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HSBC Global Research

Turkey Informer

Equity market drivers

Turkish equities have bounced back strongly from their May lows, but nevertheless still face some tough structural headwinds. Most crucially, we think the global environment still creates challenges for current account-deficit countries, although there are both upside and downside risks here. Domestically, tight monetary and fiscal policies create continued downside risk to growth and earnings estimates. There is a liquidity risk as well, in that the market remains over-owned. The change in the macro environment also threatens to raise the political temperature going into next year's elections and will probably make investors focus more on political risk than might otherwise be the case.

That said, valuation provides some comfort. On a PE basis, Turkey enjoys discounts to EMEA of 7% for 2006e and 12% for 2007e. Moreover, we see about 19% upside to fair value for the market, both for banks and non-banks. Of course, if growth is weaker than we expect, earnings erosion would undermine the room for manoeuvre on valuations. But equally, further Turkish lira (TRL) appreciation could enhance the interest rate and growth outlook – both of which would, in turn, boost valuations.

In view of this outlook, we keep the Turkish market on a Neutral weighting.

Top stock picks

Banks – our top picks remain **Garanti** and **TEB** on prospects of strong growth under the global expertise of new JV partners, GE and BNP, respectively. Both banks have attractive multiples, trading at single-digit PEs on our 2006 and 2007 estimates. Potential upside to our two-year notional target price is 32% for Garanti and 51% for TEB.

Autos/Consumer – consumer demand, especially for autos, should revive from Q4 onwards as rates stabilise and TRL recovers. Demand for white goods is still supported by ongoing momentum from the last two years' construction boom. We find value in blue chips **Arcelik** and **Ford Otosan**. **Tofas** should not disappoint investors currently buying into its long-term turnaround prospects on new models.

Construction/Building materials – we continue to favour **Trakya Cam** as it remains a strong beneficiary of ongoing strong momentum in the construction sector.

Conglomerates – **Sabanci Holding** is our top pick because of its 30% discount to target NAV, which we do not think is justified, given near-term potential catalysts such as bids for electricity tenders.

Small Cap – We like **Anadolu Cam** because of its healthy regional expansion, **Netas** on prospects of a speed-up in telecom infrastructure spending and **Eczacibasi Ilac** due to our strong growth outlook for Turkey's generic drug market and the company's M&A mandate.

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Strategy

Turkey: hostage to global economic trends

Turkish equities have bounced strongly from their May lows, but nevertheless still face some tough structural headwinds. Most crucially, we think the global environment still creates challenges for current account-deficit countries, although there are both upside and downside risks here. Domestically, tight monetary and fiscal policies create continued downside risk to growth and earnings estimates. There is a liquidity risk as well, in that the market remains over-owned. However, these risks are, to some extent, already factored into valuations – hence we remain Neutral on the market as a whole.

In terms of the global environment, it seems inevitable that the world economy will slow – but for Turkey the key issue lies in the kind of landing which results. A smooth cyclical top, where US interest rates come through quickly to support the US economy could, in principle, be quite positive for Turkish equities. Under this scenario, the Turkish lira (TRL) would appreciate versus the USD, pushing down Turkish inflation and interest rates.

By contrast, an elongated peak – where rates have to remain high to fend off the residual inflationary pressures engendered by high commodity prices – would be much less positive, and would keep the pressure on current account-deficit asset markets. This would mean ongoing pressure on Turkish macro – and in particular the delicate balance between the TRL exchange rate, inflation and the Turkish central bank's inflation target. With Turkish inflation running at 12%, meeting the central bank's 4% target for the end of 2007 is already challenging (even allowing for a 2% potential uncertainty band). Renewed exchange rate weakness would play on this vulnerability.

This creates persistent risks for the key drivers of Turkish equities. In particular, a more difficult macro environment would threaten the growth, exchange rate and interest rate projections that feed into our bottom-up forecasts. On this front, we are currently expecting 5% GDP growth this year and 5.5% in 2007e, with another 100bp increase in interest rates, to 18.5% by the end of 2006. So a further hit to the exchange rate, for example, would force up inflation and interest rates and further depress the growth outlook.

Turkey in a global context

	PE			EPS growth			PEG
	2005a	2006e	2007e	2005a	2006e	2007e	2006
Turkey	12.5	11.7	10.0	15.1	6.8	17.3	0.9
Czech Rep.	21.0	16.6	9.8	23.3	7.4	2.6	1.0
Egypt	15.5	13.7	11.4	80.2	12.9	20.2	0.7
Israel	7.4	14.1	13.1	10.3	-47.1	7.7	1.8
Hungary	10.8	10.1	9.8	23.3	7.4	2.6	3.9
Poland	14.0	11.8	11.3	16.5	18.0	4.7	2.5
Russia	13.7	12.0	11.8	25.5	14.5	1.4	8.8
South Africa	16.9	13.2	10.6	11.1	28.6	24.5	0.5
EMEA	**14.5**	**12.6**	**11.3**	**16.5**	**16.9**	**11.4**	**1.1**
EM Asia	**13.5**	**12.5**	**10.9**	**-0.1**	**8.1**	**14.5**	**0.9**
Latin America	**11.4**	**9.7**	**9.0**	**27.8**	**17.3**	**7.9**	**1.2**

Source: HSBC estimates (prices as of 25 August 2006)

There are already certain risks to GDP forecasts. On the positive side, Turkey has been able to grow rapidly in the past, with real interest rates at current levels. Hence, in this sense, the recent tightening in monetary policy should not weigh too much on growth. However, the most dynamic part of last year's performance was in interest rate-sensitive sectors (like construction). To the extent that it was because the private sector has been convinced of prospects for ongoing interest rate convergence, the recent tightening in monetary policy may, in fact, have a disproportionately negative impact. The data available since the latest round of exchange rate weakness do not, so far, provide a clear picture of which of these stories is more accurate. Still, one would expect GDP trends to be the primary influence on the quoted corporate earnings outlook. So any shortfall in GDP would similarly damage earnings prospects. On this count, bear in mind that Turkey already has the most negative trend in terms of earnings downgrades of any GEM market.

The change in the macro environment also threatens to raise the political temperature going into next year's elections. Higher inflation and weaker growth could prove to be complicating factors in the spring presidential election and autumn general election, and are likely to make investors focus more on political risk than might otherwise be the case.

There are also some liquidity issues confronting the Turkish market. Emerging Portfolio data suggest that GEM funds are still heavily Overweight Turkey – and have remained so right through the current period of macroeconomic trauma. Many Eastern European funds have also gone heavily off benchmark into the country. There also remains a lot of non-dedicated money in Turkey – crossover money from hedge funds and European long-only institutions. Equally, Gulf investors participated in the rally. With nominal and real interest rates set to remain much higher than previously expected, it's difficult to see local mutual funds boosting equity exposure. Indeed, the risk is that, given the abrupt change in the Turkish macro environment, foreign funds could use the current rally to sell. In general, the liquidity obstacles for Turkey could be quite strong.

That said, valuation provides some comfort. On a PE basis, Turkey enjoys a discount to EMEA of about 7% for 2006e and 12% for 2007e. Moreover, we see about 19% upside to fair value for the market, both for banks and non-banks. Of course, if growth is weaker than we expect, earnings erosion would undermine the room for manoeuvre on valuations. But equally, further TRL appreciation could enhance the interest rate and growth outlook – both of which would, in turn, boost valuations.

In view of these risks, we keep the Turkish market on a Neutral weighting.

Equity performance summary

Performance summary

	-1 wk	-1M	-3M	-12M	Y-t-d
Absolute %					
MSCI GEM	0.3	5.8	2.9	26.1	9.3
MSCI EMEA	-0.8	6.9	-0.8	29.7	7.2
MSCI Turkey	-0.5	14.9	-4.2	19.8	-14.9
Relative to GEM %					
MSCI Turkey	-0.8	9.2	-7.1	-6.2	-24.1
Relative to EMEA %					
MSCI Turkey	0.4	8.0	-3.4	-9.9	-22.0

Note: All data is relative to MSCI
Source: Bloomberg

Portfolio strategy

On our coverage universe of 42 stocks, we see an aggregate 19% potential upside, with our valuations based on different methodologies including DCF, NAV, PE, EV/EBITDA and P/BV. The key change in our DCF assumptions is the higher risk-free rate we now use in our dollar-based WACC calculations (8% instead of 7% previously), in order to reflect the higher risk profile of Turkey warranted by the rise in interest rates following the market turbulence in May and June. We also employ a 5.5% risk premium for equities, versus 5.0% previously. We note that we may be too conservative in our risk-free rate assumption, with Turkey's 30-year eurobonds currently yielding 7.4%. This leaves us some upside room for DCF-based valuation upgrades if we are convinced that subsiding risk aversion is sustainable.

Despite the highly volatile macro environment in Q2, Turkish banks remained resilient, coming through the negative impact relatively unscathed. We think they benefited from the intense restructuring efforts and more effective risk management policies put into place over the last few years. The sector outlook is quite promising, and foreign players agreed to pay very high multiples to enter the market, especially in 2005 and 2006. Having suffered the large sell-off, Turkish banks now trade at 10.1x PE on 2007e earnings, a discount to the average of HSBC coverage of 11.9x in EM Europe. Under this scenario, we prefer **TEB** and **Garanti**, due to their growth prospects and attractive multiples, trading on single-digit PEs, for both 2006e and 2007e.

The prevailing environment of high interest rates and a likely slowdown in economic growth represents a drawback for consumption-driven stocks, including autos and white goods. It is true that Q3 will be a weak period – especially for autos – as the slump in monthly sales figures from June onwards shows.

HSBC Turkey coverage universe (banks only)

Company Name	Last price	NTP (TRL)	Upside	Rating
T. Ekonomi Bank.	13.60	20.47	51%	Overweight
Is Bankasi (C)	8.35	11.24	35%	Neutral
Garanti Bankasi	4.26	5.64	32%	Overweight
Akbank	7.85	9.21	17%	Neutral
Denizbank	14.10	15.86	12%	Neutral
Vakifbank	6.50	7.03	8%	Underweight
Finansbank	5.85	6.22	6%	Neutral
Yapi ve Kredi Bank.	2.86	2.35	-18%	Neutral

Source: HSBC estimates
Prices are in TRL (Prices as at close of 25 August 2006)

HSBC Turkey coverage universe (excluding banks)

Company Name	Last price	NTP (USD)	Upside	Rating
Tofas Oto. Fab.	2.65	3.80	44%	Overweight
Netas Telekom.	22.07	30.83	40%	Overweight
Ford Otosan	7.13	9.40	32%	Overweight
Eczacibasi Ilac	2.50	3.29	32%	Overweight
Anadolu Cam	3.33	4.36	31%	Overweight
Adana Cimento (A)	6.42	8.39	31%	Overweight
Arcelik	6.52	8.50	30%	Overweight
Sabanci Holding	3.56	4.53	27%	Overweight
Aksigorta	3.60	4.48	25%	Overweight
Trakya Cam	2.47	3.07	24%	Overweight
Dogus Otomotiv	4.04	5.00	24%	Overweight
Cimsa	6.04	7.42	23%	Overweight
Tupras	18.16	22.20	22%	Neutral
Is REIT	1.74	2.12	22%	Overweight
Turkcell	11.63	14.20	22%	Overweight
Petkim	3.46	4.15	20%	Neutral
Anadolu Sigorta	1.69	2.02	19%	Overweight
Sise Cam	3.01	3.56	18%	Neutral
Yazicilar Holding	22.07	26.01	18%	Neutral
Akcansa	5.19	6.09	17%	Overweight
Koc Holding	3.60	4.06	13%	Neutral
Dogan Holding	4.11	4.62	13%	Neutral
Petrol Ofisi	3.77	4.19	11%	Neutral
Vestel	2.61	2.89	11%	Neutral
BIM Birlesik Mag.	34.12	37.55	10%	Neutral
Anadolu Efes	26.99	28.93	7%	Neutral
Hurriyet Gzt.	2.28	2.44	7%	Overweight
Eregli Demir Celik	4.79	5.02	5%	Underweight
Dogan Yayin Hol.	3.20	3.35	5%	Neutral
Ak Enerji	2.16	2.14	-1%	Neutral
Alarko REIT	20.20	20.04	-1%	Neutral
Migros	9.30	9.19	-1%	Neutral
Yapi Kredi Koray REIT	2.17	1.75	-19%	Neutral
Anadolu Hayat Emek.	2.89	2.29	-21%	Underweight

Notes: * prices are in USD
Source: HSBC estimates (Prices as at close of 25 August 2006)

However, we argue that as long as the markets remain stable, with rates staying high compared with pre-volatility levels, Turkish consumers are likely to adapt to the new conditions without much delay.

We calculate that vehicle loans are not actually too costly to the consumer, even though current rates are almost double their pre-turbulence levels. Monthly payments on a typical car loan are only 10% higher than previously – a burden which on a stand-alone basis would not warrant any long-term loan avoidance. After an expected dismal Q3, we anticipate a recovery in consumer spending from Q4 onwards, bringing consumption plays back into focus. We find value in blue chip stocks, **Ford Otosan** and **Arcelik**, because of their solid fundamentals, quality of earnings and high dividend-yield potential. There is still strong momentum behind the construction sector, which should benefit white goods demand and, in turn, market leader, Arcelik. On the other hand, **Tofas** offers both defensive characteristics and a long-term turnaround story due to its massive ongoing new model projects, which should boost earnings from 2008 onwards.

Private sector-driven construction activity is perhaps the most vulnerable to the high interest rate environment – a cool-down in residential construction seems inevitable. But this is unlikely to be fast since the sector still has considerable momentum from ongoing projects. This is underpinned by the substantial 25.6% growth in Q1 versus 6.4% GDP growth, which we do not expect to diminish suddenly. In our view, the 2007 outlook is still positive for building material producers, if not for REITs. In that respect, we like the flat glass monopoly and auto glass producer, **Trakya Cam**, as one of the major beneficiaries of the ongoing strong momentum in the construction sector.

Among large diversified Turkish groups, our pick is **Sabanci Holding,** whose major non-finance businesses are being listed on the stock exchange (eg retailer Carrefoursa, to be followed by global tyre cords company, Kordsa), improving the NAV transparency. Sabanci's aggressive plans to grow in the energy sector – with some solid steps already taken on the generation front and the Group's keen interest in the upcoming electricity distribution privatisations – are another positive catalyst for the share price, as well as potential developments on 34%-owned Akbank's foreign partnership mandate. These factors, together with an attractive sum-of-parts valuation underpinned by a 30% NAV discount (which we think excessive), make Sabanci the most attractive conglomerate investment in Turkey at the moment, in our view.

The market sell-off has shifted investors' focus back to large cap stocks lately, from small caps. But, as the market regains some of its losses under the leadership of blue chips, we expect the pre-turbulence quest for smaller value and growth plays to become an issue again. We like **Anadolu Cam**, the glass packaging company, which successfully traces brewery and soft drinks investments of the Efes Group in Eastern Europe, Russia and the CIS region. Another pick is **Eczacibasi Ilac**, the generic drug producer, due to its strong positioning in Turkey's promising pharmaceutical market, as well as the possibility of a foreign partnership after the company's official mandate in July 2006. We also pick **Netas** as a long-term and small cap play on prospects of a pick-up in telecom infrastructure spending, after fixed-line monopoly Turk Telekom's privatisation and Vodafone's entry to the Turkish GSM market.

Revisions to our coverage...

In this report, we have reviewed our ratings and valuation ranges on 17 out of 42 stocks currently under our coverage. For the remaining ones, in the following sections we provide a brief summary of our recent sector and company reports in which we have already undertaken forecast and rating changes. As a reminder, our ratings are relative to our coverage universe, except for six Turkish companies, which are covered relative to their respective global sectors (Akbank, Garanti, Isbank, Yapi Kredi Bank, Turkcell and Tupras).

We base our valuations on methodologies including DCF, NAV, PE, EV/EBITDA and P/BV. The key change in our DCF assumptions is the higher risk-free rate we now use in WACC calculations (8%, instead of 7% previously), in order to reflect the higher risk profile of Turkey warranted by the rise in interest rates following market turbulence. We also employ a 5.5% risk premium for equities versus 5.0% previously.

Our review of forecasts, valuation ranges and ratings resulted in an upgrade to one stock, Akcansa (to Overweight from Neutral), while we downgraded Koc Holding (to Neutral from Overweight). Ratings for the other 15 stocks remain unchanged.

Below, we provide a short summary of the underlying reasons for forecast/rating changes for each of the 17 stocks.

Adana Cimento (ADANA.IS) Overweight

We revisited our Adana Cimento valuation based on the new macroeconomic environment, underpinned by high interest rates. We think this environment is likely to slow the growth in the construction sector, particularly the housing segment. Nevertheless, we expect most of the adverse impact to be seen in 2007 rather than 2006, due to momentum from ongoing projects. The construction sector posted 21.5% growth in 2005 (versus 7.4% GDP growth) and 25.9% growth in Q1 2006 (versus 6.4% GDP growth). This indicates very strong momentum driving the sector, which should keep sector growth, including cement consumption, well above the general economic growth for a while, despite high interest rates.

We note that Adana Cimento has already been operating at full capacity; therefore, the company's sales volume growth will be limited.

Changes in valuations and/or target prices (as of 25 August 2006)

Company	Ric code	Trading volume (USDm)	Current mkt cap (USDm)	Target mkt cap (USDm)	Share price (USD)	Valuation range (USD)		Notional target price old	Notional target price new	% up/downside potential to new NTP	Rating old	Rating new
Adana Cimento	ADANA.IS	0.5	305.8	400	6.42	8.19	8.59	9.57	8.39	30.8%	OW	OW
Akcansa	AKCNS.IS	1.6	994.3	1,165	5.19	5.33	6.84	7.14	6.09	17.2%	N	OW
Aksigorta	AKGRT.IS	4.9	1,101.1	1,372	3.60	4.30	4.66	5.23	4.48	24.6%	OW	OW
Anadolu Hayat	ANHYT.IS	0.6	506.1	400	2.89	2.09	2.48	3.43	2.29	-21.0%	UW	UW
Anadolu Sigorta	ANSGR.IS	4.1	338.1	404	1.69	1.86	2.18	2.97	2.02	19.5%	OW	OW
Arcelik	ARCLK.IS	3.4	2,606.8	3,400	6.52	7.65	9.35	10.50	8.50	30.4%	OW	OW
BIM	BIMAS.IS	0.4	863.1	950	34.12	31.92	43.17	30.64	37.55	10.1%	N	N
Cimsa	CIMSA.IS	1.3	733.0	900	6.04	6.81	8.03	9.56	7.42	22.8%	OW	OW
Dogan Holding	DOHOL.IS	31.2	3,020.2	3,400	4.11	4.16	5.09	4.79	4.62	12.6%	N	N
Eczacibasi Ilac	ECILC.IS	3.3	456.6	600	2.50	3.23	3.34	4.24	3.29	31.5%	OW	OW
Koc Holding	KCHOL.IS	15.4	4,551.9	5,130	3.60	3.80	4.31	6.11	4.06	12.7%	OW	N
Migros	MIGRS.IS	4.7	1,639.5	1,620	9.30	8.90	9.48	11.78	9.19	-1.2%	N	N
Netas	NETAS.IS	1.1	143.1	200	22.07	27.46	34.20	43.20	30.83	39.7%	OW	OW
Petkim	PETKM.IS	5.7	709.0	850	3.46	3.53	4.77	4.64	4.15	19.9%	N	N
Sabanci Holding	SAHOL.IS	38.9	6,415.9	8,160	3.56	4.27	4.79	5.56	4.53	27.2%	OW	OW
Sisecam	SISE.IS	3.7	1,276.6	1,507	3.01	3.39	3.72	4.91	3.56	18.0%	N	N
Vestel Elektronik	VESTL.IS	2.8	414.8	460	2.61	2.61	3.18	3.77	2.89	10.9%	N	N

Source: Company data, HSBC Estimates

As far as pricing is concerned, since domestic prices are set in Turkish lira, the devaluation of the lira argues for a slowdown in price hikes in USD terms, keeping USD-based revenue estimates under pressure. On the cost side, the majority of the COGS are composed of Turkish lira, except for Energy, which makes up c16% of the COGS. Given the rising energy prices, we assume stable margins for the company going forward, leading to a stable trend in operational performance.

We employ a blended valuation method for Adana Cimento in order to determine our valuation range. Peer group comparison makes up the high end while the DCF analysis makes up the low end of our fair value-range calculation.

On multiples, Adana Cimento still offers an attractive valuation, despite the stock's recent outperformance; it trades at a 21% discount to its emerging market peers, on average. Based on 2007e PE, EV/EBITDA and EV/sales multiples, Adana Cimento trades at 7.3x, 4.2x, and 1.6x versus the peer group average of 8.5x, 5.0x, and 2.3x, respectively. From peer group comparison, we arrive at a fair value estimate of USD8.59 per Class A share.

By using DCF analysis, where we assume a risk-free rate of 8.0% (previously 7.0%), equity risk premium of 5.5% (previously 5.0%), terminal growth rate of 2.0% and a company beta of 0.75, we arrive at a fair value of USD8.19 per Class A share, which stands as the low end of our fair value range.

Accordingly, we set our new notional target price at USD8.39 (from USD9.57), the mid-point of the USD8.19-8.59 range. This implies 31% potential upside on the stock, based on its closing price of USD6.99 per share on 25 August, and we reiterate our Overweight rating for the stock.

The major risk to our valuation is a greater-than-expected slowdown in construction activity, which would hurt the company's sales volume and margins. Also, as its domestic sales prices are set in Turkish lira, further devaluation of TRL stands out as another risk factor to our valuation and rating for Adana Cimento.

Adana Cimento – forecast changes

(USDm)	2006e		2007e		2008e	
Forecasts	**Old**	**New**	**Old**	**New**	**Old**	**New**
Revenues	183	181	188	186	188	186
EBITDA	69	68	72	70	71	68
margin	37.9%	37.3%	38.5%	37.8%	37.5%	36.7%
Net profit	79	76	81	78	79	76
margin	43.1%	41.9%	43.2%	41.7%	42.1%	40.9%

Source: HSBC estimates

Akcansa (AKCNS.IS) Overweight

We revisited our Akcansa forecast model in light of macroeconomic turbulence and its impressive H1 2006 results.

Akcansa is a strong domestic play, with 90% of its revenues generated in Turkey and only 10% through exports, whereas exports account for 35-40% of total revenues of Cimsa and Adana Cimento. Therefore, Akcansa looks more vulnerable to the expected slow down in construction activity following the rise in interest rates. However, unlike Cimsa, Akcansa has a net cash position, which makes it more defensive against TRL weakness as far as bottom-line earnings are concerned.

The high interest rate environment signals slower growth, especially for the construction sector. Nevertheless, ongoing construction activity should support cement sales, at least for the remainder of 2006. Looking forward, Akcansa should complete its ongoing capacity expansion investment by the end of 2007. Accordingly, even if domestic cement demand does not grow significantly in 2008, Akcansa can post strong growth in sales volumes by focusing more on exports. But since export prices – and particularly margins – are not as high as domestic prices, we expect to see some decline in the company's EBITDA margin in 2008, which we have incorporated into our revised estimates for the company.

In determining our fair value range for Akcansa, we used both DCF and peer comparison methods. Our DCF analysis, with assumptions of an 8.0% (previously 7.0%) risk-free rate, 5.5% (previously 5.0%) equity risk premium, and a company beta of 0.89, yields a fair value of USD6.84 per share.

On our estimates, Akcansa trades at a 2007e PE of 9.4x, EV/EBITDA of 5.9x, and EV/sales of 2.2x, which are roughly on a par with the peer average. However, historically Akcansa has traded at a premium to its peers, as the sector leader with plants located in high-growth areas of mass population. Therefore, we believe the stock's current valuation is attractive, even though we do not attach any premium to the company's multiples in deriving our fair value estimate of USD5.33 per share.

All in all, our fair value range is calculated as USD5.33-6.84, with our new notional target price of USD6.09 (from USD7.14) per share, implying 17% potential upside from its closing price of USD5.19 on 25 August 2006. Thus, we upgrade our rating on the stock to Overweight from Neutral.

The major downside risk to our valuation would be a more severe slowdown in construction activity around the country, which would impact the company's sales volume and operational profitability.

Akcansa – forecast changes

(USDm)	2006e		2007e		2008e	
Forecasts	Old	New	Old	New	Old	New
Revenues	351	368	399	393	451	483
EBITDA	132	139	157	148	183	178
margin	37.7%	37.8%	39.5%	37.7%	40.7%	36.9%
Net profit	90	114	107	106	118	110
margin	25.7%	31.0%	26.8%	26.9%	26.2%	22.8%

Source: HSBC estimates

Aksigorta (AKGRT.IS) Overweight

Following the recent market volatility, we have revised our estimates. Aksigorta is relatively immune to changes in FX and interest rates, because most of the company's activities are denominated in TRL and it does not invest in FX financial instruments. However, it has a large security portfolio (TRL90m) and a huge participation portfolio (TRL1.6bn) recorded on a mark-to-market basis. We note though, that related losses on these items will be recorded on the equity side of the balance sheet and have no impact on the P&L.

Aksigorta – forecast changes

(USDm)	2006e		2007e		2008e	
Forecasts	Old	New	Old	New	Old	New
Premiums written	196	197	228	214	254	239
Technical income	23	23	34	33	39	35
Technical margin	12%	12%	15%	15%	15%	15%
Net income	55	55	74	70	83	79

Source: HSBC estimates

The company will also benefit from some of the forecast increasing returns on the security market this year. Meanwhile, the macroeconomic slowdown will have less impact on operations but the bottom-line will be hurt by lower dividend gains from Akbank.

We value Aksigorta through an NAV approach. For the core insurance business and cash, we use the CAPM (roe-g/coe-g) method, after making necessary adjustments to equity. In line with revisions to the individual targets of the subsidiary portfolio, we now value Aksigorta's total participation portfolio at USD1.0bn versus

USD1.3bn previously. We also increase the risk-free rate assumption from 7.0% to 8.0%, indicating a 12.9% cost of equity versus 12.5% previously. As a result, we cut our notional target price for Aksigorta by 14%, to USD4.48 per share, from USD5.23 previously, in the range of USD4.30-4.66. Our revised NTP still offers 25% upside and we maintain our Overweight rating.

A further slowdown in economic growth is the main threat to our valuation. Prolonged delays in the enactment of the new insurance framework, or sliding market share and profitability in the increasingly competitive environment are the key sector-specific and company-specific risks to our valuation in the long term.

Anadolu Hayat (ANHYT.IS) Underweight

We have revised our estimates and valuation for Anadolu Hayat, taking into account the impact of the recent macroeconomic volatility.

Anadolu Hayat operates in life insurance, which is relatively more sensitive to consumer confidence and macro slowdown, than non-life insurance companies. We think the company is immune to FX volatility. However, it has a large exposure to securities – totalling TRL234m, of which half is kept as trading securities – and could face some losses. As a result of possible losses on the trading portfolio we expect bottom-line profits to be affected due to lower financial profits.

Anadolu Hayat – forecast changes

(USDm)	2006e		2007e		2008e	
Forecasts	Old	New	Old	New	Old	New
Life tech income	16.7	9.6	21.4	12.3	25.4	13.9
Life technical margin	5.3%	3.8%	5.8%	4.4%	6.1%	4.4%
Pension tech income	-4.7	-4.1	1.5	1.3	4.0	4.0
Pension tech margin	-3%	-2%	1%	1%	1%	1%
Net income	41.9	31.8	53.4	36.5	58.1	41.3

Source: HSBC estimates

In our valuation, we have increased the risk-free rate assumption from 7.0% to 8.0% to include the country risks, indicating a 13.6% cost of equity for the company. Valuing FY 2007e adjusted equity, with 13.6% CoE and 4% terminal growth, and including the participation portfolio (worth USD66m), we reach a total value of USD400m for Anadolu Hayat. Hence we set our notional target value at USD2.29 per share, in a range of USD2.09-2.48. Our previous target was USD3.43 per share, 50% higher than our revised notional target price. Our revised NTP still implies 21% downside from its closing price of USD2.89 on 25 August 2006, hence we maintain our Underweight rating on the company.

Our valuation relies on the assumption that both life and pension businesses in Turkey grow at a moderate rate. We do not assume any major market share gains or margin expansion for Anadolu Hayat. The main upside risk to our valuation is if the sector (especially the pension business) grows faster than we expect or the company performs better than our estimates.

Anadolu Sigorta (ANSGR.IS) Overweight

Anadolu Sigorta's operations are cyclical and hence premium generation generally accelerates in the second half of the year. This has been slightly unfortunate this year, as the economy has begun to cool down in the second half. The company has little exposure to FX transactions, hence it is relatively protected against FX volatility. All investments are placed in securities, stocks and mutual funds, totalling TRL278m (34% of total assets), signalling a vulnerability to interest rates. However, the company is still relatively protected, because a large proportion of securities are 'held-to-maturity', which has no impact on either the equity or the P&L.

Anadolu Sigorta – forecast changes

(USDm)	2006e		2007e		2008e	
Forecasts	Old	New	Old	New	Old	New
Premiums written	754	679	988	732	1013	830
Technical income	21	8	24	20	46	21
Technical margin	4.0%	1.8%	2.7%	4.1%	6.7%	3.8%
Net income	34	31	48	34	55	32

Source: HSBC estimates

Accounting for the impact of the market volatility, we have revised our earning estimates for Anadolu Sigorta slightly downwards. The macro slowdown will have greater impact on premium production, which in turn will impact technical profitability and bottom-line profits.

Anadolu Sigorta holds a considerable participation portfolio, valued at USD133m and 97% driven by listed subsidiaries. This portfolio was worth USD181m when we last issued a report on Anadolu Sigorta, *Making the Crossing*, 19 April 2006. We have increased the risk-free rate assumption from 7.0% to 8.0% to include the higher country risk profile, indicating a 13.3% cost of equity. Valuing FY 2007e adjusted equity, with 13.3% CoE and 4% terminal growth, we reach a value of USD271m for the insurance business and cash. Adding the NAV of the participations to this calculation, we derive a notional target value for Anadolu Sigorta of USD404m, or USD2.02 per share in a range of USD1.86-2.19. Our previous target was USD2.97 per share, 47% higher than our revised notional target price. Our revised NTP still implies 19% upside for Anadolu Sigorta from its closing price of USD1.69 on 25 August 2006, and we maintain our Overweight rating on the company.

A further slowdown in economic growth is the main threat to our valuation. Anadolu Sigorta has been a successful player in the market so far, maintaining its market-leading position. Prolonged delays in the enactment of the new insurance framework, or sliding market share and profitability in the increasingly competitive environment are the key sector-specific and company-specific risks to our valuation in the long term.

Arcelik (ARCLK.IS) Overweight

Arcelik's Q2 results came in stronger than we expected, particularly at the bottom-line level. The reversal of tax provisions in Q2 was an important one-off driver, but performance at the operating level was also pleasing, with hardly any sign of an adverse impact of the macro turbulence on Q2 numbers. Arcelik capitalises on significant economies of scale resulting from large capacity being produced under a single roof for each of its major products (refrigerators, washing machines, dishwashers and ovens, altogether 12m units pa); it has the country's most widespread and efficient distribution system (consisting of c4,500 dealers); and has a concentration of plants in low-cost regions, including its primary market, Turkey, as well as Romania and, most recently, Russia. This regional diversification, with Western Europe being the main sales market, helps Arcelik to generate 65% of its total unit sales and 40% of total turnover from outside Turkey, at present. The key developments recently have been the initiation of production in Russia in Q2 (a plant with capacity of 900,000 units for washing machines and refrigerators) and the start of exports to China and the US. In the upcoming months, Arcelik will make the critical decision on whether or not to make a green-field investment in China.

Following Q2 results, Arcelik's management stated that for the full year it was looking for 6% unit sales growth in Turkey, 20% growth in foreign markets, year-end turnover of USD4.2-4.5bn, EBITDA margin of 11% and net margin of c7%. This guidance looks in line with our pre-turbulence estimates for 2006 for Arcelik. Nevertheless, we prefer to leave some room for downside, especially taking into account the moderate fall in Q2 EBITDA margin to 9.5%, from 11.1% in Q1. We have therefore trimmed our previous forecasts slightly; we now expect full-year EBITDA margin of 10.0% (versus 10.1% in H1 2006) and net margin of 6.2%, on a total revenue estimate of USD4.2bn.

Arcelik – forecast changes

(USDm)	2005a	2006e old	2006e new	2007e old	2007e new	2008e old	2008e new
Revenue	3,806	4,297	4,207	4,696	4,586	5,073	4,937
EBITDA	416	477	421	521	472	563	518
margin	10.9%	11.1%	10.0%	11.1%	10.3%	11.1%	10.5%
EBIT	304	361	311	399	358	436	395
Net Profit	233	274	262	299	281	317	304

Source: HSBC estimates

On our estimates, Arcelik stands on 2006e PE of 9.9x, a discount to Electrolux's 11.1x and to Indesit's 14.8x, its closest peers in Europe. Generating almost double the operating margins of European peers, we could even justify a premium to peers for Arcelik. However, our fair value estimate is DCF based. On our revised forecasts, and considering new DCF parameters (incorporating a higher country risk profile), we now calculate a new fair value range of USD7.65-9.35 per share (vs USD9.24-11.76 previously). The mid-point of our new range is USD8.50 per share (USD3,400m in market capitalisation), down 19% from the previous USD10.5 but still indicating 30% potential upside from its closing price of USD6.52 on 25 August 2006. We maintain our Overweight rating on the company.

We see the possible catalysts in reaching our fair value as new brand/company acquisitions (in parallel with management's pronounced pursuit of inorganic growth opportunities) and stronger-than-expected penetration of targeted new global markets. Risks to our valuation would include a deterioration in consumer sentiment in Turkey and a hike in global raw material prices.

BIM (BIMAS.IS) — Neutral

We reviewed our BIM forecasts after stronger-than-expected H1 2006 figures and the company's upward revision in planned store openings (from 125 to 200). We raised our sales and profit estimates significantly on the back of impressive first-half numbers. As a result, despite our new set of parameters (higher FX rate, risk-free rate and risk premium) that would normally yield a lower valuation, our new notional target price of USD37.55 is higher than our previous target of USD30.64. We utilise peer comparisons in determining the lower end of our value range, which is USD31.92 per share (USD808m market value). We use DCF to calculate the higher end of the value range, which is USD43.17 per share (USD1,092m market value). Despite a significantly higher NTP than before, there is a limited 10% potential upside on the stock based on its closing price of USD34.12 on 25 August 2006. We maintain our Neutral rating.

The major risk to our rating is further M&A activity in the retailing sector. There have been three transactions in the sector recently. If we apply the average take-out multiples to BIM, the stock would have an upside potential of 13%. Downside risk would be an increase in competition either from existing players or new entrants that may curb the company's growth prospects.

BIM – forecast changes

(USDm)	2006e old	2006e new	2007e old	2007e new	2008e old	2008e new
Revenue	1,464	1,483	1,587	1,616	1,682	1,737
EBITDA	62	82	68	94	77	100
margin	4.2%	5.5%	4.3%	5.8%	4.6%	5.8%
Net profit	32	53	36	62	43	66
margin	2.2%	3.6%	2.3%	3.8%	2.6%	3.8%

Source: HSBC estimates

Cimsa (CIMSA.IS) — Overweight

Following its acquisition of Eskisehir Cimento and activation of new kiln investment in the Kayseri plant, Cimsa started 2006 with 1.1m tons of additional annual clinker capacity, representing a 50% increase. On top of this, the company recently announced its decision to increase the capacity of its new Eskisehir plant from 0.5m pa to 1.4m tons pa by the end of 2007, indicating a further 27% capacity expansion.

Additional capacity will help the company to increase its sales volume; however, most of the investments are financed by bank loans (totalling

USD155m), which will substantially increase the financial expenses of the company in the upcoming years. Moreover, the outstanding debt is in US dollars, which should result in higher FX losses this year due to weaker Turkish lira.

We have now incorporated into our forecast and valuation model the company's planned capacity upgrade at the Eskisehir plant, which should increase sales volume starting from 2008. Accordingly, we have raised our revenue estimate, particularly for 2008 onwards. On the other hand, we have cut our EPS estimates significantly, due to the expected rise in financial expenses, especially in 2006.

All in all, with our new WACC assumptions (8.0% risk free rate, and 5.5% equity risk premium) our DCF model yields a fair value of USD8.03 per share. Using peer comparison analysis, we arrive at a fair value of USD6.81 per share. Accordingly, we set our fair value range as USD6.81-8.03, with a notional target price of USD7.42 per share, down from USD9.56, implying 23% potential upside from its closing price of USD6.04 on 25 August; thus we maintain our Overweight rating.

The major risk to our valuation is further devaluation of the Turkish lira, which would increase the company's FX losses and keep earnings under pressure. Also, if interest rates continue to rise, this would slow construction activity further.

Cimsa – forecast changes

(USDm)	2006e		2007e		2008e	
Forecasts	Old	New	Old	New	Old	New
Revenues	342	333	369	374	384	417
EBITDA	146	128	157	144	160	159
margin	42.8%	38.4%	42.5%	38.5%	41.8%	38.3%
Net profit	105	64	114	86	118	103
margin	30.7%	19.3%	30.9%	22.9%	30.8%	24.7%

Source: HSBC estimates

Dogan Holding (DOHOL.IS) Neutral

Dogan Holding has considerable exposure to the consumption-sensitive media sector and a large FX short position; as such it has been under the pressure resulting from the depreciation of TRL during May and June 2006. A slight rebound of TRL strength and cash received from the sale of its Petrol Ofisi stake to OMV provided some relief and the stock has regained some ground recently.

As a result of these developments, which led to some financial expenses due to FX losses, we have revised our forecasts for the company as shown below.

Dogan Holding – forecast changes

(USDm)	2006e		2007e		2008e	
	old	new	old	new	old	new
Revenue	8,857.3	9,440.8	7,047.8	8,135.3	7,565.6	8,749.5
EBITDA	485.5	505.5	570.8	533.6	723.8	715.1
margin	5.5%	5.4%	8.1%	6.6%	9.6%	8.2%
Net profit	607.3	427.4	287.1	161.6	302.2	303.2
margin	6.9%	4.5%	4.1%	2.0%	4.0%	3.5%

Source: HSBC estimates

Petrol Ofisi, which was previously recorded under full consolidation in the financials, will be recorded as a JV after the sale is realised (in Q2 2006). As a result, we expect net sales to be negatively affected in 2007 unless Dogan includes a new asset in its portfolio. We do not expect a contraction in EBITDA because of upward revisions in all of the existing segments of the group. On the other hand we expect Dogan to record considerable 'other income' in 2006 which, we believe, should help to generate an improvement in bottom-line profitability from USD495m in 2005 to USD427m in 2006. Since 2005 and 2006 bottom-line figures are inflated by income associated with the asset sales, there will be a virtual contraction in profitability in 2007.

We continue to be positive on the value-adding nature of Dogan's management, and growth prospects of the existing segments, and we think that there could be many more opportunities on the agenda, such as lottery, energy and telecoms deals, given Dogan's net cash position of more than USD1bn. Dogan is keen to acquire electricity distribution companies in large cities, especially Istanbul. It announced that it plans to team up with a foreign company and bid aggressively for these electricity tenders, which we expect to be launched at the end of this year. The lottery, which is currently under state control, is set to be privatised in 2007. Dogan has stated that it believes the lottery fits well with its own business, having huge media power and an extensive distribution network. The privatisation of cable TV in Turkey could also provide the group with an opportunity for growth, as previously discussed by management.

Dogan has outperformed the ISE-100 index by 6% since the end of February. Dogan currently trades at 9% discounts to its current and target NAVs. We have now removed the discount we previously applied to the cash position, since we believe the market will start to price in the upcoming electricity tenders soon. Based on the current and target NAVs, we set our new valuation range as USD4.16-5.09 per share, versus our previous range of USD4.31-5.27. Our new notional target share price is USD4.62 (previously USD4.79), which offers 13% upside potential from the share price of USD4.11 on 25 August 2006. Therefore, we maintain our Neutral rating on the stock.

Possible plans of Dogan Holding to acquire a promising business would also represent upside risk to our Neutral rating. Downside risk could include Petrol Ofisi's plans to enter into oil exploration and the refining business, which could be considered as risky investments, additionally depressing profitability because of huge financing requirements.

Eczacibasi Ilac (ECILC.IS) Overweight

We have revised our forecasts and assumptions for pharmaceutical manufacturer, Eczacibasi Ilac Sanayi (EIS), taking into account the latest macroeconomic turbulence affecting the interest rate and currency valuations. We have valued EIS using DCF analysis and peer comparison methods. Taking into account our new WACC of 11.37% and a terminal growth rate of 3%, we calculate a DCF valuation of USD590m, while our peer comparison valuation results in USD610m (EV/EBITDA multiples are 10.9x and 9.0x and EV/sales figures are 2.1x and 1.8x for 2006e and 2007e, respectively). We have given equal weight to both of these valuations and revised down our notional target price for the stock to USD3.29 per share, in a range of USD3.23-3.34 (previous range: USD3.82-4.67, NTP USD4.24). We maintain our Overweight rating, with 32% upside potential (based on closing price of USD2.50 on 25 August 2006).

In our view, the most important recent development has been the company's authorisation of an international investment bank to evaluate possible partnership opportunities for some of its affiliates. With this mandate, EIS is trying to strengthen its competitive power and growth prospects in the sector. To support its vision to grow in the pharmaceutical sector, EIS has also decided to sell some of its financial assets to its parent company, Eczacibasi Holding, through which it will generate some USD8.4m gains this year. We also note that the recent 5% drug price increases both in July and August are supportive for EIS in terms of a relief for margins as the company has been suffering from rising production costs against constant selling prices.

Eczacibasi Ilac – forecast changes

USDm	2005a	2006e		2007e		2008e	
		old	new	old	new	old	new
Revenues	630	775	731	831	760	897	791
EBITDA	42	65	58	70	63	73	64
margin	6.7%	8.3%	8.0%	8.4%	8.2%	8.1%	8.1%
EBIT	20	39	35	44	40	46	41
Net profit	27	32	30	35	34	38	37

Source: HSBC estimates

The major risk to our valuation and rating is the possibility of a change in the legal framework in the Turkish pharmaceutical sector, especially within the pricing mechanism and reimbursement lists, as the state is the major consumer (85%) of the products.

Koc Holding (KCHOL.IS) Neutral

Following acquisitions of Tupras, Yapi Kredi and Tansas, worth USD6.0bn, within the last 12-month period – which were financed to a great extent by borrowing – Koc Holding has become one of the most leveraged groups in Turkey. In that respect, Koc's consolidated profitability has been one of the most vulnerable to the sharp devaluation of the Turkish lira in Q2 2006. Nevertheless, the recent strength in TRL suggests that in Q3 onwards Koc should recover from the huge FX losses it suffered in Q2. More critically, TRL's devaluation will not create more than a pure accounting impact in terms of FX losses, given the fact that Koc will not start paying back its Tupras loans before 2008. With some non-core businesses lined up for sale (ie heating equipment manufacturer, Turk Demirdokum, insulation materials producer, Izocam, and auto-parts company, Doktas), Koc is likely to reduce its indebtedness before actual repayments begin.

Our revised estimates for Koc reflect the anticipated impact of the recent turbulence, especially on the financial costs side. We have slightly lowered our consolidated revenue and EBITDA estimates; yet we are still looking for a boost in operating performance over 2005, with the consolidation of Tupras and YKB for the full year. However, we have cut our net profit estimate by 37% and are now expecting slightly lower profits for 2006 over 2005, versus our previous forecasts of a 56% y-o-y rise in EPS. We have not made any major changes to our forecasts for 2007 and beyond. Accordingly, we expect Koc to more than double its EPS in 2007 with the removal of the sharp devaluation impact from the accounts.

Koc Holding – forecast changes

(USDm)	2005a	2006e		2007e		2008e	
		old	new	old	new	old	new
Revenue	18,163	35,304	34,932	38,014	37,586	40,937	40,469
EBITDA	1,481	2,809	2,669	3,191	3,077	3,339	3,181
margin	8.2%	8.0%	7.6%	8.4%	8.2%	8.2%	7.9%
EBIT	902	1,868	1,627	2,161	2,009	2,302	2,129
Net profit	446	694	435	834	862	894	912

Source: HSBC estimates

Our revised estimates put Koc on 2006 PE of 10.5x (vs Sabanci's 10.4x) and 2007 PE of 5.3x, particularly cheap when compared to Sabanci's 9.9x. However, as with all the Turkish conglomerates, we base our fair value calculation for Koc on NAV. Including Tupras and related loans, we calculate Koc's current NAV as USD5.3bn (using current market prices for listed subsidiaries) and its target NAV as USD6.3bn (using our notional target price estimates for the listed subsidiaries). Accordingly, Koc trades at an 11% discount to its current NAV and a 26% discount to its target NAV. We consider such a discount level justified for large Turkish conglomerates, especially for Koc, which does not offer much scarcity value beyond its listed participations that account for more than 80% of its total portfolio value. Having finalised inorganic growth plans for the foreseeable future, and thus unlikely to participate in the remaining privatisation deals (such as electricity distribution) Koc also lacks a near-term catalyst which would help narrow the NAV discount rates notably, in our view. Assuming that a discount interval of 15-25% to target NAV would be fair for Koc, we calculate a new fair value range of USD3.80-4.31 per share (USD5.68-6.54 previously). The mid-point of USD4.06 per share (USD5.13bn in market value) is our new notional target price (previously USD6.11), which indicates a limited 13% potential upside from its closing price of USD3.60 on 25 August 2006. We therefore downgrade our rating to Neutral from Overweight.

Koc Holding – summary NAV table

Current NAV			Target NAV		
	Stake value	% of NAV		Stake value	% of NAV
Total listed	6,997	132%	Total listed	8,052	127%
Total unlisted	1,608	30%	Total unlisted	1,608	25%
Net cash	-3,313	-63%	Net cash	-3,313	-52%
Current NAV	5,292		Target NAV	6,348	
Current MCAP	4,783		Current MCAP	4,783	
Prem/(disc)	-9.6%		Prem/(disc)	-24.7%	

Source: HSBC estimates

The main upside/downside risk to our valuation and Neutral rating would be a faster/lower-than-expected turnaround in new acquisitions, particularly Tupras and YKB. We would also view further market volatility and depreciation of the TRL as a downside risk, considering Koc's interest rate-sensitive businesses (such as autos and durable goods) and its higher leverage after the acquisitions.

Migros (MIGRS.IS) Neutral

We reviewed our estimates for Migros in view of our new forecasts on key macro parameters. Using a higher risk free rate (from 7% to 8%) and equity risk premium (from 5% to 5.5%) in DCF assumptions, we lowered our fair value range to USD8.90-9.48 (from USD11.40-12.15). This indicates a new notional target price of USD9.19 (from USD11.78), indicating no upside potential on the stock from its closing price of USD9.30 on 25 August 2006. Neutral rating maintained.

The main upside/downside risk to our valuation is the possibility of a higher/lower operational efficiency gain (other than we have estimated) created as a result of the Tansas merger.

Migros – forecast changes

USDm	2006e		2007e		2008e	
	old	new	old	new	old	new
Revenue	3,326	3,040	3,740	3,297	4,042	3,604
EBITDA	231	208	278	239	305	270
margin	6.9%	6.8%	7.4%	7.2%	7.5%	7.5%
Net profit	120	56	163	118	180	162
margin	3.6%	1.9%	4.4%	3.6%	4.5%	4.5%

Source: HSBC estimates

Nortel Netas (NETAS.IS) Overweight

Nortel Netas (NN), the provider of half of Turkey's fixed-line infrastructure, has also been harmed by the recent economic turbulence, which has delayed our positive expectations of the telecoms equipments sector further. Even though we believe in the urgency of some of the projects scheduled to begin next year, we think that the recent economic turbulence will result in up to 40% lower investment expenditures by the telecom operators within the next two years, compared with our initial assumptions.

Based on the Q2 results, higher monetary losses and a reduction in growth expectations, we revised our forecasts for NN downwards as per the table below. We cut our 2007 and 2008 net sales forecasts by 35% and 36%, respectively. Our EBITDA forecasts for NN are also reduced by 41% and 30% to USD16m and USD20m, respectively. This revision, coupled with higher country risk premiums (8% risk free rate instead of 7% before the economic turbulence), has led a significant reduction in our valuation range to USD27.46-34.20, implying a notional share price target of USD30.83, from USD43.20. This new price target offers 40% upside potential from the share price of USD22.07 on 25 August 2006. We reiterate our Overweight rating.

Nortel Netas – forecast changes

(USDm)	2006e		2007e		2008e	
	old	new	old	new	old	new
Revenue	106.6	102.7	187.2	121.0	240.4	154.4
EBITDA	17.4	14.7	27.6	16.3	29.0	20.3
margin	16.4%	14.4%	14.7%	13.5%	12.1%	13.2%
Net profit	12.4	7.9	20.2	11.3	21.2	14.5

Source: HSBC estimates

We think that encouraging developments in recent years – ie liberalisation, the privatisation of Turk Telekom, Vodafone's entrance, the restructuring of Avea and a stronger Turkcell – have not yet been priced into NN shares by the market. Even with a delay, we think the upcoming investments from these companies, which include the improvement and expansion of networks, switches and base stations, and the implementation of new technologies, offer enticing prospects for Turkey's telecoms equipment manufacturers. NN is among the best positioned to benefit from the expected pick up, which should start in the second half of 2007. NN's proven track record with Turk Telekom and Avea, and parent company Nortel Networks' ongoing co-operation with Vodafone Group in many countries are the major factors that we believe place NN one step ahead of its competitors.

Based on increasingly positive sector newsflow, our expectations of a recovery in financials in 2007 and an attractive valuation, we maintain an Overweight rating for the stock. However, although NN has a good relationship with the operators, this does not guarantee success in upcoming tenders, therefore tender outcomes represent the greatest risk to our rating. Owing to intensifying competition, NN might be unwilling to undertake some tenders, or could lose out to its competitors. The TT, Avea and Vodafone tenders, which we expect to be held towards the end of the year, will be critical.

Petkim (PETKM.IS) Neutral

Petkim started to benefit from higher production volumes (due to the recent capacity increase from 1.35m to 1.65m tons) and slightly better market conditions in 2006. A y-o-y recovery in the 2006 performance, due to easier comparisons with 2005, has proved to be a positive catalyst for the share price. Petkim shares have been resilient to the recent economic turbulence, since the impact on operations is limited and the company does not carry a short FX position: Since 8 May 2006 until the beginning of August, Petkim shares have outperformed the ISE-100 index by 12%.

On the other hand, the ongoing surge in energy prices, increasing import product sales and recent economic conditions continue to put pressure on margins and could therefore lead to worse-than-expected growth figures for the company. Hence, we have revised our estimates for the following years downwards. Our EBITDA forecasts for 2006 and 2007 have been revised from USD143m and USD134m to USD98m and USD95m, respectively, due to higher costs associated with the naphtha purchases.

Petkim – forecast changes

(USDm)	2006e		2007e		2008e	
	old	new	old	new	old	new
Revenue	1,298.0	1,398.0	1,369.4	1,474.9	1,273.6	1,371.6
EBITDA	143.2	97.5	133.9	95.0	65.4	50.5
margin	11.0%	7.0%	9.8%	6.4%	5.1%	3.7%
Net profit	52.1	40.7	42.0	31.0	-23.1	-22.1

Source: HSBC estimates

During H2 2007-09, we expect product prices to decline gradually to lower levels, based on the commissioning of new petrochemical capacity globally but especially in the Middle Eastern region. Therefore, we see long-term prospects as weaker vs 2006.

We have incorporated the new downgraded forecasts in our DCF analysis, which employs a risk-free rate of 8% (instead of 7% previously) and a WACC of 11.8% (instead of 10.5%). As result, we have revised our valuation range from USD4.18-5.10 to USD3.53-4.77 and notional target price from USD4.64 to USD4.15. There now exists a 20% upside potential to our new notional target price of USD4.15 per share versus its closing price of USD3.46 on 25 August 2006. However, despite our expectation of a recovery in the financials in 2006, we maintain our Neutral rating on the stock due to unattractive long-term prospects and privatisation dependent share price performance in the coming months, in our view.

Under the scenario of a block sale with strong bidders, Petkim could become a target of M&A and we may see investors reacting very positively to it. If the potential acquirer agrees to pay a significant premium (for the controlling stake) on the market value, then it could have a positive impact on the share price, even though the process does not require a mandatory tender offer for the minorities. A sharp decline/increase in oil prices and changing product prices will be the other risks to our rating.

Sabanci Holding (SAHOL.IS) Overweight

We see three potential catalysts that may affect Sabanci's NAV and share price positively:

- An improvement in NAV transparency as a result of the pending listing of the retail business, Carrefoursa, to be followed by global tyre cords business, Kordsa.
- Its growth plans for the energy sector. Sabanci has already begun some solid implementation on the generation front, and upcoming electricity distribution privatisations (expected in Q3 2006) offer further opportunities.
- Progress in Akbank's strategic partnership mandate.

Two developments which should improve Sabanci's NAV transparency are the listing of the retailing business, Carrefoursa (a JV between Sabanci and Carrefour), following its acquisition of listed retailer, Gima, and that expected for Kordsa, the tyre cords operation. In our NAV model, we attach values of USD1.5bn for Carrefoursa and USD800m for Kordsa, which together account for 15% of our estimated target NAV. The listing of the two businesses at a premium to our estimates would further deepen Sabanci's discount to NAV, and make it look even more attractive on a sum-of-parts basis.

In energy, Sabanci has officially communicated its aggressive growth plans by investing USD4.5-5.0bn to capture 10% of the market by 2015, which would correspond to a total established capacity of up to 5,000 MW. Implementation has already begun on the generation front; Sabanci has acquired two coal reserves, aims to build two power plants, and has bought a hydroelectric plant in Turkey. On the distribution front, the pending sale of regional electricity distribution rights, the single largest item left in the state's privatisation agenda, presents an attractive opportunity for Sabanci. Sabanci aims to bid for five or six of the 20 regional tenders.

On the other hand, as markets stabilise following the recent macro turbulence, foreign interest in the Turkish banking sector is likely to continue, and Akbank stands out as a potential beneficiary because it is seeking a minority stake partnership. As one of the major shareholders of Akbank (with a 34% stake), Sabanci Holding may benefit in the event of a deal with a foreign partner, which could add value to the bank's long-term strategy.

Another recent positive development has been the sale of the pet resin and bottle segment of Advansa, Sabanci's global chemicals company, to Spain's La Seda. This is part of Sabanci's restructuring efforts in its non-financial operations with the aim of improving the overall profitability of the portfolio, and is a good example of a successfully implemented exit strategy.

We are maintaining our financial forecasts, which we had set before the market volatility. Akbank achieved 19% growth in its net profit in H1 2006 y-o-y and has proved resilient to the recent turbulence, as we expected. The bank is the single largest contributor to Sabanci's consolidated bottom line and its strong performance has persuaded us to maintain our existing forecasts.

Sabanci Holding – summary forecasts

(USDm)	2005a	2006e	chg	2007e	chg	2008e	chg
Revenue	10,608	11,811	11%	12,694	7%	13,419	6%
EBITDA	2,207	2,294	4%	2,442	6%	2,583	6%
margin	20.8%	19.4%	-7%	19.2%	-1%	19.2%	0%
EBIT	1,833	1,868	2%	1,964	5%	2,052	5%
Net profit	514	615	20%	649	6%	658	1%

Source: HSBC estimates

We calculate that Sabanci trades at a 20% discount to its current NAV and a 30% discount to its target NAV, which we find excessive, especially ahead of its expected bids for regional electricity distribution rights, which may well act as a positive catalyst to help narrow its NAV discount. In our view, it would be fair to assume a discount interval of 10-20% to target NAV for Sabanci, which would yield a fair value range of USD4.27-4.79 per share (vs USD5.16-5.95 per share previously). The mid-point of the range is USD4.53 per share (USD8.16bn in market capitalisation), which is our new notional target price (previously USD5.56 per share). The implied potential upside to our new NTP is 27% based on its closing price of USD3.56 on 25 August 2006. We maintain our Overweight rating.

Sabanci Holding – summary NAV table

Current NAV			Target NAV		
	Stake value	% of NAV		Stake value	% of NAV
Total listed	5,625	67%	Total listed	6,542	68%
Total unlisted	2,528	30%	Total unlisted	2,804	29%
Net cash	250	3%	Net cash	250	3%
Current NAV	8,403	100%	Target NAV	9,597	100%
Current MCAP	6,690		Current MCAP	6,690	
Prem/(disc)	-20.4%		Prem/(disc)	-30.3%	

Source: HSBC estimates

We see as the key risk to our rating a major delay in energy privatisations and/or Sabanci's failure in terms of its growth plans in this business, particularly the electricity distribution tenders.

Sisecam Holding (SISE.IS) Neutral

We have revised our target value for Sisecam, reflecting our new targets for Trakya Cam and Anadolu Cam. Having incorporated these two changes into our NAV model, we set our new valuation range for Sisecam Holding as USD3.39-3.72 (from the previous USD4.57-5.25). We reach the lower end of our valuation range by applying a 10% discount to target NAV of the company. The higher end, on the other hand, has been calculated using 2007e average multiples of peer group (13.5x PE and 4.7x EV/EBITDA). Our notional target price is the mid-point of our range, and stands at USD3.56 per share (from USD4.91), indicating 18% upside potential based on its closing price of USD3.01 on 25 August 2006. We are maintaining our Neutral rating on the stock.

Sisecam Holding – forecast changes

USDm	2006e		2007e		2008e	
	old	new	old	new	old	new
Revenue	1,923	1,786	2,057	1,801	2,133	1,935
EBITDA	577	424	615	452	650	499
margin	30.00%	23.70%	29.90%	25.10%	30.50%	25.80%
Net profit	131	51	157	95	177	134
margin	6.80%	2.90%	7.60%	5.30%	8.30%	6.90%

Source: HSBC estimates

The main risk to our rating is the strong currency, as costs in the glass sector are mainly TRL denominated but prices are generally determined in foreign currencies. Upside risk comes from the greater efficiency that can be achieved from the energy-saving operations.

Vestel Elektronik (VESTL.IS) Neutral

As one of Turkey's leading exporters, generating 75% of its turnover from exports, Vestel has benefited at the operating level from the sharp devaluation of the Turkish lira in Q2. As opposed to 15% of COGS being denominated in TRL, revenues are fully linked to FX (including pricing in the domestic market where FX adjustments come with a 15-30 day lag versus instant adjustment for exports), which creates extra margin for the company in times of higher depreciation of TRL than inflation rate. The company also records one-off inventory gains when TRL depreciation is fast. On the other hand, Vestel is a highly leveraged company, carrying a net FX exposure of around USD400m. Therefore, the benefits created at the operational level from a depreciating TRL are given away at the bottom-line level because of greater FX losses.

The strengthening of the Turkish lira recently suggests a smoothing out of Q2 extremities from Q3 onwards; ie we expect a normalisation in both inflated operating margins in Q2 and FX losses starting from Q3. But in any case, margins should benefit from a higher devaluation of TRL this year compared with previous few years and the bottom line should suffer from a rise in financial costs. We have reflected this anticipated impact on our financial forecasts and raised our EBITDA margin estimate for 2006 but cut our net profit forecast.

Vestel Elektronik – forecast changes

(USDm)	2005a	2006e		2007e		2008e	
		old	new	old	new	old	new
Revenue	3,287	3,632	3,777	3,822	4,128	4,146	4,297
EBITDA	205	243	283	271	293	303	314
margin	6.2%	6.7%	7.5%	7.1%	7.1%	7.3%	7.3%
EBIT	115	134	170	157	169	178	185
Net profit	64	88	37	79	61	82	83

Source: HSBC estimates

We have also revisited our DCF-based valuation using new financial forecasts as well as new parameters, reflecting Turkey's higher risk profile following the recent macro turbulence. Our new fair value range, derived by flexing the stock's beta, has come down to USD2.61-3.18 per share (from USD3.39-4.15), the mid-point of which is USD2.89; our new notional target price (vs previously USD3.77), indicates 11% potential upside from its closing price of USD2.61 on 25 August 2008. We maintain our Neutral rating on the stock.

Upside risk could come from any engagement in M&A activity and/or stronger-than-expected growth in new markets such as Russia. Larger-than-expected price falls for televisions in global markets would keep Vestel's margins under pressure and represent the main downside risk, in our view.

Recent company reports

Company reports

Akenerji (AKENR.IS) **Neutral**

For more detail, please refer to reports published by Ozgur Goker, available on www.research.hsbc.com

Our most recent note on Akenerji (*Recent Power Failure: An Opportunity or a Threat?* published 13 July 2006) was a response to the major power failure on 1 July in Turkey, an incident which brought to surface problems regarding electricity tariffs in Turkey and implications on independent producers such as Akenerji. A summary of the note is presented below.

We have revised our valuation range for Akenerji to USD1.65-2.75 per share, the mid-point of USD2.14 being our new notional target price (vs USD3.90 previously). Our revision is based on the new currency, risk-free rate and electricity price expectations we used in our DCF model. With limited upside potential and considerable uncertainty for the operating environment, we maintain our Neutral rating on the stock.

Firstly, we are not expecting a electricity tariff increase in the short term, especially not while government is struggling with an inflation problem. We believe that the government is counting on the un-utilised public generation capacity.

Secondly, we believe that the elimination of some taxes levied on the cost structure of IPPs is highly likely. Media stories claim that Akenerji is planning to shut down one of its plants, as are some other IPPs, as the cost of production has reached an unsustainable level. So we believe the government may relieve some of the burden on the private sector's cost structure.

Finally, although the current tariff structure implies only losses for the company, we believe a Neutral rating is justified on the stock because of its strong position in a sector with tremendous growth prospects, if ongoing issues are resolved.

Teaming up with a strong partner in the upcoming electricity distribution tenders or in the state generation assets sale represents upside risk to our rating. Any relief in terms of the cost structure will also represent upside risk, as our model is very sensitive to prices.

On the other hand, further increase in fuel prices or a reduction in tariffs will be a downside risk for our rating. Also any news about possible legal action in the sector, even unrelated to Akenerji, would be perceived as negative for the stock.

Anadolu Cam (ANACM.IS) **Overweight**

For more detail, please refer to reports published by Gunes Ozdemir, available on www.research.hsbc.com

In a recent company update on Anadolu Cam (*Less Vulnerable to Economic Downturn*, published 14 July 2006), we upgraded our rating on the stock to Overweight from Neutral. Below we present the key points from the report.

We revisited our forecasts on the back of our new macro forecasts (both for Turkey and Russia) and recent Q1 financials. Our valuation range of USD3.84-4.88 yields a notional mid-point target of USD4.36 per share. Our valuation is based on DCF (8% risk free rate, 5.5% equity risk premium, 0.9 company beta and 2% terminal growth rate) and peer group multiples (11.3x 2007e PE and 5.8x 2007e EV/EBITDA). We rate Anadolu Cam as Overweight.

As Anadolu Cam generates c40% of its revenues from overseas operations (mainly from Russia) and as the company supplies products to those industries (mainly beverages, food and pharmaceuticals), which are more or less resilient to the turbulence in the economy, we are not changing our forecasts drastically, other than adjusting for our new FX rate assumptions. Besides this, as only 10% of the costs of the company are FX linked, the rise in FX rate will not have a major impact on the EBITDA margin, in our view. The company's bottom line, however, is vulnerable to the rise in FX rate, although the impact should not be huge. According to the Q1 2006 financials, Anadolu Cam has USD150m net short FX position. As the bulk of the financial debt is taken by the company's participation in Russia and as the rouble has strengthened against the dollar, the company will not realise any FX losses due to this portion of its short position.

Anadolu Cam is planning to increase its product prices but we believe if this materialises it will be less than the rise in FX. In our analysis we have not factored any such rise in prices in 2006. Given the new plant acquisition in the eastern part of Russia by one of the company's largest customers (Anadolu Efes), the company could initiate another furnace investment in this country; however, we have not included such an expansion in our model. Recall that Anadolu Cam's previous furnaces are very close to Anadolu Efes' factories in Russia.

Downside risks to valuation would be that growth in beer demand is slower than we expect, especially in Russia, and any further increases in energy prices. Moreover, the entry of a strong global player into this market may curb the company's expansion policy in Russia.

Anadolu Efes (AEFES.IS) Neutral

For more detail, please refer to reports published by Gunes Ozdemir, available on www.research.hsbc.com

We downgraded our rating on Anadolu Efes to Neutral from Overweight in a recent company note we published on 11 August 2006 (*Anadolu Efes: A Stock for Hard Times*). A summary of our view is presented below:

We reviewed our estimates for Anadolu Efes, taking into account our new forecasts for key macro parameters, as well as the company's recently announced first-half volume figures.

In view of the actual H1 2006 volume results, we have changed our volume forecasts slightly, incorporating the sale of the Romanian brewery unit and also using higher growth estimates for the international coke operations. However, as product price hikes in the domestic market (around 3%) following the volatility have lagged the devaluation rate (around 10%), we have revised down our revenue and EBITDA margin estimates. Our revised net profit forecast indicates a sharper decline than in EBITDA because we considered the additional negative impact on net profit from the weaker TRL, given that the company has a net FX short position of USD154m (excluding a USD500m loan raised by EBI recently, which is excluded from calculations of Anadolu Efes' FX position).

We continue to use a sum-of-parts valuation method for Anadolu Efes. We have determined the low end of our valuation range by using the current market prices for the listed operations and DCF for unlisted operations for the underlying assets. For the high end, we have mainly used peer group multiples. Using a higher risk-free rate and equity risk premium in our DCF assumptions, we lowered our fair value range to USD28.04-29.81 (from USD34.62-36.88). This indicates, at the mid-point, a new notional target price of USD28.93 (cut by 19% from USD35.75).

The main upside/downside risk to our valuation is higher/lower-than-expected growth and market share gains/losses in the Russian beer market. In our revised model, we are assuming 5% growth pa in the Russian market in 2006-10, and we project a slight improvement in its market share. The risk is that we prove too conservative in our estimates in the event that Anadolu Efes, following the acquisition of Krasny Vostok (KV), enters untapped areas in Russia more aggressively than we assume. Our new target price is also vulnerable to any hike in special consumption tax (SCT) for beer, above the CPI increase. Tax hikes on alcoholic beverages have been one of the main tools used frequently by governments in Turkey to expand tax revenues. Also, if during the remainder of the year the TRL depreciates more than we assume in our forecasts (ie 6%), then Anadolu Efes may outperform due to its defensive nature; particularly because of its huge overseas operations, especially in Russia, where the currency is doing well against the greenback.

Dogan Yayin Holding (DYHOL.IS) Neutral

For more detail, please refer to reports published by Gunes Ozdemir, available on www.research.hsbc.com

We upgraded our rating on Turkey's leading media company, Dogan Yayin Holding (DYH), to Neutral from Underweight in a recent company note published on 31 July 2006, *Both Upside Potential and Downside Risks Appear Limited*. A summary of the report follows.

We have revisited our forecasts for Dogan Yayin Holding (DYH) on the back of our revised key macro forecasts for Turkey, the company's recently announced ad revenue figures for H1 2006 (33% growth y-o-y, broadly in line with forecasts) and our revised ad market estimates. We cut our ad spending forecasts by 12% for 2006 and 21% for 2007 in dollar terms. For 2006, we slightly lowered our previous expectation of 25% growth to 20% growth (in TRY terms). For 2007, we kept our 20% growth forecast intact.

Lower forecasts for ad spending and TRL weakness were the two major factors in our revisions for DYH. Along with the drop in EBITDA estimation, DYH's substantial short FX position led us to cut the net profit of the company significantly. For 2006, we now expect USD11m net profit vs our previous USD70m net profit estimate. For 2007, we cut our net profit estimate from USD115m to USD52m.

We use a sum-of-the-parts and DCF analysis (8% risk free rate, 5.5% equity risk premium vs our previous parameters, 7% risk free rate and 5% equity risk premium) to reach our fair value for DYH. Our sum-of-the-part analysis indicates USD2,075m (USD3.41 per share). Our DCF analysis, on the other hand, indicates USD2,004m (USD3.29per share). Accordingly, the two valuation methods yield a new price target range of USD3.29-3.41 per share (previously USD3.54-3.91), and our new notional target price is set as USD3.35 (previously USD3.73). Since there is no major downside potential implied by our new NTP, we upgrade to Neutral from Underweight.

We interpret the recent entry of Rupert Murdock's News Corporation into Turkish media market (via the acquisition of 56.5% of TV channel, TGRT, from the Ihlas Group) as a clear signal of increasing competition in the TV segment. Hence, DYH's mainstream TV channels may face a challenge in terms of audience share, which in turn may adversely affect their ad shares. According to 2005 figures provided by DYH, premium mainstream channels (Kanal D, ATV, Show TV and Star TV) have a 52.5% audience share. Second-tier national channels and others have 27.7% and 19.8% audience shares, respectively. Hence, NewsCorp may target audience share from the second-tier channels and others, which may be easier than taking share from the premium ones. On the other hand, we do not expect a major pressure on ad prices, as we believe that already very low ad prices in Turkey compared to European countries will prevent

NewsCorp from competing aggressively in terms of prices. As we already expected a more competitive environment in the TV segment in the near future, we are not revising our ad share forecasts for DYH's TV channels following the entrance of NewsCorp.

The main upside/downside risk to our estimates and rating is any improvement/deterioration in Turkey's macro parameters. This would significantly affect our ad market assumptions. Apart from this, further downside risk would be an increase in the pace at which foreign players enter the sector, especially if the 25% legal limit for foreigners owning broadcasting assets is lifted. As we have previously mentioned, the government is willing to remove this cap, but due to strong opposition, especially from President Sezer, the change is not yet on the agenda. We have already witnessed NewsCorp entering the market with a local partner in order to by-pass the 25% limit. On the other hand, an upside risk would be DYH teaming up with a strong international media company, which may strengthen its dominant position in the sector.

Erdemir (EREGL.IS) Underweight

For more detail, please refer to reports published by Ozgur Goker, available on www.research.hsbc.com

In our recent company note on Erdemir, *Hard Days Ahead in a Cyclical Downturn*, published on 3 August 2006, we reiterated our Underweight rating on the stock. We summarise the key points from the note below.

We expect global steel demand to remain strong until the end of Q3 2006, leading to steel shortages and rapidly increasing prices. But it is our view that the steel demand cycle and the price cycle will turn in 2007, at least partly because of excess capacity in China. A major factor leading to a potential fall in prices is destocking – caused by apparent consumption rising faster than real consumption.

With no limitations on the import of steel products, prices in Turkey should follow global trends. Given that Eregli should experience somewhat higher prices due its monopoly position, we expect a 15% y-o-y drop in average steel prices in 2007. Lower prices and a contraction in margins could lead to a contraction in operational profitability, which would be a major negative catalyst for the stock for the upcoming quarters. Obviously, falling prices would create an overhang on the stock's performance.

Following its privatisation, we believe that Eregli has room for efficiency improvement and growth in the long run. Despite a lack of sector expertise, the new owner, OYAK Group, may apply strong logistics to future developments and improve margins in the longer term. But we still remain cautious about the new owner's strategies. Investors have not received any detailed information from top management about the details of its future strategy. OYAK Group is also constrained by the agreements it signed during the privatisation process, which limits the total number of employees to be laid off to 5% until 2007. Thus it may take until 2008 before any major improvement in operational efficiency is possible. In our model we do not factor in major productivity improvements until 2008.

Having factored a sluggish steel price outlook for 2007 and limited efficiency improvement potential under new management into our forecasts, we revised our notional target price range downwards from USD5.07-6.20 to USD3.60-6.44, and our notional target price from USD5.64 to USD5.02 per share. The lower end of our range is defined by international comparison analysis, and on our revised estimates for 2006 and 2007, Erdemir looks unattractive in terms of multiples. On the other hand, our DCF model, using a risk-free rate of 8% instead of 7% and a WACC of 11.3% instead of 10.1%, yields a higher fair value, indicating the long-run (2008 and beyond) benefits of being operated privately. Since the mid-point of the two valuation methods does not offer any potential upside, we maintain our Underweight rating on the stock.

Higher-than-expected steel prices in 2007 and 2008 provide the major upside risk to our rating. Also, any positive development regarding partnership opportunities for Erdemir would potentially be viewed as positive news for the stock. Announcements about the court cases related to privatisation and the dispute over the 2005 dividend would also affect the stock, based on the outcomes.

Hurriyet (HURGZ.IS) Overweight

For more detail, please refer to reports published by Gunes Ozdemir, available on www.research.hsbc.com

In a recent company note on Hurriyet, *Good Entry Point for Long-Term Investors*, published on 19 July 2006, we upgraded our rating on the stock to Overweight from Neutral. The key points are summarised below.

We revisited our ad market growth forecasts, in parallel with the revisions to our key macro estimates for Turkey. For 2006, we have slightly lowered our ad market estimate from USD2.1m to USD1.8m. The new figure now denotes a 0.49 ad/GDP ratio as opposed to 0.51 previously. For 2007, however, we believe that new entrants to the Turkish market, eg Vodafone (through Telsim), Oger Telekom (through Turk Telekom), NBG (through Finansbank) and Dexia (through Denizbank) will keep ad growth rates at high levels. In addition, we expect an increase in ad spending approaching the general election period. With these factors in mind, we maintain our 19% growth in TRL terms (but only 7% in USD) for 2007. Our ad/GDP forecast for 2007 now stands at 0.51, still significantly below Eastern European levels.

We reviewed our Hurriyet forecasts based on the change in our ad market forecasts and sale of a stake in its auto-dealership company to its parent company. As all of the revenues of the company are TRL based and the cost of newsprint (which makes up around 30% of the COGS) is dollar based, we expect a contraction in margins compared with our previous estimates. However, please note that our analysis does not include any cover price increases for 2006, which would be a positive surprise. Hurriyet's bottom line is also vulnerable to changes in FX due to its cUSD32m FX short position.

We value Hurriyet using a combination of DCF and peer group analysis. Our average, peer group multiples are 15.7x 2007e PE and 7.6x 2007e EV/EBITDA. A peer comparison indicates a target value of USD1,112m or USD2.67 per share. We have also changed our risk premium assumption based on the recent developments in the markets. We have increased our risk-free rate from 7% to 8% and risk premium from 5% to 5.5%, yielding a value of USD918m or USD2.20 per share. Thus, our notional target price stands at USD2.44 (previous USD4.04), which is the mid-point of our target range of USD2.20-2.67 (from previous USD3.76-4.33).

In the long term, we expect ad spending/GDP levels in Turkey to move towards Eastern European levels (according to 2005 figures, this ratio is 0.46% for Turkey, the same ratio is 2% for Hungary, 1.4% for Poland, 1.2% for Bulgaria) and with a share of c14% in the ad market, Hurriyet will be among the main beneficiaries of the sector.

The main risk to our estimates and rating is the change in macro parameters. A sharp movement in the FX rate from current levels (in either direction) may lead us to revisit our FX rate, growth and risk-free rate, and hence ad market assumptions. Besides this, being a pure domestic play the company's shares react negatively during sell-off periods.

Petrol Ofisi (PTOFS.IS) Neutral

For more detail, please refer to reports published by Bulent Yurdagul, available on www.research.hsbc.com

In a recent company update on Petrol Ofisi, *A bold but risky investment in refining segment*, published on 24 July 2006) we maintained our Neutral rating but revised our forecasts and valuation on the stock. Below is a summary of our view.

Petrol Ofisi applied to the regulatory authority to build a refinery of around 200kbpd capacity in southern part of Turkey. We agree that planned development is a must for the firm, but it might bring a multi-billion dollar financial burden and uncertainty for minorities since it is a very long-term call. The sector has experienced surprising announcements for new capacity recently from different players, eg the Indian Oil-Calik-ENI consortium, Lukoil. If all projects on the agenda are realised, this implies a doubling of refining capacity in Turkey in the coming four years, when Petrol Ofisi's refining assets are expected to become operational. The refining segment, which currently lacks competition, could become one of the most competitive within four to five years. Since the planned refinery will supply Petrol Ofisi's own retail network, the competitive environment may not be a problem, but a possible change of outlook in the refining segment in the long run is a risk for the return on the investment. In addition, a refinery with 10m tons capacity per annum will require substantial investment of up to USD2.0bn. Considering the already leveraged financial structure of Petrol Ofisi, we need more information about the financing of the project. If financed by Petrol Ofisi, larger loans and maybe shareholder support could be possible negative triggers for the investors in the short and medium term. Until clearer data are released we maintain our cautious stance on this investment project.

Shell Turkey, which has a stake in Turkey's only refinery, Tupras (TUPRS.IS), recently announced that it has completed its Turcas acquisition. Together with Turcas, Shell reached a 23% market share and announced that it aims to achieve a number one place in the retail segment by the beginning of 2008; however, we do not think that price-cutting will be a method used to achieve this target. OPET, the number four player after the Tupras acquisition, is still aggressive in terms of capturing market share and has enjoyed significant growth during the last three years. A new player, Russian Lukoil, has recently applied to the regulator to establish a distribution and refining business in Turkey. If Lukoil manages to acquire a distributor, as has recently been reported in the local press, it might have an impact on the competitive environment as well.

Petrol Ofisi is still strong and has been very successful in defending its position. But we think that the competitive environment in the retail segment will not be a positive catalyst for Petrol Ofisi, as we see no significant long-term upside potential in distribution premiums and market share for the company from next year. Defending its current share in the long run, with margins maintained at 2006e levels, will be the best-case scenario for the company, in our view.

Our DCF analysis with higher WACC and revised forecasts suggest a new fair value range of USD3.69-4.70, with a mid-point of USD4.19, compared with our previous fair value range of USD5.28-6.46 with a mid-point of USD5.87. Despite the 42% fall in the share price in USD terms in the last three months and 17%

underperformance relative to ISE-100 index, limited upside potential, along with uncertainties and possible financial burdens arising from the long-term strategies on refining investment and exploration opportunities, lead us to retain our Neutral rating on Petrol Ofisi relative to other Turkish stocks.

Possible negative impacts on Petrol Ofisi as a result of the Koc Group's Tupras acquisition on the supply side, as well as stronger competition than we assume in the distribution market, represent the major downside risks to our rating. On the other hand, a successful plan to diversify the product portfolio, positive relations with Tupras in the short-to-medium term and fewer-than-expected competitors (resulting in a sustained improvement in the distribution margins) in the market would provide the major upside risks to our Neutral rating.

Trakya Cam (TRKCM.IS) Overweight

For more detail, please refer to reports published by Gunes Ozdemir, available on www.research.hsbc.com

We reiterated our Overweight rating on Trakya Cam in a recent company update published on 11 July 2006, *Potential Upside of 36% Despite Halving Forecast*. Below we present key points from our note.

The construction sector is one of the most sensitive to the change in interest rates. After the recent turmoil in the markets, monthly housing loan interest rates increased from 1.0% levels (12% pa) to 2.0% (24% pa). We may see more noise, especially from the political arena (presidential election and EU front) during H2 2006-H1 2007, that may keep interest rates at a high level. In such an environment, we expect that new housing construction will slow down. In that context, we revisited our estimates for Trakya Cam, as the company generates c70% of its revenue from glass provided to the construction sector.

The Undersecretariat of Foreign Trade (UFT) imposed quotas on the products coming from China for 2006-09 in April and recently imposed extra financial tariffs (USD40 per ton) for products imported from Russia, Ukraine and Iran. Quotas related to products coming from Russia, Iran and Ukraine expired at the end of June (from Russia 36k tons, from Iran 13k tons and from Ukraine 5k tons, effective between June 2003 and June 2006).

When we analyse last year's import prices, the new tariff brings Russian prices to USD276 per ton, Ukraine's prices to USD322 and Iran's to USD304 compared with Trakya Cam's sale price of around USD330 (using current FX rates). Although this new tariff narrows the gap between the prices, Trakya's price is still higher than the imported products from Russia, Ukraine and Iran. While its products are of higher quality than those coming from Russia, Ukraine and Iran, for price-sensitive customers Trakya may still face stiffer competition.

In addition, we have some concerns regarding the supply/demand balance of the aforementioned countries and the region in the near term. In Russia, strong housing construction demand means that total float glass capacity is planned to be increased by about 50% in the near term by the scheduled investments starting from 2006. With the new capacity, we expect based on media reports that Russia's total capacity will exceed its demand; hence Russian producers may channel overcapacity to export markets. As it is not feasible to transport flat glass over long distances, in general neighbouring countries are good candidates for export. During the last three years when Turkey imposed quotas on Russia, Russian producers increased their exports to Bulgaria and Greece. Since Trakya Cam's new float line in

Bulgaria has also become operational this year, Russian producers will probably now want to channel the portion that they are exporting to Bulgaria to Turkey. As there is no volume limitation for Russian producers to export to Turkey, Trakya Cam may face competition from Russian producers in terms of price. Iran is also scheduled to increase its flat capacity by 20% and after this increase, Iran's total capacity will be twice as much as its demand. This may also lead to an increase in exports to Turkey, and even with extra financial tariffs Iranian products are cheaper than Trakya Cam's. In Ukraine, no capacity increase is planned. However, Russia is the main export market for Ukrainian producers. Hence, with the planned capacity expansions in Russia, it may face difficulty in selling its products to Russia and may redirect sales to Turkey. However, Ukrainian product prices (with this new tariff) are the closest to Trakya's prices, thus they are expected to provide the lowest competition among importing nations. St Gobain's float line in Romania is expected to be operational in Q4 2006, which may increase the imports from there to Turkey as well.

With these potential developments in mind and considering a likely slow-down in new housing construction projects in Turkey due to high interest rates, we cut our forecasts for Trakya Cam by 51% and 45% at EPS level for 2006 and 2007, respectively. Accordingly, we end up with a new valuation range of USD2.31-3.83 per share, which yields a notional mid-point target of USD3.07 (cut by c30% from the previous NTP). Our valuation is based on DCF (8% risk free rate, 5.5% equity risk premium, 0.78 company beta and 2% terminal growth rate) and peer group multiples (10.7x 2007e PE and 7.2x 2007e EV/EBITDA). Despite the lower valuation, we maintain Trakya Cam as Overweight, due to high potential upside to our new NTP.

A downside risk to our valuation and rating, other than the potential rise in competition from imports that we mentioned above, is the halting of production at one of its plants (which accounts for one fifth of overall capacity) due to flooding in the region. We do not yet know the degree of the damage but the company has already applied to its insurance company to cover its losses. If it takes a long time before production can be resumed, it may pose a threat to our sales, EBITDA and net earnings forecasts. Besides these risks, the degree of TRL depreciation and its negative impact on the construction sector might be higher than our current expectations.

Tupras (TUPRS.IS) Neutral

For more detail, please refer to reports published by Bulent Yurdagul, available on www.research.hsbc.com

In a recent company update on Tupras, *Not Alone Anymore*, published 17 August 2006), we reiterated our Neutral rating on the company. Below is a summary of our view in the report.

Recently, Indian Oil, Petrol Ofisi and Lukoil have applied to build three refineries in Turkey with a total capacity of 35m tons. The total capacity would be more than the overall capacity of Tupras (27.6m tons). This indicates that in five years' time the refining sector will be one of the most competitive in Turkey and this will hurt Turkey's sole refiner, Tupras, in the long run. We emphasise that realisation of all or even two of these three major projects will lead to a deterioration in long-term projections for Tupras. Even though the short-term positive outlook for the sector pushes this concern further down the agenda, we believe that it will dominate in the upcoming years.

The optimistic side of the story is that huge interest in the sector might put Tupras on the radar screen of the foreign sector players for possible partnerships or acquisition of any of the company's refineries. In this case, the replacement value of Tupras would outweigh a DCF valuation and could drive its share price to higher levels. The sale of one or several of Tupras' refineries to other investors or the sale of a stake in Tupras to a strategic partner would lead to positive expectations for the stock.

The hunt is on for a turnaround story after privatisation but we believe it is too early to judge. While we believe in the ability of Tupras' management to turn the company around, investors will focus on corporate governance and major shareholders' willingness and ability to increase shareholder value at this stage. On this front, payment and pricing terms for the crude oil purchased, especially from Shell (a minority shareholder of Tupras), as well as trade relations with the clients, who are members of the Koc Group, will be the crucial issues. More importantly, a potential merger of Energy Investments (the intermediary company established by Koc to acquire Tupras) and Tupras may be a long-term strategy of the consortium, since it would provide a tax shield for the merged company. However, such a move would improve the return on investment for the major shareholders but lift Tupras' leverage to undesirable levels and harm Tupras' minorities. We consider this very unlikely, bearing in mind the huge exposure of the Koc Group to stock markets and the possible destructive impact this action would have on the credibility of the group.

As an alternative, we think that it would be feasible for the acquirers to merge all energy-related operations under one roof (ie Aygaz-Opet-Tupras) to create further synergies, since it seems to be the only option to provide vertical integration for the firm. While we think this is a reasonable plan, based on the merger terms, we would also be concerned about dilution risk for Tupras' minorities. In this case the need for an approval of the transaction by the Capital Markets Board and high credibility of the Group are the only safeguards for the minorities.

We upgrade our forecasts on recent restructuring activities and outstanding refining margins in H1. Our DCF analysis, based on higher risk premiums (8% USD-based risk-free rate instead of the pre-turbulence level of 7%) and better forecasts yields a target share price range of USD20.0-24.4 and a notional target price of USD22.2, which is 7% higher than the previous one. However, Tupras' stock has been a strong performer recently due to its defensive character, and our new target price implies limited upside potential. Therefore, we maintain our long-term Neutral rating on the stock.

Turkcell (TKC N) Overweight

For more detail, please refer to reports published by Herve Drouet & Bulent Yurdagul, available on www.research.hsbc.com

In a recent company update on Turkcell, *Good results considering weak macro economic environment,* published on 11 August 2006) we maintained our Overweight rating and adjusted our share price target according to the recent financials. Below is a summary of our view in the report.

Turkcell reported its Q2 2006 results on 9 August 2006, in USD under IFRS. We expected a sharp correction in Q2 financials in USD due to the depreciation of the Turkish lira. In fact, both the sales figure and EBITDA margin were above our expectation. Sales were up despite a 9% depreciation of TRL against USD on a quarterly average basis. This was mainly because of 17% higher MOU compared with the last quarter due to seasonality and retention-based offers by Turkcell. EBITDA margins improved by 300bp compared with Q1 2006 and above our expectations, largely due to lower subscriber acquisition cost (SAC) of USD26.2 compared with USD37.1 in Q1 2006. Local currency depreciation and lower distribution costs associated with entry level packages contributed to the decline. Management expects full year SAC to be lower than Q1 2006 levels. Reported net profits declined to USD87m versus USD187m in Q1 2006. The difference is primarily explained by the reversal of deferred tax assets resulting from a reduction of the corporate tax rate to 20% from 30% and foreign exchange losses as a result of a 19% depreciation of TRL against USD in the second quarter of 2006. Normalised net profits, adjusted for deferred tax and foreign exchange losses, were USD216m, a decline of 10.5% y-o-y.

Following the stock bonus announcement in June 2006, the stock price was adjusted by a factor 0.843 from 26 June 2006. Our notional target price pre-adjustment was USD14.5. Multiplying our target price by the adjustment factor, our target price would have been USD12.23. We have revised our notional target price now to USD14.2, using a WACC of 12.5% and 45% long-term EBITDA margin. Our valuation incorporates a reduction in the effective tax rate of 20% from 25% and a slight decrease in long-term capex assumptions. We maintain our Overweight rating.

Vakifbank (VAKBN.IS) Underweight

For more detail, please refer to reports published by Levent Topcu and Mark Rorison, available on www.research.hsbc.com

We have recently initiated coverage on Vakifbank with an Underweight rating, (*Beneath the Beauty*, published 4 August 2006). Below is a summary of our view.

Vakifbank is the fourth-largest listed bank in Turkey, with an 8.3% market share by assets. It is partly owned by the state and is managed by the General Directorate of Foundations.

After the recent volatility in the Turkish market, we think Vakifbank is fairly well protected from FX losses and that the impact on the P&L should not exceed 2.2% of the year-end profits. However, the effect of the rising interest rates is more significant and could consume up to 7% of the bank's equity in 2006.

Vakifbank has experienced fast growth since 2002 and has secured a fourth-place ranking by asset size in the Turkish banking sector. Its clear focus is on retail banking and its privileged exposure to state companies, through its links with the state, gives it an exceptionally solid position in deposits. However, we think this position could be challenged in the future. We also think Vakifbank needs to improve its qualitative standards, such as staff profile and IT systems, if it wants to be a truly competitive retail bank.

Given the impact of the recent bout of volatility, we have factored in a TRL270m equity loss from the security book for 2006, along with some insignificant FX losses. Slowing volumes and tighter margins are likely to curb 2006 results. Note that the total stock of housing loans increased by 45% in one single quarter (Q1 2006), at a time when loan yields were at their lowest, signalling that there could be pressure on margins in future. We believe that this will be partly offset by higher yields on the security book in 2007. We forecast TRL650m earnings for 2006 and TRL829m in FY 2007, resulting in an average EPS growth of 27% between 2005 and 2008.

Using a risk free rate of 14.5%, our DCF-driven valuation gives a two-year range of TRL6.70-7.40, the mid-point being TRL7.03 per share, indicating limited potential upside from the closing price of TRL6.50 on 25 August. Static multiples suggest a slight discount, especially for P/BV; however, company-specific risks should not be overlooked, in our opinion. We initiate coverage with an Underweight rating. An upside risk to our valuation would be a reversing of the global liquidity appetite to favour Turkey again. That would bring down our risk-free rate assumption and add upside to our valuation.

Yazicilar Holding (YAZIC.IS) Neutral

For more detail, please refer to reports published by Gunes Ozdemir, available on www.research.hsbc.com

We value Yazicilar Holding, a Turkish conglomerate whose main NAV driver is the brewer Anadolu Efes, using NAV model. In our recent note on the company (*Deep NAV Discount Justified*, published 11 August 2006), we reiterated our Neutral rating on the stock; our view is summarised below.

We have updated our NAV estimate for Yazicilar considering: (i) the recent downward revision made to our Anadolu Efes target valuation; and (ii) the recent slight increase (1.1%) in Yazicilar's direct stake in Anadolu Efes as a result of buy-outs from family members. Adjusted for these two changes, our NAV estimate came down to USD1,600m (or USD40.01 per share) from USD1,842m (or USD46.05). At our revised estimate, we calculate that Yazicilar trades at a 41% discount to target NAV.

We acknowledge that, as a conglomerate, Yazicilar should trade at a discount to its NAV. This is especially true given it has no controlling stake in any of its major assets. Even conglomerates such as Koc Holding and Sabanci Holding, which are actively involved in strategic decision-making of their subsidiaries, trade at a discount to NAV (Koc at 16% and Sabanci at 22%). We think it is fair to assume an NAV discount of 33% (the average of the last 12 months' trading discount to its current NAV) in calculating the fair value for Yazicilar.

Having done so, we arrive at a new NTP of USD26.01 per share (previously USD34.75). This is the mid-point of our fair value range of USD22.00-30.01 (previous range USD32.23-37.27). The low end is derived from applying a 45% discount to our estimated NAV and the high end is derived from applying a 20% discount. We maintain a Neutral rating on the stock.

The key risks to our Neutral rating are the new areas of interest of Anadolu Endustri Holding (AEH), a 68% direct affiliate of Yazicilar, and limited coverage on some of Yazicilar's participations. We believe that the upcoming regional electricity distribution tenders, for which AEH has potential to be a bidder, may serve as a positive catalyst for the stock price. Since AEH is not a public company, Yazicilar could provide a way of gaining exposure to these privatisations. News of teaming up with strong domestic and/or global partners could improve sentiment on Yazicilar.

We might be overestimating/underestimating the relatively smaller listed businesses of Yazicilar on which we do not have coverage. Therefore, any market transaction involving one of these participations that may reveal a solid market valuation different to ours, would be an upside/downside risk to our current valuation.

Recent sector reports

Banks

- Volatility has subsided: we detail the impact on banks
- We revise downwards 2006 earnings estimates by up to 20% for big banks; notional target prices are reduced by 17-28%
- Akbank downgraded to Neutral, while Garanti and TEB are top picks in sector

Summary view

For more detail, please refer to the banking sector report, *All Too Sensitive,* by Levent Topcu and Mark Rorison published on 17 July 2006, available on www.research.hsbc.com

Applying the sensitivity analysis

During recent months, Turkey has suffered a substantial sell-off, which has also affected main macro parameters, as well as market expectations. Policy rates are up by a cumulative 400bp, bond yields touched 23% and the TRL currency has tested USD1.70 levels.

We have taken this opportunity to revise our estimates. Base-case assumptions have been revised as follows: interest rate assumption increased from 13% to 18%, USD/TRL rate increased from USD1.35 to USD1.60 and, most important, the risk-free rate assumption increased from 10% to 14.5%.

In assessing the sensitivity, we have adopted three separate cases, each investigating separately the short FX positions, interest rate vulnerability, the impact of negative carry on long-term TRL loans, and the free equity gains for the banks. We have also revised our forecasts and valuations, reflecting lower margins and loan growth figures for 2006, slower deposit growth figures, higher exposure to securities, and a higher risk-free rate of 14.5%, as noted above.

The result is a 17-28% reduction in notional target prices and 2006 earnings revised downwards by up to 20% for the big banks.

We look at different possible scenarios of the volatility to get a sense of which banks will provide a defence and which are more vulnerable. Finally, we look at the potential impact on earnings and valuations.

Three scenarios for the sensitivity analysis

	USD/TRL rate		Policy rates		GDP growth		Change in loan growth		
	2006e	2007e	2006e	2007e	2006e	2007e	2006e	2007e	RFR
Case – I (optimistic case)	1.5	1.55	16.00%	18.00%	5.50%	6.00%	42%	30%	13.50%
Case - II (base)	1.6	1.65	18.00%	20.00%	5.00%	5.50%	37%	25%	14.50%
Case – III (bearish)	1.7	1.75	20.00%	22.00%	4.00%	4.50%	30%	20%	15.50%

Source: HSBC

FX volatility impact

We think the risk to banks from their short positions on the currency is minimal compared with 2000, when Turkey experienced a similar FX crisis, as the current overall short position is just 3% of total equity vs 49% in 2000.

Our conclusion is that the sector is much better placed to weather possible FX movements than it was in previous volatile periods. In the worst case scenario, losses from short FX positions should not exceed 2.0% of total equity. As a result, considering the small likely impact, YKB and Garanti are the most defensive stocks in terms of short FX positions, whereas Isbank, Akbank and Denizbank have the largest exposures.

Interest rate volatility impact

The largest potential negative impact on the banks is likely to come from their security portfolios. In order to come up with a reliable estimation of losses from a security portfolio, one needs to know the precise breakdown of all the securities. Obviously, this is not possible. Hence, with the feedback from banks' IR departments, we have identified the approximate composition of each bank's security book according to fixed, floating and eurobond in both TRL and FX. Then, for each type of holding, we selected the benchmark papers and looked at the changes in their prices in Q2. An alternative methodology would look at the average maturity of the portfolio; however, given the sharp short-term movements in the market, we thought starting from the average maturities would give too rough an estimation.

We look at the impact on securities from three different angles. Security books basically have three lines and the accounting treatment for each line is different.

- Trading losses will dampen 2006 profits, but the impact will be marginal as most of the banks have small trading portfolios and in the worst case (for Akbank), resulting losses would not exceed 9% of 2006e earnings. Akbank is the only bank with a relatively large trading portfolio, but it is pledged in floating rate FX paper so the loss is likely to be limited.
- Equity impact: this includes trading losses plus losses from AFS, which is where all the banks carry the bulk of their securities. We think those banks with a higher security/asset ratio (especially the big four) will suffer the largest hit here. Isbank, Akbank and Garanti seem the most sensitive, whereas Deniz and Finans are the least vulnerable.
- Economic loss impact: held-to-maturity securities have no impact on the P&L or equity; however, there is an economic cost (or opportunity cost) when yields rise, as the bank is locked into lower-yielding securities until maturity while better returns are available elsewhere (hence, long-term pressure on margins). When we talk about economic loss therefore, we mean the sum of actual losses plus the opportunity cost, which will never be an actual loss but is a way of measuring exposure to securities. In this case, Garanti, Isbank and YKB are the most sensitive, while Deniz and Finans are least vulnerable.

Loan book impact

The sensitivity to rates largely comes from the fixed-rate loans, mostly comprised of consumer, car and housing loans. In this, we estimate the portion covered by long-term borrowing; the remainder is the part likely to cause the economic impact, as there is negative carry as financing costs rise and it is not possible to re-price the loan.

Akbank would appear to be the most sensitive, as it has the largest portfolio and apparently little long-term borrowing. The impact of negative carry, which will only be visible on future margins, is greatest for Akbank and Garanti Bank. Other smaller banks and Isbank are relatively covered for negative carry risk, since their margins are fixed from today via long-term financing.

Benefit of 'free equity'

On the other hand, higher interest rates should see higher returns on free equity (equity minus non-interest earning assets). Akbank, Isbank and Garanti should have the largest absolute gains as they have the highest free equity.

Putting it all together

We assess the impact on total asset size: in this scenario YKB and Isbank are the worst-affected banks. Despite Akbank's perceived interest rate sensitivity, it appears the least affected relative to its peers. Meanwhile, the smaller banks, with their low security/asset ratios, are better placed to withstand the volatility.

Note that economic loss figures aim simply to measure banks' sensitivity to different macro variables; it should not be inferred that the banks will necessarily suffer such losses in their P&Ls. Such losses will be observed through lower future margins and could be offset if rates decline again.

Revising forecasts

Having seen the volatility beginning to subside, we have therefore adapted our expectations and estimates to fit the new conditions. We now expect 9.8% inflation this year compared with 5.9% previously. The central bank's rate hikes are likely to slow growth, with the greatest impact being felt in the construction and automotive imports sectors. Our economics team have already revised 2006 growth estimates to 5.0% from 5.8%.

We now have a slower growth outlook, higher cost of borrowing for consumers and banks hesitant to increase loan exposure. Due to lags in loan decision-making, especially in housing, housing loans continued to grow until mid-June. However, there has been a visible slowdown since then and July figures show a sharp slowdown. Car loans, for example, were the first to react to volatility and have stopped growing since June.

Overall economic impact

Q1 2006 bank-only BRSA (TRLm)	Akbank	Isbank	Yapi Kredi	Garanti	Denizbank	TEB	Finansbank
Case I							
Economic loss from long-term TRL loans	-170	-51	-25	-60	-6	-4	-16
Economic gains on free equity	261	186	-15	103	34	15	29
Economic losses on security portfolio	-300	-954	-375	-475	-32	-19	-29
Implied FX loss on short-FX positions	-55	-66	-1	-9	-10	-1	-4
Overall economic impact	-263	-885	-416	-442	-13	-9	-20
Total economic impact as a % of assets	**-0.50%**	**-1.35%**	**-1.78%**	**-1.14%**	**-0.14%**	**-0.16%**	**-0.15%**
Case II							
Economic loss from long-term TRL loans	-238	-71	-35	-84	-8	-5	-22
Economic gains on free equity	366	261	-21	144	48	21	40
Economic losses on security portfolio	-550	-1343	-502	-684	-52	-36	-73
Implied FX loss on short-FX positions	-91	-108	-1	-15	-17	-2	-6
Overall economic impact	-512	-1,262	-559	-639	-29	-22	-61
Total economic impact as a % of assets	**-0.98%**	**-1.93%**	**-2.39%**	**-1.65%**	**-0.32%**	**-0.40%**	**-0.45%**
Case III							
Economic loss from long-term TRL loans	-306	-91	-45	-108	-10	-7	-29
Economic gains on free equity	471	335	-27	186	62	27	52
Economic losses on security portfolio	-795	-1714	-611	-879	-69	-52	-115
Implied FX loss on short-FX positions	-126	-150	-2	-21	-24	-3	-8
Overall economic impact	-756	-1,620	-684	-823	-42	-36	-101
Total economic impact as a % of assets	**-1.45%**	**-2.48%**	**-2.92%**	**-2.12%**	**-0.45%**	**-0.63%**	**-0.74%**

Source: HSBC forecasts

In a significant move, the banks have taken the opportunity presented by the volatility to shorten the maturities of their portfolios (which had become unprofitable), and doubled the price of housing loans in just one month.

Looking forward, we think banks will not be as aggressive in lowering housing loan rates as they were in 2005. The new law facilitating mortgage lending has been postponed until autumn, again putting a cap on growth. Therefore we see little upside to share prices this year from mortgage lending. However, housing loans make up just c10% of total loans and the overall impact of the slowdown on lending is likely to be marginal.

We do not expect a big hit to the SME and corporate loan segments. Although SMEs mainly borrow in TRL, where borrowing rose from c20% to c25%, they are generally less price sensitive and they quickly adapt to macro changes. We would only foresee a slowdown in the SME contractor segment, where there is a large exposure to housing projects, but this is not likely to exceed 10% of total SME exposure for the system. Corporates, on the other hand, generally borrow in FX and their financials are strong.

The central bank is squeezing liquidity with the result that deposit rates have just risen significantly, raising the possibility of another bout of fierce competition for deposits similar to what we saw in the second half of 2005. Given the maturity mismatch between assets and liabilities, this deposit squeeze could suppress margins if it persists. Also there may be a shift from deposits to bonds as bond yields are now more attractive. Another risk factor is that the government could lower/abolish the withholding tax on securities for domestic investors, as it did for foreign investors. Recall that the withholding tax for foreigners was 15% until June, at which time it was abolished. The government could come up with the same treatment for domestic investors, who now pay 10% withholding tax on securities. If that happens, we would expect to see a shift from deposits to securities, with an impact on bank margins.

We cut 2006 EPS by 17% and 2007e EPS by 12%

We have taken this opportunity to revise our estimates. The main changes are that margins and loan growth figures are lower in 2006, securities have increased, trading income has turned negative, FX losses have been included and deposit growth is now slower. We expect 2007 to be a better year, especially in terms of margins, given the overall increase in market rates. However, we cannot yet see which bank is likely to manage 2007 better and stay in front.

In our view, NPLs are low at this stage in the cycle, therefore they are currently more an issue of profitability rather than asset quality.

All in all, we cut our 2006e and 2007e earnings by 17% and 12%, respectively, on average.

Notional target prices revised

Apart from the cut in earnings, the main change to our valuation comes from the revision in the risk-free rate from 10% to 14.5%. It is still hard to see at what level the volatility will settle and how long it will take. We were using a 10% long-term RFR when market rates were floating around 13.5%. The central bank has hiked policy rates by 400bp since then and we have reflected the entire increase in our new RFR.

In addition, our base case has been revised as follows: interest rate assumption increased from 13% to 18%, and USD/TRL rate increased from USD1.35 to USD1.60. As a result, we cut our target prices by 26% on the average.

Along with the cut in earnings, a large percentage of the cut comes from the increase in RFR. We therefore note that, if we see a sustainable decline in benchmark yields in the coming quarters, we could become more positive about valuations.

HSBC

Garanti Bank (GARAN.IS) **Overweight**

We continue to rate Garanti as Overweight with our two-year new NTP of TRL5.64 per share indicating 32% potential upside from the closing price of TRY4.26 on 25 August 2006. Garanti has attractive multiples, is trading at single-digit PE on 2006 and 2007 estimates. Following the partnership with GE, the balance sheet has been restructured, so that it turned negative free equity into positive, which will now generate higher returns, relative to others.

Revisions to forecasts

			AKBNK	ISCTR	YKBNK	GARAN	DENIZ	TEBNK	FINBN
Loan growth									
	2006e								
		Old	60%	35%	30%	45%	30%	40%	25%
		New	30%	45%	30%	50%	25%	30%	25%
	2007e								
		Old	40%	30%	35%	30%	20%	35%	33%
		New	20%	30%	30%	20%	20%	30%	25%
Deposit growth									
	2006e								
		Old	30%	27%	25%	25%	12%	30%	25%
		New	18%	20%	20%	12%	12%	25%	20%
	2007e								
		Old	30%	15%	25%	15%	12%	30%	30%
		New	12%	18%	20%	10%	12%	25%	20%
Securities growth									
	2006e								
		Old	2%	-9%	-5%	15%	10%	2%	44%
		New	28%	-9%	1%	15%	15%	20%	35%
	2007e								
		Old	5%	-5%	5%	9%	5%	1%	-20%
		New	12%	-5%	5%	9%	5%	1%	-20%
Net fee & commission grth									
	2006e								
		Old	55%	25%	25%	25%	30%	35%	25%
		New	40%	25%	22%	40%	25%	30%	25%
	2007e								
		Old	45%	20%	35%	25%	30%	30%	30%
		New	30%	20%	30%	15%	25%	20%	25%
Net interest margin									
	2006e								
		Old	5.00%	4.90%	4.75%	5.00%	6.00%	5.00%	7.50%
		New	4.92%	4.50%	4.50%	4.90%	5.50%	4.75%	7.20%
	2007e								
		Old	4.15%	4.50%	4.75%	5.00%	5.75%	5.00%	7.00%
		New	4.48%	4.70%	4.50%	4.91%	6.00%	5.10%	6.80%
Provisions/average loans									
	2006e								
		Old	-1.8%	-3.3%	-3.2%	-2.3%	-1.9%	-1.0%	-2.3%
		New	-2.1%	-3.5%	-3.2%	-2.8%	-2.1%	-1.0%	-2.6%
	2007e								
		Old	-1.8%	-2.3%	-2.2%	-2.0%	-1.9%	-1.0%	-2.3%
		New	-2.0%	-3.0%	-3.2%	-2.5%	-2.1%	-1.0%	-2.6%
Net profit (TRLm)									
	2006e								
		Old	1,847	1,769	107	905	278	139	490
		New	1,539	1,427	3	905	207	105	398
	2007e								
		Old	2,048	1,880	474	1,294	311	178	626
		New	1,982	1,618	93	1,234	321	174	574

Source: HSBC

TEB (TEBNK.IS) **Overweight**

TEB is our top pick in smaller banks, due to its relatively lower exposure to consumer loans, outstanding asset quality, short asset maturity mismatch and immunity to FX volatility. We rate the stock as Overweight. Our two-year NTP is TRL20.47 per share, offering 51% potential upside from the closing price of TRY13.60 on 25 August 2006. As with Garanti, TEB looks still cheap on 2006-07 multiples, trading at single-digit PE.

Akbank (AKBNK.IS) **Neutral**

We downgraded Akbank to Neutral. Despite solid fundamentals, our new two-year NTP of TRL9.21 per share (previously TRL12.73 per share) offers 17% potential upside from the closing price of TRL7.85 on 25 August 2006.

Isbank (ISCTR.IS) **Neutral**

We keep Isbank at Neutral. The new two-year NTP of TRL11.24 per share (previously TRL13.62) implies 35% potential upside from the closing price of TRY8.35 on 25 August 2006, even higher than Garanti, but we think there is lack of strong catalysts, which would move the stock in the short and possibly medium term.

Denizbank (DENIZ.IS) **Neutral**

Finansbank (FINBN.IS) **Neutral**

We remain Neutral on both banks, as their share prices will be determined solely in the short term by the forthcoming USD-based tender offers for their shares. We see potential upsides of 12% for Denizbank, and 6% for Finansbank to our new two-year notional target prices of TRL15.86 and TRL6.22, respectively.

Yapi Kredi (YKBNK.IS) **Neutral**

We also prefer to remain on the sidelines for YKB and keep our Neutral rating, as the bank will soon (in October) be merged with Kocbank, to become a completely different bank. We wish to hear further official announcements from management before making a dedicated call for YKB shares, ie we still do not have clear feedback from management regarding future strategies or a detailed methodology of the merger.

Vakifbank (VAKBN.IS) **Underweight**

We have recently initiated coverage on Vakifbank with an Underweight rating (*Beneath The Beauty* published on 4 August 2006). Vakifbank is Turkey's fourth-largest listed bank, well placed in payroll accounts; but we think it needs to be restructured as competition stiffens. Cheap market ratings are not enough, as structural problems take the shine off a retail distribution story. Our two-year NTP of TRL7.03 offers 8% potential upside from the closing price of TRY6.50 on 25 August 2006.

Risks to our valuation for banks

Macroeconomic conditions are the main risk to our valuation, both on the upside and downside. Global appetite for risk against the emerging markets is another aspect of market sentiment that could significantly affect our numbers and valuations.

On a company-specific basis, for Finansbank and Denizbank, downside risks to our valuation include the possibility of the deal failing to complete. Upside risks include another wave of increased appetite for Turkish banks pushing valuations to even higher levels, which would make a tender offer irrelevant for minorities. For YKB, uncertainty surrounding the Kocbank merger is the major risk, both on the upside and downside.

HSBC valuation range revision (TRL)

		Two-year valuation range				
		Low	High	Mid-point	Curr price	Upside/down
TEB						
	old	24.39	27.38	25.88		
	new	**19.29**	**21.65**	**20.47**	**13.60**	**51%**
Garantibank						
	old	6.95	7.84	7.40		
	new	**5.30**	**5.98**	**5.64**	**4.26**	**32%**
Akbank						
	old	11.94	13.62	12.73		
	new	**8.63**	**9.85**	**9.21**	**7.85**	**17%**
Finansbank						
	old	5.16	5.71	5.44		
	new	**5.90**	**6.53**	**6.22**	**5.85**	**6%**
Yapi Kredi						
	old	2.62	3.50	3.06		
	new	**2.02**	**2.69**	**2.35**	**2.86**	**-18%**
Isbank						
	old	13.02	14.22	13.62		
	new	**10.75**	**11.74**	**11.24**	**8.35**	**35%**
Denizbank						
	old	13.90	18.00	15.94		
	new	**13.83**	**17.90**	**15.86**	**14.10**	**12%**
Vakifbank						
	old	-	-	-		-
	new	**6.70**	**7.40**	**7.03**	**6.50**	**8%**

Source: HSBC estimates

HSBC

Automotive

- Following a dismal Q3, we anticipate a recovery in Turkish vehicle demand from Q4 onwards as volatility fades out
- Deteriorating financing conditions are stabilising, but rates are not high enough to warrant long-term loan avoidance
- We reduce our sector and company forecasts and notional target prices but still see good upside potential on our coverage. We remain Overweight on Doas, Ford Otosan and Tofas

Summary view

For more detail, please refer to Cenk Orcan's report, *Turkish Automotive Sector – Stabilisation argues for a re-rating,* published 7 August 2006, available on www.research.hsbc.com

The post-turbulence stabilisation in the macro environment has prompted us to revise our estimates and valuations for Turkish autos, reflecting the new operating conditions. The recent recovery in the TRL has brought down the devaluation rate to almost 10% from as high as 30% at end-May. This puts the vehicle price hike since the start of the market volatility roughly on a par with the current devaluation rate – a considerable relief for the Turkish vehicle market given that imports account for more than 60% of all sales. We have also recently seen a relative stabilisation in interest rates and a smoothing out of the rising trend in consumer loan rates. This is as critical as the devaluation rate, since two-thirds of all vehicle sales in Turkey are on finance.

The turbulence has caused an almost 70% rise in average monthly vehicle loan rates to 2.0% (26% on an annual basis) from 1.2% (16% pa).

Turkish autos – comparison of multiples with Turkish market and global peer averages (prices as at 25 August 2006)

		MCAP		PE			EV/EBITDA			EV/revenue		
	Country	(USDm)	Rating	2006e	2007e	2008e	2006e	2007e	2008e	2006e	2007e	2008e
Doas	Turkey	436	O/W	10.3	7.8	6.0	4.4	3.6	2.7	0.2	0.1	0.1
Froto	Turkey	2,382	O/W	10.4	9.1	7.7	4.9	4.4	4.0	0.6	0.5	0.5
Toaso	Turkey	1,284	O/W	27.7	19.6	6.6	12.8	9.5	3.0	0.8	0.7	0.3
Turkish industrials sector avg.	Turkey	-	-	12.3	10.1	8.5	6.6	6.2	5.4	0.7	0.7	0.6
Denway Motors	China	2,495	U/W	10.5	9.6	10	nm	nm	nm	nm	nm	nm
Hero Honda	India	2,979	O/W	12.9	10.8	9.3	7.7	6	4.6	1.1	0.9	0.7
Hino Motors	Japan	3,194	N	12.6	10.8	11.4	8.3	8.3	7.7	0.5	0.5	0.5
Isuzu	Japan	4,054	O/W	8.6	7	6.5	7.7	6.7	6.8	0.5	0.6	0.6
Mahindra & Mahindra	India	3,122	O/W	10.8	9.2	8	6.7	5.9	5.2	1.2	1	0.9
Global peer average				**11.1**	**9.5**	**9**	**7.6**	**6.7**	**6.1**	**0.8**	**0.8**	**0.7**

Source: HSBC

Turkish vehicle market estimates

Units (x000)	2005	H1 06	H2 06e	2006e old	2006e new	2007e old	2007e new
PCV	439	200	200	475	400	500	435
LCV	272	125	145	285	270	300	280
PCV+LCV	710	326	344	760	670	800	715

Growth	2005	H1 06	H2 06e	2006e old	2006e new	2007e old	2007e new
PCV	-3%	7%	-21%	8%	-9%	5%	9%
LCV	10%	8%	-7%	5%	-1%	5%	4%
PCV+LCV	2%	8%	-16%	7%	-6%	5%	7%

Source: Turkish Auto Manufacturers' Association, HSBC estimates

However, this actually means only a 10% increase in monthly payments for the consumer on a typical car loan (24 months, TRL20,000 principal payment). In our view, the additional burden (TRL110 per month) on a stand-alone basis would not warrant any long-term loan avoidance. We believe rates are unlikely to fall, at least before year-end, with the prevalent inflation outlook and tightness in the central bank's monetary policy. But as long as the markets remain stable, with rates staying high compared with pre-volatility levels, we think Turkish consumers are likely to adapt to the new conditions without much delay.

We expect a recovery in demand from Q4 onwards

Vehicle demand was inflated in May as consumers rushed in to buy before conditions worsened. Since then we have seen a sharp downturn in loan usage and vehicle sales from June. We believe the weakness in monthly figures is likely to persist throughout Q3, as it will take some time for consumers to adapt to the new conditions, especially when the seasonality factor is likely to play against a noteworthy recovery. Overall, we expect the Turkish vehicle market to post a 6% y-o-y decline in 2006, versus our previous estimate of 7% growth. Considering that sales were up 8% y-o-y in H1, our new full-year estimate suggests that the market should shrink by 16% in H2 y-o-y. As we stated previously, a significant portion of the H2 weakness should take place in Q3, when we expect sales to bottom out. From Q4, we expect to see some gradual recovery in monthly sales figures, which should put quarterly sales roughly on a par with Q4 2005, based on our estimates.

We reduced our forecast and valuations…

…but maintained Overweight ratings on Ford Otosan, Dogus Otomotiv and Tofas

We argue that vehicle loans are still affordable at the level at which rates have stabilised. Therefore, we see a good possibility of a re-rating in sector stocks even before a recovery in monthly demand figures become visible. Looking at our revised forecasts and valuations for our coverage universe, we believe exporters Ford Otosan and Tofas, as well as importer Dogus Otomotiv (Doas) offer good return potential over a 12-month investment horizon.

We have reflected lower demand estimates for the sector in our company forecasts and valuations. We have also employed new parameters in our DCF models (an 8.0% risk-free rate versus 7.0% previously), reflecting the post-turbulence outlook for the macro economy. As a result, we have cut our financial forecasts as well as target value estimates.

Dogus Otomotiv (DOAS.IS) Overweight

For more detail, please refer to reports published by Cenk Orcan, available on www.research.hsbc.com

We have cut our valuation range for Doas to USD4.55-5.45/share, from USD8.64-9.55, leading to a sharp 45% fall in the notional target price to USD5.00/share from USD9.09 previously.

Since the start of the market turbulence on 8 May, Doas' shares fell by 52% in US dollar terms, providing an ISE-relative return of -33%. Doas has been hit more severely than exporters, Ford Otosan and Tofas, since it is a pure importer of vehicles, which makes it highly vulnerable to ups and downs in local demand. This is why we cut our financial forecasts and DCF-driven valuation for Doas more dramatically than for Ford Otosan and Tofas. However, we believe there is now some upside potential on Doas, particularly if the stabilisation in local currency is maintained. As we stated earlier, the recent strength of the TRL means the devaluation rate is now on a par with vehicle price hikes since early May, suggesting further hikes are not necessary.

Ford Otosan (FROTO.IS) Overweight

For more detail, please refer to reports published by Cenk Orcan, available on www.research.hsbc.com

Our new valuation range for Ford Otosan is USD8.55-9.69 per share (USD10.49-12.31 previously), hence our mid-point notional target price is lowered by 18% to USD9.40 per share.

Ford Otosan is fundamentally more resilient to local demand squeeze than other auto companies owing to its higher capacity utilisation rate, eg 100% vs 65% for Tofas. Its strong export base, generating almost 50% of its total turnover from exports, also adds to the relatively defensive nature of Ford Otosan among the auto stocks. This helped the stock to emerge from the market sell-off with a moderate 7% underperformance relative to the ISE-100.

Tofas (TOASO.IS) Overweight

For more detail, please refer to reports published by Cenk Orcan, available on www.research.hsbc.com

Our valuation range for Tofas has been lowered to USD3.60-4.00/share (USD3.97-4.86 previously). Our new notional target price is now USD3.80 per share, down 14% from USD4.42.

The stock outperformed the market during the sell-off, which is not surprising given the main investment story for Tofas is the upcoming new models, which should provide a boost to the company's financial performance from 2008 onwards – an issue which underplays the importance of short-term developments. A large portion of Tofas' DCF-derived fair value comes from long-term new model projects (from 2008 on) and this renders it a more defensive stock in terms of valuation dynamics, proven by recent price moves.

Risks to our valuation for autos

Stabilisation in the financial markets and the macro environment is the key factor that we depend on in our revised value estimates and bullish call for auto stocks. Volatility seems to be fading away now but its return, in the form of rising interest rates and depreciation of the local currency, would worsen consumer sentiment and be the key risk to our valuations. A tax hike for autos would be another risk.

REITs

- The doubling of housing loan rates during the past three months has slashed the appetite for real estate purchases
- We believe high rates are unlikely to fall in the near future, putting REITs that are highly exposed to residential projects at a disadvantage to those that rely mainly on rental income
- Having reviewed our forecasts and valuations, we reiterate our Overweight rating on Is REIT and our Neutral ratings on Alarko REIT and Yapi Kredi Koray; we are adjusting our fair value ranges

Summary view

For more detail, please refer to Can Oztoprak's report, *Turkish REIT Sector – Overshadowed by the rise in interest rates,* published on 10 August 2006, available on www.research.hsbc.com

Cooling off in housing demand

During the past three months, Turkish commercial banks have doubled their housing loan rates from an average of 12% on an annual basis to 24%, as a response to the hike in general interest rates caused by the recent macro turbulence. This was followed by a sharp contraction in loan applications starting from May, a clear indication of the loss of appetite on consumers' side. Rates have stabilised lately, and there have even been attempts by a few banks to cut rates, although this was on a minor scale (to the 23% pa level). Looking forward, we doubt that banks will find any solid reason to lower rates considerably on housing loans. HSBC's economics team believes that the Turkish Central Bank is unlikely to loosen its tight monetary policy before H2 2007, which, in our view, should keep banks from acting aggressively in consumer loans. We now expect banks to maintain housing loan rates at around current levels for at least the next 12 months.

In addition to the sharp fall in loan demand, another major drawback of rising rates is the possible delay in implementation of the long-awaited mortgage system in Turkey. Expectations on this front have been one of the main driving

Valuation and notional target prices for REITs under coverage (as of 25 August 2006)

Company	Ric code	Avg daily trad vol (USDm)	Current m cap (USDm)	Target m cap (USDm)	Share price (USD)	Valuation range (USD)	NTP (USD) Old	NTP (USD) New	Up/downside potential to New NTP	Rating
Alarko REIT	ALGYO.IS	0.50	111	110	20.20	19.40-20.68	30.68	20.04	-0.8%	N
Is REIT	ISGYO.IS	4.64	574	700	1.74	2.01-2.23	1.91	2.12	22.1%	O/W
Yapi Kredi Koray REIT	YKGYO.IS	0.27	87	70	2.17	1.64-1.86	2.31	1.75	-19.5%	N

Source: HSBC estimates

factors behind the sharp growth in the Turkish construction and residential housing sector throughout 2005 and until May this year, when market volatility broke out. Sector players suggest that for the mortgage system to be successfully initiated and effectively implemented, average monthly housing loan rates should be below 1% (versus 2% at present and 1% just before the market turbulence). In our view, this is another source of lacklustre sentiment for the Turkish construction sector.

New environment favours Is REIT

So far, there have not been any cancellations of new project plans, and for the time being REITs prefer to wait for the high season in Q4 to have some more visibility on demand trends. However, in light of the weak outlook that we foresee for the Turkish housing market for the next 12 months, we believe that REITs, which are highly geared to residential projects, will be hurt by a possible margin squeeze on their ongoing projects and will look less attractive in terms of growth potential, as they could be less eager to embark on new projects. On the other hand, we believe that REITs that generate strong and stable rental income will remain solid. This is especially true for REITs whose leasing agreements with tenants are in foreign currencies, considering the weaker TRL now as a result of the macro turbulence.

In our coverage universe for REITs, Is REIT stands out as the one that best complies with this profile; it relies heavily on stable income from office rental, with a significant portion (c70%) linked to foreign currencies. In contrast, Alarko REIT and, in particular, Yapi Kredi Koray REIT have higher exposure to residential projects. Five ongoing real estate projects, of which four are residential, account for almost 90% of Yapi Kredi's total NAV, while the sizable land and cash that Alarko owns (totalling 66% of NAV) are to be invested primarily in residential projects. On the other hand, developed properties from which Is REIT generates rental income make up more than 80% of the company's total NAV.

We remain Overweight on Is REIT and Neutral on Alarko and YKK

We continue to base our valuation for REITs on DCF; however, as a result of the change in Turkey's macroeconomic outlook, we have increased our risk-free rate assumption to 8.0% from the 7.0% that we had been using prior to market volatility. Moreover, we believe that Turkish equities now involve higher risk, which led us to increase our equity risk premium assumption to 5.5% from 5.0%.

Alarko REIT (ALGYO.IS) Neutral

For more detail, please refer to reports, published by Can Oztoprak, available on www.research.hsbc.com

We cut our fair value range for Alarko REIT to USD19.40-20.68 (from USD28.68-32.68), the mid-point of which is our notional target price, USD20.04 (down from USD30.68).

The most recent development has been the acquisition of new land in Tuzla/Istanbul in June at a price of USD7.4m. Located on the Marmara Coast, Tuzla is one of Istanbul's popular resort areas.

Alarko plans to develop a housing project in this area, consisting of four-story apartments with 300 residential units in total. The project is to begin by the end of 2006 and to be completed by the end of 2008. The company expects to generate cUSD45m of revenues at a cost of USD32m, excluding the land. Including the cost of the land, we estimate that the project will generate a profit of cUSD6-7m. We view this as a positive development that should enhance Alarko's NAV.

On the other hand, Alarko REIT continues with its villa projects in Buyukcekmece/Istanbul, which are due for completion by end-2007. Also, as the company has announced, there is a plan to construct a hotel and shopping mall on the Maslak site in 2008, after clearing up legal issues with the municipality.

Is REIT (ISGYO.IS) Overweight

For more detail, please refer to reports published by Can Oztoprak, available on www.research.hsbc.com

We increased our fair value range for Is REIT, factoring in a new project, to USD2.01-2.23 (from USD1.77-2.05), indicating at the mid-point a notional target price of USD2.12 (up from USD1.91).

Is REIT has recently released further details of its plans for Tatilya and the surrounding vacant land, which is a site with total area of approximately 85,000 sq m; of this land, 35,000 sq m will be let to Real, a Metro Group hypermarket chain. Based on the agreement between the two parties, Is REIT will receive annual rental income of USD2.5m, or 3.5% of Real's revenue, whichever is higher, following the development. Additionally, for the remaining land, Is REIT has an agreement with CURA/GGP, a JV between GGP of the US and Otto of Germany. Accordingly, CURA/GGP will develop a retail project (which will not involve any expenditure by Is REIT) and Is REIT will receive cUSD2.5m rental pa, as the owner of the land.

Is REIT's major development project, Kanyon, is due to be fully completed soon, and there is currently no change in plans for a shopping mall on the company's newly acquired land in Uskudar. Following completion of Kanyon, Real, the Uskudar shopping mall and the aforementioned new retail project, we estimate Is REIT's annual rental income will increase by 72%, from USD29m to USD50m in 2008.

Yapi Kredi Koray (YKGYO.IS) Neutral

For more detail, please refer to reports published by Can Oztoprak, available on www.research.hsbc.com

We reduced our fair value range to USD1.64-1.86 (from USD2.16-2.48); our new mid-point of USD1.75 (down from USD2.31).

Yapi Kredi Koray (YKK) is highly exposed to the housing segment; therefore, the company is extremely sensitive to changes in housing loan rates. As banks have raised their housing loan rates considerably since May and are unlikely lower them in the medium term (next 12 months, in our view), the impact is likely to be greater on Yapi Kredi Koray than on other REITs under our coverage. So far, the company has not cancelled or called for any delay in its housing projects scheduled to commence over the next couple of years. However, given the high level of housing loan rates, we believe that YKK may reschedule its projects, prioritising those for buyers with high incomes and keep those for the mid-income group on hold for some time until visibility for demand and the direction of interest rates improve.

Risks to our valuation for REITs

An earlier-than-expected decline in market interest rates and banks' housing loan rates should revive demand for real estate in Turkey and would be the key risk to our current valuation and rating for REITs under coverage. Also, the announcement of new and large development projects would require us to revisit our DCF models as they pertain to our ratings.

Economic environment

- With improving global risk appetite, Turkish markets have once again become attractive, although the macro environment is less compelling for equities than for fixed income
- After decades of boom and bust, it appears that Turkey will finally manage to soft-land its economy to more sustainable levels
- Large and widening external deficit remains a soft spot, thanks to ominous trend in oil prices, though spectacular fiscal consolidation is a major mitigant of vulnerability
- Relations with the EU and next year's twin elections will offer biggest tests for Turkish markets

Turkey: soft landing, at last?

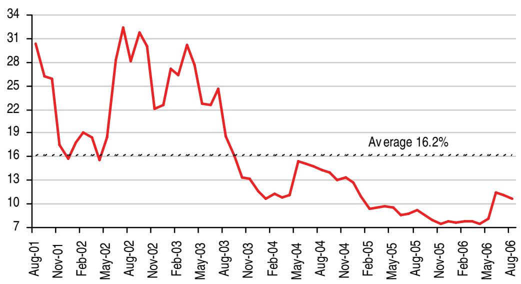
Turkish markets underwent a major correction in May and June, as a result of rising risk aversion towards emerging markets and a slew of endogenous factors (poorly-managed appointment of central bank governor, negative inflation shock, credibility of monetary policy, noise surrounding presidential and parliamentary elections, etc). However, thanks to a softer tone from FED chairman Bernanke and a pause in the two-year US tightening cycle, there has been a marked improvement in risk appetite and renewed interest in riskier assets. Hence, since early July the Turkish lira has once again begun to appreciate. TRL now offers the highest carry trade, with overnight policy rate at sa 17.50%. In a nutshell, Turkey's following dilemma is once again in the works. When risk appetite declines, investors tend to rank emerging economies by their current account deficits (irrespective of the make-up and financing) and sell Turkey due to its largest external imbalance. The mirror image is ranking countries by their rate differential with the FED when the risk aversion subsides and Turkey once again becomes the star. While the global environment has once again become supportive of high beta names such as Turkey, we maintain our rather cautious stance ahead of a precarious election year. Turkey will hold a presidential election in spring and parliamentary elections in the autumn next year. On the external front, we believe that concerns of slower global/US growth could eventually impact emerging markets negatively, but probably not very soon. Similarly, oil prices are at worryingly high levels for net energy importers such as Turkey. Finally, relations with the European Union (EU) will come under the spotlight in late October, with the publication of the progress report. Turkey-EU relations may take a more negative turn towards the end of this year, with much criticised lack of progress on democratisation reforms as well as on the contentious Cyprus issue.

Against such a backdrop, we advise investors to be cautious about Turkish assets until such risks are resolved or at least we have more clarity on both the EU and political fronts. In terms of preference, we think the backdrop is relatively more supportive of fixed income than equities, as real interest rates are high and have the potential to rise further if the Central Bank of Turkey (CBRT) were to tighten monetary policy further to anchor expectations towards an ambitious 4% inflation target for 2007. Similarly, the real economy is bound to slow down with higher interest rates and ahead of the potentially choppy election period. While we do not foresee an abrupt downturn in economic activity, the slowdown is expected to weigh on corporate profitability. Thus, the environment justifies short-term investment in rates, or the so-called 'carry trade'. We are of the view that the CBRT could mop up both hard currency and ensuing TRL liquidity to assuage the appreciation pressure on the local currency and to prevent potential upward spikes due to the aforementioned risks. However, we do not agree with the alternative view in the market that the CBRT should stop tightening, as the real macro problem in Turkey is the lack of saving in the private sector, which is also the root cause of the external imbalance. As much as the link between interest rate hikes and economic activity is not as strong as in developed markets due to the lack of proper transmission mechanism over disposable income, the former is the main credible policy tool not only to cool down domestic demand, but also to manage expectations, which we believe to be of utmost importance affecting future pricing behaviour.

Growth: economic activity towards more sustainable levels

The level of economic activity will no doubt be impacted by the significant correction in both interest rates and the currency throughout May and June. While the TRL has regained much of its losses since July, interest rates are still significantly higher compared with pre-crisis levels. However, we have never rushed to revise our economic growth estimates downwards excessively to negative quarterly growth rates. We have always maintained that this country can grow at around 10% real interest rates (see chart below), as has been the case in the past. The local confidence and expectation channels are much more important in terms of affecting decision-making of the economic agents. In our view, both the monetary and fiscal policy responses by the economy administration were eventually adequate to stabilise the financial markets and to re-anchor confidence.

Ex-ante real rates (%) based on CBRT's bi-weekly survey

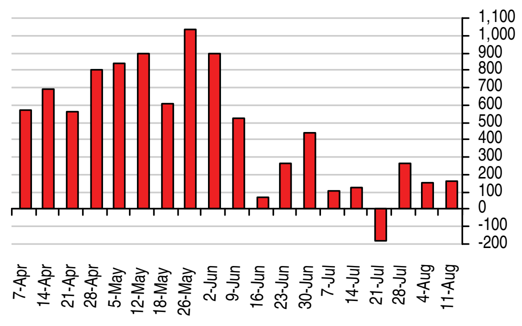


Source: Central Bank of the Republic of Turkey, Reuters

On the demand front, consumer loans continued to increase in nominal terms, even during the most volatile month, June (see chart below). Obviously, the pace has moderated markedly compared with 2004 and 2005 when the economy grew by 8.9% and 7.4%, respectively, or the robust first quarter of 2006, with 6.4% growth. However, this pace appears more sustainable to us and we maintain our 2006 growth estimate of 5% versus c4-4.5% average market estimates. After raising their rates for automotive and housing loans in May and

June, the commercial banks started to cut them in August. Granted, the CBRT's potential tightening poses a risk for economic activity, though this would in turn tackle the medium-term inflation problem and boost confidence, which would eventually have a positive impact on growth.

Consumer credit stock (nominal change, week-on-week, TRL m)



Source: Central Bank of the Republic of Turkey

The supply front has even accelerated thanks to strong external demand, with recovery in the Eurozone area, Turkey's major trading partner, leading to a boom in exports. The recent industrial production and capacity utilisation numbers for June and July, respectively, point to strong performance in export-oriented sectors such as automotive, machinery and electrical equipment. Similarly, the domestic demand indicators were also relatively encouraging. Finally, robust supply-side performance is positive for balancing any domestic demand recovery and therefore the inflationary demand-pull pressures seem rather limited for now.

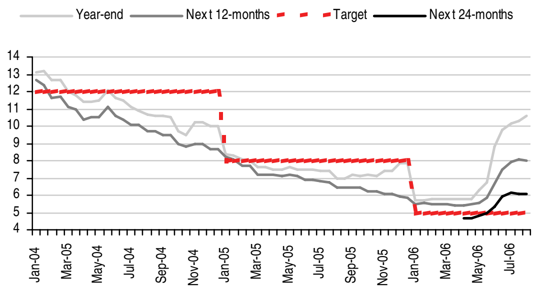
Private consumption, which makes up more than 60% of GDP, is the engine for growth. Hence, the slowdown in global growth or lower commodity prices going forward, in theory, should not impact Turkey's economic activity. However, fund flows are more dominant in the short term and could affect Turkish financial markets negatively if there is further pullout from emerging markets. In the medium term, Turkey is immune to a commodity shock (fast decline in commodity prices). The dynamics of oil prices are somewhat different though, given the geopolitical risks surrounding major oil producers. The trend in oil prices is likely to continue to negatively impact the macro picture, as Turkey is a net energy importer.

Inflation: to hike or not to hike?

Annual inflation has been on an uptrend since October 2005. It started with demand pressures due to rapid economic growth (average 7.5% between 2002 and 2005), keeping service sector prices highly sticky. With weakness in TRL throughout May and June 2006, cost side pressures started to exacerbate the inflation outlook, causing the CBRT to tighten by cumulative 425bp after a four-year easing cycle.

We expect inflation to peak between 11-12% and end this year at around 10%, almost double the 5% official inflation target of the CBRT in the first year of the inflation-targeting regime. This year's target is obviously a sunk cost and the main question is how much the economic agents are convinced by next year's very ambitious inflation target of 4%. The CBRT collects estimates from financial and real sector participants every two weeks. The most critical questions are 12-month and 24-month forward-looking inflation expectations, since they are key input parameters of the CBRT's monetary policy reaction function. However, as things stand now, it is difficult to say that the market participants are convinced by 4% inflation targets for 2007 and 2008 each, indicating that the pricing decisions are unlikely to be based on targeted inflation.

Forward-looking inflation expectations from CBRT's bi-monthly survey



Source: Central Bank of Republic of Turkey

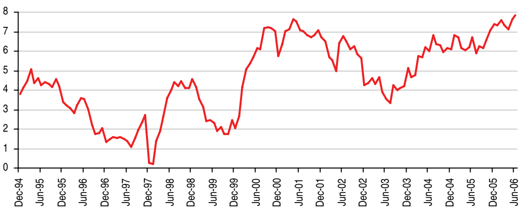
Taking this fact into account, the CBRT instituted a surprise rate hike of 25bp on 20 July, raising the overnight policy rates to a simple 17.50%. Similarly, in its third inflation report, its main communication channel of monetary policy, as well as in its letter to the government/IMF, the CBRT openly signalled a more restrictive and tighter monetary policy stance based on the significant credibility gap (12-month forward looking inflation expectations in early August at 7.98% versus 2007 year-end target of 4%). We believe that such a stance is justified, as inflation prospects in Turkey are working more swiftly over the expectations and exchange rate channels than the demand channel, while the economic activity continues to fare at a respectable pace. The flip side of tightening is higher prospects for carry-trades, as Turkey offers the highest nominal and real interest rates. There, we are of the view that the CBRT should neutralise the extra FX liquidity (under reserve management) and ensuing TRL liquidity, in order not to spur growth in the monetary base. As much as we do not see a very close link between monetary base growth and inflation, substantial TRL liquidity could prove threatening at times of reversal in global sentiment à la 23 June pressure on TRL. In that context, the CBRT could resume its FX purchase auctions halted on 16 May on the back of deteriorating global conditions.

All in all, we expect the CBRT to raise its policy rate by another 100bp by the end of this year. CBRT is highly likely to maintain its cautious stance, and not get carried away with the recent recovery of the TRL, considering the risk factors ahead. Oil prices continue to pose one of the biggest risks to Turkey's disinflation story.

Budget: fiscal performance best in decades

The impressive fiscal performance continues unabated, with the primary surplus reaching 90% of the official year-end target and 78% of the revised projection (see chart below). Similarly, the budget itself posted a surplus in the January-July period, the first time in 22 years. Recently, the Ministry of Finance revised down its year-end budget deficit projection to 1.7% of GDP from the 2.5% official target. The programme-defined fiscal criteria are also well within reach. Following the completion of the third and fourth IMF reviews and in the accompanying Letter of Intent, the government stated that the primary surplus target for last year could not be reached due to overruns in social security transfers, while health expenditures also exceeded limits early this year. However, for the remainder of the year the government pledged a cap on primary expenditure, as well as savings of additional revenues, to be able to reach year-end fiscal targets. Tighter fiscal policy at a time when the central bank also restricts monetary conditions should help in fight against inflation. Hence, we welcome the policy steps taken by the economy administration. In that context, we believe medium-term inflation expectations will improve and, assuming that the real risk premium remains unchanged, the yield curve should invert to reflect the authorities' commitment on disinflation. The biggest risk on the fiscal policy front appears to be the election process looming on the horizon. The initial clues about fiscal policy during the election year will be revealed on the income policy front, with the outcome of the ongoing collective bargaining talks between government representatives and civil servant unions.

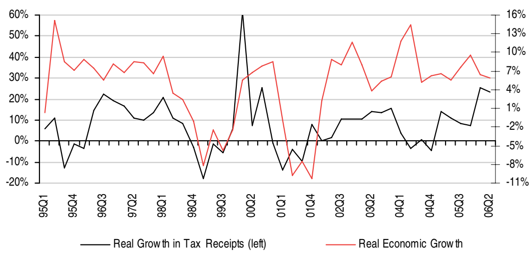
12-month rolling primary surplus / GDP (%)



Source: Ministry of Finance, Turkish Statistical Institute, HSBC estimates

Turkey's total fiscal revenues are close to 28-30% of GDP, while tax receipts make up slightly more than 80% of total revenues. Within the tax receipts, the share of indirect or transaction-based taxes rose to nearly 70%. The remainder is made up of direct taxes, roughly 20% income taxes and 10% corporate taxes. Hence, the indirect taxes, by definition, are geared into the ongoing economic activity compared with a relatively slower reaction of direct taxes to changes in growth. In that regard, we tried to look at the correlation between the quarterly real change in tax receipts and the quarterly real growth in economic activity (see chart below) starting from 1995 (after the major economic meltdown in 1994). To our surprise the correlation (or the R2 from our regression analysis) turned out to be very poor, close to a mere 33.9%. In the next stage, we looked at the same correlation when there was a lacklustre economic performance, which we define as a quarterly GDP growth below 6%. In our view, 6% level is Turkey's potential trend growth with zero output gap, i.e. with no demand-pull inflationary pressures due to balanced supply and demand conditions. The correlation has improved dramatically to 60.3%. Nonetheless, we do not consider such correlation levels encouraging and try to explain the reasons behind this lower-than-expected link between tax receipts and economic growth.

Economic growth and changes in tax receipts (quarterly, real, y-o-y)



Source: Ministry of Finance, Turkish Statistical Institute, HSBC estimates

In our view, the main reason behind the weaker link could be explained by Turkey's substantial efforts to expand the tax base and improve revenues in line with the IMF-sponsored economic reform programme. This was also the lynchpin of the spectacular fiscal adjustment. Despite lower interest expenditures and spending restraints, the revenue side far outperformed the spending side of the budget, as the latter was under the pressure of ever-increasing social security transfers. The turning point of fiscal consolidation was the adoption of the Public Financial Management and Control Law in December 2003, which increased the efficiency, transparency and credibility of fiscal administration. Similarly, the then new AKP government introduced a one-time tax amnesty in 2003 and collected some TRL4.7bn (or around USD3.5bn) in taxes in arrears. A recent restructuring of social security premiums in arrears yielded around TRL1.15bn (USD750m). Also, the fiscal reforms led to a more coherent budget, with the elimination of off-budgetary funds and inclusion of all special revenues items within the central fiscal accounts. Turkey switched from consolidated budget accounting (including 101 budgetary institutions) to a more comprehensive central administration accounting (with 142 budgetary institutions and closer to international/EU standards) in 2006 and also introduced a multi-year planning framework. The primary surplus to GNP ratio was set at 6.5% for each of 2006, 2007 and 2008. Another reason of superior revenue performance was the structural shift in Turkish economy from agriculture to service-oriented sectors. Agriculture still contributes 11-12% of the country's output versus 2% of the EU average and employs more than 20% of the workforce. Since the economic crisis in 2001, there has been a material shift from agricultural to services sector employment. This not only acts as a 'whitener of the grey economy', as the unregistered activity tends to be very high in the agricultural sector, but also helps to expand the tax base and facilitates growth in tax revenues. The expansion of the tax base was also helped by increased banking sector intermediation, thanks to declining real interest rates, and the compulsory use of the tax identification number, which will soon be merged with personal ID numbers.

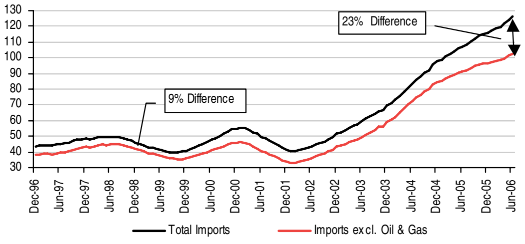
Turkey also undertook some supply-side reforms, such as lowering of value added tax (VAT) on health, education services and staple food items to 8% from 18% in January 2005. The VAT on textile, clothing and leather items was also reduced to 8% from 18% in March 2006. Other tax reforms include simplification and harmonisation of the income tax regime and reduction of the corporate tax rate to 20% from 30%. In sum, taxation and fiscal administration reforms are addressing the unregistered activity (estimated to be more than half of USD365bn official GDP) and expanding tax base, which has helped and will continue to help tax revenues on the budget. While this obviously does not mean that slower economic activity would not impact fiscal revenues, it definitely implies that the budget would be more resilient to economic downturns.

External balance: oil prices leave no room for improvement

The correction in currency and interest rates during May and June was thought to lead to some improvement in Turkey's chronic external imbalance. But rising oil prices have dashed hopes, in particular after the eruption of conflict in the Middle East, causing crude prices to rise above a new plateau of USD70-75. We have recently revised up our current account deficit forecast for this year to 6.9% of GDP, from 6.3%, mainly based on the deteriorating outlook for energy costs.

In the first half of the year, total exports rose 11.5% to USD39.5bn, while imports climbed 18.3% to USD65.2bn, yielding a 30.6% higher trade deficit of USD25.7bn. For the whole of 2006 we maintain our forecasts of USD82.8bn of exports and USD129.2bn of imports, which point to a trade deficit of USD46.4bn. While we expect economic activity to slow down in the second half of the year, this is unlikely to cause a sizable adjustment in the external gap, as growth still remains respectable and oil prices continue to cloud any improvement, as mentioned above. The latest budget data for July imply an ongoing large trade deficit and ensuing current account deficit. The 12-month rolling current account deficit as a ratio to GDP hovers around 7.5%, which is a record both in nominal and percentage terms. Nonetheless, debt dynamics are relatively unscathed despite TRL weakness and rising rates. This is partly due to quality financing of the current account deficit with foreign direct investment (FDI) and also due to spectacular fiscal consolidation. We expect net debt to GDP to rise slightly to 58.2% at the end of this year, from 55.8% in 2005.

Total imports versus imports excluding Oil & Gas (12-month rolling, USDbn)



Source: Turkish Statistical Institute

In the meantime, the non-debt creating inflows (FDI plus net errors and omissions) financed around 55.5% of the current account deficit in the first half of the year. We expect FDI to cover some 60% of this year's external gap. Depending on the outcome of the EU summit and the elections next year, the FDI momentum could continue at a strong pace. The big-ticket items on the privatisation list include the sale of the second-largest state bank, Halkbank, as well as operating rights of the electricity distribution companies. Foreign investors are following both deals very closely. Nonetheless, the election environment and slowing global activity may curb FDI appetite, to some extent, next year. While Turkey is financing a much bigger portion of its external imbalance with long-term and healthy capital inflows, its large and widening current account deficit makes it vulnerable to a reversal in risk appetite towards emerging economies. In that context, we want to underline once again the importance of fiscal discipline, which acts as a safeguard against turning tides in international markets.

Conclusion: we are neutral

To wrap up, Turkey appears to be finally realising a soft landing towards more sustainable economic growth of around 5%, with relatively slower domestic demand. This level of activity is still respectable by international standards and definitely leads to less pressure on the current account deficit. However, any potential improvement on the external imbalance is spoiled by rising energy costs. One glimmer of hope is a slowing world economy that could lower oil prices in the future, though this also has certain implications for Turkey, as discussed below.

Hence, Turkey continues to require sizable foreign capital to finance its growth given the low level of savings of the private sector. This external financing need leaves financial markets vulnerable to a reversal in global risk appetite, which lately has been on an improving trend, thanks to subsiding inflation fears in the US. On the other hand, the strongest fiscal performance in decades alleviates such susceptibility to a certain extent. In that context, the income policy will provide the early signs whether or not the superior fiscal performance will continue in the run-up to an election year. Thus, markets will closely scrutinise the ongoing collective bargaining process with civil servants.

In our view, the markets are likely to trade with a slight positive bias for the remainder of summer and early autumn. However, the final quarter of this year and the first quarter of the next appear rather precarious, with higher political risks revolving around the EU accession process as well as next year's twin elections. Similarly, the energy prices may retain their ominous trend, with heightened geopolitical risks. Finally, the state of the US economy going forward will have a major impact on risk appetite towards emerging markets. A soft US landing would be the best scenario for high beta countries such as Turkey with significant financing needs. The opposite or hard landing would spur risk aversion and could hamper Turkish financial markets. In that context, we view the macro backdrop as more rate supportive and less compelling for investment in equities. Hence, we maintain our neutral stance despite the relatively more attractive valuations of Turkish companies' shares.

HSBC

Macro framework

	2000	2001	2002	2003	2004	2005	2006e	2007e
Production, demand and employment								
GDP growth (% y-o-y)	7.4	-7.5	7.9	5.8	8.9	7.4	5	5.5
Nominal GDP (USDbn)	199.8	146.0	184.5	240.4	301.7	364.3	378.8	383.8
GDP per capita (USD)	2,962	2,127	2,650	3,399	4,202	5,024	5,160	5,165
Private consumption (% y-o-y)	6.2	-9.2	2.1	6.6	10.1	8.8	5.7	5.5
Government consumption (% y-o-y)	7.1	-8.5	5.4	-2.4	0.5	2.4	4.0	11.0
Investment (% y-o-y)	16.9	-31.5	-1.1	10.0	32.4	24.0	15.1	6.7
Industrial production (% y-o-y)	6.0	-8.7	9.5	8.8	9.8	6.5	5.5	6.0
Gross domestic saving (% GDP)	23.0	25.6	24.8	24.5	21.7	17.6	18.3	18.0
Unemployment rate end-year (%)	6.5	8.4	10.3	10.5	10.3	10.3	9.9	9.5
Prices & wages								
CPI, average (% y-o-y)	56.4	54.4	45.0	25.3	8.6	8.2	9.8	7.9
CPI, end-year (% y-o-y)	39.0	68.5	29.7	18.4	9.4	7.7	9.9	6.1
PPI, end-year (% y-o-y)	n.a.	n.a.	n.a.	n.a.	15.3	2.7	14.9	8.6
Manufacturing wages, nominal (% y-o-y)	52.7	31.4	36.3	19.5	14.9	12.7	12.3	14.5
Money, FX & interest rates								
Broad money supply M3 (% y-o-y)	44.0	47.4	31.1	36.0	31.5	42.2	11.0	17.0
Real private sector credit growth (% y-o-y)	14.3	-24.1	-25.7	31.5	43.0	39.2	27.0	32.0
Policy rate, end-year (%)	n.a.	n.a.	55.2	29.7	19.7	13.5	18.5	18.5
ILS/USD, end-year	0.67	1.44	1.63	1.40	1.34	1.35	1.56	1.65
ILS/USD, average	0.62	1.22	1.50	1.50	1.42	1.35	1.46	1.63
ILS/EUR, end-year	0.62	1.27	1.70	1.75	1.83	1.60	2.03	2.31
ILS/EUR, average	0.57	1.09	1.43	1.69	1.87	1.67	1.82	2.10
External sector								
Merchandise exports (USDbn)	30.7	34.4	40.1	51.2	63.2	73.3	82.8	93.2
Merchandise imports (USDbn)	52.7	38.1	47.4	65.2	97.5	116.4	129.2	143.4
Trade balance (USDbn)	-22.0	-3.7	-7.3	-14.0	-34.3	-43.1	-46.4	-50.2
Current account balance (USDbn)	-9.8	3.4	-1.4	-6.8	-15.6	-22.9	-26.0	-25.3
Current account balance (% GDP)	-4.9	2.3	-0.8	-2.8	-5.2	-6.3	-6.9	-6.6
Net FDI (USDbn)	0.1	2.8	0.9	1.2	1.7	8.6	16.0	5.5
Net FDI (% GDP)	0.1	1.9	0.5	0.5	0.6	2.4	4.2	1.4
Current account balance plus FDI (% GDP)	-4.9	4.2	-0.3	-2.3	-4.6	-3.9	-2.7	-4.5
Exports (% y-o-y)	6.5	11.9	16.7	27.6	30.8	16.0	13.0	12.5
Imports (% y-o-y)	35.0	-27.7	24.4	37.6	39.4	19.4	11.0	11.0
International FX reserves (ex gold) (USDbn)	22.2	18.8	26.8	33.6	36.0	50.5	59.0	62.0
Import cover (months)	5.1	5.9	6.8	6.2	4.4	5.2	5.5	5.2
Public and external solvency indicators								
Gross external debt (USDbn)	118.6	113.7	130.2	145.4	162.2	170.1	174.1	179.6
Gross external debt (% of GDP)	59.3	77.8	70.6	60.3	53.8	46.7	46.0	46.8
Short term external debt (% of int'l reserves)	127.6	87.3	61.3	68.5	90.4	75.7	71.2	76.6
Private sector external debt (USDbn)	55.8	43.1	44.6	51.2	67.1	87.1	100.6	105.0
Exports (% of total external debt stock)	25.9	30.3	30.8	35.3	39.0	43.1	47.6	51.9
Central government balance (% of GDP)	-10.6	-16.3	-14.4	-11.2	-7.0	-2.0	-1.9	-3.0
Primary balance (% of GDP)	5.8	6.7	4.2	5.1	6.1	6.6	6.3	5.5
Net public debt (% of GDP)	57.1	90.5	78.5	70.4	63.5	55.8	58.2	59.1
Gross external debt (USDbn)	118.6	113.7	130.2	145.4	162.2	170.1	174.1	179.6
Gross external debt (% of GDP)	59.3	77.8	70.6	60.3	53.8	46.7	46.0	46.8
Short term external debt (% of int'l reserves)	127.6	87.3	61.3	68.5	90.4	75.7	71.2	76.6
Private sector external debt (USDbn)	55.8	43.1	44.6	51.2	67.1	87.1	100.6	105.0

Source: Central Bank of the Republic of Turkey, Turkish Statistics Institute, Reuters, Ministry of Finance, HSBC estimates and forecasts

Valuation & performance

Performance table (USD based absolute) ranked by monthly performance

	–1wk	–1M	–3M	–12M	Y-t-d
Yapi Kredi Koray REIT	1%	39%	1%	-2%	-36%
Anadolu Sigorta	-2%	30%	6%	27%	-16%
Yapi ve Kredi Bank.	-6%	29%	16%	19%	4%
Anadolu Hayat Emek.	1%	28%	4%	121%	-4%
Adana Cimento (A)	-8%	25%	1%	77%	-4%
BIM Birlesik Mag.	-2%	23%	16%	69%	40%
Cimsa	-4%	23%	7%	5%	-12%
Akcansa	4%	19%	2%	34%	3%
Sabanci Holding	-2%	19%	12%	33%	-5%
Migros	-4%	18%	12%	28%	10%
Ford Otosan	-1%	17%	-9%	13%	-16%
Eczacibasi Ilac	-3%	17%	17%	-13%	-23%
Akbank	-1%	17%	11%	19%	-18%
Arcelik	-3%	16%	4%	20%	-3%
Aksigorta	-5%	15%	0%	56%	-3%
Dogus Otomotiv	-7%	15%	-4%	61%	-17%
Trakya Cam	-2%	14%	0%	-8%	-15%
Is Bankasi (C)	-7%	13%	-1%	7%	-34%
Vakiflar Bankasi	-2%	13%	7%	n.a.	-13%
Koc Holding	-5%	13%	-1%	-6%	-16%
Turkcell	-4%	11%	10%	-7%	-21%
Alarko REIT	0%	11%	17%	-2%	-38%
T. Ekonomi Bank.	-8%	10%	-9%	28%	-25%
ISE-100	**-4%**	**10%**	**5%**	**15%**	**-16%**
EMEA	**0%**	**9%**	**-5%**	**30%**	**8%**
Hurriyet Gzt.	-6%	9%	-11%	-8%	-41%
Yazicilar Holding	-7%	7%	-6%	9%	-17%
Tofas Oto. Fab.	-6%	7%	8%	85%	28%
GEMs	**1%**	**7%**	**-5%**	**27%**	**11%**
Petrol Ofisi	-4%	7%	-23%	7%	-17%
Netas Telekom.	0%	7%	-15%	-5%	-30%
Vestel	-2%	6%	4%	-26%	-30%
Dogan Yayin Hol.	-8%	5%	-17%	29%	-20%
Anadolu Cam	-3%	5%	6%	-16%	-24%
Is REIT	-6%	5%	14%	14%	-19%
Dogan Holding	-2%	5%	25%	60%	30%
Garanti Bankasi	-6%	4%	-1%	6%	-20%
Sise Cam	-9%	4%	-1%	-10%	-14%
Finansbank	1%	4%	9%	79%	17%
Denizbank	-1%	3%	30%	120%	47%
Anadolu Efes	-7%	3%	8%	19%	-2%
Ak Enerji	-3%	1%	-19%	-46%	-52%
Tupras	-6%	-1%	21%	24%	6%
Eregli Demir Celik	-5%	-3%	11%	0%	-26%
Petkim	-8%	-4%	-3%	-12%	-41%

Source: Finnet

Performance

	Last Price*	Market Cap (USDm)	Free float mkt cap	%of index	Performance (absolute %) -1wk	-1M	-3M	-12M	Y-t-d	USD performance (absolute %) -1wk	-1M	-3M	-12M	Y-t-d	Performance (relative to GEMs %) -1week	-1M	-3M	-12M	Y-t-d
Adana Cimento (A)	6.42	306	263	0.7%	-6%	19%	-4%	91%	5%	-8%	25%	1%	77%	-4%	-4%	6%	-18%	40%	-7%
Anadolu Efes	26.99	3,046	1,340	3.4%	-5%	-2%	3%	28%	8%	-7%	3%	8%	19%	-2%	-4%	-12%	-12%	-6%	-5%
Akbank	7.85	11,725	3,283	8.2%	2%	11%	6%	28%	-10%	-1%	17%	11%	19%	-18%	3%	0%	-9%	-6%	-20%
Akcansa	5.19	994	199	0.5%	7%	13%	-2%	45%	13%	4%	19%	2%	34%	3%	8%	1%	-16%	6%	0%
Ak Enerji	2.16	141	35	0.1%	-1%	-4%	-22%	-42%	-48%	-3%	1%	-19%	-46%	-52%	1%	-14%	-34%	-57%	-54%
Aksigorta	3.60	1,101	418	1.0%	-2%	10%	-5%	68%	6%	-5%	15%	0%	56%	-3%	-1%	-2%	-18%	24%	-6%
Alarko REIT	20.20	111	54	u.d.	3%	5%	12%	5%	-32%	0%	11%	17%	-2%	-38%	4%	-6%	-4%	-23%	-39%
Anadolu Cam	3.33	504	96	u.d.	0%	0%	2%	-9%	-16%	-3%	5%	6%	-16%	-24%	1%	-10%	-13%	-33%	-26%
Anadolu Hayat Emek.	2.89	506	101	0.3%	4%	22%	0%	138%	5%	1%	28%	4%	121%	-4%	5%	9%	-15%	75%	-7%
Anadolu Sigorta	1.69	338	162	0.4%	0%	24%	1%	37%	-8%	-2%	30%	6%	27%	-16%	2%	11%	-14%	1%	-18%
Arcelik	6.52	2,607	547	1.4%	0%	11%	-1%	30%	7%	-3%	16%	4%	20%	-3%	1%	-1%	-15%	-5%	-5%
BIM Birlesik Mag.	34.12	863	397	1.0%	1%	18%	11%	82%	54%	-2%	23%	16%	69%	40%	2%	5%	-5%	34%	36%
Cimsa	6.04	733	198	0.5%	-2%	17%	3%	14%	-4%	-4%	23%	7%	5%	-12%	0%	5%	-12%	-17%	-15%
Denizbank	14.10	3,026	757	1.9%	2%	-1%	25%	137%	61%	-1%	3%	30%	120%	47%	4%	-12%	7%	74%	43%
Dogus Otomotiv	4.04	444	151	0.4%	-5%	9%	-8%	73%	-9%	-7%	15%	-4%	61%	-17%	-4%	-2%	-21%	27%	-20%
Dogan Holding	4.11	3,020	1,027	2.6%	1%	0%	19%	72%	43%	-2%	5%	25%	60%	30%	2%	-11%	2%	26%	27%
Dogan Yayin Hol.	3.20	1,950	663	1.7%	-6%	0%	-21%	39%	-12%	-8%	5%	-17%	29%	-20%	-4%	-10%	-32%	2%	-22%
Eczacibasi Ilac	2.50	457	142	0.4%	0%	12%	12%	-6%	-15%	-3%	17%	17%	-13%	-23%	1%	0%	-4%	-31%	-25%
Eregli Demir Celik	4.79	2,335	1,098	2.7%	-2%	-7%	7%	7%	-19%	-5%	-3%	11%	0%	-26%	-1%	-17%	-9%	-21%	-28%
Finansbank	5.85	4,965	2,333	5.8%	4%	-1%	4%	94%	28%	1%	4%	9%	79%	17%	5%	-12%	-11%	42%	14%
Ford Otosan	7.13	2,502	450	1.1%	2%	12%	-13%	21%	-8%	-1%	17%	-9%	13%	-16%	3%	0%	-26%	-11%	-18%
Garanti Bankasi	4.26	6,074	3,037	7.6%	-3%	0%	-5%	14%	-12%	-6%	4%	-1%	6%	-20%	-2%	-11%	-19%	-16%	-22%
Hurriyet Gzt.	2.28	951	380	1.0%	-3%	4%	-15%	-1%	-35%	-6%	9%	-11%	-8%	-41%	-2%	-7%	-27%	-27%	-42%
Is Bankasi (C)	8.35	11,162	3,683	9.2%	-4%	8%	-5%	15%	-28%	-7%	13%	-1%	7%	-34%	-3%	-4%	-19%	-15%	-36%
Is REIT	1.74	574	264	0.7%	-3%	0%	9%	23%	-12%	-6%	5%	14%	14%	-19%	-2%	-10%	-7%	-9%	-22%
Koc Holding	3.60	4,552	910	2.3%	-3%	7%	-5%	1%	-8%	-5%	13%	-1%	-6%	-16%	-1%	-4%	-19%	-26%	-19%
Migros	9.30	1,640	803	2.0%	-1%	12%	7%	38%	20%	-4%	18%	12%	28%	10%	0%	0%	-9%	1%	7%
Netas Telekom.	22.07	143	46	0.1%	3%	2%	-18%	2%	-23%	0%	7%	-15%	-5%	-30%	5%	-9%	-30%	-25%	-32%
Petkim	3.46	709	269	0.7%	-6%	-8%	-7%	-6%	-35%	-8%	-4%	-3%	-12%	-41%	-4%	-18%	-21%	-31%	-42%
Petrol Ofisi	3.77	1,573	472	1.2%	-1%	2%	-26%	15%	-9%	-4%	7%	-23%	7%	-17%	0%	-9%	-37%	-16%	-20%
Sabanci Holding	3.56	6,416	1,604	4.0%	1%	13%	8%	44%	4%	-2%	19%	12%	33%	-5%	2%	1%	-8%	5%	-7%
Sise Cam	3.01	1,277	498	1.2%	-6%	-1%	-6%	-3%	-6%	-9%	4%	-1%	-10%	-14%	-5%	-11%	-19%	-29%	-16%
Turkcell	11.63	10,157	1,828	4.6%	-1%	5%	5%	0%	-14%	-4%	11%	10%	-7%	-21%	0%	-6%	-10%	-26%	-24%
T. Ekonomi Bank.	13.60	706	141	0.4%	-5%	5%	-13%	38%	-17%	-8%	10%	-9%	28%	-25%	-4%	-6%	-26%	1%	-27%
Tofas Oto. Fab.	2.65	1,324	318	0.8%	-3%	2%	3%	100%	41%	-6%	7%	8%	85%	28%	-2%	-9%	-12%	47%	25%
Trakya Cam	2.47	725	225	0.6%	1%	8%	-4%	-1%	-6%	-2%	14%	0%	-8%	-15%	2%	-3%	-18%	-28%	-17%
Tupras	18.16	4,548	2,229	5.6%	-4%	-5%	16%	34%	16%	-6%	-1%	21%	24%	6%	-2%	-15%	-1%	-2%	3%
Vakiflar Bankasi	6.50	5,644	1,411	3.5%	1%	7%	2%	u.d.	-5%	-2%	13%	7%	u.d.	-13%	2%	-4%	-13%	u.d.	-15%
Vestel Elektronik	2.61	415	241	0.6%	1%	1%	-1%	-20%	-24%	-2%	6%	4%	-26%	-30%	2%	-10%	-15%	-42%	-32%
Yazicilar Holding	22.07	883	194	0.5%	-4%	2%	-10%	18%	-9%	-7%	7%	-6%	9%	-17%	-3%	-8%	-23%	-13%	-19%
Yapi ve Kredi Bank.	2.86	3,683	1,547	3.9%	-3%	23%	11%	29%	14%	-6%	29%	16%	19%	4%	-2%	10%	-5%	-6%	2%
Yapi Kredi Koray REIT	2.17	87	43	u.d.	4%	32%	-3%	6%	-30%	1%	39%	1%	-2%	-36%	5%	18%	-17%	-22%	-38%

* Prices are in TRL for banks and USD for the non-bank coverage (as of close 25 August 2006)
Source: Finnet

Valuation

	Last Price*	EPS 2005	EPS 2006e	EPS 2007e	EPS 2008e	PE 2005	PE 2006e	PE 2007e	PE 2008e	Price to BV (05)	Div yield %	Rating	Notional target Price*	Upside\ (downside)
Adana Cimento (A)	6.42	0.70	0.86	0.88	0.86	9.16	7.45	7.30	7.43	3.41	8.3%	Overweight	8.39	31%
Anadolu Efes	26.99	1.92	1.72	2.04	2.43	20.71	23.16	19.44	16.36	3.24	1.6%	Neutral	28.93	7%
Akbank	7.85	0.65	0.70	0.91	1.05	12.01	11.19	8.62	7.49	2.70	2.7%	Neutral	9.21	17%
Akcansa	5.19	0.44	0.60	0.55	0.57	11.78	8.71	9.41	9.04	1.98	4.5%	Overweight	6.09	17%
Ak Enerji	2.16	-0.90	-1.17	-1.33	-0.85	n.a.	n.a.	n.a.	n.a.	0.43	0.0%	Neutral	2.14	-1%
Aksigorta	3.60	0.18	0.18	0.23	0.26	20.39	20.02	15.73	13.94	0.92	3.3%	Overweight	4.48	25%
Alarko REIT	20.20	2.76	0.96	0.92	-0.62	7.32	20.96	21.95	n.a.	1.07	0.0%	Neutral	20.04	-1%
Anadolu Cam	3.33	0.26	0.19	0.31	0.45	12.74	17.81	10.73	7.44	1.23	3.1%	Overweight	4.36	31%
Anadolu Hayat Emek.	2.89	0.17	0.18	0.21	0.24	16.87	15.92	13.87	12.26	2.39	0.9%	Underweight	2.29	-21%
Anadolu Sigorta	1.69	0.15	0.16	0.17	0.16	11.27	10.91	9.94	10.57	1.07	0.0%	Overweight	2.02	19%
Arcelik	6.52	0.58	0.65	0.69	0.80	11.20	9.95	9.41	8.18	1.93	5.7%	Overweight	8.50	30%
BIM Birlesik Mag.	34.12	0.89	2.09	2.44	2.61	38.45	16.34	13.99	13.09	13.71	1.7%	Neutral	37.55	10%
Cimsa	6.04	0.67	0.53	0.71	0.85	9.00	11.38	8.57	7.13	1.72	4.5%	Overweight	7.42	23%
Denizbank	14.10	0.63	0.66	1.01	1.22	22.21	21.50	13.89	11.57	4.08	0.0%	Neutral	15.86	12%
Dogus Otomotiv	4.04	0.76	0.39	0.52	0.67	5.35	10.38	7.82	6.02	1.40	7.6%	Overweight	5.00	24%
Dogan Holding	4.11	0.67	0.58	0.22	0.41	6.10	7.07	18.69	9.96	1.70	3.4%	Neutral	4.62	13%
Dogan Yayin Hol.	3.20	0.01	0.02	0.09	0.17	325.00	177.27	37.50	18.93	4.49	0.0%	Neutral	3.35	5%
Eczacibasi Ilac	2.50	0.15	0.16	0.19	0.20	16.71	15.41	13.48	12.33	0.72	0.0%	Overweight	3.29	32%
Eregli Demir Celik	4.79	0.29	0.17	0.13	0.81	16.24	28.87	36.82	5.90	0.72	2.9%	Underweight	5.02	5%
Finansbank	5.85	0.28	0.32	0.46	0.56	20.87	18.36	12.73	10.39	4.61	0.0%	Neutral	6.22	6%
Ford Otosan	7.13	0.85	0.69	0.79	0.93	8.42	10.38	9.06	7.66	2.30	12.5%	Overweight	9.40	32%
Garanti Bankasi	4.26	0.43	0.59	0.71	0.84	9.88	7.25	6.04	5.07	2.29	0.0%	Overweight	5.64	32%
Hurriyet Gzt.	2.28	0.16	0.16	0.18	0.22	14.63	14.63	12.85	10.33	2.13	0.9%	Overweight	2.44	7%
Is Bankasi (C)	8.35	0.49	0.72	0.82	0.88	17.20	11.52	10.16	9.46	1.79	1.3%	Neutral	11.24	35%
Is REIT	1.74	0.08	0.14	0.18	0.33	22.66	12.72	9.48	5.19	1.06	0.0%	Overweight	2.12	22%
Koc Holding	3.60	0.35	0.34	0.68	0.72	10.21	10.46	5.28	4.99	1.39	0.0%	Neutral	4.06	13%
Migros	9.30	0.31	0.33	0.68	0.92	29.92	28.58	13.77	10.06	3.42	1.2%	Neutral	9.19	-1%
Netas Telekom.	22.07	1.90	1.22	1.75	2.24	11.58	18.11	12.62	9.87	1.37	0.0%	Overweight	30.83	40%
Petkim	3.46	-0.36	0.20	0.15	-0.11	n.a.	17.42	22.87	n.a.	0.75	0.0%	Neutral	4.15	20%
Petrol Ofisi	3.77	0.40	0.29	0.58	0.62	9.48	13.08	6.45	6.10	1.06	0.0%	Neutral	4.19	11%
Sabanci Holding	3.56	0.29	0.34	0.36	0.37	12.47	10.42	9.88	9.75	1.39	11.7%	Overweight	4.53	27%
Sise Cam	3.01	0.02	0.12	0.22	0.31	169.86	24.92	13.47	9.83	0.88	1.8%	Neutral	3.56	18%
Turkcell	11.63	0.43	0.45	0.55	0.61	10.85	10.23	8.37	7.54	3.14	9.5%	Overweight	14.20	22%
T. Ekonomi Bank.	13.60	1.03	1.37	2.27	2.29	13.22	9.91	5.98	5.94	2.05	1.2%	Overweight	20.47	51%
Tofas Oto. Fab.	2.65	0.21	0.10	0.14	0.40	12.51	27.68	19.61	6.56	1.88	2.9%	Overweight	3.80	44%
Trakya Cam	2.47	0.21	0.14	0.16	0.23	11.75	17.58	15.05	10.68	1.23	6.3%	Overweight	3.07	24%
Tupras	18.16	1.97	1.94	2.42	2.10	9.23	9.36	7.50	8.63	2.06	10.7%	Neutral	22.20	22%
Vakiflar Bankasi	6.50	0.42	0.51	0.65	0.85	15.53	12.78	10.03	7.61	2.00	4.8%	Underweight	7.03	8%
Vestel Elektronik	2.61	0.41	0.23	0.38	0.52	6.44	11.29	6.84	4.97	0.58	0.0%	Neutral	2.89	11%
Yazicilar Holding	22.07	1.43	3.69	3.47	3.81	15.47	5.97	6.36	5.80	1.48	1.9%	Neutral	26.01	18%
Yapi ve Kredi Bank.	2.86	-1.58	0.00	0.05	0.14	n.a.	2018.95	58.40	20.04	3.23	0.0%	Neutral	2.35	-18%
Yapi Kredi Koray REIT	2.17	0.10	0.28	0.48	-0.16	22.43	7.69	4.48	n.a.	1.39	0.0%	Neutral	1.75	-19%

Notes: *Prices are in TRL for banks and USD for the non-bank coverage (as of close 25 August 2006)
Source: Finnet, HSBC estimates

Notes

HSBC

Notes

Disclosure appendix

Stock ratings and basis for financial analysis

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- Neutral (Hold)
- Underweight (Sell)

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Neutral (Hold)	40%	(18% of these provided with Investment Banking Services)
Underweight (Sell)	13%	(19% of these provided with Investment Banking Services)

Issuer & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Disclosure
AK ENERJI	AKENR.IS	2.13	2, 5
AKBANK	AKBNK.IS	7.65	3, 5, 6, 7
DENIZBANK	DENIZ.IS	14.10	3, 6, 7
DENWAY MOTORS	0203.HK	2.53	4
FINANSBANK	FINBN.IS	5.80	3, 6, 7
KOC HOLDING	KCHOL.IS	3.57	3, 6, 7
MAHINDRA & MAHINDRA	MAHM.NS	640.95	3, 4, 6, 7
MIGROS	MIGRS.IS	9.22	3, 6, 7
SABANCI HOLDING	SAHOL.IS	3.47	3, 6, 7
T. GARANTI BANKASI	GARAN.IS	4.26	3, 6, 7
TOFAS FABRIKA	TOASO.IS	2.64	6
TUPRAS	TUPRS.IS	18.00	3, 5
TURKCELL	TKC.N	11.68	3, 6, 7
YAPI KREDI BANKASI	YKBNK.IS	2.88	3, 6, 7

Source: HSBC

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