



CENTRAL BANK OF THE REPUBLIC OF TURKEY



# Financial Stability Report

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This report, which aims to inform the public, is based mainly on December 2005 data. However, the report also includes the developments and evaluations until the publishing date of the report in Turkish. This text is fully available at the CBRT web site. The CBRT cannot be held accountable for decisions taken based on the information and data provided in this report.

## FOREWORD

*I am glad to share with you the second issue of the Financial Stability Report, which contains detailed assessments on financial stability, in an environment where macro economic indicators show a positive trend, payment systems and the regulatory framework are strengthened, banks are focused more on their actual function of intermediation due to the reversal of the public sector crowding out effect, and where more attention has to be paid to the risks as a result of the increased interaction between the financial system and other sectors.*

*In the Report, the macroeconomic components of the financial system are examined first, with an approach that takes into consideration the interaction among sectors in line with the recent developments in the economy. In this assessment, although improvements in macro balances and particularly in public finance are noted, the increase in household borrowing, foreign exchange risk that real sector companies are exposed to due to their high foreign exchange liabilities and the current account deficit are the factors that require monitoring carefully.*

*Banks, occupying the largest share of the financial system, are the focus of our analyses and assessments. In this regard, by analyzing the main risks in bank balance sheets through stress tests and scenario analyses, it is observed that banks have adequate capital and are resilient to potential shocks. Moreover, while banks are found to be increasingly adapting themselves to the increased competitiveness in an environment of falling inflation, it is important to closely monitor the rising credit risk.*

*Inevitably, recent developments in international financial markets have had repercussions on our country. However, I take pleasure in saying that the strength of the Turkish financial system has minimized the negative effects of this volatile environment. This has once again shown us how important it is to have a sound financial system with an improved risk culture and strengthened by effective supervision.*

*Within this context, I hope that our assessments will contribute to the decision-making processes of all financial market participants.*



Durmuş YILMAZ  
Governor

Central Bank of the Republic of Turkey