ECONOMIC AND SECTORAL OVERVIEW FOR 2011

Concerns related to the debt crisis in the Euro Zone took their toll on global markets.
The debt problem in the Euro Zone, the disagreements regarding raising the debt ceiling in USA, the earthquake in Japan and the shocking increase in oil prices all negatively affected global markets in the first half of the year. In the second half, while US and Japanese economies recovered, economic activity in Europe weakened in parallel with the negative impacts of the debt crisis. On the other hand, the FED announced that it could keep the policy interest rate at the current levels until at least the end of 2014, while the ECB lowered the policy interest rate in November. In parallel with the negative effects of the debt crisis in Europe, the global growth rate fell to 3.9% in 2011 from 5.1% in 2010.

Turkey's GDP growth rate is expected to exceed 8%
Turkey's double digit rate of GDP growth in the first half of 2011 – supported partially by the base effect – slowed to 8% in response to the measures taken by the Central Bank and the BRSA in the second half of the year which were aimed at slowing the growth of credit volume and in response to the weakening in global economic activity. Within this framework, Turkey's GDP is expected to have grown by around 8% in 2011. A strong growth performance and revenues generated in the tax amnesty positively affected public finance and the budget deficit/GDP ratio was realized at 1.4% in 2011.

Inflation ended 2011 at 10.45% - about twice the Central Bank's inflation target
The Central Bank of Turkey cut the policy interest rate from 6.50% at the end of 2010 to 6.25% in January 2011, and to 5.75% in August in response to the public debt problem in EU countries and mounting concerns with respect to global growth. During this period, the CBT lowered the interest rates in money markets in a bid to curb the current account deficit; as a result, the TRY – in contrast with the currencies of other emerging economies - began to lose value.

As the debt problems in the Euro Zone deepened in the subsequent period, TRY devalued more rapidly and as a result, inflation began to creep up more noticeably. As such, the US$/TRY exchange rate, which had stood at 1.54 at the end of 2010, reached a level as high as 1.89 at the end of 2011 amid concerns surrounding the difficulties affecting Euro Zone countries in the second half of the year.

The CBT reacted to the rising inflation rate with a policy of strong fiscal tightening. The CBT reduced TRY funding, raised the overnight lending interest rate to 12.5% and began to apply the strategy known as "wide interest rate corridor". In this strategy, CBT is able to raise the average funding cost to 12% when needed. As a result of this policy, the benchmark bond's interest rate rose from 7.1% at the end of 2010 to 11% by the end of 2011.

Because of the accumulated effects of fluctuating exchange rates, increases in managed/directed prices and the negative developments in unprocessed food prices, the inflation rate is expected to remain in double digit levels in the first months of 2012. Although the slowdown in core and service price inflation rates in recent months is a positive development for the inflation outlook, the headline inflation rate, which is still at double digit levels, and the currently high core inflation rate can be deemed risky with respect to inflation expectations and pricing behavior. However, the inflation rate is expected to decline back to 6.7% by the end of 2012 – still higher than the Central Bank's target rate of 5%.

Capital inflows were strong thanks to the ongoing liquidity provided by the central banks of developed countries. Hence, a total of US$11.4bn of foreign investment entered the Turkish bond market in 2011.

Liquidity provided by the central banks of developed countries and the supply shocks affected global commodity prices.
The average oil price rose from US$80/bbl in 2010 to US$110/bbl in 2011. In addition, as strong economic growth stimulated demand for imported goods, the current account deficit/GDP ratio continued to rise. The current account

deficit/GDP ratio is estimated from 6.4% at the end of 2010 to 9.5% by the end of 2011. The current account deficit/GDP ratio is expected to recover slightly and dip to 8.7% in 2012 due to the normalization in the rate of economic growth.

The Turkish banking system maintains its strong structure

The sector's capital adequacy ratio, which had stood at 19% at the end of 2010, slipped to 16.46% by the end of 2011 – although this level can still be considered comfortably high. According to these results, the banking sector succeeded in expanding its asset base by 20%, its loan volume by 29% and its deposits by 13% by the end of 2011, when compared to its 2010 levels. Since the public sector's borrowing needs have been reduced, the banks' securities portfolio almost remained steady.

Banking Sector Data		
	2010 December	2011 December
Total Assets	1 TRY trillion	1.2 TRY trillion
Credit Volume	529 TRY billion	683 TRY billion
Marketable Securities Portfolio	288 TRY billion	287 TRY billion
Deposit Volume	617 TRY billion	696 TRY billion