Republic of Turkey

PRE-ACCESSION ECONOMIC PROGRAMME

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INDEX

LIST OF TABLES

ABBREVIATIONS

ASCUs	Agricultural Sales Cooperatives and Unions
BIS	Bank for International Settlements
BRSA	Banking Regulation and Supervision Agency
CBRT	Central Bank of the Republic of Turkey
CIF	Cost Insurance Freight
CPI	Consumer Price Index
ÇAYKUR	Tea Processing Company
DFIF	Support Price Stabilisation Fund
DIS	Direct Income Support
EBFs	Extra Budgetary Funds
ERDEMİR	Iron and Steel Manufacturer Company
FADN	Farm Accountancy Data Network
FOB	Free on Board
FDI	Foreign Direct Investment
GIS	Geographic Information System
GDP	Gross Domestic Product
GNP	Gross National Product
IBRD	The International Bank for Reconstruction and Development
IMF	International Monetary Fund
IPM	Integrated Pest Management
ISE	Istanbul Stock Exchange
MARA	Ministry of Agriculture and Rural Affairs
NDA	Net Domestic Assets
NFI	Net Foreign Investment
NIR	Net International Reserves
OMO	Open Market Operations
PCT	Petroleum Consumption Tax
PEIR	Public Expenditure and Institutional Review
PFPSAL	Programatic Financial and Public Sector Adjustment Loan
PETKİM	The Petrochemical Company
POAŞ	Petroleum Products Distribution Company
SDIF	Saving Deposit Insurance Fund
SEEs	State Economic Enterprises
SIS	State Institute of Statistics

SMEs	Small and Medium Sized Enterprises
SPO	State Planning Organisation
SRF	Supplementary Reserve Facility
TL	Turkish Lira
TEKEL	Tobacco and Spirits Company
TSFAŞ	Sugar Production Company
TÜPRAŞ	Petroleum Refining Company
TÜSTAŞ	Engineering/Consulting Company
TZDK	State Agricultural Input Supplier
VAT	Value Added Tax
WPI	Wholesale Price Index
WTO	World Trade Organisation

INTRODUCTION

In the Helsinki Summit of the European Council (EU), Turkey's candidacy was recognised by the European Union on the basis of the same criteria as applied to the other candidate countries. Following the summit, the EU Council approved the Accession Partnership Document for Turkey. Upon the approval of this Document, Turkey has first prepared and then started to implement the "Turkish National Programme for the Adoption of the Acquis", containing short and medium term priorities on which accession preparations must concentrate in the light of the Copenhagen political and economic criteria and the obligations of a member state.

In both aforementioned documents, one of the short-term priorities envisaged, *inter alia*, is to prepare a pre-accession economic programme. The objectives of the Turkish Pre-Accession Economic Programme are the fulfilment of the Copenhagen economic criteria and the preparation for participation in the European Economic and Monetary Union.

Having adopted market economy oriented policies since the 1980s, Turkey established a Customs Union with the European Community in 1996, achieving a much higher level of integration both in commercial and legislative terms.

Although the policies based on the improvement of market economy have been implemented progressively in the late 1990s, mainly because of persistent inflation and macroeconomic imbalances, a need for a comprehensive stability programme arose. Accordingly, at the end of 1999, an economic programme aiming mainly at bringing inflation down to single digits, reducing the interest rates to a reasonable level, increasing the growth potential of the economy, and ensuring the effective use of economic resources was put into practice.

Until the last quarter of 2000, important steps were taken in order to reach the targets of the programme through consistent implementation of fiscal, incomes, monetary, and exchange rate policies. After the commencement of the programme, interest rates decreased sharply, an important deceleration in the inflation rates has been observed, and inflation has dropped to the lowest levels since 1986.

However, unfavourable developments in internal and external markets caused two serious crises in November 2000 and February 2001, deteriorating economic balances. Thus, the revision of the economic programme has become inevitable.

Since February 2001, a revised programme under the floating exchange rate regime has been implemented to overcome the adverse effects of the two crises and to transform the economy.

The Pre-Accession Economic Programme, prepared under these circumstances, consists of four chapters: review of recent economic developments, framework of economic developments, public finance, and structural reforms.

In the first chapter, a short summary of recent economic developments is provided. In the second chapter, economic developments and prospects for 2001 and 2002 and major issues of the 8th Five Year Development Plan (for 2001-2005) are addressed. The following chapter outlines the framework of public finance for 2001 and 2002. Finally, structural reforms are detailed in the last chapter.

The Pre-Accession Economic Programme contains medium term projections relating to 2001, 2002, skipping 2003 and 2004. Upon the re-establishment of economic balances, the Pre-Accession Economic Programme will be revised, including projections relating to 2003 and 2004.

Since main macroeconomic variables are expected to meet the 8th Five Year Development Plan targets to a certain extent by 2005, in terms of their growth rates or ratios to GNP, the projections of the Plan for 2005 are also included in this programme.

1. REVIEW OF RECENT ECONOMIC DEVELOPMENTS

In response to unsustainable trends in public finance and substantially high real interest rates during 1999, a comprehensive macroeconomic programme covering the 2000-2002 period was launched at the end of 1999. The IMF, through a three-year Stand-by Arrangement, supported this programme.

The main goals of the programme were to:

- lower inflation rates to single digit levels by the end of 2002,
- put public finance on a sustainable path,
- put the economy on a higher and a more stable growth path,
- implement the structural reforms that are needed to achieve a more efficient, productive and flexible economic structure.

The programme was based on the following four pillars:

- tight fiscal policy, which aims at a considerable improvement in the primary surplus of the total public sector,
- forward looking incomes policy,
- rule based credible monetary policy in combating inflation,
- structural reforms in areas of agricultural support system, social security, privatisation, fiscal transparency and regulation and supervision of the financial sector.

In order to break the inflationary expectations and to decrease real interest rates, exchange rate was chosen as a nominal anchor, and daily values of the exchange rate basket consisting of 1 USD+0.77 EURO consistent with the inflation target were announced.

Just after the initiation of the programme, interest rates fell down sharply from 90 percent in December 1999 to 35 percent in January 2000 and started to fluctuate in a 35-40 percent band during the January-August 2000 period.

A sharp decline in interest rates together with the exchange rate policy stimulated domestic demand. This was mainly due to the high initial credibility of the programme, wealth effect and lagged consumption demand stemming from high real interest rates in 1999 and August 1999 earthquake.

1.1. Real Economy

As a result of the boom in domestic demand, GDP (by expenditures) grew by 7.1 percent in 2000. Total domestic demand, which decreased by 3.7

percent in 1999, increased by 9.6 percent due to a more stable political and economic outlook, falling interest rates, and a sizeable real interest payments shifting from the last year.

Table 1 : Developments in Demand Components

(Percentage Change with respect to the Same Period of the Previous Year)

	1999	2000
Total Consumption	-1.7	6.5
Private Consumption	-2.6	6.4
Public Consumption	6.5	7.1
Fixed Capital Formation	-15.7	16.5
Public	-8.7	19.7
Private	-17.8	15.4
Change in Stocks(1)	2.0	0.8
Total Domestic Demand	-3.7	9.6
Net Merchandise and Services Export(1)	-0.9	-2.9
Merchandise and Services Export	-7.0	19.3
Merchandise and Services Import	-3.7	25.4
GDP (by expenditure)	**-4.7**	**7.1**

(1) Contribution to GDP growth.
Source: SIS

In 2000, private and public consumption increased by 6.4 and 7.1 percent respectively. The leading factor of the increase in private consumption was the 27.5 percent increase in the demand for durable goods.

Private and public gross fixed capital formation increased by 15.4 and 19.7 percent respectively, due to the high increase in machinery and equipment investments.

In 2000, value added in agriculture, industry and services sectors increased by 4.1, 5.6 and 8.7 percent respectively. In the same year, industrial production increased by 6.1 percent. The highest production increases were experienced in textiles and clothing, plastic and rubber, machinery, radio-TV and communication equipment and automotive industries. Capacity utilisation rate in private manufacturing industry increased from 69.8 percent in 1999 to 74.2 percent in 2000.

Table 2 : Sectoral Growth Rates

(Percentage Change Over the Same Period of the Previous Year)

	1999	2000
Agriculture	-5,0	4,1
Industry	-5,0	5,6
Manufacturing	-5,7	5,9
Services	-4,5	8,7
Construction	-12,5	5,8
Trade	-6,3	11,6
Transportation and Communication	-2,4	5,1
Import Duties	-5,7	27,3
GDP (by production)	-4,7	7,2
NFI	-56,2	-74,6
GNP	-6,1	6,1

Source: SIS

1.2. Inflation and Wages

Despite the fact that year by year price increases realised around 15 points higher than the targeted level, monthly price increases declined significantly during 2000.

Monthly price increases remained high during the first two months of 2000. This was essentially due to the severe winter conditions, the rise in international oil prices and the pass through impact of acceleration of public sector price adjustments and faster depreciation of the Turkish Lira in the last two months of 1999.

As the impact of these temporary factors diminished, monthly price increases started to slow down considerably since March 2000. In fact, monthly price increases in Wholesale Price Index (WPI) in the period of April-December 2000 were less than 2 percentage points than monthly price increases in the same period of the previous year.

As a result, annual percentage changes of the WPI and the Consumer Price Index (CPI) as of December 2000, declined to 32.7 percent and 39 percent respectively, compared to 62.9 percent and 68.8 percent in 1999.

Incomes policies were implemented in line with the targeted inflation in 2000. In this context, civil servant salaries were increased by 15 percent in the first half and by 10 percent in the second half of 2000. In the Programme, the government committed that when the cumulative increase in CPI exceeded its targeted level, the salaries would be compensated as much as the exceeded part. In June and December, additional 3.6 percent and 5.2 percent increases in civil servant salaries were also granted for compensation. Hence, the overall increase of civil servant net salaries was realised as 37.1 percent in 2000. Net nominal wages of public and private sector workers were increased by 65.7 and 56.5 percent respectively. The high wage increase in public sector was mainly due to two-year wage contract signed in the beginning of 1999. The average monthly net minimum wage was increased by 32.3 percent in 2000.

1.3. External Balance

On the external balance side, total exports increased by 8 percent and realised as 31.7 billion dollars in 2000. Imports increased by 35.9 percent and reached to 54 billion dollars due to the real appreciation of Turkish Lira (TL), the rise in domestic demand, and the increase in energy prices like crude oil and natural gas. The imports of these inputs increased from 5.4 billion dollars in 1999 to 9.5 billions dollars in 2000. Thus, trade deficit for 2000 increased by 12 billion dollars with respect to 1999 and was recorded as 22.4 billion dollars.

Although there was an increase in net other revenues (increased from 3.9 billion dollars in 1999 to 7.3 billion dollars in 2000) with a sharp increase in tourism revenues, the current account deficit increased by 8.5 billion dollars in 2000 reaching 9.8 billion dollars resulting from the deterioration of the trade balance.

Despite the fact that part of the deficit in the current account was financed by short term capital inflows, the sharpening in the current account deficit together with the lack of Foreign Direct Investment (FDI) raised concerns regarding the sustainability of the crawling peg exchange rate regime. In 2000 total capital inflows increased by 4.8 billion dollars.

Table 3 : Current Account Balance

(Million Dollars)

	1999	**2000**
I. Trade Balance	-10,443	-22,377
II. Services Balance	3,908	7,333
1.Other Goods and Services Income	18,748	22,320
Travel	5,203	7,636
Interest	2,350	2,836
Other	11,195	11,848
2.Other Goods and Services Exp.	-14,840	-14,987
Travel	-1,471	-1,711
Interest	-5,450	-6,299
Other	-7,919	-6,977
III. Unrequited Transfers (Official+Private)	5,175	5,225
Workers' Remittances	4,576	4,603
Current Account Balance	-1,360	-9,819

Source: CBRT

1.4. Fiscal Policy

Based on the three-year programme initiated in 2000 the primary objective of the fiscal policy was to reduce the net public debt-to-GNP ratio over the medium term through raising primary surplus of the public sector from -2.8 percent of GNP in 1999 to 2.2 percent of GNP in 2000. Improvement in adjusted primary surplus was mainly targeted in consolidated budget performance at 3.9 percent of GNP in 2000.

To reach the targeted fiscal adjustment and generate revenues for earthquake-related expenditures, several measures, especially in the revenue side were taken. A major tax package consisting of additional personal and corporate income tax payments, a doubling of motor vehicle and property taxes, a special transaction tax, a special surtax on mobile phone bills, a withholding tax on government securities issued before 1 December, 1999, a three-month temporary tax and an increase in the remittances of surpluses generated by regulatory bodies was approved in November 1999. Following these adjustments, additional tax measures increasing Value Added Tax (VAT) rates, withholding tax rates on interest income and repos and personnel tax rates exempting for wage and salary earners were adopted by the Cabinet Decision in December 1999. In addition, tax brackets were increased according to the targeted inflation.

At the same time, a package of budgetary expenditure measures was introduced. Within this context, a 2 percent cut in all primary spending excluding personnel and some other transfers, and limits on replacement hiring of at most 15 percent in SEEs were imposed.

In addition, the Government engaged in important revisions to reinforce the budget preparation, execution and control through enhanced fiscal transparency and accountability. In this respect, 25 of the existing 61 budgetary funds and 2 non-budgetary funds were abolished in 2000. In 2001, excluding the six extra-budgetary funds, all funds were abolished.

The strict implementation of these measures brought about a significant turnaround in the primary balance of the public sector, particularly in the central government budget. The primary consolidated budget surplus rose up to 5.5 quadrillion TL at the end of the year, corresponding to 4.3 percent of GNP. Consequently, the primary surplus of the public sector (in total) was realised as 1.5 percent of GNP in 2000.

On the financial side, borrowing ability from international markets improved until the November Crisis and the share of net external borrowing in net total borrowing rose from 5.8 percent in 1999 to 24.4 percent in central government budget.

Interest rates on Treasury’s domestic borrowing declined sharply from over 100 percent in 1999 to around 38 percent. This obviously helped to stabilise the net public debt to GNP ratio in 2000. This ratio decreased from 61 percent of GNP in 1999 to 58.4 percent of GNP in 2000.

The fiscal adjustment was accompanied by a more active and diversified debt management policy and privatisation. In order to limit the domestic borrowing requirement of the public sector, the Government aimed at obtaining at least 7.6 billion dollars of privatisation proceeds for the public sector in 2000. At the end of the year, privatisation proceeds amounted to 3.1 billion dollars.

1.5. Monetary and Exchange Rate Policies

The Stand-by Arrangement contained obligations to follow strict monetary and exchange rate policies, as well as structural revisions especially in the banking sector. The basic guidelines of the Stand-by Arrangement might be defined as an exchange rate based stabilisation programme.

Following a crawling-peg regime, the Central Bank of the Republic of Turkey (CBRT) had to comply with ceilings on Net Domestic Assets (NDA) and had a pre-determined symmetrical corridor around NDA. In addition, floor values for Net International Reserves (NIR) were announced. The monetary and exchange rate policy implementation for the three-year stabilisation programme consisted of two stages. In the first 18 months of the programme, the pre-announced nominal exchange rate path for the TL against the basket guided the exchange rate policy and the exchange rate target was an intermediate target in this crawling-peg regime. In the second stage, which was to start by July 2001, a shift to a gradually widening symmetrical band around a central parity system was announced. The width of the band was to reach 7.5 percent by the end of 2001, 15 percent in mid-2002 and 22.5 percent at the end of 2002.

According to the “crawling peg” exchange rate policy, TL values of the exchange rate basket composed of 1 USD+0.77 EURO were announced on a daily basis in 2000. For the same year, the nominal depreciation rate of exchange rate basket was determined to be 20 percent, being equal to the targeted year-end WPI inflation. At the end of every three months, the CBRT announced the depreciation rate of TL against the currency basket for an additional three months, while keeping the pre-announced rates for the previous 9 months unchanged, hence, providing a clear perspective for the economic agents on exchange rate for the following 12-month period.

In the context of the exchange rate band system that was to be implemented after June 2001, the central parity and related upper and lower limits of the exchange rate basket were also announced on a daily basis by the end of September 2000. Accordingly, the monthly depreciation rate of the central parity was set as 0.85 percent for the second half of 2001.

At the end of 2000, WPI increased faster than the exchange rate basket did, and the real appreciation of TL against the basket was realised as 6.92 percent.

Under the new regime, the CBRT imposed a floor to NIR in addition to upper and lower limits for the NDA item. NIR item was a performance criterion for the six months of 2000 and an indicative floor value for the second half of 2000. During the first stage of the programme, net domestic assets would fluctuate roughly within a parallel band whose upper and lower limits would be determined as ±5 percent of previous end-quarter base money figures.

Table 4 : Net Domestic Assets and Net International Reserves Targets and Realisations

	Net Domestic Assets (Trillion TL)		Net International Reserves (Million Dollars)	
Period	**Target**	**Realised**	**Target**	**Realised(1)**
2000 March (2)	-1,200	-1,260.2	12,000	16,589.7
2000 June (3)	-1,200	-1,295.1	12,750	17,578.2
2000 September (4)	-1,200	-1,307.6	12,750	17,626.5
2000 November (5)	-1,200	1,938.8	-	15,917.6
2000 December (6)	-1,200	-	13,500	-
2000 December (7)	1,650	1,060.0	10,400	12,400.0

(1) Excluding the figure in December, figures are determined by using current dollar rates. Source: CBRT, Weekly Press Bulletin.
(2) NDA realised figure as in CBRT, Press Review in 3 April 2000.
(3) NDA realised figure as in CBRT, Press Review in 3 July 2000.
(4) NDA realised figure as in CBRT, Press Review in 2 October 2000.
(5) NDA realised figure in last day of the month.
(6) Targets before the November 2000 crisis.
(7) Targets suggested after the crisis. NDA realised value is the average of those in 21 December 2000 and 11 January 2001. NIR realised value is the average of those in 21 December 2000 and 11 January 2001.

According to the exchange rate-based stabilisation programme, the open market operations (OMO) were not to be resorted freely due to the constraint on the NDA. With the implementation of this programme, the monetary authorities started to implement OMO with the aim of compensating the effects of changes in other sub-items of NDA. Therefore, the daily OMO lending may be above or below markets' requirements and this resulted in volatility in the short-term interest rates. In this system, the CBRT had a limited initiative to intervene in the interest rates which was linked to the width of the NDA corridor.

Following the announcement of the programme, the short-term interest rates, the Treasury auction rates, and the rates of the government securities in the secondary markets decreased rapidly. The decline in the inflationary expectations and Treasury's domestic debt roll-over ratio and the removal of the exchange rate risk premium on the interest rates as a result of the new exchange rate regime played an important role in the reduction of the interest rates. The slowdown in the interest rates was sharper in the first four months of the year than that in the following May-August period.

Although the substantial decline in the interest rates prevented rapid foreign portfolio flows to the secondary markets in the first months of the programme, the Treasury's successful borrowing at the international markets highly contributed to the increase in NIR of the CBRT.

Total credit used by the non-financial sector increased by 22.6 percent in real terms compared with the end of the 1999 value. One of the reasons for this increase is the decline in the domestic borrowing of the Treasury in 2000. This caused a contraction in the securities portfolio of the commercial banks and an increase in the commercial banks' loans to non-financial sector. The other reason was the increase in the aggregate demand observed after the implementation of the stabilisation programme. As of August 2000, consumer credits increased by 287 percent in nominal terms and 220 percent in real terms with respect to the end of 1999.

The Crisis in November 2000 and Developments between November 2000-February 2001:

With the start of the programme at the outset of 2000, interest rates fell from 96 percent in December 1999 to 36 percent in the first quarter of 2000. This made the banking system become more vulnerable to increases in interest rates. Because of this vulnerability, banks financed T-bills with short-term resources, such as overnight repos.

Furthermore, sharply decreasing interest rates revoked the lagged consumption and investment demand, which led to a slowing down in TL deposits, a boom in credit demand and also increasing import demand due to the overvalued TL, which caused unsustainable levels of current account balance. Related with these reasons, credit volume of the banking sector increased and its date of maturity extended.

Due to the incompatibilities between the realised capital inflow and the inflow needed to finance the high rate of economic growth, short-term interest rates began to increase in August. Average interest rates in Repo-Reverse Repo in Istanbul Stock Exchange (ISE) were 25.5 percent in July, 29.5 percent in August, 47.7 percent in September and 53.8 percent in October 2000. Despite the increase in interest rates in secondary markets, the money market rates on T-bills did not reflect a similar trend. Such a mismatch could be signed as a liquidity problem.

From the standpoint of international markets, in 2000 Turkey was the second trustworthy market after Mexico among the emerging markets. However, signals of a slowdown in the US economy, discouraging oil price trends and related global economic slowdown sentiments made international investors prefer to hold liquid positions. Moreover, it was observed that the risk premiums of the emerging markets were increasing.

Hence, interest rates on emerging market-debt instruments started to increase in international financial markets, which caused foreign borrowing become more costly. As a matter of fact, whereas spread for Turkey in September 2000 was around 490 basis points (bps), it became 560 bps in October. Meanwhile, the risk premium of emerging markets increased sharply due to the problems occurred in Argentina. Therefore, at the end of October 2000, spread for Turkey increased to 620 bps, reflecting a more costly foreign borrowing and a need to meet margin calls for the collaterals of the syndicated loans.

For the period January-October 2000, the announced programme was successfully executed. However, in November 2000, Turkish financial markets had a crisis due to internal negative impacts and distortions at international financial markets, as well as facing a liquidity squeeze arising in the domestic money markets due to the sudden jump in the FX demand of the market participants. At this stage, Turkish banks demanded foreign exchange due to decreasing value of their guarantees against the syndicated loans. Following the interest rate hikes, the balance sheets of the banking sector deteriorated, giving way to increase the burden of the SDIF. As these developments occurred, adverse sentiment against Turkey in the international market grew further, exacerbating the capital outflow, which in turn aggravated the crisis. As a result, the basic performance criteria pertaining to the monetary policy, namely NDA and NIR, stated in the original letter of intent, were revised. However, at that period, the CBRT was successful enough to retain the crawling peg regime.

Increased liquidity congestion led the CBRT to fund the market. However, this funding turned out to satisfy the foreign currency demand, which threatened the level of international reserves, instead of eliminating the rapidly developing liquidity crunch. Hence, at the end of November 2000, considering the reserves, the CBRT let interest rates to be high, which caused overnight interbank interest rates to be as high as 999 percent. Net Foreign Exchange Reserves decreased from 24.1 billion dollars on November 16 to 17.9 billion dollars on December 5th, 2000. Between the 6th and the 19th of December, the Central Bank recovered part of its reserves and bought back 1.9 billion dollars. In this process, the Supplementary Reserve Facility (SRF) extended to Turkey by the IMF constituted the crucial part of the newly gained reserves. In the last 5 working days of December, the Bank accommodated the surge in currency demand due to the long holiday and end-year closing books of the banking sector.

As a consequence of the crisis, basic magnitudes of monetary programme, namely NDA and NFA, were revised. The radical change was the termination of the corridor band application for NDA. The other change was that the TL required reserves were reduced from 6 to 4 percent on the 12th of January 2001, which provoked a sharp shrinkage in base money which was around 18 percent in nominal terms as of 8th of February.

Table 5 : Revised Performance Criteria Values for Net Domestic Assets and Net International Reserves in 2001

	NDA Upper Bounds (Trillion TL)		NIR Lower Bounds (million dollars)	
31 January 2001	900	Perf. Crit.(1)	10,700	Perf. Crit.
28 February 2001	800	Perf. Crit.(1)	10,900	Perf. Crit.
31 March 2001	650	Perf. Crit.(1)	11,000	Perf. Crit.
30 June 2001	200	Perf. Crit.(1)	12,000	Perf. Crit.
30 September 2001	480	Ind. Target (1)	12,200	Ind. Target
31 December 2001	950	Ind. Target (1)	12,400	Ind. Target

(1) Those limits will be determined as the average of values realised at last 5 working days.

Despite the abandonment of the monetary policy due to the above mentioned shock experienced in November 2000, the exchange rate regime was survived, letting the CBRT to stick to the pre-announced TL values against the currency basket.

Crisis in February 2001:

As stated in the previous section, the programme performance aggregates values were revised after the November 2000 crisis. In addition, due to the surge in capital inflows more than expected, the gap between the realised NDA stock and the NDA ceiling was widened. Accordingly, in order to increase the operational predictability of monetary policy, the NDA ceilings were readjusted downwards. Similarly, the NIR floors were readjusted upwards.

However, the fragile state of confidence in the financial markets gave way to a second financial crisis in February 2001; exchange rates boosted to very high levels and average overnight interest rates climbed to 4,019 percent on 21 February 2001. During the first two days of the crisis, the Central Bank lost 5 billion dollars in FX reserves. Consequently, the CBRT has abandoned monetary and exchange rate policies and shifted to a floating exchange regime on 22 February 2001.

Following the crisis in February 2001, indicative and performance criteria exceeded the announced targets. Targeted NIR of 12.6 billion dollars for February realised as 9.8 billion dollars. NDA was realised as 2,869.4 trillion TL in February as compared to the targeted upper value of 0 TL and 0.9 percent target increase in currency basket turned out to be 35.9 percent.

Table 6 : Developments in Performance Criteria Monetary Aggregates

	2000				2001	
	Jan.	Sept.	Nov.	Dec.	Jan.	Feb.
Exchange Rate Basket % Change (1USD+0,77EURO)						
Target	2.1	1.3	1.0	1.0	0.9	0.9
Realised	2.1	1.3	1.0	1.0	0.9	35.9
Net Domestic Assets (Trillion TL.)						
Target[1]	-	-1,200.0	-	1,650.0	900.0	0.0
Realised[1, 3]	-1,164.4	-1,164.4	1,938.8	1,060.0	-495.4	2,869.4
Net International Reserves (Billion USD)						
Target[2]	-	12.75	-	10.4	10.7	12.6
Realised (estimated with current dollar rate)[4]	16.4	17.6	15.9	12.4	14.0	9.8

[1] NDA targets for 2001 were suggested as upper limits. Realised NDA in November is as the last day of the month, others are as the last Friday of the month.
[2] It is an indicative floor value after the second quarter of 2000.
[3] Realised NDA on December is the average of those on 11 December 2000 and 11 January 2001.
[4] Realised NIR on December is the average of those on 21 December 2000 and 11 January 2001.

2. FRAMEWORK OF ECONOMIC DEVELOPMENT

2.1. Developments and Prospects for 2001

After the crisis in February, exchange rate policy was shifted from pegged to floating and TL started to depreciate significantly. In addition, increase in public debt due to covering the losses incurred by the state banks, necessitated further fiscal tightening. In this context, under the new fiscal and monetary scheme, the macroeconomic targets were revised.

The main revised macroeconomic goals of the programme are:

- to keep the rate of increase in CPI limited,
- to resume growth and to maintain a sustainable growth path,
- to keep the current account balances close to zero in 2001 and 2002.

These goals will be achieved through a three-pronged approach based on:

- structural policies aiming to correct the distortions directly underlying the recent crisis, including banking sector and enhance the transparency of economic management and the role of the private sector in the restructuring of the economy,
- fiscal and monetary policies geared towards restoring financial stability and resuming the disinflation process,
- an enhanced social dialogue aimed at price and wage policies consistent with macroeconomic stability, growth, and the protection of the most vulnerable parts of the society.

2.1.1. Real Economy

After increasing 6.1 percent in 2000, GNP declined by 8.5 percent in the first half of 2001. Although value added produced by the industry and the services sectors decreased respectively by 5.2 and 7.1 percent, the drastic drop in the net foreign income in this period caused a decrease in GNP which was 2.4 points higher than the decrease in GDP.

The decrease in GNP for the first half of 2001 has mainly stemmed from the falling private consumption and private investment. While the drop in the demand for durable goods has been influential in the decrease of private consumption, which was recorded as 7.5 percent. The fall in the machinery and equipment investment has led to the sharp decline in private investment, which was realised as 23.3 percent. As a result of these developments, total domestic demand decreased by 17.8 percent in the first half of 2001.

According to the monthly production index, the average industrial production declined by 6.9 percent in the first seven months of 2001, in relation to the same period of 2000. Average capacity utilisation rate in private manufacturing industry decreased by 9.4 percentage points in the first eight months of 2001 compared to the same period of last year.

In spite of the increase in exports and good performance in tourism sector in the second half of 2001, GNP is expected to decrease by 8.5 percent in year 2001 as a whole, due to the continued contractions especially in agriculture, industry and trade sectors.

2.1.2. Inflation and Wages

Transition to a floating exchange rate regime after the financial crisis and implementation of price adjustments in the public sector had a significant impact on WPI and CPI indices in March and April 2001. However, considerable decline in prices increases was observed in May and June 2001. Due to the seasonal factors, monthly increases in CPI realised close to the targeted values in July and August. In August, cumulative increases in WPI and CPI with respect to the end of year 2000 were registered as 54.6 percent and 39.5 percent and 12 monthly increase in two indices were recorded as 69.6 percent and 57.5 percent respectively. At the end of 2001, 12 monthly increase in WPI and CPI are projected to reach to around 80 percent and around 65 percent respectively.

Avoiding a wage-price spiral in the following period requires a more structured incomes policy including a closer cooperation with the social partners. The wage policy in the public sector also supported the disinflation effort and was fully consistent with the fiscal targets. Rational wage and price setting behaviour in the private sector is also essential for the success of the programme. Protecting the social welfare of all citizens is a fundamental component of the programme.

To this extent, civil servant salaries were raised by 10 percent in January 2001 for the first six-months of the year, and 5 percent in July 2001 for the second part of the year. Additionally, those salaries were adjusted by 2.5 percent in April, 10.1 percent in May, 5.4 percent in June, and 3.4 percent in September. As laid down in the Budget Law, adjustments will be continued in October, November and December 2001. The annual average increase in net nominal salaries (excluding the increases since October 2001) is about 45 percent.

Workers wages in the public sector increased by 15 percent for the first and second half of the first year of the collective agreements, which were renewed by the General Protocol, signed in May 2001. The 80 percent difference between the indicative inflation rate and the realised inflation rate will be reflected to the wage increases in the second half of the year. The wage increases in the first half of the first year will be paid in February 2002. Expected annual average increase in the net monthly wage in this sector is about 36.6 percent. The minimum wage was increased by 17.8 percent in January 2001 and 5 percent in July 2001 and 14.3 percent in

August 2001. In 2001, the expected increase in average monthly net minimum wages is about 33 percent for the workers in industries over 15 years old.

2.1.3. External Balance

Imports decreased by 21.6 percent and realised as 23.6 billion dollars in the first seven months of 2001. Shrinkage in imports gained momentum after the implementation of the floating exchange rate regime at the end of February. As a result, imports (CIF) are projected to be 41.0 billion dollars at the end of 2001.

Exports increased by 9.2 percent and reached 17.6 billion dollars during the first seven months of 2001. Real depreciation of TL and shrinkage in domestic demand has positively affected the export growth and the programmed level is attainable in spite of the fact that there is a declining trend in the growth of the world economy. As a result, exports (FOB-including shuttle trade) are expected to reach 34.3 billion dollars in 2001.

Tourism revenues were realised as 3.1 billion dollars in the January-June period of 2001, reflecting a 20 percent increase, in relation to the same period of last year. Tourism revenues are estimated to reach the level of 8.3 billion dollars at the end of the year.

Capital account during the first six months of 2001 displayed that after February 2001 there has been a significant capital outflow of 8.8 billion dollars.

Due to the improvements in foreign trade balance and increase in tourism revenues, a surplus of around 2.9 billion dollars in current account is expected in 2001.

2.1.4. Monetary and Exchange Rate Policies

Following the crisis experienced in February 2001 the Central Bank aborted the crawling peg regime and adopted a floating exchange rate regime along with announcing the prospect of shifting to inflation targeting as the monetary policy by the end of 2001, which turned out to be a solid and confirmed policy shift.

Following the stabilisation on exchange rates, the Central Bank aims to focus on controlling the monetary aggregates in order to fight inflation for the rest of 2001. Hence, the monetary policy of 2001 is based on the following matters; monitoring the restrictions on NDA account and if needed, making the required revisions, amount of foreign funding and its implications on its distribution between the Central Bank reserves and the consolidated budget funding, and to alleviate the additional burden to public finance resulting from restructuring the banking system.

As opposed to the nominal anchor of the monetary policy in 2000, the path of the monetary base will be utilised as the nominal anchor of 2001. The restrictions as indicated as the upper bound of the named aggregate is presented below:

Table 7 : Monetary Base

MONETARY BASE	Upper Bound(Trillion TL)
31 August 2001 – Realised Monetary Base [2]	6,748
31 August 2001 (indicative upper bound) [1]	7,175
31 October 2001 (indicative upper bound) [1]	7,550
31 December 2001 (indicative upper bound) [1]	7,750

1 - Those limits will be determined as the average of values realised in last 5 working days.
2 - Average of values realised in last 5 working days. (CB – Press Review in 4 September 2001)

Indicated values of the monetary base will be given emphasis as referencing the monetary policy. However in the case that inflationary pressures accumulate by unexpected events, the Central Bank is to shift its priority to easing such pressures by increasing short-term interest rates instead of strictly adhering to the announced monetary aggregates.

Table 8 : Net Domestic Assets

NET DOMESTIC ASSETS	Upper Bound(Trillion TL)
31 August 2001 – Realised stock [2]	16,437
31 August 2001 (performance criterion) [1]	17,250
31 October 2001 (performance criterion) [1]	21,150
31 December 2001 (indicative upper bound) [1]	22,400

1 – Consistency with performance criteria (indicative upper bound) will be determined as the average of stock
2 - Average of values realised in last 5 working days. (CB – Press Review in 4 September 2001)
3 - NDA ceilings will be adjusted for any change in the definition of the aggregate to which the reserve requirement applies according to the following formulae:
$\Delta NDA=R*\Delta B$ and $\Delta NDA=B*\Delta R$
where: R denotes the 4 percent reserve requirement plus the 2 percent liquidity requirement coefficient, B is the level of the base to which the reserve requirement applies on the test date and Δ denotes the change in corresponding aggregate.

Foreign funding, used in the scope of the programme, is expected to provide confidence in financial markets and to contribute to decrease the interest rates instead of being used in the stabilisation of exchange rates by increasing the foreign currency supply to the market.

In the programme, performance criteria for NDA and NIR were determined in parallel with the use of foreign funding as stated before.

Table 9 : Net International Reserves (NIR)

NET INTERNATIONAL RESERVES (NIR)	Lower bounds for changes for stated periods (Million Dollars)
July-August 2001 – realised changes at NIR [2]	-1,370
July - August 2001 (Performance Criterion) [1]	-2,500
September - October 2001 (Performance Criterion) [1]	-3,250
November - December 2001 (Indicative Lower Bound) [1]	-600

(1) Those limits will be determined as the average of values realised in last 5 working days.
(2) Source: CB-Press Review in 4 September 2001.

If interest rates decrease sharply as expected, these limits will be reconsidered.

To address these goals, the CBRT Law No. 1211 was amended by the Law No.4651. According to this amendment, price stability is now the primary objective of the Central Bank. Thus, the Bank gained autonomy to determine the monetary policy tools to reach that target with a view to a shift towards a full-fledged inflation-targeting framework, as early as possible. With the amendment, it is also aimed to reshape the CBRT into a more independent, more credible, more transparent, and more reliable central bank. Furthermore, after the transition period ending in November 2001, direct lending from Central Bank to the Treasury will be terminated completely.

2.2. Macroeconomic Projections for 2002

The main priorities of the macroeconomic programme for 2002 are to strengthen the disinflation efforts; to maintain the current account near balance, and to achieve a fiscal adjustment that is compatible with the goal of lowering inflation and the resumption of growth on a sustainable basis.

GNP is expected to pick up from a 8.5 percent decline in 2001, reaching a growth rate of 4 percent in 2002. This improvement in the growth rate is expected to be led by the increase in domestic demand.

12 monthly changes are targeted to be 31 and 35 percent for WPI and CPI respectively in 2002.

For 2002, total exports (including shuttle trade) and imports (FOB) are projected to amount to 36.1 and 44.5 billion dollars. With the increase in the trade deficit and with the assumption of stability in other revenues, current account surplus is projected to be 0.1 billion dollars in 2002.

Fiscal policy will remain focused on the process of fiscal adjustment aiming at stabilising the debt over GNP ratio, increasing fiscal discipline, decreasing inflation as well as keeping the current account deficit under control.

The primary surplus of the public sector is targeted to reach 6.3 percent of GNP in 2002.

The level of the targeted primary surplus accompanied by privatisation and the expectations that real interest rates will decline from their current high levels, will result in a sharp decrease in the net public debt ratio from around 80 percent in 2001 to around 70 percent of GNP in 2002.

Table 10: Main Economic Indicators

	2000	2001 Estimate	2002 Program	2005 (1) Projection
GNP Growth (% Change)	6.1	-8.5	4.0	7.0
GNP (Trillion TL.)	125,971	184,767	280,550	-
Exports (FOB) (Billion $) (2)	31.7	34.3	36.1	48.8
Imports (FOB) (Billion $)	54.0	39.8	44.5	77.4
Current Acc. Balance (Billion $)	-9.8	2.9	0.1	-7.7
Current Acc. Balance/GNP (%)	-4.8	1.9	0.1	-2.5
GNP Deflator (%)	51.6	60.3	46.0	2.0
WPI (Dec.-Dec.) (%)	32.7	80.0	31.0	-
CPI (Dec.-Dec.) (%)	39.0	65.0	35.0	-
Consolidated Budget Overall Balance/GNP (%)	-10.9	-16.5	-10.4	-2.1
Total Public Sector Overall Balance/GNP (%)	-12.4	-16.4	-8.8	-3.0
Consolidated Budget Primary Balance /GNP (%) (Excl. Privatisation, interest receipts, central bank profits)	4.3	5.1	5.4	-
Total Public Sector Primary Balance /GNP (%) (Excl. Privatisation interest receipts, central bank profits)	2.3	5.6	6.3	-

(1) 8th Plan Target
(2) Including Shuttle Trade.

2.3. Major Issues of the 8th Five Year Development Plan (2001-2005)

The major objectives of the 8th Five Year Development Plan are; raising the living standards of the society, accelerating integration with the world within the perspective of European Union membership.

In order to attain these basic objectives, the Plan aims at:

- ensuring macroeconomic stability;
- achieving sustainable development through the improvement of a competitive economic structure;
- raising technological capacity;
- developing human resources;
- increasing employment;
- expanding reforms in the social security system;
- reaching to a balanced income distribution and alleviating poverty;
- decreasing inter-regional development disparities;
- improving public administration and justice system;
- preventing corruption;
- protecting cultural and historical heritage;
- ensuring sufficient energy generation;
- developing other infrastructure services and protecting the ecological balance.

In line with these targets, Turkey will give priority to the following issues:

- reducing public deficits and accelerating privatisation;
- realising necessary structural transformations in the education system and increasing efficiency in health services;
- developing industrial and services sectors with high value added products;
- improving information and communication networks;
- increasing research and development expenditures;
- supporting small and medium size enterprises;
- improving competitiveness;
- increasing the volume of foreign direct investments;
- increasing employment through productive investments;
- registration of unregistered economy;
- providing sufficient infrastructure for services and energy in a reliable and cost-effective manner.

Within the context of the economic stabilisation programme, combating inflation will continue and a sustainable public sector balance will be ensured. The privatisation procedure will be accelerated. Turkey aims to meet the Copenhagen economic criteria and come closer to the Maastricht criteria within the Plan period. In line with this target, the budget deficit over GNP ratio is envisaged to be approximately 2 percent, and the GNP deflator to be 2 percent in 2005.

GNP growth will be increasingly based upon investment and foreign demand, and contribution of factor productivity will be increased. It is estimated that average annual growth rate will be 6.7 percent within the Plan period. Consequently, the per capita income, which is around 3000 dollars in 2000, is expected to reach 4300 dollars in 2005.

The tax system will be simplified and revised in a more comprehensive approach, and an efficient auto-control mechanism will be developed.

The financial system will be restructured, transparency will be ensured, an efficient auditing and monitoring system will be established in line with the international norms and standards.

The industrial sector will be endowed with a structure capable of producing technology and creating original designs and trademarks, and will consider the R&D activities, environmental norms, and consumer health in line with the modern management approaches.

The share of high-tech and high value-added goods within exports will be increased.

The labour market will be structured in a flexible manner considering the norms and standards of the International Labour Organisation (ILO) and the EU.

3. PUBLIC FINANCE

Since the exchange rate policy was revised, reassessment of the fiscal targets for 2001 and 2002 concerning new macro policies aiming at minimising negative impacts of the recent economic crisis proved inevitable.

The key fiscal policy goal of the following programme is to reduce the public sector borrowing requirement and set up sustainable public finance by increasing primary balance.

Major fiscal targets of the revised programme are as follows:

Primary surplus of the public sector for 2001, which was determined as 5 percent in December 2000, was increased to 5.5 percent of GNP in the revised programme.

The net public debt-to-GNP ratio including the net asset position of the Central Bank is expected to rise sharply in 2001, i.e. from 58.4 percent in 2000 to around 80 percent in 2001. This increase mainly flows from the following four factors;

- effect of the devaluation on the value of external debt expressed in domestic currency;
- exceptionally high level of interest rates during the crisis, which led to an explosion of the borrowing costs of the public sector, particularly state and Saving Deposit Insurance Fund (SDIF) banks;
- taking over and the covering of the losses of insolvent private banks and securitising the duty losses of the state banks;
- fall in GDP.

To achieve the targeted primary surplus, the Government has taken the following measures;

- advance payment scheme for personnel and corporate income taxes was shortened from 6 months to 3 months as it was implemented in the second half of 2000;
- advanced corporate income tax rate was raised from 20 to 25 percent;
- rates for the withholding tax on deposits, repurchase agreements, and investment allowances were increased;
- personal income tax brackets were indexed to targeted inflation;
- presumptive income taxation (based on living standards) was reintroduced,
- the special surtax on mobile phone bills and transaction taxes were extended to 2001-2002, while doubling the rates of the latter;
- VAT rates for telephone services (suspended by the Supreme Court later on) and natural gas were increased;

- the rates and levels of taxes on motor vehicles, taxes on vehicles using LPG (suspended by the Supreme Court later on), and other fees were increased.
- the special education levy was extended to 2001-2002;
- the levy on the ISE and other boards were renewed,
- certain fees were increased further,
- 1.5 percent cut was imposed on all primary spending, excluding personnel and transfers to the social security institutions.

As of 2000, the Ministry of Finance issued a directive in January 2001 aiming at reducing all primary expenditures (excluding personnel, transfers to social security funds, and tax rebates) by 5 percent with respect to budgetary allocations.

Additional saving was targeted in other current expenditure (defence expenditure) as laid down in Article 53 of the Budget Law.

During the January-August period of 2001, consolidated budget expenditures were realised as 47,162 trillion TL, which indicated a 45.2 percent increase compared to the same period of 2000. Revenues rose by 45.6 percent and were realised as 32,250 trillion TL for the same period. Hence, budget balance yielded a deficit of 14,912 trillion TL and primary surplus was realised as 10,228 trillion TL, while adjusted primary surplus was realised as 7,250 trillion TL.

Civil servants' salaries were raised by 10 percent in January, and have been adjusted further during the first and second half of 2001 by the difference between the CPI inflation rate and 10 percent. A 2 percent adjustment was granted in accordance with the Budget Law during the first half of the year to compensate for the one-month lag in salary adjustments existing under this system. Salaries were raised by 5 percent in July 2001.

The hiring of civil servants in 2001 was limited to 80 percent of civil servants retired in the previous year (except in the sectors of education, health, and security sectors).

In the framework of the revised programme, the primary surplus of the consolidated central government is targeted at 5.1 percent of GNP in 2001.

Table 11 : Adjusted Public Sector Primary Surplus 2001-2002 (As a Percentage of GNP)

	2000	2001 Estimate	2002 Program
Total Primary Surplus	**2.4**	**5.6**	**6.3**
Central Government	4.3	5.1	5.4
Unemployment Fund	0.3	0.6	0.5
Extra-Budgetary Funds	-0.1	0.0	-0.2
Revolving Funds (Including Soc. Sec. Ins.)	-0.1	-0.2	0.1
Local Authorities	-0.1	0.2	0.2
SEE	-1.8	-0.1	0.4

To realise these goals, the Government has taken the following supplementary measures:

- petroleum consumption tax (PCT) was increased by 15 percent in May 2001 following a 20 percent increase in April 2001. Besides, PCT has been increased monthly at least equal to the increases in WPI.

- the VAT rate were increased from 17 percent to 18 percent and from 25 percent to 26 percent for certain goods and services.

- minimum contribution base in social security payments was increased by 40 percent.

On the expenditure side, the Government envisaged keeping the growth rate of primary expenditure well below that of GNP, which will lower the level of public expenditure.

Due to the unexpected increases in inflation rates and exchange rate depreciation accompanied by sharp increases in interest payments, a supplementary budget was needed. The supplementary budget for fiscal year 2001 was adopted by the Parliament on 21 June 2001.

Following the adoption of the Supplementary Budget Law, budget figures increased both in the revenue and expenditure side. Total revenues rose up to 49.0 quadrillion TL, while total expenditures rose up to 79.0 quadrillion TL. The main revision was realised in total interest payments (from 16.7 quadrillion TL to 41.3 quadrillion TL) with a sharp increase in interest rates, a significant decrease in maturity of government bonds and the securing of its obligations to the SDIF-owned banks and state banks. The Treasury has securitized all its duty losses debts to the state banks.

It is expected that budget revenue will increase to 50.1 quadrillion TL (27.1 percent of GNP) and budged expenditure will increase to 80.6 quadrillion TL

(43.6 percent of GNP) in 2001. Thus, budget deficit is expected to increase to 16.5 percent of GNP in 2001. In addition, primary surplus is expected to reach 5.2 percent of GNP.

Table 12 : Consolidated Budget Figures

(trillion TL)

		Revised Bud.	As a Share of GNP	
	2000	**2001**	**2000**	**2001**
EXPENDITURES	**46,970**	**80,575**	**37.3**	**43.6**
NON-INTEREST EXP.	26,530	40,458	21.1	21.9
CURRENT EXP.	13,590	19,581	10.8	10.6
-Personnel	9,979	14,781	7.9	8.0
-Other Current	3,611	4,800	2.9	2.6
INVESTMENT	2,767	3,750	2.2	2.0
TRANSFER	30,613	57,244	24.3	31.0
- Non-Interest Transfer	10,173	17,127	8.1	9.3
- Interest Expenditures	20,440	40,117	16.2	21.7
REVENUES	**33,245**	**50,100**	**26.4**	**27.1**
GENERAL BUDGET	32,939	48,760	26.1	26.7
- Tax Revenues	26,504	38,487	21.0	20.8
- Non-Tax Revenues	3,486	6,873	2.8	3.7
- Special Revenues and Funds	2,949	4,339	2.3	2.3
ANNEXED BUDGET	306	401	0.2	0.2
TOTAL DEFICIT	**-13.725**	**-30,475**	**-10.9**	**-16.5**

In 2002, the fiscal policy is expected to remain focused on the process of fiscal adjustment stabilising the debt to GNP ratio, increasing fiscal discipline, decreasing the inflation, as well as keeping the current account deficit under control.

The primary surplus of the public sector is targeted to reach 6.3 percent of GNP in 2002.

The primary surplus is expected to increase due to privatisation and expectations that real interest rates decline from their current abnormally high levels. Thus the net public debt ratio is expected to decrease sharply from 78.5 percent in 2001 to 70.4 percent of GNP in 2002.

4. STRUCTURAL REFORMS

4.1. Enterprise Sector

Privatisation in Turkey, aims to minimise state involvement in economic activities and lessen the financial burden of State Economic Enterprises (SEEs) on the national budget on the one hand, and to improve the capital markets and direct the resources toward new investments on the other.

Since 1985, state shares in 219 companies, 4 power generations, 21 incomplete plants and 5 real estates have been taken into the privatisation portfolio. Later, 20 of the companies, 4 power generations and 4 real estates were excluded from the portfolio for various reasons. Currently there are 40 companies in the privatisation portfolio.

By 2001, the state has withdrawn completely from some industries such as animal feed, dairy products, forestry products, tourism and cement. Additionally, more than half of the public shares was privatised in companies in the textile sector. Privatisation of public banks has commenced and important steps have been taken towards lessening the state influence in the financial sector. Along with raising proceeds, cost saving aspects of privatisation were also addressed in a number of loss making state-owned companies (i.e. Kardemir and Sivas Demir Çelik-iron and steel company-, PETLAS-tire manufacturing company).

In 1986, privatisation gained momentum and 163 companies have been privatised by July 2001, with no more government shares exist in 144 of these.

Since 1985, the total proceeds from privatisation are recorded as 7.3 billion dollars. The total revenue generated from entities within the privatisation programme between 1985-December 2000, together with 1.9 billion dollars dividend income and 0.7 billion dollars other income, has amounted to 9.5 billion dollars. In the same period, total privatisation expenses were 9.2 billion dollars. The largest item in privatisation expenditures (with about 90 percent) is the financing of the companies in the privatisation portfolio in the form of capital increases and loans.

During 2000, a total of almost 2.5 billion dollars in cash worth of transactions were finalised under the projects in the portfolio of the Privatisation Administration, including the sale of 51 percent of POAŞ (petroleum products distribution company), Deniz Nakliyat AŞ, two insurance companies, twenty four participation shares, Asil Çelik (steel manufacturer), TÜSTAŞ (engineering/consulting company), several premises of seven companies and the global offering of 31.5 percent of TÜPRAŞ shares (petroleum refining company).

In the global offering of TÜPRAŞ, a total of 1.1 billion dollars worth of stock was tendered for the domestic and international investors. The distribution rate among the local and international market placement was 77 percent and 23 percent respectively. This offering with 375,000 local investors and net proceeds worth of 1.1 billion dollars was the largest government equity offering in Turkey. A total of 1.3 billion dollars in cash was accrued from the sale of POAŞ to a strategic investor. In addition, revenues from power plant privatisation were realised as 84 million dollars. During the tender held in 2000, one of the two GSM 1800 licences was sold for 2.525 billion dollars.

The Privatisation Administration's tenders have been announced and sale approval processes and contract negotiations continue for the sale of textile plants, fertiliser plants, agricultural industries, meat processing plants, pulp and paper production plants and several participation shares.

The privatisation process of PETKİM (the petrochemical company) has also started and the sale of its Yarımca Plant to TÜPRAŞ was finalised in 2001.

In 2001, privatisation continues with the remaining companies in the portfolio of the Privatisation Administration. TEKEL (tobacco and spirits company) was taken into the privatisation portfolio on 5 February 2001. According to the privatisation programme, other state owned companies, which are presently not covered by the privatisation programme will be taken into the privatisation portfolio. These contain some factories or subsidiaries of TŞFAŞ (sugar production), ÇAYKUR (tea processing) and ETİ Holding (mining company). In this respect, the TŞFAŞ has been taken in the scope of privatisation while preparatory studies regarding its privatisation are continuing. The studies regarding the public offerings of POAŞ and TÜPRAŞ are in progress, however, due to unfavourable market conditions, these offerings may not take place in 2001, but rather be realised during 2002. Block sale preparations for the majority stake of PETKİM are in progress. Once the block sale is realised, the rest of PETKİM shares will be offered to the public in the coming years. Privatisation studies of the Turkish Air Lines are intact.

In 2001, Sugar Law, Electricity Market Law, Natural Gas Law and Telecom Law, all significant for the privatisation process have been put into force. Sugar Law establishes a Sugar Board endowed with the task of regulating the sugar market and setting sugar production quotas. An Energy Market Regulatory Board has been established as the regulatory body for the electricity and natural gas sector in accordance with the relevant provisions of Electricity Market Law and Natural Gas Law.

In the medium term, privatisation in Turkey will gradually encompass the banking sector and the state will only concentrate on its regulatory role as currently observed in banking and telecom sectors.

4.2. Banking Sector Reform

4.2.1. A Brief Overview of Banking Sector Developments

In Turkey, a majority of financial flows go through the banking sector. Although there has been an increase in the size and number of non-bank financial institutions in recent years, the banking sector accounts for about 75% of the total financial sector assets. The importance of the banking sector is even greater as most of the non-bank financial institutions are subsidiaries of banks. The Turkish banking sector has gone through a major structural change as a result of the financial liberalisation programme that started in the early 1980s. The abolition of directed credit policies, liberalisation of deposit and credit interest rates and liberal exchange rate policies have accelerated the structural transformation of the Turkish banking sector.

The banking sector legislation and regulations have also been designed in line with BIS (Bank for International Settlement) principles and EU directives. In particular, the Banking Law (No. 4398) effective as of June 1999, established the Banking Regulation and Supervision Agency (BRSA) as the independent authority to regulate and supervise the banking sector. BRSA started to operate on 31 August 2000. This board has administrative and financial autonomy, and this is in line with the Fundamental Principles for the Efficient Control of Banks (BIS). Authority for issuing licenses to banks, annulling them, and approving the regulations of the banks rests with the Banking Regulatory and Supervisory Board.

Despite all these positive developments, the Turkish banking sector has moved away from traditional banking activities. The ratio of loans to deposits decreased from 84% in 1990 to 51% in 2000. The credit to GNP ratio is about 25%; the lowest among the emerging market countries. Macroeconomic instability, high public sector deficit, systemic distortions created by the state banks, and weaknesses in risk assessment and management systems have contributed to the decline in the financial intermediation function of the banking sector.

In fact, the Turkish banking sector was severely tested in the aftermath of the 1994 financial crisis and three small banks were put on liquidation process in 1994. However, the banking sector recovered rapidly from the 1994 financial crisis and posted an average annual growth rate of 18% in the post-1995 period. The East Asia and Russian crises of 1997-98 and the devastating earthquakes of 1999 had a negative impact on the Turkish economy and the banking sector.

Recently, the disinflation programme which was adopted at the beginning of 2000 had a major impact on banks' balance sheets. The pre-announced exchange rate path and the real appreciation of the Turkish lira meant lower cost of funding for foreign currency liabilities. As a result, a number of banks borrowed in short-term foreign currency terms and lent in longer term Turkish lira terms. This led to a sharp increase in maturity mismatch and foreign currency open position of the private banks.

The composition of the asset structure of the banking sector changed significantly during 2000 with an increase in the share of loans and a decline in liquid assets. Especially consumer credits four folded during 2000. The banks also increased their exposure to fixed rate treasury securities during this period. As a result of these changes, the exposure of the banking sector to liquidity, interest rate and exchange rate risks increased during 2000.

The November 2000 crisis which resulted in a significant outflow of foreign funds from Turkey and the sharp increase in treasury bill rates led to financing difficulties and erosion of the capital base of the banking sector. In particular, the financial health of the state and SDIF banks that relied heavily on overnight funding deteriorated sharply.

The rapid announcement of the additional 7.5 billion dollars under the Supplementary Reserve Facility (SRF) of the IMF in December 2000 could only calm the market for a limited period. The loss of credibility of the exchange rate regime and the abolition of the exchange rate peg in February 2001 further hit the banking sector. As a result, the banks were hit by three main shocks: (1) sharp increase in funding costs due to the increase in interest rates and maturity mismatch, (2) capital losses due to a sharp mark-to-market decline in the value of government securities holdings, and (3) capital losses due to a sharp change in foreign exchange rate and open foreign currency position. Furthermore, asset quality is expected to deteriorate as a result of the contraction in the real sector and the subsequent deterioration in the repayment capacity of borrowers.

4.2.2. Banking Sector Restructuring and Rehabilitation Programme

In response to November and February crises, the government adopted a new programme "Transition to a Strong Economy" in order to eliminate the confidence crisis and the financial instability. Structural reforms in the area of banking constitutes the most significant component of the new programme. The main goal of the Banking Sector Restructuring and Rehabilitation Programme is to eliminate the distortions in the financial sector and to adopt regulations to promote an efficient, competitive and sound banking sector. The strategy under this programme rests on four main pillars: (1) the financial and operational restructuring of state banks, (2) restructuring and resolution of SDIF banks, (3) strengthening of private banking; and, (4) strengthening of the legal and regulatory environment.

Very important steps have been taken regarding these four areas and various measures have been initiated to strengthen the system. The progress achieved and the details of the time-bound action plan are provided below.

4.2.2.1. Progress in Banking Sector Restructuring and Rehabilitation Programme

Privatisation and corporation of the State Banks

- A new and independent joint management has been appointed to state banks and these banks were recapitalised and their duty losses were eliminated.

- The license of Emlak Bank was revoked on July 6 and its banking assets and liabilities were transferred to Ziraat Bank. Ziraat Bank has been adequately capitalised to absorb the transfer of those assets.

- A monitoring system has been introduced to monitor profits/losses, liquidity and interest rate margins of the state banks.

- The independent audit of the state banks has been completed, and outside advisors have been appointed to guide the operational restructuring of state banks.

- An omnibus law to facilitate the restructuring of the state banks has been passed including the elimination of the authority of the government to impose duty losses in these banks.

Resolution of Savings Deposit Insurance Fund (SDIF) Banks

- SDIF took over 18 banks during the last five years. The restructuring and sale process of these banks have been substantially accelerated in recent months. Of these 18 banks, deposit-taking license of one bank was revoked. Five SDIF banks were merged into Sumerbank forming the first transition bank. The Second transition bank was also created through the merger of two banks into Etibank. As a result of the sale of three banks, including Sümerbank, 7 banks remained under SDIF. The sale process of the three banks out of the remaining seven is expected to be completed by the end of October 2001. All remaining banks under SDIF are expected to be sold or resolved by the end of the year.

- Significant progress has been achieved regarding the financial restructuring of the SDIF Banks. In this context; (1) the programme that aims to reduce overnight liabilities of the SDIF Banks has been carried on decisively, (2) BRSA continued to ensure that the deposit interest rates offered by the SDIF banks are in line with those of private banks, (3) the capital base of the SDIF banks was strengthened by injection of government funds, (4) the loss accumulation by the SDIF Banks is halted, and (5) the net open foreign exchange position, which was about

4-5 billion dollars until May 2001, has retreated to 600 million dollars after the second half of May.

- Important steps are also being taken regarding operational restructuring of the SDIF banks. In this framework; between the date of transfer to SDIF and July 31, 2001, the number of branches and total personnel of these banks were reduced by 34 percent and 42 percent, respectively.

- The Collection Department (COD) of the SDIF is fully operational. A large component of the non-performing loans of some intervened banks have been already transferred to the COD. The SDIF has achieved important progress in loan loss recovery and encourages debt workout schemes with former owners of SDIF banks.

Establishing a Sound Private Banking Sector

- Time bound commitment letters with plans to raise banks' capital adequacy ratios to 8 percent by end-2001 have been agreed with private banks which became capital deficient after the crises. The private banks have committed to a capital injection of 1.4 billion dollars, of which 1.1 billion dollars has already been realised as of the end of July. The Recapitalisation plans of five banks were considered either unacceptable or the banks were not able to comply with their plans. These banks were intervened on July 10, 2001.

- Measures to reduce financial intermediation costs, increase attractiveness of TL deposits, and lengthen the maturity of savings deposits were announced on July 26, 2001. Differential withholding tax rates with lower rates for longer maturity deposits were introduced. The Central Bank will start paying market interest rates on required reserves for TL deposits. Also, to encourage the holding of treasury bills by households, tax exemption on government bonds earnings has been raised from about 3,750 dollars to about 38,500 dollars.

- An omnibus law to facilitate the mergers of banks and their subsidiaries has been passed. The law provides tax incentives for corporate mergers and acquisitions. The BRSA also issued a communiqué to define the general principles and procedures regarding mergers and acquisitions of banks on June 27. In this context, the BRSA gave permission for the merger of Osmanlı and Körfez banks on July 26.

- A voluntary debt swap has been done by the Treasury on June 15. The swap was a significant success both in terms of its size and its design. As a result of the swap, TL 9,335 trillion (8 billion dollars) of local currency debt with an average maturity of 5.3 months has been converted into foreign currency and TL-denominated instruments with an average maturity of 37.2 months. This operation led to an extension of average maturity of cash debt stock from 6 months to 18 months. The swap operation also allowed the private local banks to substantially reduce their open currency position.

- The Capital Markets Board of Turkey issued the necessary regulations to establish a derivatives market under the roof of the Istanbul Stock Exchange on July 19. Having a derivatives market will provide the Turkish banking sector with a variety of tools to hedge against risks.

- Projects and plans are being formulated by the World Bank (IBRD), the Treasury, and other government entities to enhance the repayment capacity of the corporate sector. These include work on policy alternatives to deal with a potential non-performing loan build-up problem in the banking sector.

Strengthening Regulatory and Supervisory Framework

- In coordination with the financial and operational restructuring of the banking sector, legislative amendments and institutional changes are being adopted. These efforts aim to promote efficiency and competition in the banking sector, facilitate sound banking practices and thus establish confidence in the sector.

- Some of the legislative changes have been incorporated to the amendments to the Banking Law, which were enacted in June 2001. In this context;

  - The legal amendment defining “consolidated own funds” is introduced to allow consolidation of related parties lending and make the regulation fully consistent with EU standards.

  - Banks’ non-financial subsidiaries are limited to 15% of total net worth and the total sum of all such subsidiaries are limited to 60% of total net worth with a transition period until 2009.

  - Forward contracts, option contracts and other similar derivative type operations will be included under the definition of “credit” to limit the overall exposure to individual and related counter parties.

  - The corporate tax deductibility of loan loss provisions has been clarified, which would remove the uncertainties on tax relief to the banking system.

  - The collection ability and procedure of the SDIF banks is improved with the changes made in the Banks Act.

- The BRSA will introduce the following measures and take prompt actions to strengthen supervisory infrastructure:

- Communiqué on the "Accounting Practices" will be issued in January 2002. The Communiqué will aim to cover the inclusion of repo transactions on balance sheets and full adoption of international accounting standards.

- In order to prevent loan concentration, direct and connected lending will be amalgamated in the calculation of lending limit to a group.

- The establishment of Banks' Internal Control and Risk Management System, which is scheduled to take effect as from 1 January 2002, will be closely monitored.

- Banks will be obliged to take into account market risks in the calculation of capital charges on an individual basis by January 1, 2002, and on a consolidated basis by July 1, 2002.

- Banks will be encouraged to utilise independent external audit in assessing their internal control and risk management systems as well as loan and trading portfolios.

- Off-shore banks owned by Turkish entities will be supervised in cooperation with the host country supervisory agency.

- Turkish banks' foreign branches will be subject to on site supervision.

4.2.2.2. Action Plan for Banking Sector Restructuring and Rehabilitation Programme

I. Strengthening Regulatory and Supervisory Framework		
***a**-Capital Adequacy*	**Timing**	**Current Status/Remarks**
-Incorporation of the market risks on solo and consolidated basis in the calculation of capital adequacy ratio.	On Solo basis: January 2001 On Consolidated basis: July 2002	Regulation on Measurement and Assessment of Capital Adequacy of Banks was published on February 10, 2001. This regulation lays down the principles and procedures related to calculation of capital adequacy standard ratio of banks both on consolidated and unconsolidated basis with a view to ensure that they maintain an adequate amount of capital to cover losses which may result from existing and potential risks. Further works on reporting format for market risks is about to be completed and will be sent to the banks as soon as it is finalised. Also a manual for procedures to approve risk measurement models has been under study.
b- Foreign Exchange Exposure Limits		
-To set up a working group to identify and classify the use of structured finance products by banks to cover FX exposure, and to formulate remedial regulatory action to minimise risks originating from the use of such instruments.	December 2001	The committee is to be established in October 2001 and findings and needs for regulations are expected to be determined by December 2001
-To undertake on-site examinations, in coordination with foreign supervisors where necessary, to verify compliance with consolidated FX open position limits between reporting dates.	December 2001	13 branches and 1 participation in Bahrain-Manama, Luxemburg and Malta were audited on-site. Auditing of a bank's participation in Netherlands is continuing. Compliance with foreign exchange position regulations are audited during these inspections. Such inspections will continue in the future as well.

c- Loan Loss Provisioning Rules and Connected Lending Limits		
-Banks that do not comply with the new connected exposure limits and BRSA to agree on time-bound action plans.	Continuous	Agreements were completed in August, 2001 and will be monitored on a continues basis.
-To review the decree on loan loss provisioning with a view to make amendments to facilitate corporate sector restructuring		
d- Repurchase Agreements (repos)		
-To set up a committee to recommend measures to reduce the risks caused by excessive use of retail repos/short-term liabilities in the banking sector	December 2001	The Committee has been finalised its work in July 2001 and proposals were submitted to the related State Minister. In this framework withholding tax rate on repo transactions was increased.
-Inclusion of repo transactions on balance sheet	January 2002	
e – Risk Management		
-To monitor the establishment process of internal control and risk management systems of banks	January 2002	Regulation on Banks' Internal Control and Risk Management System was issued on 8 February, 2001. The regulation aims at determining the principles and procedures of the internal supervision systems and risk management system that the banks shall establish in order to monitor and control the risks that they are exposed to. Further work on additional regulation is continuing and will be finalised by the year -end.
f- Accounting and Auditing		
-Publication of The Regulation of Accounting Practices	January 2002	Related regulation will be issued in January 2002 and will be put into effect in consecutive periods.
-To complete full introduction of International Accounting Standards (IAS) for banks	June 2002	
-Revision of the licensing regime for auditors of banks and other financial institution.	June 2002	
-The revision of the establishment and operation principles for independent auditing firms		A draft revision has been prepared, an is expected to be finalised by November 2001.
-To encourage banks to give importance to internal and external supervision and ensure examinations of internal control and risk management systems and lending portfolio and market risks during independent auditing.	December 2001	
g- Financial Conglomerates		
-To create legal basis for formation of financial conglomerates and amend corporate and tax legislation to facilitate transformation of financial-industrial groups into separate financial and corporate conglomerates	December 2001-December 2002	The necessary tax adjustments were made by Law No. 4605 and 4684.
-To introduce effective consolidated regulation and supervision of financial activities of conglomerates	June 2002	
h- Supervisory Activities of BRSA		
-Close monitoring of the off-shore banks established by Turkish Banks or their dominant share holders	Continuous	Drafts Memorandum of Understanding (MoU) have been sent to Netherlands, Malta, Luxemburg, Bahrain, Albania, Romania, Switzerland, and Ireland. A MoU agreement was signed between BRSA and the Central Bank of The Turkish republic of Northern Cyprus on September 17, 2001. Auditing of offshore branches will start in October 2001.
-On-site supervision of branches in foreign countries	Continuous	13 branches and 1 participation in Bahrain-Manama, Luxemburg and Malta were audited on-site. Auditing of a bank's participation in Netherlands is under progress.
-To undertake projects and training activities in coordination with the Board for Investigation of Financial Crimes in the Ministry of Finance to struggle with money laundering and fraud.	January-December 2002	
i-Other Regulations		
-To review tax legislation with a view to eliminate any biases in favor or against certain types of financial sector activity	June-December 2002	
-To amend prudential regulations for banks and non-bank financial institutions.	June-December 2002	

-Coordinated review of the improvements required in the legal framework for bankruptcy and collateral foreclosure, and enactment of the changes required to allow accelerated/more efficient non-performing loan (NPl) resolution, and preparation of a plan to set up a moveable goods register	December 2001	
-To determine principles and procedures in storing files in the form of microfilms and/or electro-magnetic environment.	June 2002	
II. Resolution of SDIF Banks and Strengthening Private Banking Sector		
-Resolution of SDIF Banks		
Finalizing the bidding process of Etibank and İktisat Bank	October 2001	-Koç Group's bidding deadline for Etibank was extended to October 1, 2001 -Uni Credito Italiano SPA's bidding deadline for İktisat Bank was extended to October 15, 2001.
Finalizing the bidding process of Sitebank	October 2001	Nova Bank S.A.'s bidding deadline was extended to October 17, 2001.
Resolution process of Tarişbank, Bayındırbank, Kentbank and EGS Bank		Sales and other resolution process will start as soon as transfer balance sheets are prepared.
-SDIF Collection Department to adopt procedures for packaging and selling bad assets and to initiate third party sale of such packages on a pilot basis and for accelerated in house foreclosure of bad assets using new special powers granted to it in the amendment to the banking law, and to initiate such foreclosures on a pilot basis.	June-December 2002	
-To initiate binding legal time constraints for resolution of bad assets	December 2002	
To complete transfer of all problem loan files above TL 75 billion to the Collection Department of SDIF, and to reach a negotiated settlement with the loan defaulters, or to initiate legal action for all problem files, and resolution of problem loans concerning exposure below 75 billion TL	December 2001	The transfer of 2.300 files above TL 75 billion has been completed. Approximately 2.000 files below TL 75 billion have been transferred to the Collection Department of SDIF.
-Implementation of capital restoration plans by capital deficient banks	December 2001-December 2002	The observance of the performance criteria will be strictly enforced. 5 banks that were not able to commit to a credible Recapitalisation plan were taken over by SDIF. 2 investment banks have been closed for the same reasons.
-Encouraging mergers, entry of foreign banks and forming Joint Ventures with foreign banks		Legal arrangements that support bank mergers and acquisitions have already been realised. Projects on removal of bureaucratic obstacles on foreign bank entry are at the completion stage.
III. Corporation and Privatisation of State Banks		
-Privatisation of Vakıfbank		Privatisation procedures shall be resumed as soon as the market conditions allow.
-Restructuring and privatisation of Halk Bank and Ziraat Bank.	November 2003	The deadline could be extended for an additional 18 months by a decree.
-To identify all public service functions of Ziraat that should be transferred to other entities as well as the recipient entities for these functions, and to adopt a transfer plan	December 2001	

-To allocate the sufficient appropriation within the budget for subsidies through state banks	Continuous	
-Closing of inefficient branches and downsizing of personnel	Continuous	

4.3. Labour Market

Although Turkey has a relatively large labour market owing to its high population and its age structure, participation rates are low compared to the developed countries. As of 2000, the total participation rate is 49.2 percent, of which 73.1 percent are men and 25.5 percent are women. One of the main reasons for the low participation rate of women in the general labour market is the fact that their participation in the urban labour market remains rather low.

According to the data from the State Institute of Statistics (SIS), there was only a limited increase in employment between 1995 and 1999. In this period, the annual average growth rate of employment was realised as 1.8 percent, while the labour force grew by 1.5 percent on the average. In 2000, the rate of unemployment was 6.6 percent and the rate of underemployment, was 7.0 percent, indicating a 13.6 percent of idle labourforce.

In 2000, the urban unemployment rate was 8.9 percent, whereas the rural unemployment rate was 3.7 percent. Unemployment among young people still preserves its importance. More strikingly, the unemployment rate of the educated youth in urban areas is as high as 22.4 percent.

The low unemployment rate in the rural areas stems from a rather high rate of unpaid family workers and self-employed persons. As an effect of continuous migration from rural to urban areas, unpaid and unskilled family workers have little chance to participate in the labour market, which force them to work in marginal jobs or illegal employment.

Table 13 : Developments in Domestic Labour Market

(15+ Age, In Thousands)

	1995	1996	1997	1998	1999	2000 (1)	2001(2)
Civilian Labour Force	**21,907**	**22,236**	**21,899**	**22,513**	**23,187**	**22,029**	**21,853**
Civilian Employment	**20,394**	**20,894**	**20,505**	**21,084**	**21,413**	**20,164**	**20,164**
Agriculture	9,538	9,379	8,584	8,918	8,872	7,187	7,227
Industry	3,111	3,327	3,529	3,536	3,580	3,733	3,608
Services	7,745	8,188	8,392	8,630	8,962	9,658	9,331
Unemployed	**1,513**	**1,342**	**1,394**	**1,429**	**1,774**	**1,451**	**1,689**
Unemployment Rate (%)	**6.9**	**6.0**	**6.4**	**6.3**	**7.7**	**6.6**	**7.8**
Underemployment	**1,474**	**1,401**	**1,237**	**1,324**	**2,043**	**1,541**	**1,318**
Underemployment Rate (%)	**6.7**	**6.3**	**5.6**	**5.9**	**8.8**	**7.0**	**6.0**
Rate of Idle Labour Force due to Unemployment and Underemployment (%)	**13.6**	**12.3**	**12.0**	**12.2**	**16.5**	**13.6**	**13.8**

Source: SPO, SIS
(1) Provisional
(2) Provisional Results of the 1st and 2nd Quarter of Household Labour Force Statistics.

The structural change in the sectoral distribution of employment persists with declining employment in the agricultural sector. As of 2000, the shares of agricultural, industrial and services employment were 35.8 percent, 17.9 percent and 46.3 percent, respectively.

Table 14 : Developments in Urban Labour Market

(15+ Age, In Thousands)

	1995	1996	1997	1998	1999	2000	2001(1)
Civilian Labour Force	**9,942**	**10,151**	**10,496**	**10,753**	**11,405**	**12,213**	**12,221**
Civilian Employment	**8,927**	**9,216**	**9,513**	**9,691**	**10,147**	**11,128**	**10,945**
Agriculture	413	513	457	509	522	448	437
Industry	2,479	2,582	2,779	2,833	2,799	3,081	3,017
Services	6,035	6,121	6,277	6,349	6,826	7,599	7,491
Unemployed	**1,015**	**935**	**983**	**1,062**	**1,258**	**1,085**	**1,276**
Unemployment Rate (%)	**10.2**	**9.2**	**9.4**	**9.9**	**11.0**	**8.9**	**10.6**
Underemployment	**724**	**623**	**660**	**744**	**986**	**907**	**809**
Underemployment Rate (%)	**7.3**	**6.1**	**6.3**	**6.9**	**8.6**	**7.4**	**6.6**
Rate of Idle Labour Force due to Unemployment and Underemployment (%)	**17.5**	**15.3**	**15.7**	**16.8**	**19.6**	**16.3**	**17.2**

Source: SPO, SIS
(1) The average of the first and second quarters of 2001

For providing employment and encouraging investments in Priority Regions, incentives have been introduced for enterprises employing at least 10 persons. These incentives include tax exemptions, state payments of employer's shares of insurance premiums, deferral of income taxes and stamp duties of employees and free allocation of Treasury-owned lands to investors.

As for the public employment services, there have been some developments in recent years. A professional counselling system is being set up within the Turkish Employment Office for providing better services to unemployed persons and job seekers. Under IBRD-financed Employment and Training Project, employment-guaranteed independent courses were organised and 84.242 people attended these courses since 1993.

The activities to improve occupational standards, which have an important function in providing the labour force with skills, have reached an advanced stage. So far, the standards of 250 occupations have been determined under the Employment and Training Project. Efforts are continuing for the creation of a test-bank for occupations whose standards are determined. This test-bank will serve as a basis for examinations and certifications.

Regarding employment and labour market policies, the main objective is to implement active policies. Within this context, the implementation of the Active Employment Programmes have been further carried on, with the aim of increasing efficiency in employment services, enabling functioning of private employment agencies, raising the quality of the unemployed and unskilled workers so as to encourage them to work in a productive manner, establishing a testing and certification system on professional standards, setting up a vocational guiding system, and increasing efficiency in the formation of labour market decisions.

Within the framework of the Employment and Training Project, the officers of the Turkish Employment Office have been given in-service training. Studies on establishing a vocational guiding system, updating the Turkish glossary on occupations, and developing an information system have been carried on within the project.

For the near future, the 8th Five Year Development Plan envisages the following labour market policies for the problem of unemployment;

- decreasing unemployment by increasing productive investments and achieving sustainable economic growth,

- changing the sectoral composition of employment in favour of non-agricultural labour, increasing the average skills of the labour force in compliance with the needs of the economy and the information society,

- utilising the employment creating potential of the SMEs. For that reason, supports granted to SMEs and individual undertakings shall be extended by contributions in the fields of education, projects, funding, organisation, marketing and technology,

- taking measures reducing the unemployment rate of the youth, women and disabled persons. Implementing active and passive employment policies, which prevent redundancy of unqualified people working at a low wage level,

- establishing an Occupational Standardisation, Examination and Certification System to enhance the efficiency of the labour market,

- developing income generating projects for unpaid family workers in the agricultural sector, housewives and the unemployed urban youth,

- supporting the expansion of employment by incorporating new and other non-standard working styles into the legal arrangements,

- enhancing the development potential of employment by upgrading the labour force quality in harmonisation with the EU and in line with the technological developments,

As economies and societies become much more dependent on information, the main objective should be to equip manpower with the necessary information and skills required by the information society, as well as the international community and the EU. For this purpose, it is very important to develop skills in technological literacy, particularly of computer technology.

According to current trends, it is expected that the demand for public services will change as a result of the aging population. It is also expected that the demand for educational and health services at all levels rises. Hence, it is expected that the rates of dependency will decrease. In addition, it is estimated that there is greater pressure on social insurance systems as a result of higher average life expectancy leading to a growing elderly population.

4.3.1. Social Security Reform

The social security reform programme has two phases. The first phase aims to take the most immediate measures (redesigning of public pay-as-you-go scheme's parameters such as increase in the minimum retirement age, minimum contribution period, and contribution base, indexation of pensions to CPI, extension of the reference period to life time earnings, reduction in replacement rates etc.) and to introduce an unemployment insurance system. A new law (Law on Unemployment Insurance) covering these measures was adopted on 25 August 1999.

The second phase aims to increase the coverage and compliance rates, transparency, and efficiency of the social insurance system, minimise the contribution arrears, operate the pension and health insurance accounts, provide protection for vulnerable groups through a sound and fair social assistance scheme, and introduce an individual retirement scheme.

The first part of this stage was the restructuring of the pension administration, meaning the Ministry of Labour and Social Security and three pension funds. The proposed system was designed to allow better alignment of the administrations of the Social Insurance Institution and Bağ-Kur, to strengthen the capacity of Ministry of Labour and Social Security's for better monitoring the functioning of Social Insurance Institution and Bağ-Kur. The legislative arrangements envisaged to realise these objectives were put into force in October 2000 through two Decrees in Law.

The regulatory and supervisory framework of the individual retirement scheme and the corresponding tax arrangements were put into force in October 2001.

The third part of the second stage, which foresees some additional changes in the legislation for the Social Insurance Institution and Bağ-Kur aims to increase their compliance and coverage rates. Since the Decrees were annulled by the Decision of the Constitutional Court, these provisions have been included in the draft laws, which are expected to be put into force by the end of 2001.

The restructuring of the social assistance system is the fourth part of the second stage reforms. The main objective of this part is to integrate all social assistance programmes under a single agency, introduce means test and income-test mechanisms, and establish a national database for this purposes. This part is still under preparation.

4.4. Administrative Reform

Major pillars of the economic programme are to make the fiscal adjustments sustainable, strengthen public finances and reduce waste in public expenditure.

Fiscal management and transparency were defined as keys of the stabilisation programme. To this end, important changes are required to strengthen the budget preparation, execution, and control; enhance transparency and accountability of fiscal operations; and improve the tax system and its administration.

The government programmed to end all budgetary funds gradually in 2000 and 2001. Further progress in this area was targeted in achieving by introducing in 2001 accounting and reporting on a commitment basis for the consolidated central budget and implementing an integrated financial information system based on a treasury single account and a general ledger.

To enhance transparency and accountability in budgetary operations, government intended to achieve following policies: indicating the cost of credit subsidies of state banks in the 2000 budget; taking stock of existing contingent liabilities, most notably government guarantees by making this information publicly available; eliminating some extra budgetary funds (EBFs).

Considerable progress was achieved in structural reforms in the first part of 2000. However, reform process slowed down in the second part of the year in closing the remaining budgetary funds scheduled for 2000, setting up treasury single account and a general ledger with accounting and reporting on a commitment basis for the consolidated central budget, and reporting all contingent liabilities except government guarantees. On the other hand, all of the funds that are planned to be closed were abolished in 2001.

After two crises, structural reforms and part of the economic programme were also revised in terms of new macroeconomic and fiscal framework. Besides the banking sector reform, the Government has devised detailed and developed structural reform policies in the public expenditures and fiscal transparency.

To accelerate policy formulation and budget decision process in terms of budget preparation, implementation, internal control and public procurement structure, the Government has already made progress by scheduling following steps in the revised programme;

- a draft law has been submitted to the Parliament on public finance and debt management that defines clear borrowing rules and limits for the public sector, and incorporates into the budget on-lending and debt guarantee operations of the Treasury.

- a public procurement law in line with UN rules (UNCITRAL) will be submitted to the Parliament by October 15, 2001. This is an important issue in the government agenda to increase the efficiency of public procurement system aiming at functionally working procedure and also harmonising with the EU legislation.

- all budgetary funds (with the exception of DFIF) were eliminated in the 2001 budget. The number of EBFs was limited to five (the Social Aid and Solidarity Fund, the Defence Fund, the Promotion and Publicity Fund, the Savings Deposit Insurance Fund, and the Privatization Fund). No new budgetary funds or EBFs will be created.

- a lending minus repayments item following the IMF's Government Finance Statistics have been reported monthly since May thus expanding the coverage of the budget balance to include net treasury payments of guaranteed debt. This item will be included in the 2002 budget.

- the draft budget submitted to the Parliament for 2002 will be accompanied by the accounts and financial outlook for: (i) all EBFs and social security institutions (including a report on social security contribution arrears); (ii) revolving funds; (iii) contingent liabilities of the

Treasury; (iv) all SEEs, including state-owned banks; and (v) local authorities. Moreover, as of 2003, the budget will include the implications for projected medium-term current spending of public investment programmes.

- a new budget classification in line with international standards was completed by the end of June 2001. In 2002 budget, this new budget classification will be implemented on a pilot basis in six agencies.

- the Government have formed a steering committee consisting of representatives of the Treasury, the Prime Minister's Inspection Board, the Ministry of Finance, the Ministry of Justice, and the Ministry of Interior. This committee, in collaboration with the World Bank, has held a conference about combating corruption and improving governance, and will design an action plan in relation to the necessary adjustments in order to improve good governance and eliminate corruption until the end of 2001.
- after completing and publishing Public Expenditure and Institutional Review (PEIR) Report as a joint effort that could form a basis for a Programatic Financial and Public Sector Adjustment Loan (PFPSAL) from the World Bank, the government initiated public and financial sector reform programmes. This report requested by the Government is a part of requirement of Economic Reform Loan.

4.5. Agriculture

In line with the 8th Five Year Development Plan, the fundamentals of the agricultural policies is being determined within the framework of commitments, envisaged in the Agricultural Agreement of the World Trade Organisation and developments in international trade and in the Common Agricultural Policy of the EU, on the path to the membership.

However, An Agricultural Reform Program has been drawn up and put into practice in line with the Economic Reform Program which has been brought into force to overcome the economic difficulties, that the country is facing. When the economic stability is achieved, the agricultural programs, necessary for the adaptation of the Turkish agriculture to the Common Argicultural Policy of the EU, will be set up and implemented.

The current Agriculture Reform Programme encompasses three main initiatives. The first one is to phase out existing support policies and replace them with a direct income support system for the poorer farmers. Secondly, the system of price and credit subsidies will be rationalised and phased out gradually. Most of the State Enterprises and facilities of the Agricultural Sales Cooperatives and Unions (ASCUs) operating in the marketing and processing of agricultural products will be privatised.

Significant steps have been taken in the agricultural sector reform in 2000 and 2001, and further progress is envisaged for 2002. In this context:

The Board for Restructuring and Support in Agriculture has been established in order to coordinate the studies carried out by the public institutions. There is a need for the Board to function more actively to ensure a much more effective coordination between these institutions during the adoption and implementation of the Community acquis.

The Turkish Government submitted a letter of intent to IMF on December 9, 1999 within the framework of the Stand-by Arrangements supporting its disinflation programme for a three-year period, from 2000 to 2002. Submitted as a continuation, the additional letters of intent dated 18 December 2000 and 3 May 2001 comprise a section for agricultural policies under the structural reform chapter. The Turkish Government aims at:

- phasing out indirect support policies by end-2002 and replacing them with Direct Income Support (DIS),
- phasing out input subsidies,
- privatising some of the SEEs in the agri-food sector,
- reducing sugar beet quotas from 12½ to 11½ million tons, and increase the support price of sugar beet by no more than targeted inflation,
- limiting the volume of support purchases of cereals and offload additional grain stocks,
- keeping support price increases in 2001 not exceeding the targeted inflation rates in parallel to the introduction of direct income support to farmers (the margin for the support price for wheat over world prices will be further reduced to at most 20 percent by June 2001 subject to the provision that the increase will not exceed targeted inflation; the tariff on grain imports will be lowered to at most 45 percent).

As the purchasing price of sugar beet has been high in real terms, sugar stocks have reached very high amounts. Since 1998, these high stocks have led to the implementation of quotas in sugar beet production. In April 2001, a new sugar law has been put into force with a scope of privatization in the sugar industry. The Tobacco Law - which liberalizes the tobacco sector, phases out the support purchases of tobacco, and allows for the sale of TEKEL assets - is expected to be approved by the Parliament. Following the approval of this law, the privatisation of TEKEL and TSFAŞ, which is expected to be completed by end-2002, will be coordinated with other components of the agriculture reform programme that will be supported by a loan from the World Bank.

The strategy for implementing the direct income support programme over the 2000-2005 period has been adopted and announced. In line with this strategy, a pilot project for direct income payments in four selected regions (Ankara, Antalya, Adıyaman, Trabzon) has been launched by the Ministry of Agriculture and Rural Affairs (MARA). The results of the project and the final report were issued at the end of 2000. Based on the results of pilot project, the scope of the programme was extended nation wide in 2001 and its rollout will be completed in 2002.

The decree for the implementation of the DIS was enacted in December 2000 (decree number 2172 dated 12.12.2000) and the official commiuniqué for the implementation of the DIS programme was published in the Official Gazette on June 21, 2001. Farmer’s registration and land registration system on a nation-wide scale will begin in 2001 with the target of registering and making payments to farmers by the end of this year.

As regards the official commiuniqué, the related payments shall be made nation-wide to the farmers who are dealing with agricultural production and are registered, taking into consideration the size of the farm area cultivated by the farmer. For each registered farmer who deals with agricultural production and whose cultivated farm area is annually 20 hectare at maximum, 100 million Turkish Liras shall be paid per hectare. For farms covering less than 0.5 hectare land, the payments shall be equal to the amount paid for the farms covering 0.5 hectare land.

A Farmer Transition Programme will be implemented for hazelnut and tobacco sector, as there has been a large expansion of cropping area in these crops because of high support prices with significant amounts of surplus production.

A set of policy changes that introduce a link between support prices and relevant world market prices were initiated in Agricultural support prices. A programme phasing out the government subsidies for support prices by 2002 was also announced. In this regard, support prices for wheat in 2000 and 2001 was linked to an appropriate world reference and set at a level which reduced the premium over the world price to approximately 35 percent in 2000 and 5 percent in 2001. Support prices for tobacco and sugar beet was also determined in line with the inflation target. Purchase prices determined by the ASCUs followed the same line, with a policy of purchasing crops not more than they can sell.

In May 2001, average interest rate of agricultural loans provided by the Agricultural Bank of the Republic of Turkey was around 118 percent for small and medium size farms as well as contracting farms.

The fertiliser subsidy, which is among the input subsidies, has been held constant in nominal terms since 1997. It remained constant in nominal terms in 2001 and will be eliminated in 2002.

The legislation that gives complete autonomy to the ASCUs was approved by the Parliament in June 2000. Starting in 2001, the ASCUs will no longer be eligible to receive annual allocations or other subsidies from the fiscal budget. ASCUs will be restructured to function as effective cooperatives owned and operated by and for the members; ASCUs that are not operating effectively will be closed down or liquidated by end-2005. The law eliminates all preferences and government's role in the operation of ASCUs, and establishes a framework for carrying out their restructuring into private cooperatives. The restructuring of ASCUs will be carried out in the following four year period, by decreasing the number of workers and excessive wage costs, and focusing on their core businesses. A "Restructuring Board" was established to provide various types of assistance to the ASCUs and their partner ASCUs, for a period of 4 years.

With regard to the restructuring and privatisation of state assets in the agricultural sector a hard budget constraint was imposed on agricultural SEEs, including specific enterprise-by-enterprise limits on Treasury loan guarantees, equity injections and budgetary transfers.

TZDK, the state input supplier, was transferred to the Privatisation Administration and is soon expected to be liquidated. TSFAŞ will be fully transferred to the Privatisation Administration's portfolio as of the beginning of 2002. Privatisation Administration is currently working together with TSFAŞ for the possible methods of privatisation. TEKEL had already transferred to the Privatisation Administration's portfolio and the new Tobacco Law facilitating the privatisation process of TEKEL's assets will be enacted by the end of this year. Privatisation process of ÇAYKUR will be seriously considered in 2002.

The 8th Five Year Development Plan (2001-2005) also addresses several policies regarding the agricultural sector. The most important policies and policy tools are as follows:

- Establishing of non-governmental, non-profit producers' organisations and supporting the existent ones (e.g. Coops and Union of Turkish Chambers of Agriculture),
- A law on crop insurance system,
- Rural Development Projects based on a participatory approach with farmers,
- Establishing and developing registry systems such as, Geographic Information System (GIS) and Farm Accountancy Data Network (FADN).

In addition to the aforementioned policies, the main issues covered in Turkish National Programme for the Adoption of the Acquis and the developments on these issues are as follows:

Veterinary and Plant Protection

Two important issues covered in the Accession Partnership are veterinary and phytosanitary measures.

Within this context, the necessary works have been initiated in order to align Turkish legislation with EU veterinary and animal health legislation and to transfer the implementation of Turkish legislation from the central to regional administrations effectively. In the field of animal health, the

Community Acquis related to veterinary procedures and the EU procedures to the combat contagious animal diseases need to be adopted as soon as possible, with the objective of eliminating such diseases. Furthermore, it is necessary to establish Quarantine Laboratories in conformity with Community standards at border inspection posts, in order to ensure efficient inspection during the customs clearance of livestock and animal products. For exports of livestock and animal products, new International Veterinary Health Certificates are being prepared in accordance with EU norms.

Harmonisation has not yet been achieved in the creation of a supplementary protection certificate for plant protection products. Priority will be given to alternative combat methods, particularly to the Integrated Pest Management (IPM) methods and biological control methods. In this framework, the following factors shall be taken into consideration in agricultural combat; international commitments of Turkey, contemporary understanding of plant protection, food safety, ecological balance, and an environmental dimension. With the aim of providing protection to product species, the Ministry of Agriculture and Rural Affairs has prepared a “Draft Law on the Protection of Breeders Rights Concerning New Plant Varieties”.

Animal Identification System

Establishment of an Animal Identification System plays an important role in terms of taking contagious animal diseases under control. Upon the establishing this, it will be possible to ensure safe animal movements and trade. In the absence of a properly functioning Animal Identification and Registry System it is not possible to include farmers who are producing dairy and meat products in the Direct Income Support System for Farmers, within the framework of the Common Agricultural Policy. To this end, the Animal Identification System must be extended nation-wide and the required administrative structure for this matter must be developed. According to the National Programme, the development of the Animal Identification System is to be initiated in the short term and completed in the medium term.

Plant Passport System

EU Member states uses Plant Health Certificate System instead of Plant Passport System, which is based on the principle of control at the production site. Plant Health Certificates are used in trade with third countries according to the EU rules. However, a Plant Passport System does not exist in Turkey. Currently, there is not any implementation regarding the registration of producers (with the exception of producers of seeds and vegetative propagation materials), which is a prerequisite for the implementation of Plant Passports. This issue is set forth as short-term priority. A draft law has been prepared and submitted to the Parliament on the establishment of non-governmental, non-profit Producers’ Organisations and supporting the others (e.g. Coops and Union of Turkish Chamber of Agriculture).

Rural Development

Establishing a rural development policy taking into account the conditions of Turkey and functioning in parallel with the rural development policies of the EU, is a priority requirement.

A rural development concept should be considered within the context of the related EU policies. Rural areas in Turkey should be treated as viable entities, incorporating social, economic, cultural and natural resources, rather than to be considered simply as agricultural areas with an agricultural population. The required studies have already been initiated and, expected to be completed in the short term.

Monitoring of the Market

Studies on establishing and developing registry systems such as Geographic Information System (GIS), Farm Accountancy Data Network (FADN) and IACS system with a view to monitor the market effectively are underway.

Fisheries

With a view to developing the sector, the items listed below are being financed from the general budget:
- Construction of fishing boat inlets (currently 147, out of 248 coast structures are fishing boat inlets),
- Research activities carried out in the sea and inland waters,
- Protection and control services for fishery products,

In addition to these items, Fishing activities are supported by loans granted by Agricultural Bank of the Republic of Turkey that can be grouped in three categories: fishing loans, agricultural loans and industrial loans. These loans also cover investment (fishing vessel, immovable properties), operation (fingerling, feed, rent, staffing etc.) and marketing expenses.

Currently, 7 unions of fisheries cooperatives and more than 404 cooperatives function as producer organisations. However, there exists no organisation in the form of central unions or producer unions.

Although the licensing of new fishing vessels has been restricted since 1997 in order to keep the expansion of fishing fleets under control, the deadline for registration is extended to December 31, 2001. There is a registry system, which keeps a record for fishing vessels bigger than 12 meters. At the same time, aquaculture production has been steadily increasing.

In the short term, the administrative structure monitoring the structural development of the fisheries market through inspection and control measures is expected be established, and fishing fleet records is expected to be improved. In the medium term, preparations for the implementation of the Common Fisheries Policy will be completed, and efforts on the improvement of quality standards and safety of fishery products will continue.

Single Market

Foodstuff

There is a need for restructuring and reinforcement of the administration of foodstuffs control in order to keep up with the recent technology, guide the industry, protect the consumer, facilitate national and international trade, and implement legislation nation-wide effectively.

The “Project for Improvement of Food Inspection Services” included in the Annual Investment Programme has been revised according to the EU principles. The grant to be received from the MEDA resources will help to finance the purchase of laboratory equipment, personnel training and acceleration of the harmonisation process. Furthermore, the amount of investment should be determined for the establishment of the infrastructure for the adoption of Food Safety policies developed within the EU.

The legal basis for legislative arrangements has already been established. Based on the studies of the Ministries, the arrangements “on product basis” are proposed to be adopted in the short term, while more technical issues such as foodstuff analysis methods and determination of purity tolerances of food additives are planned to be harmonised in the medium term.

Alcoholic Beverages

Turkish Parliament introduced a Law aiming to remove the TEKEL monopoly on the distribution and import of alcoholic beverages amending Law No. 4250 on the Monopoly on Spirits and Spirit Drinks on 11 January 2001. The harmonisation processes on this issue are expected to be completed in 2001.

Fertilizers

Turkish legislation on fertilizers need to be harmonised with that of the EU Directives.

4.6. Additional Reform Areas

4.6.1. Energy

The energy demand in Turkey has been increasing rapidly in recent years. In order to meet the demand in an economic and secure way, liberalisation and the establishment of a regulated market with clear rules are needed. This will facilitate Turkey to keep pace with the world and especially the EU energy markets.

To address the necessity above, an Electricity Market Law was enacted on 20 February 2001. This Law introduces a restructuring for the electricity sector and enables the free market rules to apply in that market.

According to this Law major issues introduced into the electricity market are as follows: shifting of decision-making from public bodies to the market forces; increasing the degree of competition in electricity generation and distribution, definition of eligible consumers; market operation (legal framework, the financial environment and market conditions); transparency of the rules and pricing of access to the transmission grid; transparent and non-discriminatory criteria for the construction of new generating capacity and the role of the regulatory authority.

The purpose of this Law is to establish an electricity market which is financially strong, stable and transparent. Currently, the electricity market is subject to civil law provisions and aimed to operate in a competitive environment. The Law provides an independent Supervisory and Regulatory Board in to the market to ensure supplying cheap and high quality electricity to consumers in an adequate, continuous, and environmental friendly manner.

As a first step towards the new market model, TEAŞ was separated into three distinct companies, in generation, transmission, and electricity trading areas.

In the natural gas sector a Natural Gas Market Law was enacted in May 2001. This Law aims at establishing an independent regulation, de-monopolising the natural gas sector in line with the EU standards, and privatising state-owned natural gas distribution companies.

4.6.2. Telecommunication

Since 1980s there have been significant developments in the Turkish telecommunications sector with regard to physical infrastructure and supply of services. The telephone mainlines increased to 20.8 millions in 2000. The telephone density increased from 3.5 percent in 1983 to 28 percent by the end of 2000. Although the infrastructure has grown considerably with significant investment, the efficiency and investment per capita remained insufficient. Hence, to keep up pace with the dynamics of the sector, there have been some efforts for the privatisation of incumbent operator and liberalisation of the market in late 1990s. However, except for the issuance of two GSM 900 mobile licences in 1998 and DCS 1800 mobile licences in 2000, not much progress has been achieved up until date.

The Law No. 4502, amending the Telecommunications Act, enacted in January 2000, has been a milestone with regard to regulation and liberalisation of the telecommunication sector. The regulatory framework outlined by the Law is in compliance with the EU and World Trade Organisation (WTO) regulatory legislation.

The most significant novelties that are brought by the Law No. 4502 are the separation of the operation, policy determination and regulatory functions.

A new independent regulatory body called "Telecommunications Authority" was established to regulate the telecommunications sector. The Telecommunications Authority has began to perform its duties in August 2000. The Authority issued a tariff regulation on 28 August, 2001, which will be applicable to the regulated activities of the incumbent operator or to any operator that may have significant market power. The Authority has also renewed the concession agreements with the mobile operators.

The Government's role in the sector has been redefined by the Law. Prior to this Law, the Ministry of Transportation was the policy maker on behalf of the Government, as well as the regulatory body for the sector. Enactment of the Law No. 4502 has changed the sectoral dynamics such that, policy making and regulation tasks are now separated from each other. The Ministry of Transportation is currently only responsible for setting the general guidelines and the overall sector policy, while the Telecommunications Authority undertakes regulatory functions.

According to the Law No. 4502, all telecommunications services ought to be carried under a mission contract, a concession agreement, a telecommunications license or a general authorisation to be obtained from the Ministry of Transportation. Under the terms and conditions set out in such agreements, private operators are free to provide all kinds of telecommunication services. This Law, also envisages full liberalisation in value added services and prescribes clear guidelines for the licensing, pricing and interconnection regimes.

Law No. 4502 enables Türk Telekom to be converted into a joint stock company subject to the Commercial Code and foresees to terminate Türk Telekom's monopoly power after December 31, 2003. The Law allows private provisions for all value-added and wireless services. Türk Telekom's mobile phone services have also been placed into separate subsidiaries in accordance with the EU arrangements.

In addition to above mentioned legal studies, the privatisation of the incumbent operator Türk Telekom has been tendered twice in the course of 2000. The first tender for a 20 percent block sale of Türk Telekom was issued in June 13, 2000. It was stipulated by the tender specifications that, the shares would be sold to a strategic core investor consortium, which will include at least one international basic telecom operator. This basic telecom operator(s) had to represent the majority within the investor consortia. As the underlying reason of this block sale was the need for the expertise and know-how of a global telecommunications operator during Türk Telekom's commercialisation process, appropriate management rights was planned to be given to the buyer within the scope of the block sale.

A number of domestic investors have shown interest, however the tender could not be finalised. A second tender under modified terms was commenced on December 14, 2000. In the second tender, 33.5 percent share sale was offered with remarkable management rights attached. Various Turkish conglomerates have bought tender specifications, but due to the lack of interest from the international side, this tender was also cancelled.

Especially conjunctural (PSTN loosing ground vs mobile communications, funding problems encountered by international telecommunications operators) and the structural factors (inadequacy of shares proposed, problem of full management control) have complicated the above mentioned block sale tender process. The need to improve the terms of Türk Telekom privatisation, the quest for a more transparent Telecommunications regime also led to a modification in the legal framework. In this respect, Law No. 4673, which amended certain articles regarding Türk Telekom's privatisation procedures and the licensing regime was adopted on 23 May 2001. Major novelties introduced by this Law include:

- issuing a golden share with a view to protection of national interests and for reasons of national security,
- authorising the sale of 100 percent of Türk Telekom’s shares except for the golden share,
- limiting foreign ownership of Türk Telekom shares up to 45 percent,
- changing the composition of Türk Telekom Tender Committee,
- authorising the independent Telecommunications Authority for the award of all concessions, authorisation agreements, and licences,
- removing Türk Telekom's current exclusive rights over telecommunications infrastructure and fixed voice telephony, even prior to the liberalisation deadline of 31 December 2003, if state ownership falls below 50 percent.

Law No. 4673 envisages that 5 percent of Türk Telekom shares are reserved to be sold to the employees of Türk Telekom, Postal Administration and retail domestic investors through a domestic public offering. The sale strategy for the rest of the shares is to be determined by the Council of Ministers.

Türk Telekom has invited the tenders at international level to procure consultancy services and to develop an incorporation plan so as to streamline operations of the company in line with the privatisation efforts. The privatisation strategy reflecting new market conditions are to be declared until the end of 2001.