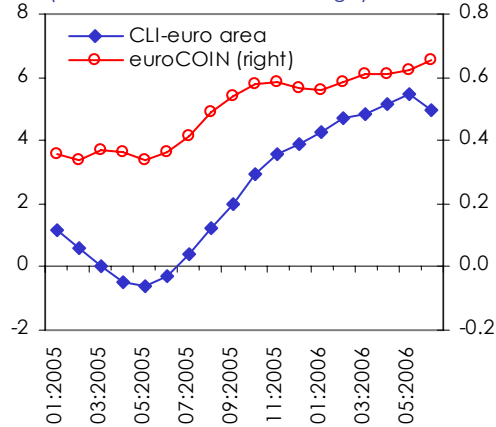
1. Despite natural disasters and high oil prices, the world economy continued to grow at high rates in 2005. While China continued to become the main determinant of the ongoing strong growth tendency of the world economy in the first half of 2006, a slowdown was observed, in the USA in the second quarter.

2. Uncertainties about oil prices and international liquidity conditions, and global instabilities are the leading risks for the growth of the world economy throughout 2006. Geopolitical uncertainties, the political tension in the Middle East and increasing production uncertainties arising from technical problems experienced in Alaska oil drilling zone led to historical record levels of increase in crude oil prices in August. In the meantime, although there are doubts about their pace, interest rate hikes in the USA, EU and Japan are expected to continue. The impact of the said situation on capital inflows to emerging markets still preserves its uncertainty.

### Euro Area Leading indicators:

€COIN (3-month % change),

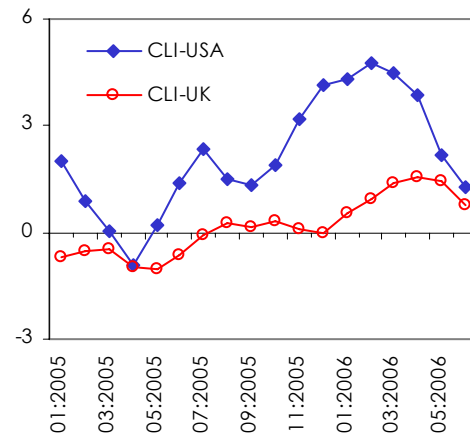
CLI (annualized 6-month % change)



Source: OECD, CEPR.

### USA and UK Leading indicators:

CLI (annualized 6-month % change)



Source: OECD.

3. The US economy, which maintained its rapid growth performance in the first quarter of 2006, lost pace in the second quarter of the year and declined by 2.9 percent on an annual basis in the second quarter. The loss of pace in US economic growth reflects the lagged effects of interest rates and the rise in energy prices as well as the impact of the gradual cooling in the housing market. The core inflation rate in the US economy displays increases in recent months. It is predicted that though increased energy and commodity prices are expected to continue to exert pressure on inflation, curbing of inflation expectations combined with sluggish demand will limit the said inflationary pressures. At its meeting of August 8th 2006, The Federal Reserve Bank (FED) decided to keep interest rates at 5.25 percent and stated that further decisions on interest rates would be formed in view of the indicators relating to inflation and growth.

4. The Euro zone GDP, which had increased by 2 percent on an annual basis in the first quarter of 2006, rose by 2.4 percent on an annual basis in the second quarter of the year, displaying a strong performance above expectations. Growth is expected to follow a horizontal course for the rest of year. Nevertheless, the ongoing oil price increases and the change in the course of global capital movements come to the forefront as risk elements that will slow down the growth process. Despite the strengthening of the possibility of further interest rate hikes by the ECB against increasing inflationary risks, strong growth is expected to continue throughout 2006. Besides, the July data of the ECOIN index, which is the leading indicator of the Euro zone related to economic activity, also points to the ongoing favorable outlook.

5. The Japanese economy, which had experienced high growth in 2005, which is 2.6 percent, displayed a growth performance beyond expectations in the first quarter of 2006 with 3.6 percent growth in annual terms. However, in the second quarter of 2006 growth lost pace and increased by 2 percent in annual terms. It is also observed that the slow-down in growth mainly stemmed from the decline in public investment and consumption expenditures and that growth was realized in line with the domestic demand. The Japanese economy is expected to maintain its current course in the rest of 2006. Meanwhile, the Chinese economy also maintained its strong growth in 2006. It is observed that the high growth - which was realized as 10.2 percent in the first quarter of the year compared to the same period of the previous year, and 11.3 percent above expectations in the second quarter of the year - stems from the rapid increase in fixed investments and industrial production.

6. These developments are believed to point to a strong foreign demand that will support Turkey's exports throughout 2006.

## II. CURRENT ACCOUNT

7. As of March 2006, the current account reached 6.9 percent of the GNP in annual terms. The upward trend in the current account deficit continued in the first half of 2006 and the current account registered a deficit of USD 18.7 billion.

8. In the first quarter of the year, imports maintained an upward trend, while exports displayed poor performance. In the second quarter, both imports and exports gained momentum. Thus, in the January-June period, the ratio of exports to imports and to short-term foreign debt stock fell to 0.68 and 1.97, respectively. The ratio of reserves; the indicators that are based on the Central Bank reserves; to short-term foreign debt stock and to the imports increased compared to 2005, while the ratio of reserves to current account deficit and to the financing requirement, made up of the current account deficit plus the net errors and omissions item, decreased.

### Selected indicators related to the current account deficit and financing structure

	2000	2001	2002	2003	2004	2005	2006*
Exports / Imports	0.58	0.90	0.85	0.79	0.74	0.70	0.68
Exports / Short-Term External Debt	1.09	2.10	2.44	2.23	2.06	2.01	1.97
Exports / External Debt Service	1.40	1.40	1.39	1.84	2.20	2.11	2.32
Tourism Revenues / Trade Balance	0.35	2.17	1.16	0.94	0.67	0.55	0.47
CBT Reserves / Short-Term External Debt	0.82	1.21	1.71	1.53	1.16	1.37	1.43
CBT Reserves / Financing Requirement	1.84	-	19.97	11.71	2.82	2.54	2.17
CBT Reserves / Current Account Balance	2.36	-	18.42	4.38	2.41	2.27	2.05
CBT Reserves / Imports	0.44	0.52	0.59	0.54	0.41	0.48	0.49

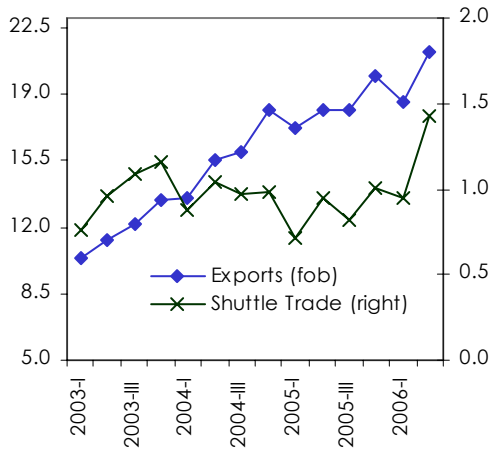
Source: CBRT, TURKSTAT.

\* 12-month data as of June.

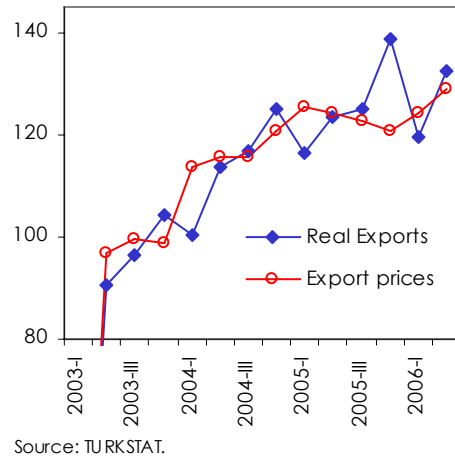
### Exports of Goods

9. According to exports data issued by TURKSTAT (Turkish Statistical Institute), exports (FOB) growth that was 7.4 percent in the first quarter of 2006, became 15.5 percent in the second quarter of the year. Hence, exports (fob) increased by 11.5 percent in the January-June period. In the same period, the growth rate of the total exports of goods became 13 percent as a result of the 43.9 percent rise in revenues from shuttle trade. Meanwhile, exports prices, which decreased in the first quarter of 2006, increased in the second quarter and contributed to the nominal export growth. According to index data issued by TURKSTAT, the exports unit value index rose by 1.4 percent in the January-June period of 2006 compared to the same period of the previous year. When adjusted according to the price effect, the real increase in exports was 5.1 percent in the said period.

**Exports**  
(billion US dollars)

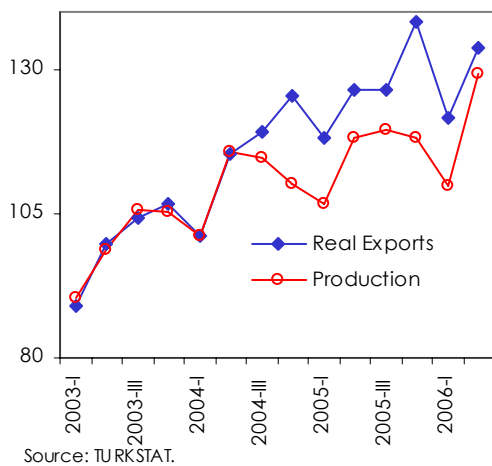


**Exports - Real and Unit Value**  
(2003=100)

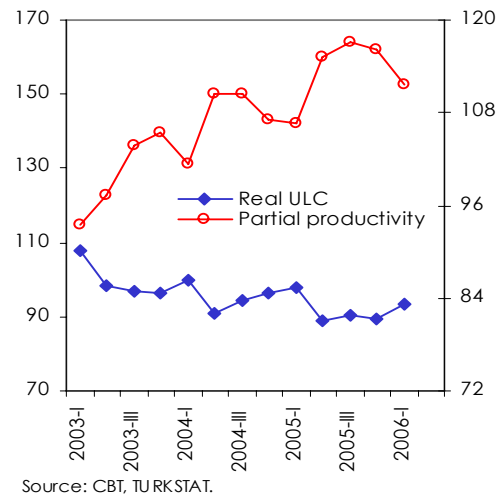


10. Increases in productivity has been one of the main determinants of the boost in exports, by means of reducing the real unit labor costs to give way to the external competitive advantage offsetting the unfavorable impact of the strong position of the New Turkish lira (YTL) on external competitiveness. Besides, as a result of the fluctuations observed in financial markets in May, the depreciation of the YTL and strong foreign demand are expected to contribute to the increase in exports in the upcoming period, especially in labor-intensive sectors.

**Production and Exports in Manufacturing Industry (2003=100)**



**Real ULC and Productivity Indices (2003=100)**



11. Analyzing export developments by sub-items, it is observed that the exports of the textile and clothing sectors that had displayed low performance since the last quarter of 2005 increased in May and June even though the increase in exports of these sectors still remained below the total growth in exports. In the first half of the year, the biggest contribution to total exports sourced from the motor vehicles sector. In this period, the said sector displayed growth beyond the total exports performance, with a 14.5 percent increase. Exports of coke coal, refined petroleum products and nuclear fuel rose by 43.8 percent in the first half of the year due to high price increases and contributed to the total growth in exports by 1.4 points. After the decline in 2005, exports of the basic metal industry increased by 13.4 percent in the January-June period of 2006. In the said period, exports of machinery-equipment and electrical machinery and appliances continued to grow in a stable manner, increasing by

18.1 percent and 25.1 percent, respectively and contributed to the growth in exports by 1.8 points.

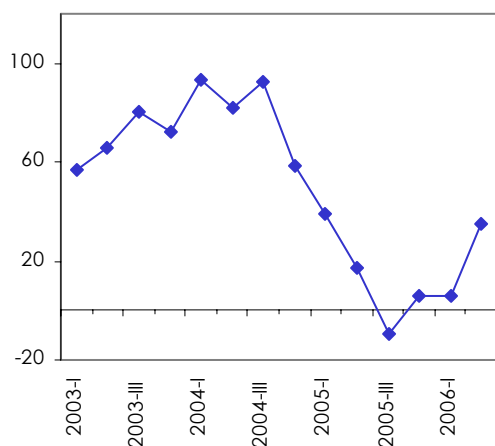
**Exports**  
(million US dollar)

	January-June				
	2004	2005	% Change	% Contrib.	\$ Contrib.
<b>Total</b>	<b>35385</b>	<b>39461</b>	<b>11.5</b>		
Capital Goods	4074	4375	7.4	0.8	300
Intermediate Goods	14881	17231	15.8	6.6	2350
Consumption Goods	16302	17525	7.5	3.5	1223
Other	128	331	159.0	0.6	203
<b>Selected Items (ISIC Rev.3):</b>					
Agriculture and farming of animals	1327	1619	22.0	0.8	292
Food products and beverages	1927	2014	4.5	0.2	87
Textiles	4080	4189	2.7	0.3	109
Wearing apparel	5068	4932	-2.7	-0.4	-137
Petroleum products and nuclear fuel	1116	1604	43.8	1.4	488
Chemicals and chemical products	1367	1605	17.5	0.7	239
Rubber and plastic products	1181	1344	13.8	0.5	163
Other non-metallic minerals	1314	1326	0.9	0.0	11
Manufacture of basic metals	3629	4115	13.4	1.4	486
Manufacture of fabricated metal prod(exc machinery)	1262	1441	14.2	0.5	179
Manufacture of machinery and equipment	2256	2664	18.1	1.2	408
Electrical machinery and apparatus	935	1170	25.1	0.7	235
Communication and apparatus	1326	1498	13.0	0.5	172
Motor vehicles and trailers	5321	6095	14.5	2.2	774
Other transport	794	1145	44.2	1.0	351

Source: TURKSTAT.

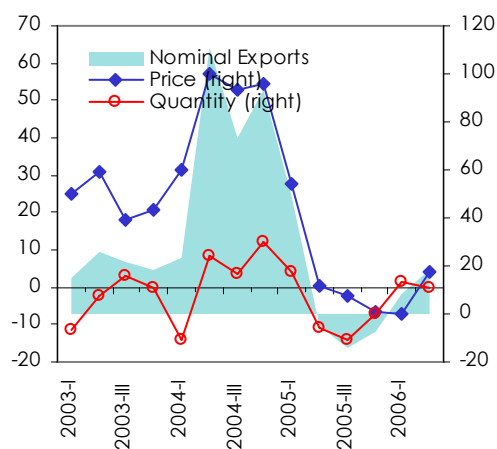
12. Exports of motor vehicles, which displayed poor performance in the January-March period of 2006, once again increased at high rates in the second quarter of 2006. The start of the production of new products in the sector is believed to be effective on the said increase. Automobile exports increased by 21.6 percent in the January-June period. Despite the 43.7 percent increase in automobile imports during this period, net export position of the sector was also sustained in this period.

**Automobile Exports**  
(Annual percentage change)



Source: TURKSTAT.

**Basic Metal Industry Exports**  
(Annual percentage change)



Source: TURKSTAT.

13. Textile and clothing exports that displayed a low performance in exports throughout 2005 and dropped by 4.1 percent in annual terms in the January-April period of 2006,



increased by 7.6 percent in the May-June period. The difficulty in competing with countries like China and India, which especially dominate the US market in terms of exports of textiles and clothing owing to their low labor costs, was the main factor leading to loss of performance in the sector. On the other hand, high quality and geographical closeness to Europe continue to be advantageous to textile and clothing exports to EU countries. In addition, the sector's access to new markets had a favorable impact on its latest performance.

**Exports – Unit Value Indices (2003=100)**  
Annual Percentage Change

	2005	2006 I	2006 II
Total	5.7	-0.9	3.7
Capital Goods	1.5	-3.0	4.6
Intermediate Goods	6.9	-1.5	6.0
Consumption Goods	6.3	-0.7	1.0
Selected Items (ISIC Rev.3):			
Agriculture and farming of animals	27.8	-0.8	-13.9
Food products and beverages	9.8	1.7	-0.3
Textiles	4.6	-3.1	1.0
Wearing apparel	4.7	1.8	1.8
Petroleum products and nuclear fuel	25.0	24.7	28.7
Chemicals and chemical products	7.7	-0.3	3.3
Rubber and plastic products	7.7	0.0	4.4
Other non-metallic minerals	9.6	7.4	6.4
Manufacture of basic metals	2.3	-7.3	4.1
Manufacture of fabricated metal prod(exc machir	11.7	2.6	9.2
Manufacture of machinery and equipment	4.7	-1.8	1.1
Electrical machinery and apparatus	10.2	10.6	19.5
Communication and apparatus	-18.3	-16.8	-9.4
Motor vehicles and trailers	1.9	-4.8	5.1

Source: TURKSTAT.

**Exports – Quantity Indices (2003=100)**  
Annual Percentage Change

	2005	2006 I	2006 II
Total	10.5	2.9	7.2
Capital Goods	-3.7	11.1	0.0
Intermediate Goods	10.6	7.1	8.3
Consumption Goods	7.9	-0.9	5.4
Selected Items (ISIC Rev.3):			
Agriculture and farming of animals	3.3	9.7	43.0
Food products and beverages	16.8	-4.8	-3.4
Textiles	4.1	0.0	-0.6
Wearing apparel	1.7	-11.1	-6.4
Petroleum products and nuclear fuel	53.7	-14.4	14.8
Chemicals and chemical products	4.5	6.5	13.7
Rubber and plastic products	18.1	13.0	3.5
Other non-metallic minerals	6.1	-12.2	-8.1
Manufacture of basic metals	-0.1	13.2	10.5
Manufacture of fabricated metal prod(exc machi	9.4	7.2	0.5
Manufacture of machinery and equipment	18.7	15.8	14.0
Electrical machinery and apparatus	11.4	2.4	5.0
Communication and apparatus	33.9	35.3	23.8
Motor vehicles and trailers	13.5	5.1	18.0

Source: TURKSTAT.

14. The decline that had been observed in exports of the basic metal industry since the second quarter of 2005 came to a halt in 2006, and the sector's exports rose by 13.4 percent in the first half of the year. In the second quarter of the year, the rise in basic metal industry prices contributed to nominal exports.

15. The exports unit value index, which fell by 0.9 percent in annual terms in the first quarter of 2006, rose by 3.7 percent in the second quarter. As exports prices recorded increases in sectors such as refined petroleum products, electrical machinery and appliances and clothing, they went down in sectors such as the basic metal industry, radio, TV, communication equipment and apparatus, and textiles.

**Exports – Country Decomposition**  
(million US dollar)

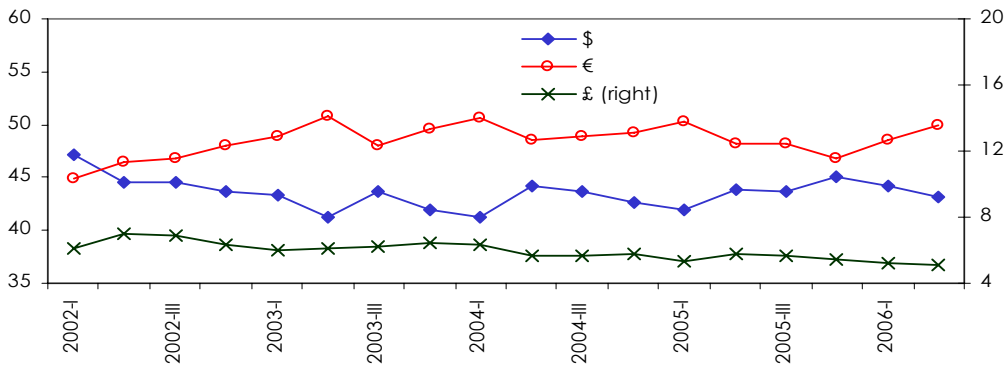
	January-June						
	2005		2006		% Change	% Contrib.	\$ Contrib.
	Value	Share (%)	Value	Share (%)			
Total	35385	..	39461	..	11.5		
EU countries	18564	52.5	20908	53.0	12.6	6.6	2344
EU 15	17420	49.2	19507	49.4	12.0	5.9	2087
EU 10	1144	3.2	1401	3.5	22.5	0.7	257
Other countries	15353	43.4	17122	43.4	11.5	5.0	1769
Other European	4020	11.4	5013	12.7	24.7	2.8	992
East Asian	1433	4.0	1747	4.4	22.0	0.9	315
Other	9900	28.0	10362	26.3	4.7	1.3	462
Free Zones in Turkey	1468	4.1	1431	3.6	-2.5	-0.1	-37
Selected countries and country groups							
OECD	21,445	60.6	24,117	61.1	12.5	7.6	2672
Germany	4,563	12.9	4,607	11.7	1.0	0.1	44
UK	2,795	7.9	3,143	8.0	12.4	1.0	348
USA	2,362	6.7	2,562	6.5	8.5	0.6	200
Italy	2,633	7.4	3,387	8.6	28.6	2.1	753
France	1,921	5.4	2,324	5.9	21.0	1.1	403
Spain	1,441	4.1	1,756	4.5	21.9	0.9	315
Netherlands	1,285	3.6	1,161	2.9	-9.6	-0.3	-123
Other OECD	4,445	12.6	5,178	13.1	16.5	2.1	732
Middle East countries	4,957	14.0	4,957	12.6	0.0	0.0	0
Russian Fed.	1,042	2.9	1,323	3.4	27.0	0.8	281

Source: TURKSTAT.

16. Analyzing exports by country groups, it is observed that growth in exports to EU countries, which comprises the largest share in total exports, displayed a remarkable increase in the second quarter of the year. The revival observed in the domestic demand and economic activities of EU countries was effective in this development. In the first six months of the year, exports to the said country group including France, Spain, Italy and the United Kingdom increased at high rates, while exports to Germany, the biggest trade partner, increased only by 1 percent. Similarly, it is observed that exports to Middle Eastern countries remained at the level of the previous year and their share in total exports dropped.

17. In terms of the currency composition of exports, the share of the euro increased in the first half of 2006 in line with the increase in exports to EU countries. The share of Euro with 48.3 percent in 2005, rose to 49.2 in the January-June 2006 period. Moreover, a decline was observed in the share of US dollar and Sterling in the same period.

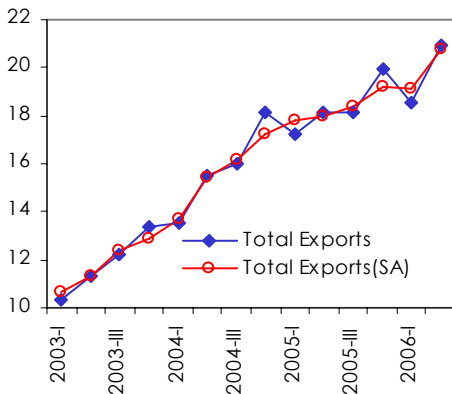
**Currency Composition of Exports**  
(% share)



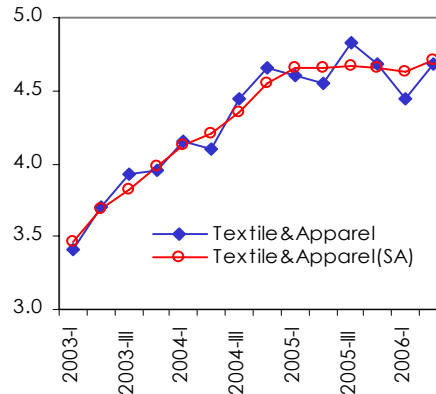
Source: TURKSTAT.

18. Seasonally adjusted (SA) data also support the increase in exports in the second quarter. According to SA data, US dollar-denominated nominal exports increased by 8.7 percent in the second quarter of 2006 compared to the previous quarter. Seasonally adjusted nominal exports of the textile and clothing sector – one of the leading export sectors – remained below the general exports performance and rose by 1.9 percent compared to the previous period, while the seasonally adjusted nominal exports of motor vehicles and machinery-equipment rose by 14.6 percent and 7 percent, respectively.

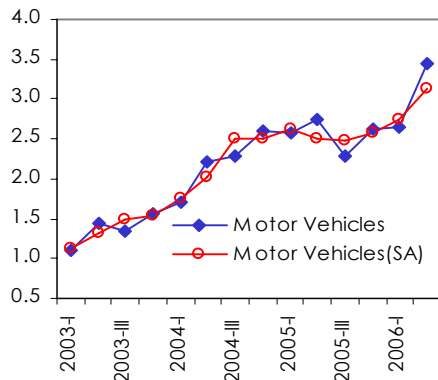
**Total Exports**  
(billion US dollar)



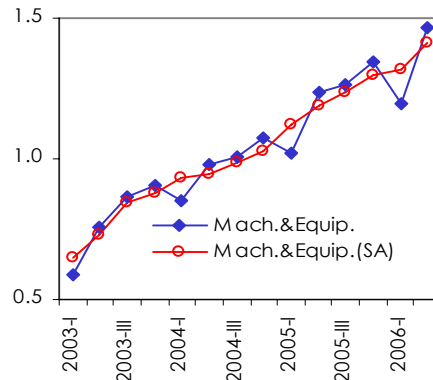
**Textile&Apparel Exports**  
(billion US dollar)



**Motor Vehicles**  
(billion US dollar)



**Machinery&Equipment Exports**  
(billion US dollar)



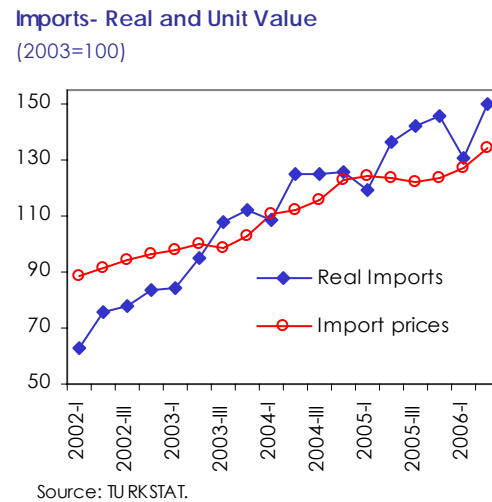
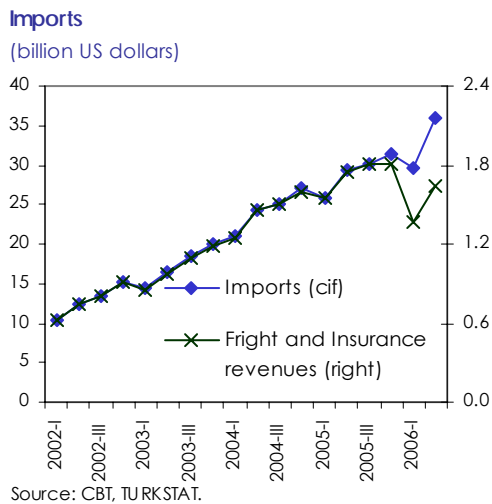
Source: TURKSTAT, CBRT.  
SA: Seasonally adjusted.

19. Data announced by the Turkish Exporters Assembly (TEA) in July 2006 show that the increasing trend of exports continued and that exports rose by 22.4 percent compared to the same month of last year, thus exports increased by 14.2 percent in the January-July period. According to TEA data, exports of motor vehicles, electrics-electronics and machinery-equipment increased remarkably in July, continuing to make the largest contribution to total exports. Meanwhile, growth in textile and clothing exports remained at 3.8 percent.

20. Indicators in the April Business Tendency Survey for exports in the upcoming period show that in the next quarter orders to be received from the exports market and growth in the volume of goods sold to foreign markets will continue to increase.

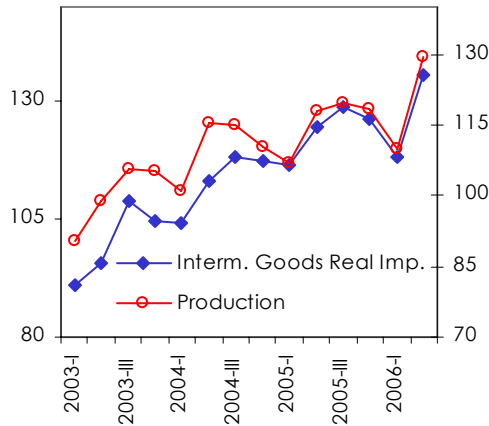
### Imports of Goods

21. Imports, (including freight and insurance costs), increased by 20.9 percent in the first quarter of 2006. With the addition of the "other goods" item related to freight and insurance revenues and financial leasing, the rate of growth for the total imports of goods amounts to 21.1 percent. In the first three-month period of 2006, the effects of price movements started to decline and in the second three-month period prices of imports rose by 8.3 percent. According to the quantity index excluding price movements, the real increase in imports in the first and second quarter of the year were 10 percent and 10.3 percent, respectively.



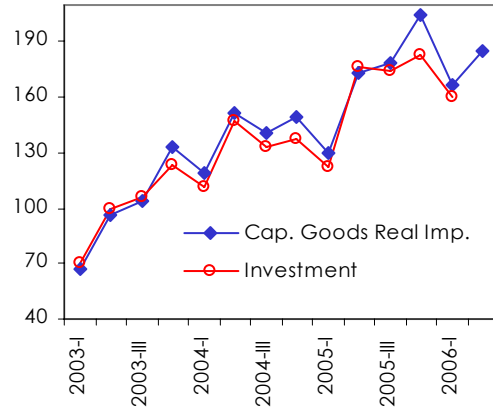
22. The strong position of the YTL together with the increase in industrial production was effective in the growth of imports of intermediate goods, which comprise 71 percent of total imports. Even though the growth rate of intermediate goods imports in the first quarter of 2006 dropped as a result of the slowdown in industrial production, it started to rise again in the second quarter. As a matter of fact, the annual growth rates of total industrial production and manufacturing industry production, which were realized as 5.3 percent and 4.8 percent in 2005 respectively, became 6.6 percent and 6.3 percent in the January-June period of 2006.

**Man. Ind. Prod. & Int. Goods Imports** (2003=100)



Source: TURKSTAT.

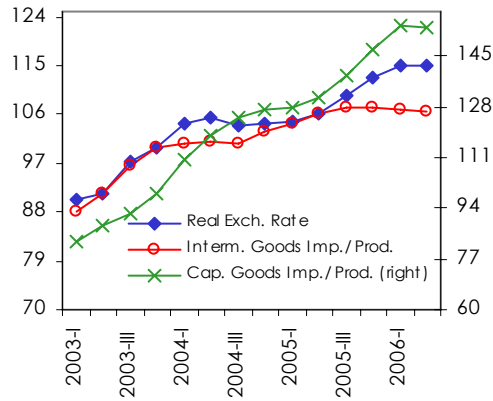
**Invest. Expend. & Cap. Goods Imp.** (2003=100)



Source: TURKSTAT.

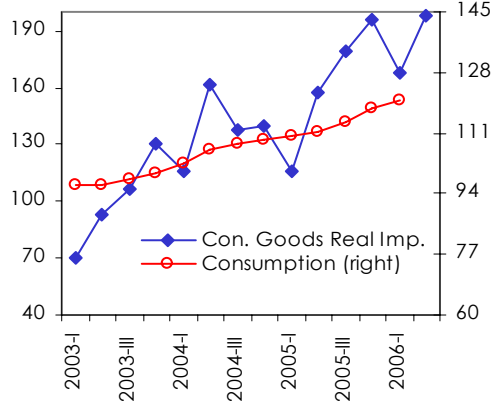
23. Although the growth rate of imports of intermediate goods declined, as a result of the rise in price, this group of goods made the largest contribution to the increase in total imports in the January-June period. The capital goods imports, with their high-rated upsurge, was prominent in 2005 and also continued to increase at a rate higher than the increase in imports of intermediate goods in the first quarter of 2006 but remained below the imports of intermediate goods in the second quarter. This development shows that investment expenditures slowed down in the second quarter of 2006. However, the striking development in the first half of 2006 is that consumption goods imports recording an increase of 31.1 percent, which is above not only intermediate, but also capital goods imports growth.

**Interm. & Cap. Imp./Manuf. Ind. P. Ratio and REER (PPI)** (12-month, ave.)



Source: TURKSTAT, CBT.

**Consum. Exp. & Con. Goods Imp.** (2003=100, 12-month, ave. for cons.)

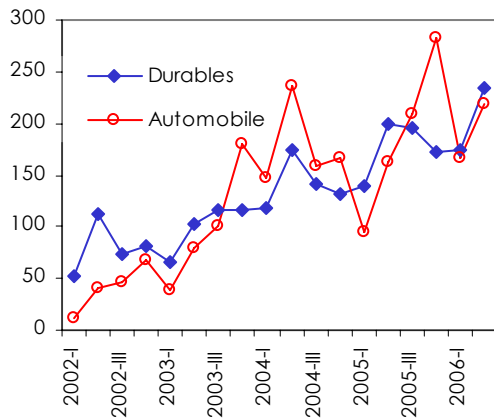


Source: TURKSTAT.

24. Analyzing quantity indices, imports of automobiles, which make up an important share of the imports of consumption goods, dropped by 33.1 percent in the first half of 2005, whereas they surged by 50.2 percent in the same period of 2006. Meanwhile, imports quantity indices of durable and semi-durable consumption goods, rose by 21 percent and 30.3 percent in the January-June period of 2006, respectively.

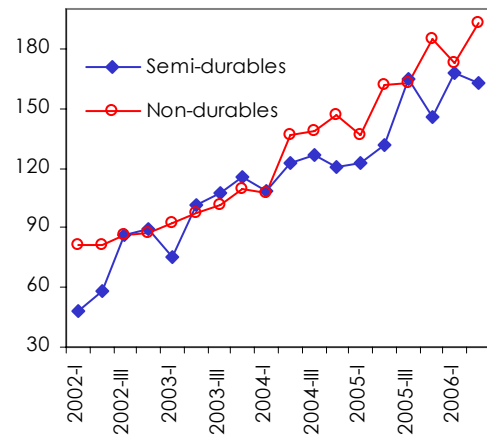
25. Analyzing by consumption tendencies, while the indices compiled by the CNB Ce indicate a decrease in consumer confidence since October 2005, the indices compiled by the CBT and TURKSTAT (CBT/TURKSTAT indices) state that these trends started as of May 2006.

**Durables & Automobile Imports**  
(2003=100)



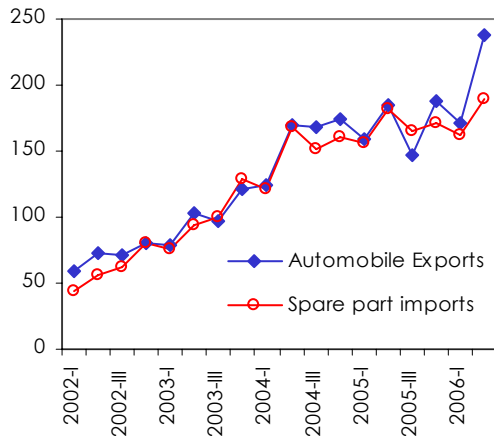
Source: TURKSTAT.

**Semi and non-durables Imp.**  
(2003=100)



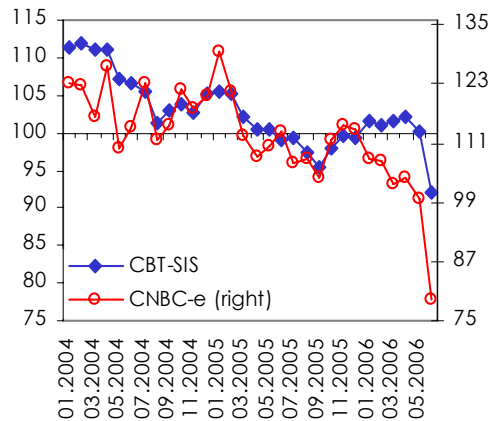
Source: TURKSTAT.

**Spare part imp. of trans. vehicles & Auto. Exports** (2003=100)



Source: TURKSTAT.

**Confidence Index**



Source: CBT, TURKSTAT, NTVMSNBC.

26. In the January-June period of 2006, the mining and quarrying sector, including crude oil, and motor vehicles-and-trailers with refined petroleum products, made the biggest contribution to the increase in imports. Imports of the basic metal industry, which had recorded a significant rise since the last quarter of 2004, increased by 23.5 percent in 2005, but declined by 11.3 percent in the first quarter of 2006. However, with an increase of 31.7 percent in the April-June period, the performance of the basic metal industry for the first half of 2006 rose by 10.1 percent. In the second quarter of 2006, the 20.8 percent rise observed in imported metal prices contributed to increase in nominal imports of the sector.

27. Imports of motor vehicles continued to be important within total imports. Compared to the first half of 2005, imports of motor vehicles increased by 23.0 percent in the first half of 2006. In the said period, automobile imports rose by 43.7 percent, whereas imports of transport vehicles' spare parts increased by 15.7 percent.

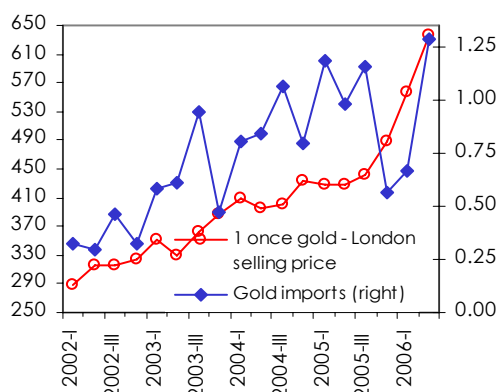
**Imports**  
(million US dollar)

	January-June				
	2005	2006	% Change	% Contr.	\$ Contr.
<b>Total</b>	<b>55094</b>	<b>65196</b>	<b>18.3</b>		
Capital Goods	9280	10491	13.0	2.2	1210
Intermediate Goods	39448	46500	17.9	12.8	7052
Consumption Goods	6101	8000	31.1	3.4	1899
Other	265	205	-22.6	-0.1	-60
<b>Selected Items (ISIC Rev.3):</b>					
Mining and Quarrying	6942	10283	48.1	6.1	3341
Crude oil	3782	5115	35.2	2.4	1332
Natural gas	2285	3944	72.6	3.0	1658
Textiles	1932	1921	-0.6	0.0	-11
Paper and paper products	1004	1086	8.1	0.1	82
Coke, petroleum products and nuclear fuel	2288	3511	53.4	2.2	1223
Chemicals and chemical products	8794	9347	6.3	1.0	553
Rubber and plastic products	1039	1233	18.7	0.4	194
Manufacture of basic metals	6976	7680	10.1	1.3	704
Manufactof fabricated metal prod(exc machinery)	930	1105	18.8	0.3	175
Manufacture of machinery and equipment	5723	6687	16.9	1.8	965
Electrical machinery and apparatus	1927	2317	20.3	0.7	390
Communication and apparatus	2220	2264	2.0	0.1	44
Medical, precision and opt. instr., watches	1207	1398	15.9	0.3	191
Motor vehicles and trailers	5478	6739	23.0	2.3	1261
Other transport	934	843	-9.8	-0.2	-91
Waste and scrap (Wholesale and retail)	1746	1870	7.1	0.2	124

Source: TURKSTAT.

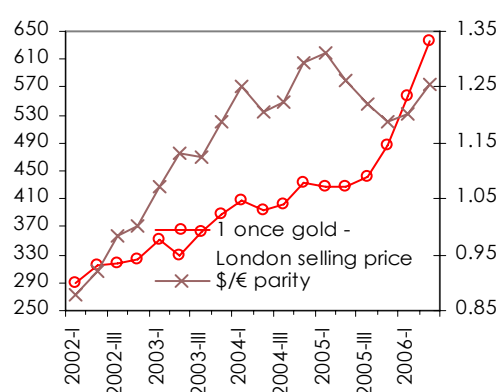
28. Gold imports, that had recorded high-rated growth since 2002, maintained their upward trend in the first nine months of 2005, however they rolled back in the last quarter of 2005, compared to the same period of the previous year. In the second quarter of 2006, imports of gold started to increase. As a matter of fact, in the first quarter of 2006, imports of gold dropped by 43.5 percent compared to the same period of the previous year, and increased by 29.9 percent in the second quarter. Meanwhile, gold prices, which displayed a rapid increase from the third quarter of 2005 onwards, rose by 39.5 percent in the first half of 2006 compared to the same period of the previous year.

**Gold Imports (billion US dollars) and Gold Prices (3-month ave., US dollars)**



Source: CBT, TURKSTAT.

**USD/EUR Parity and Gold Prices (monthly ave., US dollars)**

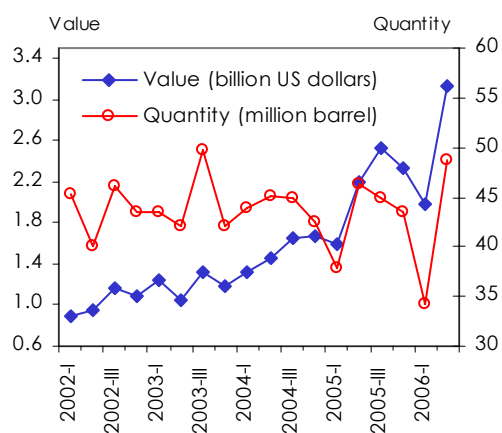


Source: CBT.

29. In the first quarter of 2006, high demand as a result of the high global growth and the uncertainties related to Iran and Nigeria caused crude oil prices to resume their ascent, which had decreased at the end of 2005. In the second quarter of 2006, although the crude

oil import quantity index declined by 1.5 percent compared to the same period of 2005, imports of crude oil increased by 35.2 percent in value, due to the fact that the crude oil import price per barrel rose by 37.2 percent.

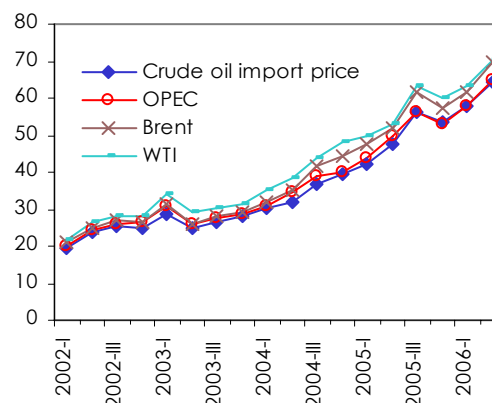
**Crude Oil Imports**



Source: TURKSTAT, SPO.

**Crude Oil Prices**

(US dollar per barrel, average)



Source: SPO, OPEC, EIA.

30. The increase in natural gas and other energy prices as well as in crude oil prices made a significant contribution to the rise in imports in the first half of 2006. According to the ISIC Rev.3 classification, total imports of energy, which is composed of crude oil, natural gas, black coal, lignite and turf in the mining and quarrying sector and coke coal, refined petroleum products and nuclear fuels in the manufacturing industry sector, climbed by 49.2 percent in the first half of the year. This increase contributed 8 percentage points to the 18.3 percent increase in total imports.

**Imports – Unit Value Indices**  
(annual percentage change)

	2005	2006 I	2006 II
Total	7.1	2.0	8.3
Capital Goods	-3.7	-9.0	-2.1
Intermediate Goods	11.0	6.5	13.0
Consumption Goods	-0.3	-6.9	-1.7
Selected Items (ISIC Rev.3):			
Food products and beverages	-7.8	-2.0	-5.7
Textiles	2.6	-2.4	-2.1
Paper and paper products	3.4	-3.0	4.2
Coke, petroleum products and nuclear fuel	29.3	29.1	22.7
Chemicals and chemical products	5.0	-6.8	-2.2
Rubber and plastic products	8.8	-4.2	3.6
Manufacture of basic metals	9.7	3.5	20.8
Man. of fabricated metal prod(exc mach)	7.7	-3.2	4.1
Manufacture of machinery and equipment	-1.1	-9.1	-2.1
Electrical machinery and apparatus	-7.4	-2.7	2.2
Communication and apparatus	-6.0	-16.2	-4.8
Medical, precision and opt. instr., watches	-0.3	-4.4	-0.7
Motor vehicles and trailers	-1.6	-5.6	3.6
Waste and scrap (Wholesale and retail)	1.2	-11.5	5.3

Source: TURKSTAT.

31. In addition to the import prices of basic metals and crude oil, the import prices of refined petroleum and by-products also increased. Meanwhile, in general import prices in



sectors that have significant shares in imports (food, textiles, chemical substances, machinery and equipment and communications) fell, with those of food products, radio, TV, communication equipment and apparatus recording particularly high rates of decrease.

32. When the import quantity indices of sectors are analyzed, with the exception of textile products, real imports are seen to have gone up, despite price decreases in the said sectors. As for textile products, both price and quantity indices registered a decline.

**Imports – Quantity Indices**  
(annual percentage change)

	2005	2006	2006
		I	II
Total	11.9	10.0	10.3
Capital Goods	22.2	29.2	6.9
Intermediate Goods	9.4	1.2	9.1
Consumption Goods	16.6	45.5	25.9
Selected Items (ISIC Rev.3):			
Food products and beverages	20.7	6.0	31.3
Textiles	2.3	0.8	-5.4
Paper and paper products	12.9	10.4	5.7
Coke, petroleum products and nuclear fuel	13.1	22.6	16.8
Chemicals and chemical products	10.1	9.1	7.7
Rubber and plastic products	1.1	18.6	12.4
Manufacture of basic metals	12.1	-14.9	8.4
Man. of fabricated metal prod(exc mach)	14.4	19.7	11.4
Manufacture of machinery and equipment	19.1	20.2	18.4
Electrical machinery and apparatus	43.3	35.3	2.8
Communication and apparatus	7.8	21.7	3.1
Medical, precision and opt. instr., watches	27.4	20.7	10.1
Motor vehicles and trailers	6.2	28.8	12.9
Waste and scrap (Wholesale and retail)	0.8	-7.5	29.5

Source: TURKSTAT.

33. Compared to the first half of 2005, the total share of imports from the EU decreased. On the other hand, non-member European countries, Asian and Middle Eastern countries made a significant contribution to the growth in imports. When analyzed on a country basis, the high-rated increases in imports from Russia and China attract particular attention. The increase in imports from these countries made a contribution of 3.9 points and 2.7 points to total growth in imports, respectively. In addition to Russia and China, the large share of Germany continued, while imports from France, Japan and Spain recorded high-rated increases. However, the decline in imports especially from Switzerland, the USA, South Korea and Ukraine is noteworthy.

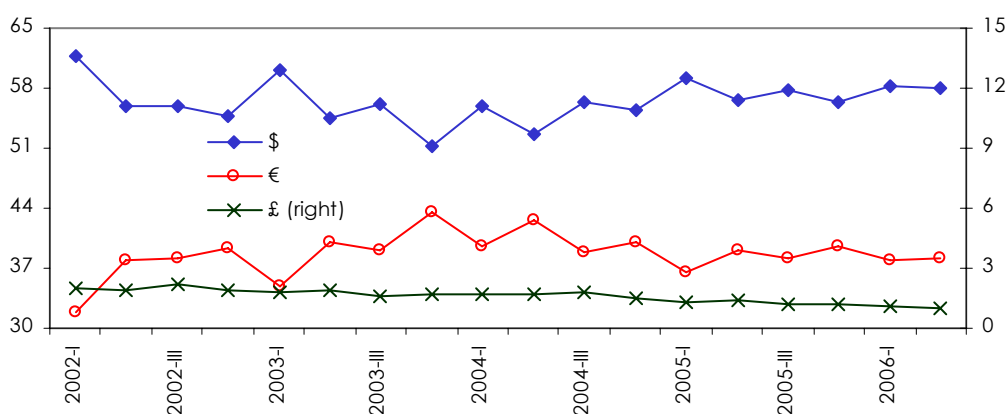
34. The share of US dollar imports, which dropped in the 2002-2003 period, resumed an upward trend as of 2004, whereas the share of euro imports went into a decline. Accordingly, the share of US dollar imports in total imports, which was 55.0 percent in 2004, rose to 57.5 percent in 2005 and was realized as 58.2 percent in the first half of 2006. The total share of euro imports, which was 40.3 percent in 2004 dropped to 38.4 percent in 2005 and became 38.1 percent in the first half of 2006. Meanwhile, the share of Sterling imports in total imports continued to decline steadily. The share of Sterling imports, which stood at 1.7 percent in 2004, dropped to 1 percent in the first quarter of 2006.

**Imports – Country Decomposition**  
(million US dollar)

	January-June						
	2005		2006		% Change	% Contrib.	\$ Contrib.
	Value	Share (%)	Value	Share (%)			
Total	55094	..	65196	..	18.3		
EU countries	23393	42.5	26275	40.3	12.3	5.2	2882
EU 15	21677	39.3	24277	37.2	12.0	4.7	2600
EU 10	1716	3.1	1998	3.1	16.5	0.5	283
Other countries	31345	56.9	38508	59.1	22.9	13.0	7163
Other European	11737	21.3	13913	21.3	18.5	3.9	2176
East Asian	9375	17.0	11855	18.2	26.5	4.5	2480
Other	10234	18.6	12740	19.5	24.5	4.5	2506
Free Zones in Turkey	356	0.6	413	0.6	15.9	0.1	57
<b>Selected countries and country groups</b>							
OECD	31,876	57.9	35,028	53.7	9.9	5.7	3151
Germany	6,442	11.7	7,107	10.9	10.3	1.2	665
Italy	3,572	6.5	4,064	6.2	13.8	0.9	492
France	2,824	5.1	3,390	5.2	20.0	1.0	565
USA	2,748	5.0	2,709	4.2	-1.4	-0.1	-39
İngiltere	2,278	4.1	2,514	3.9	10.4	0.4	236
Switzerland	2,255	4.1	2,090	3.2	-7.3	-0.3	-166
Spain	1,631	3.0	1,920	2.9	17.7	0.5	289
Japan	1,421	2.6	1,596	2.4	12.3	0.3	174
Korea	1,696	3.1	1,671	2.6	-1.5	0.0	-26
Other OECD	7,008	12.7	7,968	12.2	13.7	1.7	959
Middle East countries	1,613	2.9	1,917	2.9	18.8	0.6	304
Russian Fed.	5,837	10.6	7,982	12.2	36.7	3.9	2145
China	2,966	5.4	4,464	6.8	50.5	2.7	1498
Ukraine	1,490	2.7	1,486	2.3	-0.2	0.0	-4

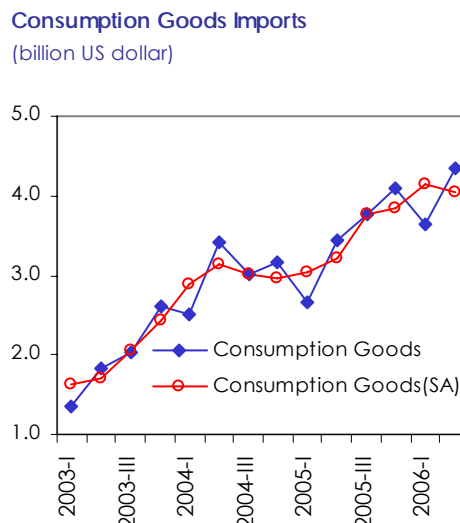
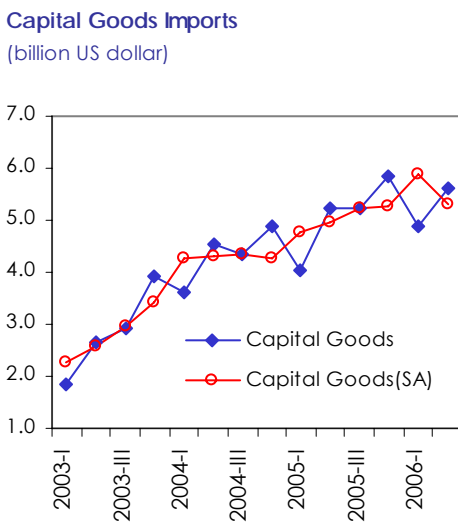
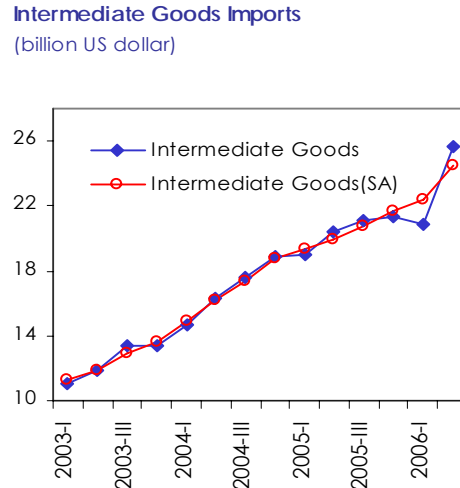
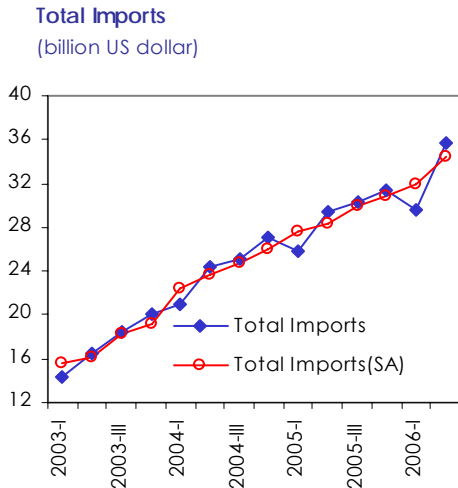
Source: TURKSTAT.

**Currency Composition of Imports**  
(% share)



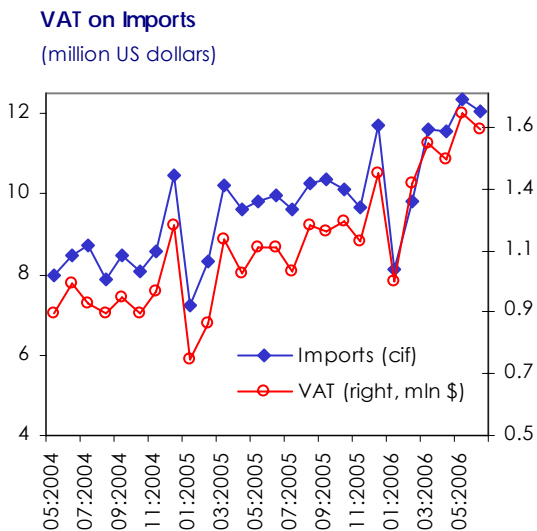
Source: TURKSTAT.

35. According to seasonally adjusted data, nominal imports in terms of USD increased by 7.7 percent in the second quarter of 2006, compared to the previous quarter. When analyzed in terms of sub-items, intermediate goods imports increased by 9.7 percent, while capital goods imports and consumption goods imports decreased by 9.4 percent and 2.4 percent, respectively.

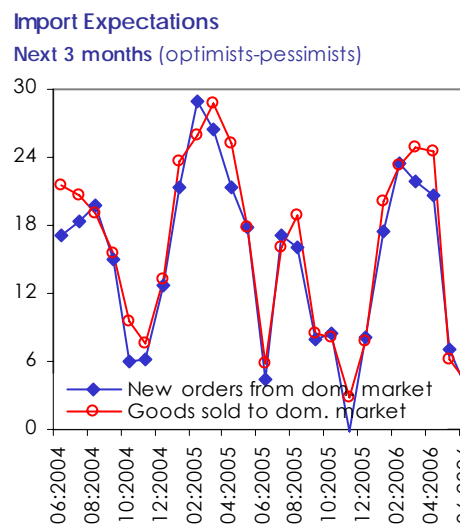


36. VAT on imports has been rising rapidly since the beginning of 2006 and VAT rates on imports that declined during the last months of 2005 seem to have been offset.

37. In the Business Tendency Survey for July, the indicators related to imports in the upcoming period point to a decline in the import tendency.



Source: TURKSTAT, Ministry of Finance.



Source: CBT Business Tendency Survey.

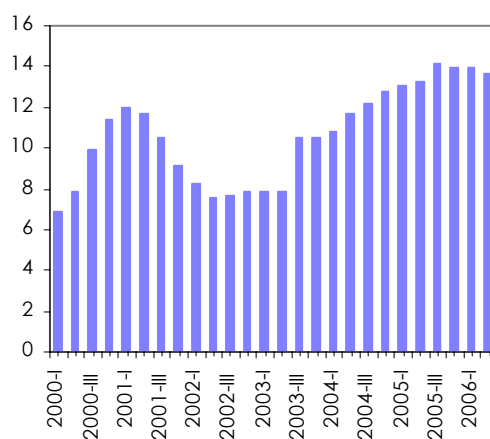
## Services Balance

38. Due to the slowdown observed in the growth of tourism revenues, the services balance in the second quarter of 2006 was realized below the level recorded in the same period of the previous year. Revenues from construction services increased during this period, while revenues from transportation and financial services decreased.

39. According to data released by TURKSTAT, tourism revenues dropped by 0.2 percent in the second quarter of 2006. During this period, despite the 5.9 percent decline in the number of visitors departing from Turkey (citizens + foreigners), average spending per tourist increased by 4.3 percent; however this increase was not enough to curb the negative impact of the decline in the number of tourists. Meanwhile, tourism expenditures rose by 10.1 percent in the same period, which resulted in a 4.4 percent decline in net tourism revenues.

### Services

(12-month ave., billions US dollars)



Source: CBT.

### Services Balance (million US dollar)

	2005				2006	
	I	II	III	IV	I	II
Services	1195	2755	7682	2334	1144	2454
Total income	3777	5568	10769	5735	3606	5273
Total Expenses	-2582	-2813	-3087	-3401	-2462	-2819
Transportation	-325	-360	-302	-310	-211	-476
Credit	840	955	1042	1190	861	624
Debit	-1165	-1315	-1344	-1500	-1072	-1100
Tourizm	1316	3082	8054	2828	1434	2946
Credit	1995	3760	8817	3580	2002	3693
Debit	-679	-678	-763	-752	-568	-747
Construction serv.	162	216	256	240	212	249
Credit	162	216	256	240	212	249
Debit	0	0	0	0	0	0
Financial serv.	-8	-22	1	-12	-82	-34
Credit	82	88	89	86	61	69
Debit	-90	-110	-88	-98	-143	-103
Other serv.	50	-161	-327	-412	-209	-231
Credit	698	549	565	639	470	638
Debit	-648	-710	-892	-1051	-679	-869

Source: CBT.

## Tourism Statistics

	2005				2006	
	I	II	III	IV	I	II
Tourism Revenues (million US dollars)	1995	3760	8817	3580	2002	3693
Departing foreigner visitors (x1000)	2376	5340	8452	4355	2138	4912
Departing citizen visitors (x1000)	480	546	1826	750	597	629
Tourism Expenditures (million US dollars)	-678	-678	-763	-751	-568	-747
Arriving citizen visitors (x1000)	889	1159	1045	1137	905	1170

Source: TURKSTAT, CBT.

40. In the second quarter of 2006, there was a decline in the number of foreign visitors departing from Turkey by 8.0 percent, compared to the same period of the previous year. This figure is significant as it is taken as the basis for calculating tourism revenues.

### Investment Revenues Account

41. The investment revenues account yielded a deficit of USD 1.6 billion in the second quarter of the year. The determinant of this deficit was interest expenditures. Although the interest expenditures of banks and the private sector increased compared to the same period of the previous year, those of the Central Bank and the Government decreased. Consequently, there was no significant change in the investment revenues deficit compared to the same period of last year, due to the increase in interest revenues during the same period.

### Investment Revenues Account (million US dollar)

	2005				2006	
	I	II	III	IV	I	II
Income (net)	-1380	-1622	-1324	-1333	-1375	-1598
Total income	1084	742	1046	812	1263	951
Total Expenses	-2464	-2364	-2370	-2145	-2638	-2549
Direct investment	-79	-435	-102	-118	-138	-374
Credit	83	123	43	28	59	65
Debit	-162	-558	-145	-146	-197	-439
Portfolio investment	-405	-143	-198	-178	-347	-35
Credit	814	436	687	465	908	585
Debit	-1219	-579	-885	-643	-1255	-620
Other investment	-896	-1044	-1024	-1037	-890	-1189
Interest income	187	183	316	319	296	301
interest expenses	-1083	-1227	-1340	-1356	-1186	-1490
Long-term	-974	-1099	-1174	-1206	-1048	-1294
Monetary A.	-262	-201	-394	-192	-186	-135
Gen. Gov.	-372	-510	-374	-509	-359	-531
Banks	-42	-40	-77	-98	-109	-136
Other sector	-298	-348	-329	-407	-394	-492
Short-term	-109	-128	-166	-150	-138	-196

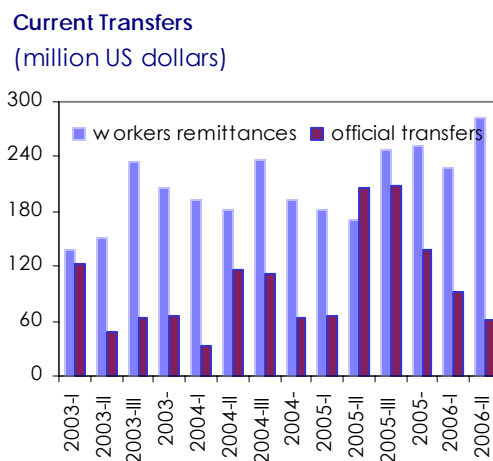
Source: CBT.

42. Portfolio revenues rose by 11.5 percent in the first quarter and by 34.2 percent in the second quarter, while portfolio expenditures increased by 3 percent and 7.1 percent during the same periods, respectively. Thus, the portfolio revenues deficit narrowed during this

period. This trend is expected to continue with growing revenues from Eurobonds throughout 2006.

### Current Transfers

43. The current transfers item, composed of workers' remittances and official transfers, increased by 29.1 percent in the first quarter of 2006, whereas it decreased by 10.6 percent in the second quarter of 2006. Thus, the said item yielded a surplus of USD 337 million in the second quarter of 2006.



Source: CBT.

### **III. CAPITAL MOVEMENTS**

44. The external financing requirement, which is defined as the sum of the current account item and net errors and omissions, became USD 8.7 billion in the second quarter of 2006. Despite the fact that the net errors and omissions item was realized as a credit item of USD 1.5 billion, the widening of the current account deficit compared to the same period of last year has increased the financing requirement. When the financing structure is compared with that of the same period of 2005, it is observed that there has been a significant rise in inflows of direct investments and long-term credits. Nevertheless, a portfolio-based outflow was observed due to the financial turbulence in May.

45. Accordingly, Central Bank reserves decreased by USD 3 billion in the second quarter and became USD 59.0 billion by the end of June. Meanwhile, the FX assets of banks increased by USD 3.3 billion in the second quarter of the year.

### Direct Investments

46. Net direct investments increased substantially in 2005 and reached 2.4 percent of the GNP. The historically high levels observed in direct investments stemmed mainly from privatization and mergers. In the second quarter of 2006, the amount of net direct investment to Turkey became USD 7.6 billion. The amount of net foreign direct investment for the first half of the year stands at USD 8.8 billion. The bulk of this amount came from the transfer of Telsim's assets to Vodafone in May and the sale of 34 percent of Petrol Ofisi AŞ to the Austria based oil and natural gas company OMV Aktiengesellschaft. Provided that mergers, the privatization program and payments continue, direct investments are also expected to increase substantially in 2006 and reach a record high level.

47. Non-residents' real estate purchases in Turkey form a significant portion of the direct investment inflows. This item accounted for USD 1.6 billion-worth of direct capital inflow in the first half of 2006.

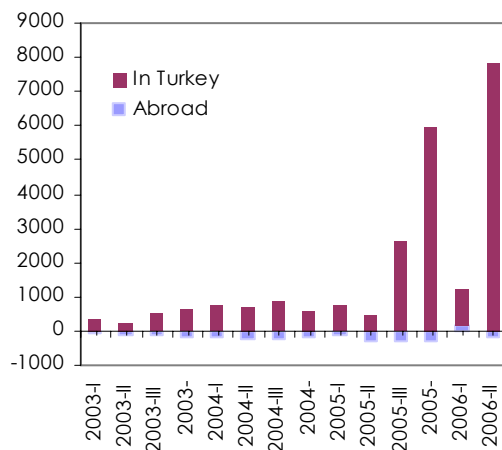
48. In the January-June period, foreign capital companies in Turkey repaid net USD 0.1 billion of the credits they used from their affiliates abroad – accepted as direct capital investments.

External Financing Requirement and Sources  
(billion US dollar)

	2004	2005	2005				2006	
			I	II	III	IV	I	II
<b>1. Current Account</b>	<b>-15.6</b>	<b>-23.2</b>	<b>-6.2</b>	<b>-7.0</b>	<b>-2.7</b>	<b>-7.3</b>	<b>-8.5</b>	<b>-10.2</b>
<b>2. Net Errors and Omissions</b>	<b>2.3</b>	<b>2.2</b>	<b>0.4</b>	<b>2.8</b>	<b>-0.6</b>	<b>-0.4</b>	<b>-1.2</b>	<b>1.5</b>
<b>I. Total Financing Requirement (=1+2)</b>	<b>-13.3</b>	<b>-20.9</b>	<b>-5.7</b>	<b>-4.2</b>	<b>-3.2</b>	<b>-7.7</b>	<b>-9.7</b>	<b>-8.7</b>
<b>II. Total Financing (=1+2+3)</b>	<b>13.3</b>	<b>20.9</b>	<b>5.7</b>	<b>4.2</b>	<b>3.2</b>	<b>7.7</b>	<b>9.7</b>	<b>8.7</b>
<b>1. Capital Flows (net)</b>	<b>23.6</b>	<b>44.5</b>	<b>6.4</b>	<b>12.1</b>	<b>10.9</b>	<b>15.1</b>	<b>17.5</b>	<b>10.9</b>
<b>Direct Investment (net)</b>	<b>2.0</b>	<b>8.7</b>	<b>0.6</b>	<b>0.2</b>	<b>2.3</b>	<b>5.6</b>	<b>1.2</b>	<b>7.6</b>
<b>Portfolio Investment (net)</b>	<b>8.0</b>	<b>13.4</b>	<b>3.8</b>	<b>3.1</b>	<b>2.1</b>	<b>4.5</b>	<b>3.6</b>	<b>-4.6</b>
General Gov. Eurobond Issues	2.0	3.4	1.8	0.2	0.3	1.2	2.3	-0.6
Nonresidents' Security Buyings in Turkey	7.5	11.6	3.5	2.8	2.1	3.2	1.6	-3.8
Residents' Security Buyings Abroad	-1.4	-1.2	-1.1	0.1	-0.3	0.2	-0.3	-0.1
<b>Credit Drawing (excl. IMF loan, net)</b>	<b>13.8</b>	<b>20.9</b>	<b>1.5</b>	<b>7.7</b>	<b>5.3</b>	<b>6.4</b>	<b>11.6</b>	<b>7.8</b>
General Government	-1.2	-2.2	-0.4	-0.6	-0.3	-0.8	-0.2	-0.2
Banks	5.7	9.2	0.8	4.1	2.0	2.5	2.4	3.0
Long-term	2.4	6.5	-0.1	4.0	1.1	1.6	1.3	3.2
Short-term	3.3	2.7	0.8	0.1	0.9	0.9	1.1	-0.2
Other Sector	9.3	13.8	1.1	4.3	3.7	4.8	9.3	5.0
Long-term	4.7	9.9	0.6	2.5	2.2	4.6	8.8	3.0
Short-term	0.3	0.4	-0.1	0.4	0.8	-0.7	0.1	0.1
Trade Credits	4.2	3.6	0.7	1.4	0.7	0.9	0.4	2.0
<b>Deposits</b>	<b>0.6</b>	<b>0.5</b>	<b>-0.1</b>	<b>0.7</b>	<b>1.0</b>	<b>-1.1</b>	<b>1.5</b>	<b>0.3</b>
in Central Bank	-0.2	-0.8	-0.1	-0.2	-0.3	-0.2	-0.2	-0.3
in banks	0.9	1.3	0.0	0.9	1.3	-0.9	1.6	0.6
<b>Other</b>	<b>-0.8</b>	<b>0.9</b>	<b>0.6</b>	<b>0.5</b>	<b>0.1</b>	<b>-0.3</b>	<b>-0.3</b>	<b>-0.3</b>
<b>2. IMF Loans</b>	<b>-3.5</b>	<b>-5.4</b>	<b>-1.0</b>	<b>-1.5</b>	<b>-2.3</b>	<b>-0.6</b>	<b>-1.8</b>	<b>-1.8</b>
Central Bank	-4.4	-2.9	-1.0	-0.9	-0.6	-0.3	0.0	0.0
General Government	0.9	-2.5	0.0	-0.6	-1.7	-0.3	-1.8	-1.8
<b>3. Change in Reserves (- increase)</b>	<b>-6.8</b>	<b>-18.2</b>	<b>0.3</b>	<b>-6.3</b>	<b>-5.4</b>	<b>-6.8</b>	<b>-6.0</b>	<b>-0.3</b>
Banks' FX assets	-6.0	-0.4	3.6	-3.0	-3.5	2.4	1.1	-3.3
Official Reserves	-0.8	-17.8	-3.3	-3.4	-1.9	-9.3	-7.1	3.0

Source: CBT.

Direct investments  
(million US dollars)

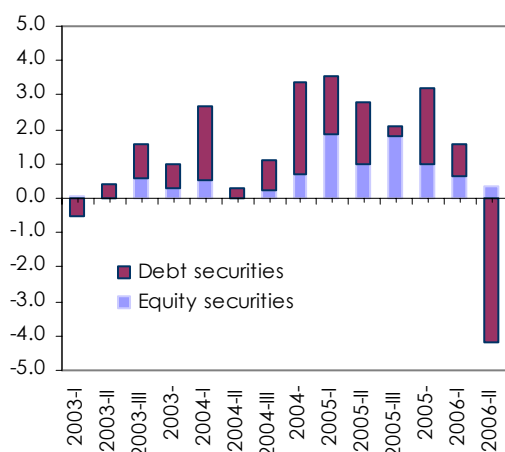


Source: CBT.

## Portfolio Investments

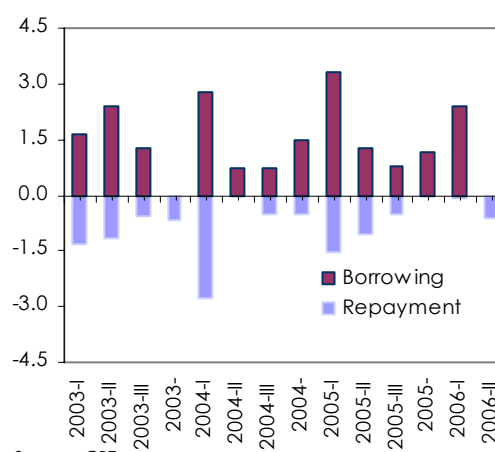
49. Non-residents continued to purchase equities and government securities in the ISE in the first two months of the year. However, the ECB's and FED's decisions to raise interest rates in March and expectations for further increments in interest rates initiated an exit from emerging markets. Parallel to this development, non-residents sold USD 23 million worth of equities and USD 130 million worth of government securities in March. In April, non-residents bought a sum of USD 0.2 billion in the equities market while they sold USD 20 million in the government securities market. As a result of the activities in financial markets in May, non-residents materialized the sale of USD 3.1 billion worth of government securities and the purchase of USD 0.2 billion worth of equities in the said month. The continuation of the activities in financial markets in June led non-residents to persist with the sale of securities to the sum of USD 1.0 billion for government securities and USD 0.1 billion for equities. Accordingly, in the January-June period, non-residents bought a net sum of USD 1.0 billion equities and sold net USD 3.2 billion worth of government securities. Meanwhile, the Treasury borrowed USD 2.4 billion via bond issues and repaid net USD 0.7 billion in the same period.

**Security buyings of non-residents**  
(billion US dollars)



Source: CBT, ISE.

**Eurobond issues of General Gov.**  
(billion US dollars)



Source: CBT.

50. In January and February 2006, the Treasury issued USD 1.5 billion-worth of bonds with a maturity of 30 years and EUR 750 million-worth of bonds with a maturity of 10 years. In July, the Treasury released a second issue amounting to USD 500 million. Favorable developments in the Turkish economy in recent years were reflected in the costs of bond issues. As a matter of fact, the bond issue in January has the longest maturity of those bonds currently available, as well as possessing the lowest coupon rate among USD denominated bonds. Moreover, the coupon rate and rate of return of the issue in February were realized as having the lowest rates among Euro denominated bonds with matching maturities.

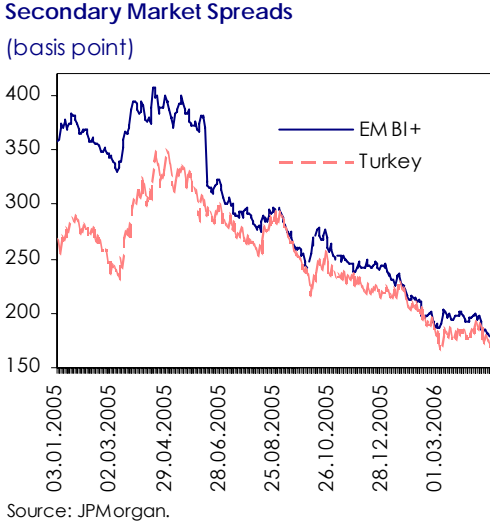
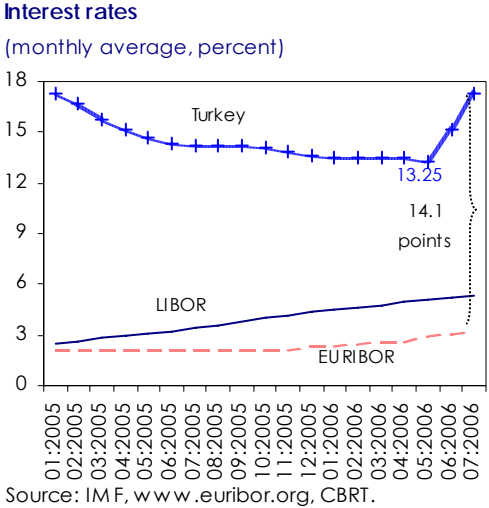
51. International liquidity conditions started to change in May 2006 due to the fact that some of the funds that were directed to developing countries headed to developed markets. Turkey was more severely affected by these developments because of the structure of the portfolios held by non-residents. As a result of the fluctuations in financial markets, volatilities in exchange rates started to reflect on prices. In order to prevent permanent impacts of the said developments on medium-term expectations and pricing behaviors, the Monetary Policy Committee (MPC) held extraordinary meetings on the 7th and 25th of June 2006 and decided to increase policy interest rates by 1.75 points and 2.25 points, respectively. In addition, considering the persistence of the increases in oil and other commodity prices and the inconsistency between expectations and medium-term targets, at its meeting dated July 20th, 2006, the MPC decided that measured monetary tightening was necessary and



increased policy interest rates by 0.25 points. Hence, as of July 20, 2006, overnight borrowing and lending interest rates applicable to the Interbank Money Market and the ISE Repo/Reverse Repo Market were set as 17.5 percent and 22.5 percent, respectively.

52. The Federal Reserve also continued to raise policy rates in 2006. The FED raised interest rates four times consecutively on 31st January, 28th March, 10th May and 29th June 2006; each time by 25 basis points and interest rates became 5.25 percent. Meanwhile, the European Central Bank (ECB) raised lending interest rates to 3.0 percent with increases of 0.25 point on 8th March, 15th June and 9th August 2006. The Bank of England raised lending interest rates that were cut by 0.25 point (4.5 percent) on 4th August 2005 to 4.75 percent with a further increase of 0.25 point on 3rd August 2006. In the meantime, due to the developments in financial markets, the Bank of Japan (BoJ), raised overnight interest rates from 0 percent to 0.25 percent in July.

53. The comparative analysis of developing countries demonstrates that even if yield spreads narrowed and interest rates fell throughout 2005, portfolio investments continued to be in the form of inflows. This shows that, besides interest rate differentials, sustained economic stability as a result of structural reforms and positive expectations about the future have an important impact on the investments in question. As for the second quarter of 2006, interest rates increased due to fluctuations in the financial sector. Accordingly, the downward trend of yield spreads reversed.



LIBOR: Interest rate for 1-month US dollar deposit  
 EURIBOR: Interest rate for 1-month Euro deposit  
 Turkey: Overnight interest rate in the Interbank Money Market

Spread: Difference between government paper yields of countries and US Treasury bond yields.

Other Investments

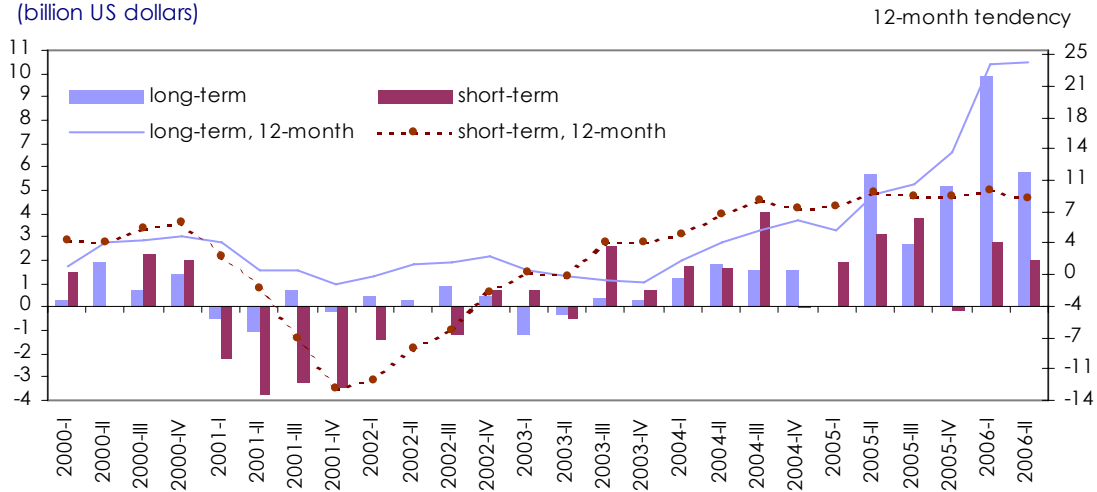
54. There was a capital inflow of net USD 12 billion in the January-March period of 2006, registered under the other investments item and capital inflow dropped down to USD 2.7 billion in the third quarter. The main source of this inflow was the net USD 10.2 billion-worth of long-term foreign credits obtained by the private sector and banks in Turkey. In this period, long-term credits used by the private sector and banks amounted to net USD 6.2 billion. Again, in the same period, net USD 2.0 billion-worth of trade credits originating from forward imports, were utilized.

55. Long-term credits, the share of which increased significantly in overall financing in 2005, continued to increase in the first half of 2006. Foreign credits obtained by the private sector for privatization payments became the primary factor of long-term credit utilization in the said period. While the banking sector used net USD 3.2 billion-worth of long-term credits, it paid net USD 0.2 billion-worth of short-term credits. Thus, while long-term credits of the banking sector reached USD 4.6 billion, short-term credits realized as USD 0.9 billion in the first

half of the year. Meanwhile, the private sector used USD 0.2 billion-worth of short-term credits in the first half.

### Long and Short-term capital

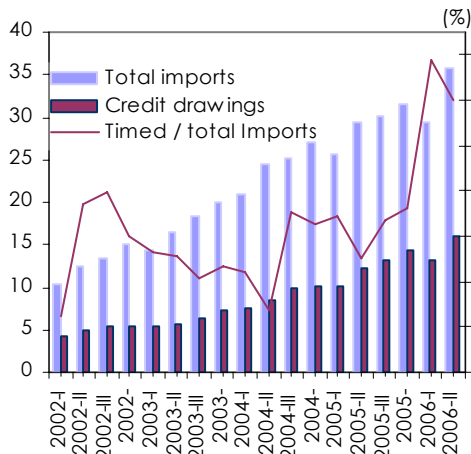
(billion US dollars)



Note: Excluding direct and portfolio investment, IMF loans and banks' FX assets

### Trade credit drawings and imports

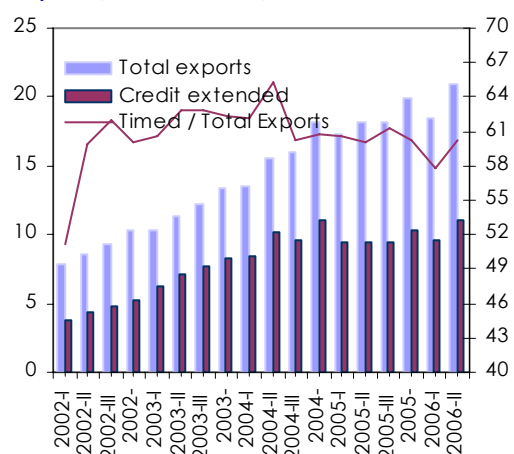
(billion US dollars)



Source: CBT, TURKSTAT.

### Trade credits extended abroad & exports

(billion US dollars)

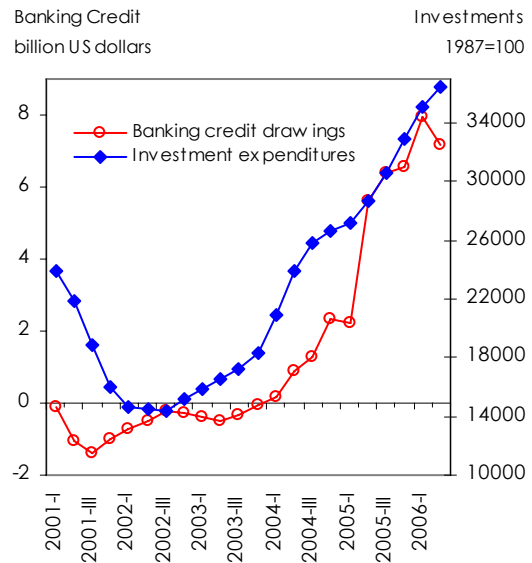
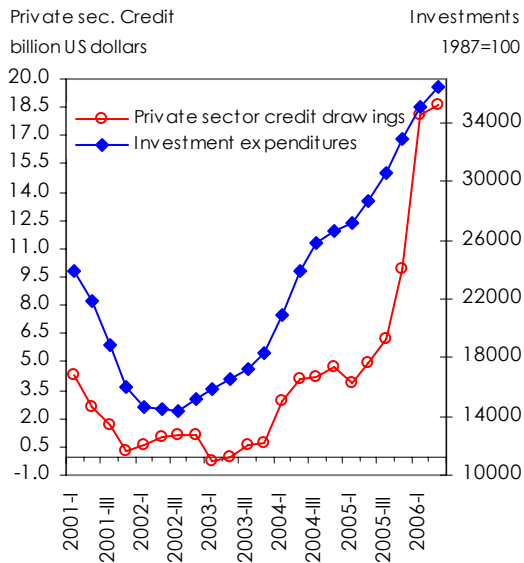


Source: CBT, TURKSTAT.

56. In line with the continued increase in imports in the first half of the year, forward imports and trade credit utilization increased by 47.6 percent and 29.9 percent, respectively, compared to the same period of the previous year. Meanwhile, parallel to the 11.5 percent rise in exports, the volume of trade credits extended abroad increased by 9.0 percent. The recovery in trade credits became more apparent in the second quarter.

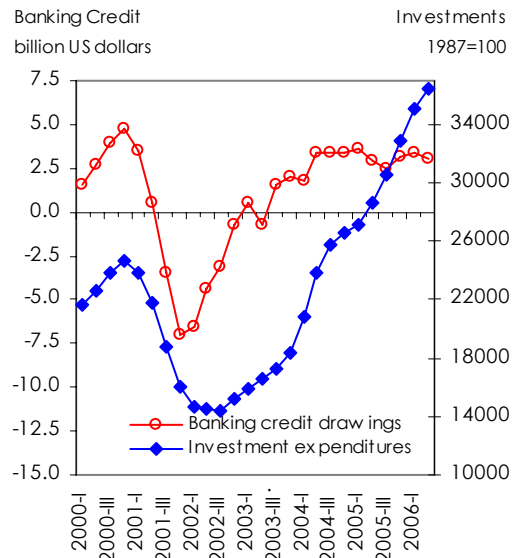
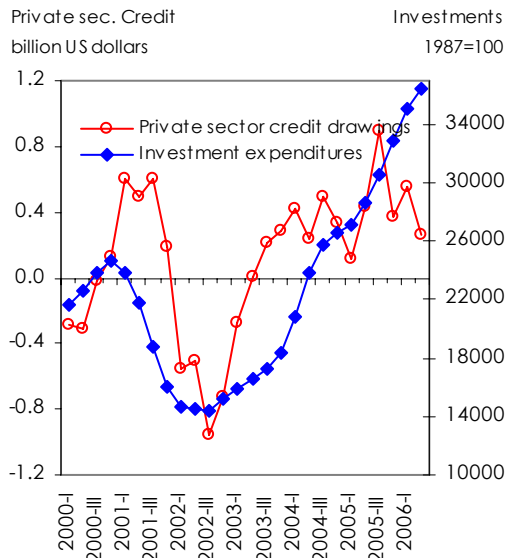
57. Parallel to the 7.4 percent growth in the GDP and the 23.6 percent increase in private sector investment expenditures in 2005, long-term credit utilization also displayed a substantial increase. This trend continued in the first quarter of 2006 as well and private investment expenditures increased by 30.2 percent. The continued rise in long-term credit utilization in the second quarter of 2006 confirms that the upward trend in investment expenditures continues. However, the environment of uncertainty stemming from financial turbulences in May and June are expected to have an adverse impact on investment expenditures in the third quarter.

**Long term net credit use and private sector investment expenditures**  
(12-month cumulative)



Source: CBT, TURKSTAT.

**Short term net credit use and private sector investment expenditures**  
(12-month cumulative)



Source: CBT, TURKSTAT.

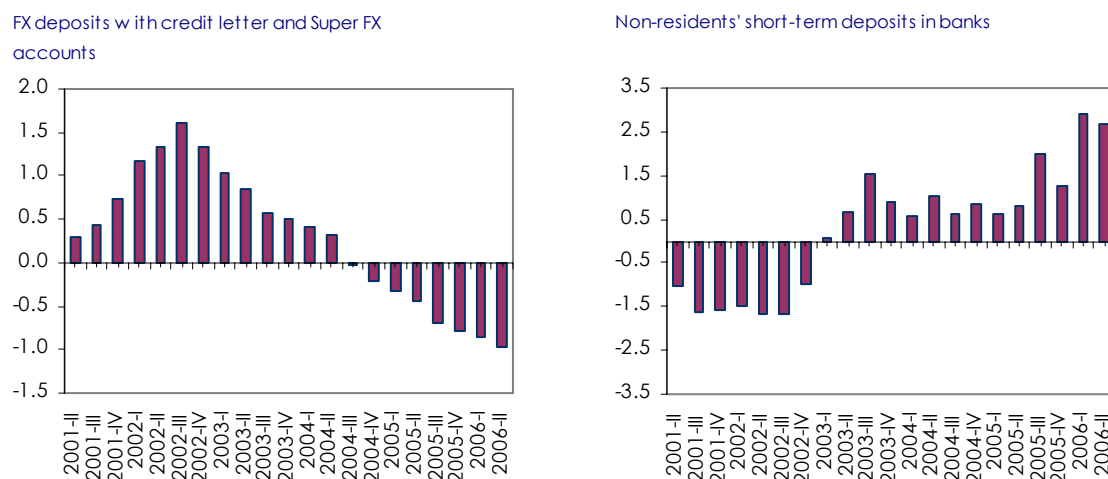
58. By the end of 2005, the Central Bank repaid all IMF credits that were extended in 2001 and before. Meanwhile, the Treasury continued to repay IMF credits and repaid IMF credits totaling USD 3.6 billion in the first quarter of the year.

59. Since April 2003, there has been an outflow from long-term FX deposit accounts with credit letters and super FX accounts opened at the Central Bank by Turkish workers abroad. Outflow from short-term accounts, which started in the second quarter of 2004, also continues. Accordingly, deposits with the Central Bank dropped by net USD 0.5 billion in the first half of 2006. The outflows are attributed to the gradual cuts in interest rates in both FX deposit accounts with credit letters and super FX accounts. Hence, while interest rates of the

euro-denominated super FX accounts with 1, 2 and 3-year maturities were 8, 9 and 10 percent in 2002, respectively, the said rates were reduced to 2.25, 3.25 and 3.75 percent, respectively, from March 6th 2006.

60. FX deposits of non-residents in domestic banks, which increased by USD 1.3 billion in 2005, increased by USD 2.3 billion in the period of January-April 2006, but this rise was followed by decline of USD 1 billion in May due to financial turbulences. In June, non-residents' deposits in domestic banks increased by USD 1 billion again, thus capital inflow through the item in question became USD 2.3 billion by the end of the first half of the year

#### Deposit belonging to non-residents (12-month, million US dollar)



Source: CBT.

61. By the end of the first quarter of 2006, total external debt stock increased by USD 15 billion compared to the same period last year and became USD 185.1 billion. While medium and long-term external debt increased by 8.6 percent, short-term debt rose by 7.9 percent compared to end-2005. The increase in short-term debt stock stemmed from the rise in trade credits utilized by the private sector, short-term credits utilized by the banks and the increase in deposits of foreign banks.

62. The improvement in external debt indicators also continued in 2005. Despite the current account deficit of USD 23.1 billion in 2005, the ratio of external debt stock to GDP decreased to 47.1 percent by the end of the year. However, the current account deficit in annual terms increased to USD 25.5 billion in the first quarter of 2006 and the ratio of external debt stock to GDP became 50 percent. The ratio of external debt stock to exports increased in the first quarter of 2006.

63.

#### External debt ratios (Percentage)

	2004				2005				
	I	II	III	IV	I	II	III	IV	I
External Debt Stock / GDP	55.1	53.4	53.2	54.0	51.7	50.0	48.2	47.1	50.0
External Debt Stock / Exports*	287.8	270.1	260.5	256.8	240.4	234.5	232.8	231.7	247.6
Debt Service / GDP	11.4	10.7	10.5	10.1	9.7	10.2	10.1	10.1	9.4
<i>Memo:</i>									
External Debt Stock (billion \$)	145.0	147.5	152.2	162.2	160.9	163.0	166.8	170.1	185.1
GDP (billion \$)	263.1	276.3	285.7	300.6	311.2	326.2	346.3	361.5	370.4

\* Excluding shuttle trade and other goods.

Source: TURKSTAT, Undersecretariat of Treasury.

## IV. APPENDIX

### CURRENT ACCOUNT (USD Million)

	Current Account										
	Net	Foreign Trade			Services		Income		Transfers		
	Net	Exports (FOB)	Shuttle Trade	Imports (CIF)	Net	Travel Revenues	Net	Interest Expenditure	Net	Workers Remittances	
	<i>(annual)</i>										
2000	-9821	-21959	27775	2946	-54503	11366	7636	-4002	-4825	4774	4560
2001	3392	-3733	31334	3039	-41399	9132	8090	-5000	-5497	2993	2786
2002	-1524	-7283	36059	4065	-51554	7879	8479	-4556	-4416	2436	1936
2003*	-8036	-14010	47253	3953	-69340	10504	13203	-5557	-4579	1027	729
2004	-15604	-23878	63167	3880	-97540	12784	15888	-5637	-4343	1127	804
2005	-23235	-32925	73476	3473	-116773	13966	18152	-5744	-5006	1468	851
	<i>(quarterly)</i>										
2005 I	-6203	-6243	17241	713	-25740	1195	1995	-1402	-1083	247	181
II	-7034	-8523	18144	942	-29354	2755	3760	-1643	-1227	377	171
III	-2696	9487	18131	813	-30234	7682	8817	-1345	-1340	454	247
IV	-7302	-8672	19960	1005	-31445	2334	3580	-1354	-1356	390	252
2006 I	-8460	-8548	18510	951	-29520	1144	2002	-1375	-1186	319	228
II	-10195	-11388	20951	1430	-35676	2454	3693	-1598	-1490	337	276
	<i>(monthly)</i>										
2005 Jul	-1126	-3058	5764	204	-9596	2143	2602	-380	-303	169	78
Aug	-1203	-3794	5553	307	-10272	3033	3453	-594	-649	152	85
Sep	-367	-2635	6814	302	-10366	2506	2762	-371	-388	133	84
Oct	-902	-2361	6772	366	-10090	1649	1899	-328	-410	138	93
Nov	-2634	-2851	5943	328	-9673	631	944	-510	-525	97	74
Dec	-3766	-3460	7246	311	-11683	54	737	-516	-421	155	85
2006 Jan	-2241	-2421	5100	238	-8140	379	722	-319	-314	120	77
Feb	-3206	-2932	6020	328	-9797	257	549	-622	-497	91	68
Mar	-3013	-3195	7390	385	-11583	508	731	-434	-375	108	83
Apr	-3922	-4068	6420	460	-11566	499	937	-424	-452	71	71
May	-3773	-4176	6949	495	-12312	880	1245	-634	-589	157	126
June	-2500	-3144	7582	475	-11798	1075	1511	-540	-449	109	79
	<i>(12-month)</i>										
2005 Jul	-19275	-28458	69653	3572	-108190	13601	17107	-5690	-4761	1271	790
Aug	-20498	-29996	70499	3510	-110579	13877	17536	-5696	-4833	1316	792
Sep	-20954	-30665	71657	3455	-112458	14150	17815	-57775	-4892	1335	792
Oct	-21675	-31644	72562	3461	-114460	14324	17985	-5760	-4993	1404	827
Nov	-22379	-32479	72771	3478	-115565	14378	18073	-5693	-4965	1415	830
Dec	-23235	-32926	73476	3473	-116774	13966	18152	-5744	-5006	1468	851
2006 Jan	-23927	-33761	73579	3505	-117694	13892	18184	-5557	-5043	1499	868
Feb	-24873	-34757	73947	3597	-119167	13949	18185	-5585	-5044	1520	878
Mar	-25430	-35231	74745	3711	-120554	13915	18159	-5654	-5109	1540	898
Apr	-26820	-36738	75037	3842	-122525	13867	18236	-5483	-5241	1534	910
May	-28289	-37970	76009	4029	-125025	13710	18081	-5513	-5273	1484	978
June	-28612	-38096	77552	4199	-126876	13614	18092	-5630	-5372	1500	1003

Source: CBT.

\* Due to the change in definition, 2003 travel revenues revised upward, while workers' remittances revised downward. Since this change is not applied to previous years, travel revenues and workers remittances should not be compared.

CAPITAL and FINACILA ACCOUNT (USD million)

	Capital and Financial Account																
	Net		Financial Account														
	Net	Foreign Direct Investment	Portfolio Investment					Other Investment				Liabilities					
			Net	Assets	Liabilities		Net	Currency and Deposits	Net	Trade Credits	Credits			Deposits			
Equity Securities	Debt Securities	Monetary Authority	General Gov.	Banks	Other Sectors	Monetary Authority					Banks						
	(annual)																
2000	12581	12581	112	1022	-593	489	1126	11801	-1690	13740	805	3348	117	4378	5025	622	-642
2001	-1633	-1633	2855	-4515	-788	-79	-3648	-2667	927	-2066	-1930	10229	-1977	-8076	438	736	-1568
2002	1406	1406	962	-593	-2096	-16	1519	7190	594	7967	2483	-6138	11834	-1028	371	1336	-988
2003	3095	3095	1253	2465	-1386	905	2946	3424	724	4410	2181	-1479	-765	1975	1022	497	871
2004	13336	13336	1978	8023	-1388	1427	7984	4159	-5965	11114	4201	-4414	-267	5708	5081	-209	856
2005	20775	20775	8589	13437	-1233	5669	9001	16596	-351	16346	3581	-2881	-4637	9247	10234	-787	1276
	(quarterly)																
2005 I	5719	5719	604	3796	-1138	1851	3083	4594	3622	387	650	-1008	-381	754	462	-113	11
II	4172	4172	119	3062	90	991	1981	4370	-2953	6993	1368	-945	-1189	4055	2903	-191	870
III	3249	3249	2336	2062	-335	1828	569	758	-3462	4251	709	-603	-1983	1979	2949	-269	1310
IV	7635	7635	5530	4517	150	999	3368	6874	2442	4715	854	-325	-1084	2459	3920	-214	-915
2006 I	9699	9699	1233	3578	-307	641	3244	11996	1134	11219	421	0	-1993	2433	8899	-184	1635
II	8710	8710	7589	-4555	-136	367	-4786	2693	-3326	6469	1962	0	-2012	2985	3084	-296	632
	(monthly)																
2005 Jul	1314	1314	1103	1025	-715	571	1169	2204	-317	2285	101	-153	-248	879	1476	-30	205
Aug	594	594	484	-619	-31	501	-1089	-1526	-2291	509	345	-114	-1388	151	786	-118	789
Sep	1341	1341	749	1656	411	756	489	80	-854	1457	263	-336	-347	949	687	-121	316
Oct	924	924	243	-244	-162	-174	92	3910	4837	-640	525	0	-621	-744	183	-73	69
Nov	1089	1089	3118	2471	326	977	1168	-696	-1311	93	-140	0	-1712	1743	1588	-63	-1322
Dec	5622	5622	2169	2290	-14	196	2108	3660	-1084	5262	469	-325	1249	1460	2149	-78	338
2006 Jan	2986	2986	680	2069	-151	465	1755	2185	-2272	3814	-516	0	-305	-236	4773	-50	148
Feb	4787	4787	241	1211	284	199	728	7346	1859	5444	256	0	-1407	1348	3182	-55	2119
Mar	1926	1926	312	298	-440	-23	761	2465	1547	1961	681	0	-281	1321	944	-79	-632
Apr	2968	2968	455	-585	-161	223	-647	3490	1177	2131	510	0	-470	1053	468	-85	640
May	3110	3110	6634	-3107	-220	226	-3113	-1748	-2253	376	809	0	-1608	637	1620	-118	-1010
June	2632	2632	500	-863	245	-82	-1026	951	-2250	3962	643	0	66	1295	996	-93	1002
	(12-month)																
2005 Jul	14121	14121	2455	11959	-3295	4272	10982	10663	-3951	13861	3508	-4170	-2120	9149	6359	-510	1386
Aug	14463	14463	2906	11328	-3009	4820	9517	7705	-4021	11377	3399	-3808	-4060	8051	6627	-635	1512
Sep	15895	15895	2417	12488	-2197	5393	9292	7910	-4960	13073	3458	-3683	-4250	8905	7056	-690	1976
Oct	16889	16889	3433	11076	-1854	5182	7748	12712	490	12287	3841	-3528	-4592	8241	6915	-710	1807
Nov	17258	17258	6480	13224	-1275	5947	8552	13069	624	11793	3867	-3035	-6111	8121	8451	-726	914
Dec	20775	20775	8589	13437	-1233	5669	9001	16596	-351	16346	3581	-2881	-4637	9247	10234	-787	1276
2006 Jan	21303	21303	9131	12438	-528	5281	7685	17439	-3525	20471	3285	-2719	-4809	8623	15105	-800	1475
Feb	24339	24339	9046	12170	-290	4954	7506	25424	-2073	27195	3771	-2222	-6084	10513	18024	-826	3709
Mar	24755	24755	9218	13219	-402	4459	9162	23998	-2839	27178	3352	-1873	-6249	10926	18671	-858	2900
Apr	25271	25271	9606	12759	-307	4371	8695	25744	-962	26949	3070	-1714	-6390	11407	18296	-890	2864
May	27016	27016	16283	8674	-955	4501	5128	24316	-1474	26075	3471	-1264	-7276	11485	18989	-925	1296
June	29293	29293	16688	5602	-628	3835	2395	22321	-3212	26654	3946	-928	-7072	9856	18852	-963	2662

Source: C.B.T.