



**THE BANKING REGULATION  
AND SUPERVISION AGENCY**

**BANKING SECTOR  
RESTRUCTURING PROGRAM:  
PROGRESS REPORT**

**July 2002**



## **FOREWORD**

The Banking Sector Restructuring Program, announced in May 2001, aims to eliminate distortions in the financial sector and adopt regulations to promote an efficient, globally competitive and sound Turkish banking sector.

The restructuring program was based on the following main pillars: (1) Restructuring of the state banks (2) prompt resolution of SDIF banks (3) Strengthening of the private banks and (4) Strengthening the regulatory and supervisory framework.

Banking Regulation and Supervision Agency periodically updates and publishes the developments realized within the restructuring program in the form of “Progress Reports”. This issue of “Progress Report” presents in detail the developments realized in the program as of July 15, 2002.

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## BANKING SECTOR RESTRUCTURING PROGRAM: PROGRESS REPORT<sup>1</sup>

### 1. DEVELOPMENTS PRIOR TO THE RESTRUCTURING PROGRAM (1980-2001)

A significant part of the flow of funds are performed through the banking sector in Turkey. Although the number and size of non-bank financial institutions tended to increase in the recent years, the banking sector has still a share of 75 % in total financial sector assets. The fact that a significant part of non-bank financial institutions are subsidiaries of banks increases the dominance of the banks in the financial sector.

Turkish financial system underwent significant structural changes and gained dynamism as a result of the liberal policies adopted starting from 1980 onwards. Along with deregulation measures introduced, such as removal of selective credit policies, free determination of interest rates on deposits and credits, and liberalization of foreign exchange transactions, efforts to increase the level of compliance of the legislations with the international norms also played a contributing role in this development.

With the help of legislative and institutional arrangements that eased the entry, competition and growth in the sector, the Turkish banking sector experienced a process of fast expansion in terms of bank number, employment, service diversity and technological base. More specifically;

**Table 1: Number of Banks**

	1980	1990	1994	1999	2002(*)
Commercial Banks	31	54	55	62	43
Public	8	7	6	4	3
Private	19	25	29	31	20
Foreign	4	22	20	19	15
SDIF	-	-	-	8	5
Investment and Development Banks	6	10	12	19	14
Public	4	3	3	3	3
Private	2	4	6	13	8
Foreign	-	3	3	3	3
<b>Total</b>	<b>37</b>	<b>64</b>	<b>67</b>	<b>81</b>	<b>57</b>

*Source: BRS A, Banks Association of Turkey.*

*(\*) As of July 15, 2002*

- The number of banks which was 37 in 1980 increased to 64 in 1990 and to 81 in 1999.
- A significant progress was made in opening-up and integrating the banking sector with the international financial system during the 1990s. The number of foreign banks in the form of financial subsidiary or branch

<sup>1</sup> The developments experienced in banking sector after 1980 and information regarding the BRS A's goals and strategies in the original text of "Banking Sector Restructuring Program" which was announced to public on May 15, 2001 are also included in the Progress Report in order to allow for monitoring of the restructuring process in an integrated manner.

reached to 18 in 2000 from 4 in 1980. Share of foreign banks in the sector increased to 5,4% in 2000 from 3,7% in 1992. However the weight of foreign banks in the sector is still low compared to a number of countries having similar characteristics with Turkey.

- Together with the increase in the number of domestic and foreign banks in banking sector, weight of state-owned banks in the system decreased. Share of state-owned banks in total assets of banking sector went down to 34% in 2000 from about 45% in 1980 and 1990.
- Banking sector took important steps towards adapting itself to developments in technology and improving its technological infrastructure. In the last decade, a rapid progress has been observed in the number of ATMs, number of branches having on-line connection, use of the Electronic Fund Transfer (EFT) and SWIFT systems, interactive banking services and internet banking.
- There has been a significant progress in the diversification of banking services and use of bank cards/credit cards has expanded rapidly. Number of credit cards which were about 1 million in 1992 increased to 13,4 million at the end of 2000.

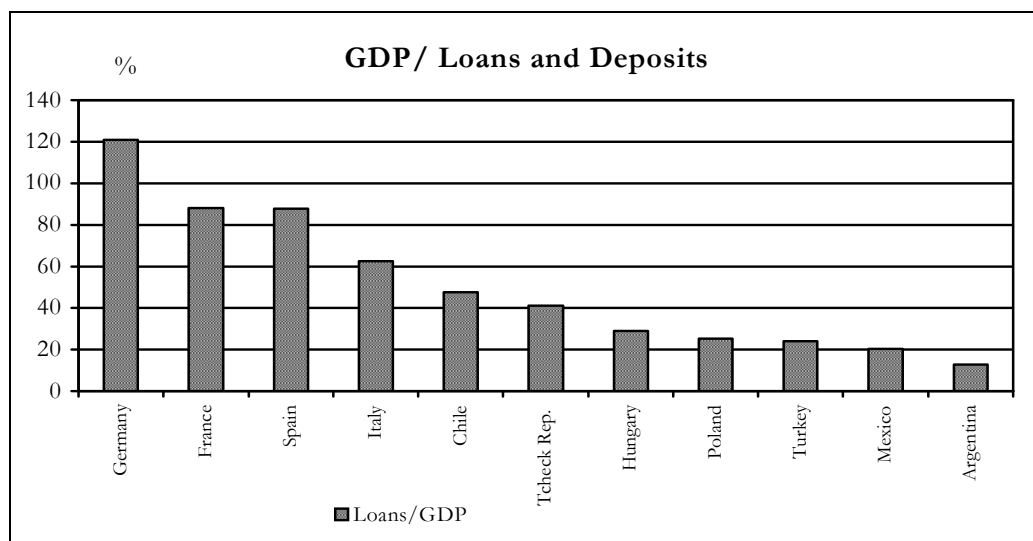
Despite a number of serious economic and financial crises experienced during the post-1980 era, some important positive developments in the aggregate financial indicators of the banking sector have been observed. Along these lines;

- Total asset size of banking sector increased to USD 58,2 billion in 1990 (%38,2), and to USD 155 billion in 2000 (%76,9) from a level of USD 20,8 billion in 1980 (28,6 % of GNP).
- There has also been a rapid increase in the volume of deposits. Total savings deposits which were USD 4,3 billion in 1980 have reached to USD 64,4 billion in 2000. The increase realized in foreign currency accounts during the second half of the 1980s was particularly effective in this outcome. As the use of repurchasing agreements became widespread from the second half of the 1990s onwards, part of savings were started to be held in the form of repo also. Indeed, the ratio of repo volume realized with clients to savings deposits was about 15% as of end of 2000.
- Off-balance sheet transactions increased rapidly as a result of the diversity in banking services in 1990s, the increase in funding the Government Securities through repo and in F/X forward transactions. The ratio of off-balance-sheet transactions to total assets which was 41,4 % in 1992 increased to 100,8 % as of end 2000.

**Important steps have been taken regarding the adaptation of legal and institutional regulations in banking sector in Turkey to the changing conditions and to the developments in international standards. In that respect, Banks Act Nr. 4389 entered into force in June 1999 has been an important landmark. Regulation and supervision of the banking sector have been transferred to the Banking Regulation and Supervision Agency having the status of administrative and financial autonomy by this Act. All resolutions to be taken in the process from establishment till liquidation of banks have been granted to the Agency with the Act dated December 19, 1999, Nr 4491, and the BRSA 's autonomous status has been strengthened. Public units**

responsible for monitoring and supervising of the banking sector has been combined under the structure of the Banking Regulation and Supervision Agency, and the Agency started to operate as of August 31, 2000.

Despite all these positive developments, the Turkish banking sector has moved away from traditional banking activities. The share of loans in total assets of the banking sector declined from 47% in 1990 to about 33% in 2000. The credit to GNP ratio is about 25%; lowest among the emerging market countries.



The following factors have contributed to the decline in the financial intermediation function of the banking sector:

- **Macroeconomic Instability:** The high and volatile inflation rates of 1990s, the boom-bust cycles of economic growth and the fragility of external capital inflows all contributed to the uncertainties and led to a domination of “short-term” behavior of economic agents. The confidence in the Turkish lira also deteriorated leading to an extensive currency substitution. As a result, the maturity of bank funding sources have shortened substantially and the share of foreign currency liabilities in total liabilities have increased sharply.
- **High Public Sector Deficit:** The increase in public sector deficit and its financing with high real interest rates from the domestic financial markets led to a sharp decline in the allocation of resources to the real sector. The arbitrage opportunities due to the high domestic real interest rates made it attractive for banking sector to borrow abroad and finance public sector deficits leading to an increase in foreign exchange open position of the banking sector. As a result, the share of government securities in deposit

money banks' total assets increased from 10% in 1990 to about 25% in recent years.

- ***Systemic Distortions Created by the State Banks:*** The financial health of the state banks deteriorated rapidly as a result of the accumulation of duty losses and inefficient management. The illiquid state banks covered their financing needs from the markets borrowing at very high rates and at short maturities. This led to an increase in interest rates and created an uneven playing field for the other banks in the sector. As a result, the state banks became unable to fulfill their banking functions; although state banks accounted, for 40% of total deposits their share in total loans was only 26%.

***Inadequate Risk Assessment and Management Systems:*** Although the banking sector became more exposed to liquidity, interest rate and foreign exchange rate risks, macroeconomic policies followed especially during the late 1990s, which tended to ease the financing of public debts, made the perception and management of these risks an issue of secondary priority for the banks. The lack of independent and effective supervision and regulation and the existence of deposit insurance also contributed to the weaknesses in risk management.

As a result of all these developments, the Turkish banking system as a whole became subject to the following structural weaknesses:

- Inadequate capital base
- Small and fragmented banking structure
- Dominance of state banks in total banking sector
- Weak asset quality (concentrated credits, group banking and concentrated risks, mismatch between loans and provisions)
- Extreme exposure and fragility towards market risk (maturity mismatch, F/X open position)
- Inadequate internal control systems, risk management and corporate governance

Eventually, above-mentioned structural problems made the banking sector highly sensitive and fragile to domestic and foreign shocks. Banking sector faced important losses as a result of the crisis experienced in Turkish economy in 1994 and three banks were put under liquidation process. Negative effects of the 1994 crisis were overwhelmed in a short period and banking sector grew about 18% on dollar basis annually in the period after 1995. However, the serious narrowing in Turkish economy due to the crises of the Far East and Russia in this period as well as the earthquake experienced in 1999, had a negative impact on the banking sector.

### ***November 2000-February 2001 Crises and Their Effects On Banking Sector***

Turkey adopted a comprehensive disinflation program at the beginning of 2000. The main pillars of the program were tight fiscal and monetary policies, ambitious structural reforms and the use of a pre-determined exchange rate path as a nominal anchor. Monetary policy was conducted under a currency board type arrangement with liquidity expansion being strictly linked to foreign currency inflows.

The disinflation program had a major impact on banks' balance sheets. First and foremost, with the initial sharp decline in market interest rates and the expectation of further fall in these rates, the banks also reduced deposit and lending rates. The banks also increased their exposure to fixed rate treasury securities during this period. On the other hand, the pre-announced exchange rate path and the real appreciation of the Turkish lira meant lower cost of funding for foreign currency liabilities. As a result, a number of banks borrowed in short-term foreign currency terms and lent in longer term Turkish lira terms. This led to a sharp increase in maturity mismatch and foreign currency open position of the private banks.

The composition of the asset structure of the banking sector changed significantly in 2000 with an increase in the share of loans and a decline in liquid assets. Especially consumer credits four folded during 2000. Unlike the change in the currency composition of deposits (towards an increase in foreign currency deposits) the currency composition of loans increased in favor of the Turkish lira. As a result of these changes, the exposure of the banking sector to liquidity, interest rate and exchange rate risks increased during 2000.

The subsequent November 2000 crisis led to a significant erosion of the capital base of the banking sector and revealed further the fragility of the system. In particular, the financial health of the state and SDIF banks that relied heavily on overnight funding deteriorated sharply.

The rapid announcement of the additional USD7.5bn under the Supplementary Reserve Facility of the IMF in December 2000 could only calm the market for a limited period. The escalating political uncertainties and the loss of credibility of the exchange rate regime and finally the abolition of the exchange rate peg in February 2001 further hit the already weak banking sector.

In sum, the banks were hit by three main shocks:

- Sharp increase in funding costs due to the increase in interest rates and maturity mismatch.
- Capital losses due to a sharp mark-to-market decline in the value of government securities holdings
- Capital losses due to a sharp change in foreign exchange rate and open foreign currency position.

The crises experienced led to a serious contraction in the private sector which, in turn, exerted an adverse impact on the asset quality of the banking sector and increased the credit risk of banks.

In consequence, the government adopted a new program "Transition to a Strong Economy" in order to eliminate the confidence crisis and financial instability. The

strategy is strongly based on market-orientation and openness to the world economy. An important pillar of the program consists of a renewed effort to eliminate structural weaknesses that had not been fully tackled by the 2000 program, particularly by strengthening governance and good economic management. The key elements in the area of banking include: a deep financial restructuring of state and SDIF banks; measures to facilitate the participation of private capital in the strengthening of the private banking system; and, a further improvement of banking regulation and supervision. In this context, the underlying strategy of the BRSA towards establishing a sound banking sector and the action plan for the restructuring of the banking sector are outlined in the next two sections.

## 2. MAIN GOALS AND STRATEGY OF THE BANKING REGULATION AND SUPERVISION AGENCY

The **mission** of the Banking Regulation and Supervision Agency is to create the proper environment in which banks and financial institutions can operate with market discipline, and in a healthy, efficient and globally competitive manner. The creation of a sound banking system is key to achieve long-run economic growth and stability of the country.

In order to fulfill its mission BRSA aims to establish, implement and develop the necessary regulatory and supervisory framework. In this framework, the main goals of the BRSA are:

- *To enhance banking sector efficiency and competitiveness*– elimination of distortions created by the state banks; strengthening of the banks’ capital base; reduction of the banks’ intermediation costs; minimization of group banking and non-financial activities.
- *To maintain confidence in the banking sector* – in accordance with market discipline and “self responsibility” principle, to design the proper regulation for public awareness; making adequate, understandable and accurate information accessible to the markets in a timely manner; promoting international best standards in accounting and reporting systems; providing a transparent environment in which information on risks is clear and accessible for all parties.
- *To minimize the potential risks to the economy from the banking sector* – prevention of all kinds of transactions and practices that can jeopardize the smooth and safe operation of the banks; developing early warning and prompt correction systems to prevent individual problems from causing systemic risk.
- *To enhance the soundness of the banking sector* - enhancing the flexibility of the sector against risks; giving importance to the improvement of corporate governance; developing internal control and risk management systems; taking market risk into account in calculation of capital adequacy; improving the BRSA’s capacity for risk-focused and consolidated supervision and control.
- *To protect the rights of the depositors* - establishing a balance between the adverse effects of deposit insurance, such as erosion in market discipline and increase in moral hazard, and the need to protect the rights of depositors.

In order to fulfill these goals the main values that the BRSA needs to establish are the following:

- *Cost Effectiveness:* Regulatory and supervisory practices shall be carried out regarding cost/benefit approach; and regulation and supervision activities shall be conducted in order to promote competitiveness of the banking sector.
- *Approach Based on Internal Accountability:* Even if regulatory and supervisory function is carried out at optimum, this function cannot go beyond being a secondary means for ensuring soundness and efficiency of the banking sector. The primary means is market discipline. An approach, which emphasizes internal accountability, such as improvement of internal control mechanisms and use of independent auditing/rating institutions shall be adopted.
- *Impartiality:* The BRSA shall equally treat all institutions that operate in its scope, and fulfill its responsibilities with care and impartiality.
- *Responsiveness:* The BRSA shall adapt itself to policies and practices necessitated by the developments in national and international financial system in a rapid and effective manner, and work with other public institutions in harmony.
- *Participation:* During the formulation of regulations and direction of practices, importance shall be given to the participation of banks, customers and the professional associations in the sector and academicians; communication channels shall be kept open.
- *Transparency and Accountability:* In order to make the BRSA operate in a transparent manner public and the relevant public agencies shall be informed about the operations and operation results.
- *Consumer Focus:* Besides the service for financial institutions, a service approach focused on consumer demand and needs shall be placed in the structure of the BRSA. For this purpose, a “consumer relations unit” shall be established within the BRSA; and a “consumer affairs page” shall be maintained on the BRSA’s Internet site. With these two services, the BRSA shall make the consumers conscious of financial services, and it shall review its regulations and policies in the light of suggestions and complaints from the consumers.
- *International Cooperation:* The Agency shall be in a close cooperation with foreign regulatory and supervisory agencies and international organizations in order to follow rapid change and developments in financial markets, to achieve an effective supervision on banks on a consolidated basis, and to get information relating to potential investors in the sector.
- *Expertise and Efficient Organizational Structure:* In order to develop the expertise necessitated by changes in financial sector, the BRSA will give importance to employment of personnel with analytical capability and professionalism, and review its organization structure in accordance with the developments in financial activities and information technology.

- *Performance Assessment:* The BRSA shall conduct public opinion surveys, effectiveness surveys and employee surveys in order to assess public opinion about the performance of the BRSA.

### 3. DEVELOPMENTS REALIZED WITHIN THE RESTRUCTURING PROGRAM

#### 3.1. Restructuring of State-Owned Banks\*

In 2001, financial restructuring of state-owned banks was completed and significant steps were taken regarding operational restructuring.

**Restructuring of state-owned banks has been carried out with the ultimate aim of privatizing these banks.**

Within this framework, the priority regarding restructuring of state-owned banks has been given to strengthening the financial structures of the banks in question. Simultaneously with strengthening the financial structure, operational restructuring studies have also been initialized. Within the restructuring process, the management of the banks in question have been transferred to Common Board of Directors as the first step and the Board has been granted the authority of restructuring and preparing the state-owned banks for privatization.

##### *3.1.1. Financial Restructuring*

Financial restructuring of the state banks concentrated on; (1) liquidation of duty losses; (2) elimination of short term liabilities; (3) strengthening of capital base; (4) determination of deposits rates in line with the market rates, and (5) efficient management of loan portfolio.

##### *Liquidation of the Duty Losses*

- State banks' claims on Treasury arising from the subsidizing lending (duty losses) and the interest accrued to these loans were securitized in 2001. The Treasury supplied special issue government bonds of TL 23 quadrillion in 2001 to securitize the state banks' receivables from the government.

- A number of regulations (around 100 Council of Ministers' Decrees and/or Laws) that allowed subsidized lending through state banks (creating duty losses) were annulled in order to prevent generation of new duty losses.

- The practice of appropriating in the central budget the resources required for government supports to be provided through state-owned banks and transferring these funds to the banks in question in advance has been initialized.

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\* Information in this section consist of Ziraat, Halk and Emlak banks.

### Resources Transferred for the Restructuring of State Banks

Duty Loss receivables of state banks from the Treasury began to generate in 1999 and reached TL 17,3 quadrillion as of end 2000. TL 2,1 quadrillion of this amount was securitized, while the remaining TL 15,2 quadrillion consisted of unsecuritized duty loss receivables. Unsecuritized duty loss receivables and all interest accrued on them have been securitized in 2001 through granting special issue government bonds amounting to TL 23 quadrillion.

Also, within year 2001, an additional support has been given to state banks in order to strengthen their capitals. Within this scope, in-cash capital injections have been made, amounting to TL 217,6 trillion to Ziraat Bankasi in March, TL 67,2 trillion and TL 40,8 trillion in April respectively to Halk Bankasi and Emlak Bankasi. In addition, government securities have been granted to Emlak Bankasi amounting TL 624 trillion and to Halk Bankasi amounting TL 900 trillion in May on their capital. The TL 1,7 quadrillion cost generated in July from the transfer of Emlak Bankasi to Ziraat Bankasi has been covered by giving-out special issue government bonds to Ziraat Bankasi.

The overall total resources transferred to state banks with the aim of tying the duty loss receivables to securities and providing capital support amounted TL 28,6 quadrillion.<sup>1</sup>

#### Resources Transferred to State Banks (TL Trillion)

	Inventory as of December 2000 (1)	Increase in year 2001 (net) (2)	Total (1)+(2)
<b>Liability Generated from Duty Loss</b>	<b>17.279</b>	<b>7.759</b>	<b>25.038</b>
-Tied to Securities	2.083	22.955	25.038
-Ziraat Bankasi	1.220	12.113	13.333
-Halk Bankasi	863	10.797	11.660
-Emlak Bankasi	0	45	45
-Untied	15.196	-15.196	0
<b>Capital Support (Subordinated Debt)</b>	<b>-</b>	<b>3.224</b>	<b>3.224</b>
-Ziraat Bankasi	-	1.700	1.700
-Halk Bankasi	-	900	900
-Emlak Bankasi	-	624	624
<b>Capital Support (Cash Injection)</b>	<b>-</b>	<b>326</b>	<b>326</b>
-Ziraat Bankasi	-	218	218
-Halk Bankasi	-	67	67
-Emlak Bankasi	-	41	41
<b>Total</b>	<b>17.279</b>	<b>11.309</b>	<b>28.588</b>

Resource: Treasury, BRS.A.

1. While unsecuritized duty loss receivables amounting to TL 15,2 quadrillion as of end 2002 were not mentioned in debt stock data, the amount was included within debt stock in the publications of the International Monetary Fund. When evaluated from this view, the real increase in public debt stock within year 2001 due to the restructuring of state banks is approximately TL 11,3 quadrillion.

### Reducing Short Term Liabilities

- State banks provided liquidity through outright sale of government securities or repo transactions made with the Central Bank (CBRT) and eliminated their short-term liabilities to the private banks and clients which was around TL 8,5 quadrillion as of March 16, 2001.

**Table 2: Short Term Liabilities of State Banks**

	TL Quadrillion		% Share	
	March 16, 2001	July 9, 2002	March 16, 2001	July 9, 2002
<b>1. Central Bank</b>	<b>5,5</b>	<b>0,0</b>	<b>39,3</b>	<b>0,0</b>
- Open Market Operations	5,5	0,0	39,3	0,0
Total Repurchase Agreements	5,5	0,0	39,3	0,0
O/N Repurchase Agreements	0,2	0,0	1,4	0,0
Long Term Repurchase Agreements	5,3	0,0	37,9	0,0
- Interbank Market (O/N)	<b>0,0</b>	<b>0,0</b>	0,0	0,0
<b>2. Private Banks+ Customer Repurchase Agreements and O/N Deposits</b>	<b>8,5</b>	<b>0,0</b>	<b>60,7</b>	<b>0,0</b>
<b>Private Banks(O/N)</b>	<b>4,2</b>	<b>0,0</b>	<b>30,0</b>	<b>0,0</b>
- CBRT Interbank Market	0,4	0,0	2,9	0,0
- Interbank Money Market	1,9	0,0	13,6	0,0
- ISE Repurchase Agreements Market	1,9	0,0	13,6	0,0
<b>Customer Repurchase Agreements and O/N Deposits</b>	<b>4,3</b>	<b>0,0</b>	<b>30,7</b>	<b>0,0</b>
<b>Total</b>	<b>14,0</b>	<b>0,0</b>	<b>100,0</b>	<b>0,0</b>

Source: CBRT

- In order to reduce maturity mismatch and liquidity risk, minimum maturity on repo transactions with clients and institutional investors has been extended to a week or longer.
- The Treasury contributed to the stabilization of liquidity position and cash inflow of state banks through early redemption of government securities. This in turn helped to ease the pressure on short term borrowing market arising from the liquidity needs of the state banks.

### ***Strengthening the Capital Structure***

- Since March 2001, Treasury injected securities and cash to state banks in order to strengthen their capital base. Hence, paid-in capital of the state banks rose from TL 477 trillion in December 2000 to TL 3.4 quadrillion in December 2001, while shareholders' equity rose from TL 712 trillion to TL 4.1 quadrillion during the same period.

**Table 3: Own Funds of State Banks(\*)**

TL Trillion	December 2000	December 2001	May 2002
<b>Ziraat Bank</b>			
-Paid-in capital	261	2.222	2.222
-Reserves +FARF +SRF	180	470	596
-Profit/Loss	65	543	-6
Total Equity	506	3.235	2.812
<b>Halk Bankasi</b>			
-Paid-in capital	145	1.150	1.150
-Reserves +FARF +SRF	171	249	298
-Profit/Loss	5	-570	191
Total Equity	321	829	1.639
<b>Emlak Bankasi</b>			
-Paid-in capital	70		
-Reserves +FARF +SRF	121		
-Profit/Loss	-305		
Total Equity	-114		
<b>STATE BANKS (Total)</b>			
-Paid-in capital	477	3.372	3.372
-Reserves +FARF +SRF	472	719	894
-Profit/Loss	-235	-27	185
Total Equity	713	4.064	4.451

Source: BRS/A, Joint Board of Directors of State Banks

(\*) Previous Years' profit/loss is not included to the total own funds amount.

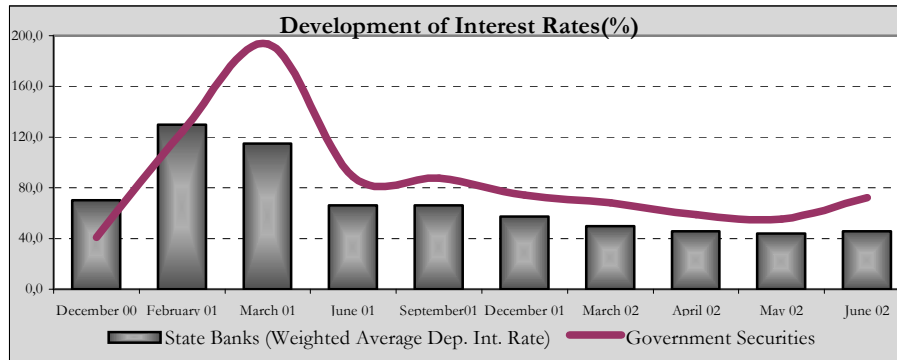
(\*\*) Emlak Bank has been transferred to Ziraat Bank in July 9, 2001

FARF: Fixed Assets Revaluation Fund, SRF: Securities Revaluation Fund.

- Despite the sharp increase in non-performing loans, the capital adequacy ratio of state banks improved considerably in 2001. This improvement was due to the capital injections as well as the increase in the share of government securities, which has zero credit risk weight in the calculation of CAR, in the total assets of the state banks.

### ***Determination of Deposit Rates in Line with the Market Rates and Efficient Management of Loan Portfolio***

- State banks' deposit interest rates have been determined uniformly and below the interest rates of the government securities.
- Significant reduction in the short term liabilities and strengthening of capital base have contributed to the elimination of distortions created by the state banks in the deposit market and the deposit interests of the banks in subject showed a development parallel to the decrease in general interest rates.



Note: As there is no auction in December 2000, November auction rates used instead.

- In accordance with the principles of efficiency and productivity, state banks were enabled to determine all their loan interest rates by taking the resource costs into account.

- State banks have become more prudent about identifying problem loans and reserving appropriate provisions for such loans, which in turn resulted in a more transparent balance sheet. With a more adequate classification, non-performing loans of state banks rose to TL 3,680 trillion in May 2002 from TL 1,017 trillion in end-2000, while provisions for non-performing loans increased to TL 2.605 trillion from TL 296 trillion during the same period.

### 3.1.1. Operational Restructuring

Operational restructuring of state banks aims at restructuring of these banks in terms of organization, technology, human resources, financial control, planning, risk management and service quality so that they could operate according to the requirements of the modern banking and international competition. Developments regarding these issues are summarized below:

- State banks are organized in a pyramid structure where the Board of Directors are at the top with 5 sub-departments including non-branch profit centers, marketing, operations, loans and risk management and control, under this Board.
- The banking and deposit taking licenses of Emlak Bank were revoked and the bank was transferred to Ziraat Bank. The number of branches which was 2.494 as of December 2000 was brought down to 1.792 by May 2002, while the number of personnel was reduced to 38.303 from 61.601 in the same period.

**Table 4: Number of Branches and Employees**

	Dec. 2000	March 2001	June 2001	Sept. 2001	Dec. 2001	March 2002	May 2002
<b>Number of Employees</b>	<b>61.601</b>	<b>59.831</b>	<b>51.975</b>	<b>48.511</b>	<b>47.985</b>	<b>43.907</b>	<b>38.303</b>
-Ziraat Bankasi	36.576	35.334	29.903	35.565	33.023	29.173	23.993
-Halk Bankasi	10.000	14.699	13.207	12.946	14.962	14.734	14.310
-Emlak Bankasi	15.025	9.798	8.865	-	-	-	-
<b>Number of Branches</b>	<b>2.494</b>	<b>2.488</b>	<b>2.476</b>	<b>2.418</b>	<b>2.398</b>	<b>2.052</b>	<b>1.792</b>
-Ziraat Bankasi	1.287	1.281	1.270	1.615	1.499	1.383	1.233
-Halk Bankasi	804	804	803	803	899	669	559
-Emlak Bankasi	403	403	403	-	-	-	-

Source: BRSA, Joint Board of Directors of State Banks

- A program has been set up to monitor the profit and loss accounts, liquidity position and interest rate spreads of the state banks. Hence, the assets' yield and liabilities' cost can be monitored on a weekly basis, while balance sheets and income statements of the branches are monitored on a daily basis.

### 3.1.2. Developments in the Balance Sheet and Profitability Performance of State Banks

• **Positive impact of financial and operational restructuring was already reflected in profitability performance of the state banks in 2001.** Total losses of Ziraat Bank and Emlak Bank, which was TL 598 trillion in April, turned to a profit of TL 543 trillion in December 2001. During the same period, the loss of Halk Bankasi declined to TL 570 trillion from TL 740 trillion.

Ziraat Bankasi, which made a TL 640 trillion profit in the first quarter of 2002, has generated TL 6 trillion loss as of May 2002 due to the effects of the provisions set aside for agricultural loans. The fact that evaluation of the Banks' securities portfolio, which consisted of long term papers, with respect to the Code of Tax Procedure resulted in a high tax provision contributed to this outcome. By the profit generated by Halk Bankasi in end-May, the total profit of state banks has become TL 185 trillion in the same period.

**Table 5: Profits and Losses of State Banks**

(TL Trillion)	2001										2002(*)				
	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.	Jan.	Feb.	March	Apr.	May.	
Ziraat Bankasi	-279	459	225	255	118	215	349	438	526	625	606	640	63	-6	
Emlak Bankasi	-319	-331	-425	-	-	-	-	-	-	-	-	-	-	-	
Ziraat+Emlak Bankasi	-598	128	-201	255	118	215	349	438	526	625	606	639	63	-6	
Halk Bankasi	-740	-576	-759	-703	-674	-627	-562	-496	-581	49	92	142	135	191	
<b>Total</b>	<b>-1.338</b>	<b>-448</b>	<b>-960</b>	<b>-448</b>	<b>-555</b>	<b>-412</b>	<b>-213</b>	<b>-58</b>	<b>-55</b>	<b>674</b>	<b>698</b>	<b>781</b>	<b>198</b>	<b>185</b>	

Source: BRSA, JBDST

(\*) Temporary figures.

**Table 6: Consolidated Balance Sheet of State Banks**

(TL Trillion)	Dec. 2000	Dec. 2001	May 2002 (*)	% Share		
				Dec. 2000	Dec. 2001	May 2002
<b>Assets</b>						
-Cash & Claims on Banks	2.555	4.760	4.475	8,3	10,7	9,2
-Securities Portfolio	1.759	25.746	31.027	5,7	57,8	64,1
-Loans	6.525	5.453	4.926	21,2	12,2	10,2
-Loans under Follow-Up (Net)	722	1.065	1.075	2,3	2,4	2,2
-Loans under Follow-Up (Gross)	1.017	3.365	3.680	3,3	7,5	7,6
-Provisions for Loans under Follow-Up (-)	296	2.301	2.605	1,0	5,2	5,4
-Duty Losses	15.196	-	-	49,3	0,0	-
-Other Assets	4.061	7.554	6.883	13,2	16,9	14,2
<b>Liabilities</b>						
-Deposits	20.234	30.351	33.151	65,7	68,1	68,5
-Borrowings from Banks	4.612	3.561	3.369	15,0	8,0	7,0
-Other Liabilities	5.258	6.599	7.415	17,1	14,8	15,3
-Shareholder's Equity	712	4.065	4.451	2,3	9,1	9,2
<b>Balance Sheet Total</b>	<b>30.817</b>	<b>44.576</b>	<b>48.386</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>

Source: BRSA, JBDST(\*) Temporary figures.

Note: Consolidated balance sheets of Ziraat, Halk and Emlak Bankasi

### Regulations Regarding State Banks

- The legal framework concerning the restructuring of state banks has been established with the “Act No: 4603 on Ziraat, Halk and Emlak Bank” published in the Official Gazette dated November 15, 2000.
- With the Act No: 4743 published on January 31, 2002, some additional regulations on state banks have been put into force. In summary:
  - √ State banks shall not employ personnel who are not subject to provisions of private law after December 12, 2002.
  - √ Within the scope of restructuring of state banks, 20 percent addition to retirement bonuses has been provided in order to encourage early retirement.
  - √ Members of the Board of Directors, Board of Auditors and Board of Liquidation will not be deemed as civil servants from the standpoint of the criminal law and administrative law, and their legal liabilities will be subject to the legislation and provisions applied to the private banks operating in the banking sector.
  - √ Members of the Board of Directors, Board of Auditors and Board of Liquidation of Ziraat Bank, Halk Bank and Emlak Bank Under Liquidation are authorized to restructure loans extended before February 31, 2002 (loans extended to artisans and craftsman, small and middle sized enterprises, and agricultural loans). Also, it has been foreseen that Emlak Bank Under Liquidation may participate the debt restructuring process but is not to provide any additional financing.
  - √ Ziraat Bank and Halk Bank are required to extend an additional loan of at least 1.5 quadrillion TL from their own resources to the agricultural sector, tradesmen and artisans, small and medium sized enterprises and exporters. Additional loan will be extended in accordance with prudent banking procedures.

### 3.2. The Restructuring of the SDIF Banks

The strategy for the restructuring of SDIF banks embodies the following four major components: (1) the resolution of the SDIF banks through merger, transfer, sale or liquidation (2) financial restructuring (3) operational restructuring and (4) management of the assets of the SDIF banks.

#### 3.2.1. Resolution of SDIF Banks By Merger, Acquisition, Sale or Liquidation

Within the period of 1997-2002, 20 banks were transferred to the SDIF. The immediate resolution of the banks in subject constituted an important part of the banking sector restructuring program.

Of 20 banks taken over by the SDIF, 5 banks (Egebank, Yurtbank, Yasarbank, Bank Kapital and Ulusal Bank) were merged under Sumerbank, 2 banks (Interbank and Esbank) under Etibank, and 1 bank (EGS Bank) under Bayindirbank.

Sale of four SDIF banks (Bank Ekspres, (joint)Sumerbank, Demirbank and Sitebank) to foreign investors were completed.

Banking licenses of Iktisat Bank, Etibank and Kentbank were revoked and the banks in subject were merged under Bayindirbank.

Banking and deposit accepting licenses of T. Ticaret Bank was revoked on July 01, 2001. The Council of State's General Assembly of Administrative Lawsuit Departments made a ruling that halted the execution of the process but this was refused by the 10<sup>th</sup> Department of the Council of State.

Tarisbank was put up for sale on May 30, 2002. However, as the financial strength of the investors interested in the bank were deemed insufficient they were not allowed to perform due diligence in the bank.

The sale process of Toprakbank was initiated on January 30, 2002. However the offer given by the consortium composed by local and foreign investors was deemed insufficient and the bank in subject was re-offered to sale on May 13, 2002. Two investors have been given the permission to carry out due-diligence, one of which submitted its offer on July 5, 2002. The offer is being evaluated.

The sale process of Pamukbank which was taken over by the SDIF was initiated on June 29, 2002. The investors concerned shall apply until July 19, 2002 and submit their offers by October 4, 2002.

As regards Bayindirbank, the plan is to restructure it as a bridge bank.

**Table 7: The Restructuring Process of the SDIF Banks**

	1997	1998	1999	2000	2001	As of July 15, 2002	Total
Number of Banks Taken Over	1	1	6	3	8	1	20
Number of Merged Banks	-	-	-	-	7	1	8
Number of Sold Banks	-	-	-	-	3	1	4
Number of Banks, Licenses of which were Revoked	-	-	-	-	3	-	3
<b>Number of Fund Banks</b>	<b>1</b>	<b>2</b>	<b>8</b>	<b>11</b>	<b>6</b>	<b>5</b>	<b>5</b>

Source: BRSA

**Table 8: List of Banks Transferred to the SDIF**

Banks	Date of Transfer to the Fund	Current Situation
<b>Sold Banks</b>		
Sumerbank	December 22, 1999	Merged Sumerbank was sold to the OYAK Group on August 9, 2001. Merger of Sumerbank and Oyakbank was approved on January 11, 2002.
-Egebank	December 22, 1999	-Merged into Sumerbank on January 26, 2001.
-Yurtbank	December 22, 1999	-Merged into Sumerbank on January 26, 2001.
-Yasarbank	December 22, 1999	-Merged into Sumerbank on January 26, 2001.
-Bank Kapital	October 27, 2000	-Merged into Sumerbank on January 26, 2001.
-Ulusal Bank	February 27, 2001	-Merged into Sumerbank on April 17, 2001.
Bank Ekspres	December 12, 1998	Sold to the Tekfen Holding on June 30, 2001. Approval of the transfer was made on October 10, 2001. Operating as Tekfenbank A.S.
Demirbank	December 6, 2000	Sold to HSBC on September 20, 2001. Approval of the transfer was made on October 30, 2001. Operating as HSBC Bank.
Sitebank	July 9, 2001	A share transfer agreement was signed with Novabank on January 11, 2002. The transfer procedure was carried out on January 16, 2002.
<b>License Withdrawals</b>		
Etibank	October 27, 2000	Banking and deposit taking license of the bank was revoked as of December 28, 2001 and the liquidation process has been initiated. <sup>(1)</sup>
-Interbank	January 7, 1999	-Merged into Etibank on June 15, 2001
-Esbank	December 22, 1999	-Merged into Etibank on June 15, 2001.
Iktisat Bank	March 15, 2001	Banking and deposit taking license was revoked as of December 7, 2001 and the liquidation process has been initiated. <sup>(1)</sup>
Kentbank	July 9, 2001	Banking and deposit taking license was revoked as of December 28, 2001 and the liquidation process has been initiated. <sup>(1)</sup>
<b>SDIF Banks</b>		
T. Ticaret Bank	November 6, 1997	Banking and deposit taking license of the bank was revoked as of July 1, 2001. A ruling was made by the Council of State's General Assembly of Administrative Lawsuit Departments suspending the execution but it was dismissed by decision rendered by the 10 <sup>th</sup> Department of the Council of State
Bayindirbank	July 9, 2001	Being re-structured as a bridge bank to focus on asset management.
EGS Bank	July 9, 2001	-Banking and deposit taking license was revoked as of January 18, 2002. Merged into Bayindirbank.
Tarisbank	July 9, 2001	Tarisbank was offered to sale on May 30, 2002. However, as the financial strength of the investors were deemed insufficient, their due diligence has not been deemed appropriate.
Toprakbank	November 30, 2001	The sale process of Toprakbank was initiated on January 30, 2002, the offer given by an investor group has been deemed insufficient and the bank has been re-offered to sale. An offer made by an investor group is being evaluated.
Pamukbank	June 19, 2002	The sale process of Pamukbank was initiated on June 29, 2002. The investors concerned shall apply until July 19, 2002.

Source: BRS.A

(1) In the General Meeting held on April 4, 2002 within the framework of the decisions dated March 20, 2002 No: 653 of the BRS.A and March 20, 2002 No: 177 of the SDIF, it has been decided to cancel the liquidation and merge these banks under Bayindirbank.

### **3.2.2. Financial Restructuring**

#### **Government Securities Issued to SDIF by Treasury and Capital and Deposit Support from SDIF Sources**

Within the borrowing agreements made with the SDIF, the Treasury issued government securities a number of times since December 2000 in order to strengthen the capital structures and balance sheets of the banks taken over by the SDIF.

Using the conversion rates of December 31, 2002, the TL equivalents of F/X denominated and F/X based securities issued by the Treasury within the borrowing agreements made with the SDIF amounts to TL 21,6 quadrillion.

**Table 9: Resources Transferred to the SDIF by the Treasury**

(As of December 31 <sup>st</sup> , 2001)	TL Denominated (TL Trillion)	Dolar Denominated and Dolar Based (USD Million)	Euro Denominated and Euro Based (EUR Million)	Total (TL Trillion)
Government Securities issued to the SDIF	8.492	8.297	897	21.581

Source: Undersecretariat of Treasury

Within the provisions of the agreement made with the Treasury, the SDIF paid back the Treasury TL 378 Trillion on April 3, 2002, TL 357 trillion on May 8, 2002 and TL 265 trillion on May 15, 2002, giving a total amount of TL 1 quadrillion.

A total of TL 2,6 quadrillion capital support has been provided from the SDIF's own resources to the SDIF banks, TL 1,1 quadrillion of which in the form of capital and TL 1.2 quadrillion in the form of deposits. In addition, a subordinated capital support amounting to TL 410 trillion was provided to Banks from the SDIF resources.

**Table 10: Capital and Deposit Support from SDIF Sources**

(As of July 4, 2002)	TL Trillion	USD Million	Gen. Total (TL Trillion)
1. Cash Payment as Capital	1.507	-	1.507
2. Deposited Funds (1)	857	193	1.108
<b>TOTAL</b>	<b>2.364</b>	<b>193</b>	<b>2.615</b>

Source: BRSA

(1) The advances totaling TL 750 trillion received from CBRT against Special Issue Securities were deposited in to SDIF Banks. When this amount included in the securities issued by Treasury is added, deposited funds become TL 1,858 trillion. When subordinated capital amounting to TL 410 trillion granted to Pamukbank from the Fund's own resources is included, the capital support amounts to TL 1.917 trillion.

### *Elimination of Short-Term Liabilities*

- SDIF banks eliminated their short term liabilities to clients and private banks by using the funds generated through out-right sale of TL 5.2 quadrillion special issue bonds to Central Bank as of March 16, 2001. Also, short term liabilities of the SDIF banks to the Central Bank were eliminated in 2002.

**Table 11: Short Term Liabilities of the SDIF Banks**

	TL Quadrillion			% Share		
	March 16- 2001	May 4, 2001	July 9, 2002	March 16- 2001	May 4, 2001	July 9 <sup>h</sup> , 2002
<b>Central Bank</b>	<b>2,6</b>	<b>5,6</b>	<b>-0,3</b>	<b>33,3</b>	<b>87,5</b>	<b>100,0</b>
- Open Market Operations	2,6	5,6	0,0	33,3	87,5	0,0
Overnight Repo	0,3	0,0	0,0	3,8	0,0	0,0
Longer Term Repo	2,3	5,6	0,0	29,5	87,5	0,0
- Interbank Market (O/N)	0,0	0,0	-0,3	0,0	0,0	100,0
<b>Private Banks (O/N)</b>	<b>1,7</b>	<b>0,0</b>	<b>0,0</b>	<b>21,8</b>	<b>0,0</b>	<b>0,0</b>
- Interbank Market within CBRT	0,3	-0,1	0,0	3,8	-1,6	0,0
- Interbank Money Market	0,3	0,0	0,0	3,8	0,0	0,0
- ISE Repo Market	1,1	0,1	0,0	14,2	1,6	0,0
<b>Customer Repos and O/N Deposits</b>	<b>3,5</b>	<b>0,8</b>	<b>0,0</b>	<b>44,9</b>	<b>12,5</b>	<b>0,0</b>
<b>Overall Total</b>	<b>7,8</b>	<b>6,4</b>	<b>-0,3</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>

Source: CBRT, BRSA

### *Closing of F/X Open Positions*

- Open F/X positions of SDIF banks, which were around USD 4-5 billion prior to May 2001, decreased substantially as a result of the injection of F/X indexed bonds during the second half of May 2001 and became USD 561 million as of end-June, 2001. Due to inclusion of the net open positions of 5 banks intervened

in July, SDIF banks' net F/X open position rose to USD 1.1 billion during July-November period, but then decreased to USD 408 million by January 18, 2002. With the transfer of Pamukbank to the Fund in June the on-balance sheet open positions have increased, however the net open position amount then decreased to USD 209 million due to the increase of USD 746 million in forward positions.

**Table 12: Foreign Exchange Positions of the SDIF Banks**

(USD Million)	April 13, 2001	May 18, 2001	June 29, 2001	Aug. 31, 2001	Dec. 28, 2001	June 21, 2002
1. On-Balance Sheet F/X Position	-4.812	-2.764	-3.894	-3.673	-1.197	-1.373
2 F/X Indexed Position	630	2.233	3.383	2.490	748	418
<b>3. On-Balance Sheet F/X Position (1+2)</b>	<b>-4.182</b>	<b>-531</b>	<b>-511</b>	<b>-1.183</b>	<b>-449</b>	<b>-955</b>
4. Forward Position	-132	-116	-50	66	0	746
<b>5. Net General F/X Position (3+4)</b>	<b>-4.314</b>	<b>-647</b>	<b>-561</b>	<b>-1.117</b>	<b>-449</b>	<b>-209</b>

Source: BRSA

### *Bringing of Deposit Rates in Line with the Market Rates*

- SDIF banks' deposit interest rates were determined uniformly and below the interest rates on government securities, and brought down to the market level since March 2001.

### *Sale of Deposits to Other Banks*

- An important portion of the SDIF Banks' deposits were sold to other banks through a series of auctions, backed by matching government securities portfolios. Auctions were realized with separated bidding process for TL and F/X deposits pools in 5 stages. As a result of these auctions, TL 479 trillion in Turkish Lira and USD 2,587 million in F/X denominated deposits were transferred to 8 private banks.

**Table 13: Sale of SDIF Banks' Deposits**

	TL Deposits (TL Trillion)	F/X Deposits (USD Million)
1 <sup>st</sup> Stage	193.3	233.0
2 <sup>nd</sup> Stage	-	692.6
3 <sup>rd</sup> Stage	-	687.9
4 <sup>th</sup> Stage	-	409.5
5 <sup>th</sup> Stage	285.5	563.0
<b>Total</b>	<b>478.8</b>	<b>2,586.8</b>
Iktisat Bankasi	85.4	121.4
EGS Bank	36.7	111.6
Etibank	353.7	1,181.9
Kentbank	-	1,171.9

Source: SDIF

### **3.2.3. Operational Restructuring**

#### *Reducing the Number of Branches and Personnel*

- The number of branches of SDIF banks was brought down from 1,815 at the date of transfer to 873 by June 30, 2002. Excluding the sold banks, the number of branches decreased by 659 and fell to 519 from 1,178 during the same period.
- The number of personnel of Fund banks has been brought down to 18,134 through a 52,1% reduction(19,755 persons) by June 30, 2002 when compared to the dates of transfer. Excluding the sold banks, the personnel number of SDIF banks was brought down to 10,607 as of end-June, 2002 from a level of 23,317 as of the transfer date, constituting a 54,5% reduction.

**Table 14: Number of Branches and Employees of SDIF Banks (\*)**

Banks	Number of Branches (*)			Number of Employees (*)		
	As of Transfer Date	Dec. 31, 2001	June 30, 2002	As of Transfer Date	Dec. 31, 2001	June 30, 2002
Bayindirbank	22	16	10	381	414	581
EGS Bank	49	13	-	918	409	-
Etibank	283	159	-	6.171	2.734	-
Iktisat Bankası	62	62	-	1.305	1.177	-
Kentbank	86	44	-	1.422	961	-
Milli Aydın Bankası	41	41	33	528	526	451
T.Ticaret Bank	274	168	150	4.790	2.439	2.298
Toprakbank	165	165	130	2.482	2.458	1.982
Pamukbank	196	196	196	5.320	5.320	5.295
<b>Sub Total 1</b>	<b>1.178</b>	<b>864</b>	<b>519</b>	<b>23.317</b>	<b>16.438</b>	<b>10.607</b>
<b>Sold Banks</b>						
Sumerbank	401	135	135	9.357	3.198	3.198
Bank Express	25	26	26	721	618	618
Sitebank	13	5	5	253	146	146
Demirbank	198	188	188	4.241	3.565	3.565
<b>Sub Total 2</b>	<b>637</b>	<b>354</b>	<b>354</b>	<b>14.572</b>	<b>7.527</b>	<b>7.527</b>
<b>Total (1+2)</b>	<b>1.815</b>	<b>1.118</b>	<b>873</b>	<b>37.889</b>	<b>23.965</b>	<b>18.134</b>

Source: SDIF

\* The numbers belonging to sold and merged banks under the dates of January 31, 2002 and June 30, 2002 in the table are as of the date these banks are sold or merged.

### ***Sale of Branches***

- A total of 163 branches belonging to Etibank, Kent bank and Iktisat Bank, which are in the liquidation process, was sold to other banks and 1,601 of the personnel have started to work in the buyer banks.

**Table 15: Sale of Branches**

	Number of Sold Branches	Number of Transferred Personnel
Etibank	91	975
Kentbank	46	456
Iktisat Bankası	23	131
EGS Bank	3	39
<b>Total</b>	<b>163</b>	<b>1.601</b>

### ***3.2.4. Asset Management and Collection***

#### ***Transfer of Loan Files Subject to and Not Subject to Follow-Up to the Collection Department***

As of June 30, 2002, a total of 127.951 files, 11.069 of which institutional, 113.307 individual and 3.575 non-loan proceeding files, were transferred to the Collection Department (COD) of the SDIF.

The amount of loans under the follow up taken over from the Fund banks is approximately TL 5,2 quadrillion. Sums of TL 456 trillion and USD 24,8 million were paid to the banks based on the total book value of the loans taken over.

**Table 16 Loan Files Transferred to the SDIF (As of June 30, 2001)**

	Number of Files
Institutional Loans	11.069
Individual Loans	113.307
Non-Loan Proceeding Files	3.575
<b>Total</b>	<b>127.951</b>

Source: BRSA

### ***Cash Inflows Realized by the SDIF***

- A collection of receivables under follow-up of the SDIF banks amounting to TL 1,1 quadrillion has been realized between their date of transfer and June 30, 2002. TL 889,1 trillion of this amount was collected by the Fund banks, and the remaining TL 227,5 trillion by the Collection Department (COD).

**Table 17: Collections Realized from the Receivables under Follow-Up (As of June 30, 2001)**

	<b>TL Trillion</b>
Collections Realized by the COD of the SDIF	227,5
- Institutional Collections	196,9
- Individual Collections	30,6
Collections Realized by the SDIF Banks	889,1
<b>Total Collections</b>	<b>1.116,6</b>

Source: BRS.A

### ***Sale of Subsidiaries, Tangible and Intangible Assets***

- To improve efficiency in realizing the sale of the Fund banks' subsidiaries, and tangible and intangible assets, two new departments-namely the Subsidiaries Department and the Real Estate Department-were established within the SDIF.
- As of June 30, 2002, TL 270,3 trillion was raised from the sale of Fund banks' subsidiaries (including those sale, decisions of which have been made but waiting for the completion of approval procedures).

**Table 18: SDIF's Subsidiary Sales (As of June 30, 2002)**

Number of the Subsidiaries Taken Over by the SDIF	134
Number of the Subsidiaries, Sale Processes of which were Finalized by the SDIF	30
Number of the Subsidiaries, Sale Processes of which Continues	12
Number of the Remaining Subsidiaries under the SDIF	92
Income Generated through the Completed Sales of the Subsidiaries (TL Trillion)	207,6
Expected Income from the Ongoing Sales of Subsidiaries (TL Trillion)	62,8
<b>Total Income (TL Trillion)*</b>	<b>270,3</b>
<b>Total Income (USD Million) **</b>	<b>193,5</b>

Source: BRS.A.

(\*) Besides, TL 30,9 trillion (USD 22,4 million) was generated from the sale of 41 subsidiaries by the SDIF banks themselves.

(\*\*) Calculated by using the exchange rate on the date of collection.

- As of June 30, 2002, the income collected from the sale of SDIF banks' real estates amounted to TL 86,5 trillion.

**Table 19: SDIF's Real Estate Sales (As of June 30, 2002)**

Number of Real Estates Under the Coverage of SDIF's Take Over	2.634
Number of Real Estates sold by the Real Estate Department of the SDIF	116
Income Generated by the Sales Carried Out by the Real Estate Department of the SDIF (TL Trillion)	34,6
Income Generated from the Sales Carried Out by the SDIF Banks (TL Trillion)*	51,9
<b>Total Income (TL Trillion)</b>	<b>86,5</b>
<b>Total Income (USD Million) **</b>	<b>56,2</b>

Source: BRS.A (\*) Besides, an income of TL 23 trillion (USD 16,2Mmillion) was generated from the sale of securities by the SDIF banks.

(\*\*) Calculated by using the exchange rate on the date of collection.

### *Follow-Up and Lawsuits Statistics*

- The number of lawsuits filed by the SDIF for various reasons rose to 157 by July 11, 2002 from that of 80 as of August 16, 2001, while the number of lawsuits filed against the Fund increased from 270 to 626 during the same period. Thus, the number of lawsuits dealt with by the Department of Legal Affairs of the SDIF has increased to 804.

**Table 20: SDIF Follow-Up and Lawsuit Statistics**

Type of Lawsuits	August 16, 2001	December 25, 2001	July 1, 2002
<b>Lawsuits filed by SDIF</b>	<b>80</b>	<b>104</b>	<b>157</b>
-Individual bankruptcy	22	37	64
-Actions of debt (Reimbursement-Indemnification)	7	8	9
-Precautionary measures	12	14	11
-Wealth declaration fails	8	8	15
-Execution proceedings	31	37	55
-Annulment of securities	-	-	1
-Mesne Lawsuits	-	-	2
<b>Lawsuits filed against SDIF</b>	<b>270</b>	<b>307</b>	<b>626</b>
-Lawsuits related to off-shore accounts	206	222	304
-Actions of debt	8	16	81
-Lawsuits concerning stocks	12	18	37
-Action for negative declaration	1	2	3
-Lawsuits related to payment of uninsured deposits	2	2	2
-Lawsuits related to complaints	5	5	5
-Payment orders	9	11	15
-Annulment of transaction	2	5	14
- Cancellation of objection	-	-	4
-Lawsuits related to adjustment on terms of contract	1	1	3
-Lawsuits related to provisional article 3	24	25	33
-Action for recovery	-	-	2
- Premium claims	-	-	2
- Compensation lawsuits	-	-	3
- Real Estate Value Assessment and Cancellation of the Registry Record	-	-	1
- Ceasing of joint ownership	-	-	1
- Lawsuits denounced to the SDIF	-	-	116
<b>Files Transferred to SDIF from banks sold</b>	<b>-</b>	<b>7</b>	<b>21</b>
<b>Overall Total</b>	<b>350</b>	<b>418</b>	<b>804</b>

Source: SDIF

Note: Lawsuits filed for loans are not included. The banks themselves file loan lawsuits; and the legal procedures for the transferred files are carried out by the Collection Department of the SDIF.

### Legal and Institutional Arrangements Regarding SDIF

In 2001, necessary amendments were made in the Banks' Act and new regulations were issued for the organizational structure of the SDIF in order to establish the legal infrastructure to accelerate the follow-up and collection process of SDIF banks' receivables. Along these lines;

- With the Act No.4672, so as to accelerate the follow-up and collection process of receivables of the SDIF, especially regulations aiming rapid collection of the funds misused by the majority shareholders and directors of the bank (Establishing Special Courts, clarification of the enforcement of the Act No.6183 for the collection of Fund receivables) have been issued.
- With the Act No.4743;
  - √ In case all shares of a bank, the management and control of which is transferred to the SDIF, can not be owned by the SDIF following the take over of the bank's losses, the SDIF is authorized to take over those shares by paying the shareholders within the time period to be determined by the Board and on the basis of the value of shares to be found after subtracting the taken over losses from the equity capital.
  - √ Banks, shares of which completely or partially belong to the SDIF are also authorized to participate in the Financial Restructuring Framework Agreements alongside the financial restructuring contracts to be signed with debtors whose debts are restructured or tied to a new redemption plan within the framework of the afore-mentioned agreements.
  - √ The SDIF is authorized to participate in Financial Restructuring Framework Agreements alongside the Financial Restructuring Framework Contracts to be signed in accordance with these agreements on condition that it does not provide any further financing.
  - √ Of the loans and other receivables which were restructured or tied to a new redemption plan, SDIF may defer or settle in installments some of these loans and receivables which are subject to the "Code of Collection Procedures of Public Claims" in accordance with the Financial Restructuring Framework Agreements.
  - √ Certain transactions and contracts made by the SDIF were exempted from all sorts of taxes, duties, fees and fund levies, except the contribution to education levy.
  - √ The SDIF is authorized to take all kinds of measures, with a view to restructure the subsidiaries of the banks under its administration which have economic values including the providence of sources within the framework of the principles and procedures determined by the Board.
  - √ Within two years following the completion of mergers, acquisitions and sales of the SDIF banks, the SDIF may file lawsuits against former auditors and board members of these banks.
  - √ The scope of the SDIF's powers on its claims was re-arranged.
  - √ In case the execution proceedings and any lawsuits, engendered by execution proceedings within which SDIF takes part due to the banks under the scope, result completely or partially against the SDIF, compensations and fines stipulated in the Execution and Bankruptcy Act shall not apply to the SDIF.
  - √ Halt of prescription periods for a certain time (9 months) concerning the execution proceedings and the lawsuits filed or to be filed for debts and commitments undertaken or receivables taken over by the SDIF has been allowed.
- Substantial steps have been taken towards strengthening of the organizational structure of the SDIF. Within this framework;
  - √ Human Resources and Budgeting Department was established under the SDIF in order to perform all kinds of activities concerning workforce and manpower planning along with personnel policy, estimation of all expenses and activities regarding these expenses.
  - √ Internal Auditing Department was established under the SDIF in order to supervise the compliance of the execution of the services by the service units to the Act, resolutions of both the Banking Regulation and Supervision Board and the Board of Directors of the SDIF as well as other existing regulations.
  - √ In order to ensure the management, liquidation, collection and sale of the individual and institutional deferred payments along with subsidiaries and real estates in a rational and income generating manner, and with a view to increase the efficiency and productivity of subsidiaries and Real Estate Departments through re-organization, a consultancy service contract was signed with a private company.
  - √ An "Audit Agreement" was signed between the SDIF and an audit company on 10.01.2002 for independent audit of the balance sheet and the income statements of the SDIF as of 2001 year-end. The report of the independent audit company was announced to the public on 05.05.2002.

### 3.3 STRENGTHENING THE PRIVATE BANKING SYSTEM

Financial structure and profitability of the private banks deteriorated sharply in the aftermath of the crises experienced. Implementation of a program to ensure soundness and sustainability of the private banking system is the remaining most important component of the banking sector restructuring program. **At first stage of the program, measures regarding the recapitalization of private banks, resolving the Non-Performing Loans (NPLs), limitation of F/X open positions and encouragement of mergers and acquisitions have been put into place.** Within this framework;

- In order to solve capital inadequacy problem in banking sector which became evident in the aftermath of the November and February crises and to increase the support of the bank owners and shareholders to capital increases; commitment letters with a time schedule were received from the private banks and accordingly, private banks realized capital increases amounting to TL 2,2 quadrillion as of December 31, 2001. 5 banks which could not fulfill their commitments were taken over by the SDIF in July, 2001.
- High foreign exchange rate fluctuations and increased uncertainty in the aftermath of November and February crises encouraged private banks to close their F/X open positions. With the help of domestic debt swap auctions conducted by the Treasury in June, 2001 private banks managed to close their F/X open positions to a great extent. Indeed, balance sheet F/X open positions decreased from USD 8,4 billion in end-2000 to USD 1,5 billion by the end of 2001. With the positive effects of the take over of Pamukbank by the SDIF, on-balance sheet F/X positions amounted to USD 274 million as of June 21, 2002.

**Table 21: F/X Positions of Private Banks**

USD Million	2001				2002					
	Nov. 2000	19 Feb	June	Dec.	Jan.	Feb.	March	Apr.	May 21	July
On-Balance Sheet Position	-10.674	-8.960	-2.056	-1.487	-1.225	-1.325	-991	-936	-654	274
Forward Position	9.720	7.911	2.196	1.597	1.362	1.384	1.312	1.015	952	4
Net General Position	-954	-1.049	140	110	137	59	321	80	298	279

*Balance Sheet Position: F/X Position (Except Forward Transactions)*

*Net General Position: F/X Net Position (Including Forward Transactions)*

*Source: BRSA*

- Increase in the share of floating rate, F/X indexed and F/X denominated bonds in Treasury's borrowing has also contributed to the limitation of the interest rate risk.

**Table 22: Domestic Debt Stock by Instruments**

	DECEMBER 2000		DECEMBER 2001		JUNE 2002 (provisional)	
	TL Quadrillion	%	TL Quadrillion	%	TL Quadrillion	%
Fixed Rate Notes	20,4	56,0	17,7	14,5	28,4	22,4
Floating Rate Notes	13,0	35,7	60,9	50,0	60,8	47,9
F/X denominated and F/X indexed	3,0	8,2	43,5	35,6	37,7	29,7
<b>Total</b>	36,4	100,0	122,2	100,0	126,8	100,0

*Source: Undersecretariat of the Treasury*

*Note: Indicates the distribution of cash and non-cash bonds. A significant decrease is also observed in the share of fixed rate bonds in total cash stock of bonds, compared to the year-end 2000.*

- Tax incentives were introduced to encourage mergers and acquisitions of banks and their subsidiaries. With the contribution of these incentives, number of mergers and acquisitions have increased in 2001 and 2002.

**Table 23: Mergers and Acquisitions of Banks**

Banks Subject to Merger and Acquisition		New Bank	Explanation
Osmanli Bankasi	Korfezbank	Osmanli Bankasi	The status of Birlesik Turk Korfez Bank was withdrawn and the acquisition of the bank, with all its rights, receivables, debts and liabilities, by Osmanli Bank was realized on 31 August, 2001.
Garanti Bankasi	Osmanli Bankasi	Garanti Bankasi	The Acquisition of Osmanli Bankasi by Garanti Bankasi was realized on December 14, 2001.
HSBC Bank Plc.	Demirbank	HSBC Bank Plc.	The Acquisition of Demirbank by HSBC Bank A.S. was realized on December 14, 2001.
Tekfen Yatirim	Bank Ekspres	Tekfen Bank A.S.	The Acquisition of Bank Ekspres by Tekfen Bank A.S was finalized on October 26, 2001 and its title was changed as Tekfenbank A.S. as of the date of the acquisition.
Oyak Bank	Sumerbank	Oyak Bank	The sale of Sumerbank was finalized on January 11, 2002 and the bank started to operate under the title "Oyakbank A.S."
Morgan Guaranty	The Chase Manhattan	JPMorgan Chase & Co	Merger of the banks was registered on December 14, 2001.
Sinai Yatirim Bankasi	T. Sinai Kalkinma Bankasi	T. Sinai Kalkinma Bankasi	The Acquisition of Sinai Yatirim Bankasi by T. Sinai Kalkinma Bankasi was realized on March 29, .2002.

The impact of the recession in economy in 2001 was more profound than expected and lasted longer, while uncertainties in the global economy under such an environment domestic/foreign investors' hesitation towards the sector became stronger and the possibility to convert tangible assets into cash were extremely limited. These adverse developments led to an increase in capital needs, while also severely constraining the private sector's ability to raise new capital.

In consequence, the need to strengthen the strategy regarding private banks with new instruments became evident. These new instruments are; (1) strengthening of private banks' capital through public support if necessary, (2) resolution of NPL's in banking sector through the Istanbul Approach and establishment of asset management companies. "Act on Restructuring of the Debts to the Financial Sector and Amendments to Be Made to Some Laws", Act No.4743 which established the legal framework and grounds for these instruments was put into force on January 31, 2002.

- As stipulated by the Provisional Article 4 added to the Banks' Act through the above stated amendment, privately owned deposit banks shall go through a three stage audit. Those which satisfy certain conditions can receive a one time support in the form of SDIF's participation in Tier 1 capital or subordinated debt (Tier 2 capital) as necessary<sup>2</sup>.
- **The Act No: 4743 also includes tax incentives to encourage the establishment of asset management companies (AMCs) and arranges the framework for voluntary corporate debt restructuring.**

The SDIF may participate in %20 of an AMC. Within this framework, the SDIF has initiated feasibility activities and action plan thereof has been announced to the public. According to the action plan, operations regarding

<sup>2</sup> Detailed explanations and results of audit and assesment phase of the program have been announced to the public through "Introductory Report" and "Progress Report". These reports are also available in full text at BRSA's web site ([www.bddk.org.tr](http://www.bddk.org.tr)).

the establishment of an asset management company are aimed to be finalized in September, 2002.

- Also, with the Act No. 4743, regulations related to restructuring of debts to financial sector, aiming to help private sector companies which became insolvent due to financial crises continue to operate and re-gain solvency, were issued. Within this framework, restructuring of bank's receivables or tying them to a new redemption plan became possible, in accordance with the "Financial Restructuring Framework Agreements" and through tying these agreements to "Financial Restructuring Contracts" within three years as from the date of their approval by the BRSA and through providing additional finance to debtors if necessary.

Within the framework of the regulations issued for restructuring of debts to financial sector, Financial Restructuring Framework Agreement issued by the Banks Association of Turkey (BAT) was submitted to the creditor firms on May 24, 2002 with a view to be signed. The Agreement was signed by 25 banks, 17 financial institutions, Emlak Bankasi under liquidation process and the SDIF and was approved by the BRSA on July 4, 2002. The BAT completed "Application Form" and "Letter of Commitment" to be signed by debtor firms and sent them to banks and other financial institutions who have already signed the Framework Agreement. Also, "Report on Working Principles and Procedures of Arbitration Council" was completed and Turkiye Sinai Kalkinma Bankasi was charged with the task of "Coordination Secretariat".

#### **Creditor Institutions which have Signed the Financial Restructuring Program Framework Agreement**

<b>Banks</b>	
1. Turkiye Cumhuriyeti Ziraat Bankasi	14. Turk Dis Ticaret Bankasi
2. Turkiye Halk Bankasi	15. Turk Ekonomi Bankasi
3. Turkiye Vakiflar Bankasi	16. Turkiye Garanti Bankasi
4. Akbank	17. Turkiye Imar Bankasi
5. Denizbank	18. Turkiye Is Bankasi
6. Fiba Bank	19. Yapi ve Kredi Bankasi
7. Finans Bank	20. Toprakbank
8. Milli Aydin Bankasi	21. Turk Ticaret Bankasi
9. Oyak Bank	22. Turk Eximbank
10. Pamukbank	23. Turkiye Kalkinma Bankasi
11. Sekerbank	24. Nurol Yatirim Bankasi
12. Tekfenbank	25. Bayindirbank
13. Tekstil Bank	
<b>Financial Institutions</b>	
1. Garanti Factoring	10. Garanti Leasing
2. Aktif Leasing	11. Vakif Leasing
3. Ulus Factoring	12. Albaraka Turk Special Finance Institution
4. Is Genel Leasing	13. Yapi Kredi Factoring
5. Imar Leasing	14. Finans Leasing
6. Vakif Deniz Leasing	15. Finans Deniz Leasing
7. Ziraat Leasing	16. Dis Ticaret Leasing
8. Yapi Kredi Leasing	17. Dis Ticaret Factoring
9. Asya Financial Institution	
<b>Other</b>	
1.	Emlak Bankasi under liquidation process
2.	Savings Deposit Insurance Fund

### 3.4 Strengthening the Framework of Surveillance and Supervision and Increasing the Efficiency in the Sector

In parallel to the financial and operational restructuring of the banking sector, legislative and institutional regulations are being adopted. These efforts aim to strengthen regulatory and supervisory framework, ensure efficiency and competitiveness in banking sector, facilitate sound banking practices and thus establish confidence in the sector.

Prudential regulations are concentrated on the following areas: capital adequacy, risk management, loan exposures, loan loss provisioning, compliance with the International Accounting Standards, independent auditing and cooperation with foreign supervisory authorities.

#### *Regulations on Capital*

- With the amendments made to the Banks Act in June 2001, definition of “consolidated own funds” was introduced in compliance with EU Directives and subject to the calculation of lending limits and standard ratios on a consolidated basis to this definition was ensured. Regarding the excessive limits that may arise within this framework, a transition period until December 31, 2003 was granted to the banks.
- “Regulation on Measurement and Assessment of Banks’ Capital Adequacy” that defines principles and procedures for the calculation of banks’ CAR both on consolidated and unconsolidated basis by taking into consideration market risks- namely interest rate, exchange rate and equity risks- was published on February 10, 2001. This regulation has been null and void as of January 31, 2002 with the enforcement of a new regulation under the same title which draws up additional regulations on capital adequacy. The new regulation brings forth following amendments:
  - Principles and procedures regarding the measurement of risks and capital adequacy issues related to banks’ option operations are defined.
  - Directives about the standards of the risk measurement models are re-arranged.
  - Risk weights are re-arranged to comply with the inclusion of the repo transactions in the balance sheet.
  - “Structural Position” is defined to prevent erosion of banks’ own funds from steep price and foreign exchange rate movements. Principles and procedures regarding the structural positions to be taken into consideration in the calculation of CAR were published on May 08, 2002.
  - In accordance with the provisional Article 1 of the Regulation, the application of market risks on a consolidated basis in the calculation of capital adequacy was initiated on July 01, 2002.
- With the amendments to the Regulation on Banks’ Establishment and Operations on January 31, 2002, definition of own funds was changed, and the addition of general loan loss provisions to Tier 2 capital without netting out was brought. Additionally, capital supplements to all financial institutions were included in the amounts to be deducted from the capital. As a result of these changes, a single own fund definition has been set for the system, which provides uniformity both in the calculation of credit limitations and in the application of financial ratios.

### ***Regulations on Risk Management***

- With the “Regulation on Banks’ Internal Audit and Risk Management Systems” which was put into force on February 8, 2001, principles and procedures of establishing an efficient internal auditing system and an efficient risk management system to manage the risks to be encountered have been set out. Following the efficient operating of the afore-mentioned systems and within the framework of this regulation, risk-focused monitoring of the banking system on an activity-basis is intended. After July 2001, banks started to report their activities and their organizational preparations according to the regulation on quarterly basis. These reports are evaluated regularly and monitored closely.
- “Regulation on Principles and Procedures about the Implementation of the Foreign Exchange Net Position/Own Funds Standard Ratio for Banks on both Consolidated and Unconsolidated Basis” was published on January 31, 2002. With this regulation, compliance with the amendments to own funds and consolidated own funds definitions was provided. Also, the practice of treating the part of net general open positions exceeding the required level as commitment in the application of disponibility requirement was annulled.

### ***Regulations on Lending and Subsidiary Limits and Loan Loss Provisioning***

- With the introduction of “Regulation on Establishment and Operations of Banks” on June 27, 2001, risk group definition and calculation of loan exposures for a single group considering direct and connected lending were established in order to prevent (credit) risk concentration. This regulation, which includes banks’ shareholders and subsidiaries in the same risk group, shall prevent risk concentration on a particular group and improve the asset structure of the banking sector in accordance with the safety, resolution and productivity principles. Banks, total loans of which extended to a risk group exceed the required levels stipulated in the Banks’ Act, shall not extend further loans to natural persons and legal entities included in this risk group. Besides, banks are required to gradually remove the amounts exceeding the required levels by end-2006.
- With the amendments made to Banks Act by Act No.4672;
  - Banks’ non-financial subsidiaries are limited to 15% of their own funds and the total sum of all such subsidiaries are limited to 60% of the banks’ own funds with a transition period until 2009.
  - Starting from January 1, 2002, forward contracts, option contracts and other similar derivative type operations are included under the definition of “credit”.
  - Corporate tax deductibility of specific provisions is clarified.
- With the amendment made by Act No.4743 on January 31, 2002, existing four-year transition period granted to banks for loan loss provisioning was eliminated.
- Regulation on Loan Loss Provisioning was introduced on June 30, 2001. Provisions of this regulation regarding the principles and procedures of restructuring of loans and other receivables or of tying them to a new redemption plan were amended on January 31, 2002 and a circular for the enforcement thereof has been published. With this circular, the issues on classification of loans

and other receivables, principles for collaterals and provisioning and whether non-deposit money banks are subject to provisions of the regulation, have been clarified. With the amendments made to the regulation, existing practice on restructuring of loans and other receivables was revised, in order to introduce flexibilities which improve the efficiency of the regulations on restructuring debts to financial sector through providing additional loans or tying these debts to new redemption plans.

### ***Regulations on Accounting Standards, Independent Audit and Mergers and Acquisitions***

- In order to ensure the accounting of repo and reverse-repo transactions be compliant with International Accounting Standards and in accordance with the “priority of the core” principle of accounting required for a sound monitoring of banking risks, amendments were made to “Accounting Standards, Uniform Accounting Plan and Explanations Thereof to be Implemented by Banks” on December 13, 2001 and January 31, 2002 taking effect as of February 01, 2002.
- In accordance with Article 13 of the Banks’ Act, “Regulation on Accounting Practices”, along with its annexes was introduced on July 01, 2002. It prevents transactions from not being recorded and ensures transparency and uniformity in banks’ accounts and records, sound and reliable accounting of activities in compliance with their essential characteristics; timely and accurate preparation of financial statements; independent auditing; reporting and publication of these statements. With this regulation, which entered into force as of July 01, 2002, compliance of the banks’ 2002 year-end balance sheets with International Accounting Standards (IAS) have been targeted.
- “Regulation on Principles for Independent Auditing” was published on January 31, 2002. It sets out the principles and procedures of auditing of; the compliance of accounts and records of the banks and special finance institutions covered by the Act No.4389 with the legislation on accounting and recording plan which has been put into force pursuant to afore-mentioned Act’s Article 13 and the approval of balance sheets, profit/loss statements and consolidated financial statements to be published within the framework of auditing results. With this regulation, principles and procedures to be employed in independent auditing were re-arranged in compliance with international auditing standards and in a more detailed manner.
- “Regulation on Authorization of the Auditing Institutions and Permanent or Temporary Withdrawal of Their Authorities”, which sets out the authorization of the independent auditing institutions that can approve the balance sheets and profit/loss statements of banks along with special finance institutions and draws up permanent or temporary withdrawal of their authorities, was published on January 31, 2002. Provisional Article 2 of this Regulation was abrogated by the Regulation published on March 29, 2002.
- “Regulation on Mergers and Acquisitions of Banks” which was issued by the BRSA and published on June 27, 2001, sets out the principles and procedures; for the merger of a bank operating in Turkey with a bank or several banks; or for acquisition of its all debts, receivables and deposits by a bank operating in Turkey. Article 20 of this Regulation was amended on September 14, 2001.

### ***Regulation issued Within the Framework of Bank Capital Strengthening Program***

“Regulation on Principles and Procedures of Banking Sector Restructuring Program” dated February 01, 2002 draws up the details of the capital support program under the scope of the restructuring program. Within this framework, this Regulation lays down the principles and procedures of the recapitalization scheme designed for the private owned deposit-taking banks established in Turkey. In compliance with Provisional Article 4 of the Banks Act No. 4389, the Regulation stipulates principles, procedures, and other details on the following issues: The general assembly to be held by banks; increasing or decreasing of the banks’ capital; measures that need to be taken based on assessments of the Banking Regulation and Supervision Agency; the transfer period for shares which are subject to the capital increase; the issuance of convertible bonds and conversion of these bonds into shares; the sale of banks’ shares taken over by the Savings Deposit Insurance Fund; and conversion of subordinated debts to capital.

- “Regulation on Principles and Procedures of Independent Audit to Be Carried Out in Banks According to Provisional Article 4 of the Banks Act No. 4389” was published on February 01, 2002. Articles regarding inflation accounting and some other articles of this Regulation were amended on 02.03.2002 and articles regarding the scope of the auditing activity to be carried out by the first institution were amended on March 29, 2002.
- “Regulation on Principles and Procedures of Second Independent Audit to Be Carried Out in Banks According to Provisional Article 4 of the Banks Act No. 4389” was published on March 27, 2002. It sets out; the principles and procedures for the auditing of the independent audit reports drawn up pursuant to "Regulation No. 4389, Concerning the Principles and Procedures of Independent Auditing to be Carried Out in Banks according to Provisional Article 4 of the Banks Act No. 4389" by a second independent audit institution for purposes of ensuring compliance with the independent auditing rules and the principles, and procedures and principles concerning the determination of the second independent audit institutions by the Agency. Article 5 of this Regulation regarding the determination of the second institution was amended on March 29, 2002.
- “Regulation on General Conditions for the Approval and Implementation of Financial Restructuring Framework Agreements” was published on April 11, 2002.

### ***Regulations on Special Finance Institutions***

- In accordance with the Act No.4672, Association of Special Finance Institutions of Turkey was established. With a view to protect deposits in Special Finance Institutions, the Association has been authorized to establish “Assurance Fund” and to determine the principles and procedures of the assurance fund.
- “Regulation on Establishment and Operations of Special Finance Institutions” was published on September 20, 2001. The definitions entitled “Own funds” and “Consolidated Own Funds” and some articles were amended on March 07, 2002.
- “The Status of Special Finance Institutions Association” was put into force by the Decree No.2001/3138 of Council of Ministers dated October 26, 2001.

### ***Memorandum of Understandings Signed between Supervisory Authorities of Foreign Countries and the BRSA***

The soundness of Turkish banks' operations carried out through their foreign subsidiaries, branches and representative offices closely influence the stability and the safety of Turkey's financial markets as well as that of host countries. In this respect, it is important to set up an institutional framework on the international platform which will allow the evaluation of foreign banking operations' nature, their links with the parent company, to have access to the related right information so as to ensure the regulation and supervision of these operations and to facilitate cooperation between countries on supervision and monitoring.

- Within this framework, memorandum of understandings are signed with supervisory authorities of the other countries. With the enhanced mutual cooperation, supervision and due diligence are performed on off-shore banks established by banks or by their majority shareholders. Along these lines, 13 banks and a subsidiary in Bahrain-Manama, Luxembourg and Malta and a subsidiary bank in Holland were supervised and assessments were finalized. Besides, on-site supervision of off-shore banks belonging to Turkish banks operating in Cyprus were done.
- Within the scope of the mutual cooperation with supervisory authorities of other countries, the BRSA signed Memorandum of Understanding (MoU) with the Central Bank of the Republic of Northern Cyprus, the Central Bank of Albania and National Bank of Romania on September 17, 2001, October 19, 2001 and February 19, 2002 respectively. Draft MoU's have been sent to Holland, Malta, Luxembourg, Bahrain, Switzerland and Ireland.

#### **Other Regulations for Increasing Efficiency of the Sector**

- By the amendment to the Banks' Act, provisions of the Turkish Commercial Code No. 6762 and provided that the ratio of total assets of banks, which are to be acquired or merged, to aggregate assets in the sector does not exceed twenty percent, the provisions of the Consumer Protection Act No. 4054 shall not apply to mergers and acquisitions with a view to accelerate the merger and acquisition processes.
- Tax incentives have been introduced with a view to facilitate the mergers and acquisitions of banks and their subsidiaries. Besides, the Act No.4603 which allows the application of tax incentives stated in the Act No.4605 for the mergers of banks' subsidiaries entered into force on July 3, 2001.
- Upon the Decree dated July 27, 2001 of the Council of Ministers, differentiation in withholding tax rates on repo and TL as well as F/X deposit interest earnings according to their maturities was introduced. Within this framework, withholding rates on TL deposit accounts were brought down to; %14 for maturities from 3 to 6 months, %10 for from 6 to 12 months and %6 for those exceeding 12 months. Withholding rates on F/X deposit accounts did not change for those maturities exceeding one year, but the rates on the accounts with a less than one year maturity were raised from %16 to %18. Withholding rates on repos were raised from %16 to %20.
- On August 8, 2001, the Central Bank of the Republic of Turkey initiated the practice of paying interest on required reserves set aside for deposits so as to reduce resource costs of banks.
- The Central Bank changed the implementation of reserve and liquidity requirements on March 29, 2002 with a view to contribute to lowering of financial intermediation costs and to provide liquidity management with a more flexible structure. Within this framework, reserve and liquidity requirement ratios were reduced by a total of 2 points and interest payment on F/X denominated required reserves was decided to be introduced.

