REPUBLIC OF TURKEY

PRE-ACCESSION ECONOMIC PROGRAMME 2006

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BOXES

ABBREVIATIONS

ADSL	Asymmetric Digital Subscribers Line
APL	Applicable Program Loan
ARIP	Agricultural Reform Implementation Project
BAĞ-KUR	Social Security Organization of the Self-Employed
BO	Build-Operate
BOT	Build-Operate-Transfer
BOTAŞ	Petroleum Pipeline Corporation
BRSA	Banking Regulation and Supervision Agency
CBRT	Central Bank of the Republic of Turkey
CHSC-H	CPI Having Specified Coverage with H Code
CMB	Capital Market Board
CPI	Consumer Price Index
DIS	Direct Income Support
EIA	Environmental Impact Assessment
EIEI/UETM	Electrical Power Resources Survey and Development Administration-National Energy Savings Center
EMRA	Energy Market Regulatory Authority
ESA 95	European System of Accounts 1995
EU	European Union
EU-15	The EU Member Countries Before Enlargement on May 1, 2004.
EU-25	The EU Member Countries After Enlargement on May 1, 2004.
EUR	Euro
EUROSTAT	European Union Statistics Office
FX	Foreign Exchange
GDBI	Government Domestic Borrowing Instrument
GDP	Gross Domestic Product
GFSM	Government Finance Statistics Manual
GMPCS	Global Mobile Personal Communications by Satellite
GNP	Gross National Product
GSM	Global System for Mobile Communications
IACS	Integrated Administration and Control System
IDABC	Interoperable Delivery of pan-European Services to Public Administrations, Businesses and Citizens
ILO	International Labour Organization
IMF	International Monetary Fund
IPA	Instrument for Pre-Accession
IPARD	IPA Rural Development Funds
ISCED	International Standard Classification of Education
ISE	İstanbul Stock Exchange
İŞKUR	Turkish Employment Agency
JPY	Japanese Yen
KOSGEB	Small and Medium Industry Development Organization

KPS	Identification Data Sharing System
LPG	Liquefied Petroleum Gas
M&A	Mergers and Acquisitions
MEDA	Euro-Mediterranean Partnership
MERNİS	Central Demographic Administration System
MLSS	Ministry of Labour and Social Security
NAIRU	Non Accelerating Inflation Rate of Unemployment
NFRS	Supporting Farmer Registration System
NUTS	Nomenclature of Territorial Units for Statistics
OECD	Organization for Economic Co-operation and Development
PA	Privatisation Administration
PEP	Pre-Accession Economic Programme
PETKİM	Petrochemical Corporation
PHARE	Poland and Hungary: Action for the Restructuring of the Economy
PPI	Producer Price Index
PSSP	Privatisation Social Support Project
R&D	Research and Development
RUSF	Resource Utilization Support Fund
SAC	Special Ad-hoc Committees
SCT	Special Consumption Tax
SDIF	Savings Deposit Insurance Fund
SEEs	State Economic Enterprises
SHGM	General Directorate of Civil Aviation
SMEs	Small and Medium Sized Enterprises
SPO	State Planning Organization
SSI	Social Security Institutions
SSK	Social Insurance Institution
TCDD	Turkish State Railways
TEDAŞ	Turkish Electricity Distribution Company
TEKEL	General Directorate of Tobacco, Tobacco Products, Salt and Alcohol Enterprises
TFP	Total Factor Productivity
TGNA	Turkish Grand National Assembly
TINA	Transport Infrastructure Needs Analysis
TOR	Transfer of Operation Rights
TR31	İzmir Province
TR52	Karaman and Konya Provinces
TR62	Adana and Mersin Provinces
TR72	Kayseri, Sivas and Yozgat Provinces
TR82	Çankırı, Kastamonu and Sinop Provinces
TR83	Amasya, Çorum, Samsun and Tokat Provinces
TR90	Artvin, Giresun, Gümüşhane, Ordu, Rize and Trabzon Provinces
TRA1	Bayburt, Erzincan and Erzurum Provinces
TRA2	Ağrı, Ardahan, Iğdır and Kars Provinces

TRB1	Bingöl, Elazığ, Malatya and Tunceli Provinces
TUBITAK	the Scientific and Technological Research Council of Turkey
TURKAK	Turkish Accreditation Agency
TURKSTAT	Turkish Statistical Institute
TÜPRAŞ	Turkish Petroleum Refineries Corporation
UCTE	Union for the Coordination of Transmission of Electricity
USD	US Dollar
VAT	Value Added Tax
VEDOP	Tax Office Full Automation Project
YOİKK	Coordination Council for the Improvement for the Investment Environment
YTL	New Turkish Lira

INTRODUCTION

In the framework of Pre-Accession Fiscal Surveillance Procedure, Turkey that acquired candidate statute after the Helsinki summit in December 1999 has prepared Pre-Accession Economic Programme (PEP) in line with the European Union (EU) procedures and has submitted it to the European Commission since 2001. The sixth PEP prepared in 2006 for 2007-2009 period set forth economic policies and the works related with structural reforms necessary for the completion of candidacy period successfully.[1]

By the official commencement of the negotiations with the EU on 3 October 2005, Turkey entered into an important phase in the membership process. In this context, screening procedure in 35 chapters were started towards ensuring the harmonization of Turkey's legislations with the Community acquis, and the explanatory and detailed meetings were concluded as of the end of October 2006.

In EU membership process, it is crucial to ensure economic and social transformation in Turkey. This situation is taken into account in the Ninth Development Plan that coincides with the period of EU financial programming. As a matter of fact, Ninth Development Plan that covers 2007-2013 period has been prepared with the vision of *Turkey, growing with stability, sharing her income more equitably, having competitiveness at the global scale, being in the process of transforming into the information society and having completed her coherence process for EU membership*. This Plan that undertakes, the fundamental problematic fields of Turkey in five development axes, provides a strategic framework for the main economic policies and structural reforms emphasized in 2006 PEP.

In line with the priorities of the Plan, the main priority of Turkey's macroeconomic policies to be implemented during the 2006 PEP period is to ensure the sustainability of growth, and thus the continuation of per capita income convergence with the EU average. In this context, ensuring price stability, decreasing the ratios of public deficit and public debt stock to Gross Domestic Product (GDP) and hence fulfilling the Maastricht criteria in this respect and the continuation of structural reforms are among the fundamental goals of the policies to be implemented. In the period of 2006 PEP, the economic policies to be implemented have been designed in a way to contribute to the process of convergence to the Maastricht criteria, where remarkable progress has been achieved especially in the recent years.

Economic policies have been undertaken with a holistic approach to ensure macroeconomic stability. In this context, the main objective of fiscal, monetary and incomes policies is to pursue sustainable growth environment through achieving price stability. In 2006 PEP period, the main goals of fiscal policy are permanently decreasing the public deficits and the ratio of the public debt stock to national income and continuing the improvement in the budget structure. By introducing explicit inflation targeting regime in 2006, the framework of monetary policy has been constituted with a medium-term perspective towards the primary goal of price stability. Single digit

[1] The PEP 2006 has been prepared under the coordination of Undersecretariat of State Planning Organization (SPO) with the contributions of Ministry of Finance, Ministry of National Education, Ministry of Health, Ministry of Transportation, Ministry of Agriculture and Rural Affairs, Ministry of Labour and Social Security (MLSS), Ministry of Industry and Trade, Ministry of Energy and Natural Resources, Undersecretariat of Treasury, Undersecretariat of Foreign Trade, Central Bank of Republic of Turkey, Turkish Statistical Institute (TURKSTAT), Capital Markets Board of Turkey, Turkish Competition Authority, Banking Regulation and Supervision Agency, Saving Deposit Insurance Fund, Telecommunications Authority, Energy Market Regulatory Authority and Council of Higher Education.

medium-term inflation targets confirm the decisiveness for ensuring price stability, and thus fulfilling the related Maastricht criterion. Incomes policy will be determined considering the inflation targets in the short-term and price stability, productivity and profitability in the medium-term.

During the 2006 PEP period, great importance is attached to structural reforms in terms of making economic and social transformations possible. In this context; strengthening the market mechanism, increasing the role of the private sector in the economy through decreasing the share of the state, developing the intermediary capacity of the financial sector in a way to meet the funding needs of the real sector and improving the qualifications of the labour force as required by the contemporary world, are the main goals of structural reforms. In addition, it is foreseen to continue the administrative reforms in order to increase efficiency in the public services, and to pursue reform efforts in agricultural sector in order to increase productivity and competitiveness and ensure efficient utilization of resources.

The Pre-Accession Economic Programme for 2006 comprises of four chapters. In the first chapter, recent economic developments in the Turkish economy are summarized. In the second chapter, the macroeconomic targets for the period of 2006-2009 are stated and the economic policies to be implemented in order to attain these targets are presented. In the third chapter, fiscal policies as well as the projections and various risk analyses for the budget and debt management covering the PEP period are presented. In the fourth chapter, developments related to the structural reforms implemented in various fields as well as reform calendar and predicted costs are given for the PEP period.

1. RECENT ECONOMIC DEVELOPMENTS

1.1. Growth and Employment

The GDP growth was realised as 7.4 per cent in 2005 and continued its performance of the recent years. With regard to the sectors, while the value-added of the agricultural sector increased by 5.6 per cent in 2005, the increase in the value-added of industry and services sectors were 6.5 per cent and 8.2 per cent, respectively. Thanks to the stability environment that was achieved, a 21.5 per cent increase was recorded in the value-added of the construction sector with the decline in interest rates and the expansion of the real credit volume.

The total final domestic demand increased by 12.1 per cent in 2005. Increases at the rates of 8.8 per cent and 23.6 per cent in private consumption and private sector fixed capital investments, respectively, played an important role in this development. A 21.4 per cent increase in private sector machinery and equipment investments and a 29.9 per cent increase in private sector total construction investments were the determinants of the increase in private fixed capital investments.

Table. 1. 1: Growth Rates and Demand Components

(Annual Percentage Change at 1987 Prices)

	Annual		By Quarters					
			2005				2006	
	2004	2005	I	II	III	IV	I	II
Agriculture	2.0	5.6	4.3	8.2	7.5	-0.1	6.2	-1.1
Industry	9.4	6.5	6.6	3.9	5.7	10.1	4.5	10.5
Services	10.2	8.2	6.8	6.0	8.7	10.9	7.5	6.9
GDP	8.9	7.4	6.6	5.5	7.7	9.5	6.5	7.5
GNP	9.9	7.6	7.5	4.7	8.0	10.2	6.4	8.5
Total Consumption	9.0	8.1	4.1	3.9	9.8	14.1	8.6	10.8
Public	0.5	2.4	4.4	4.0	3.2	0.0	8.1	18.0
Private	10.1	8.8	4.1	3.9	10.4	16.7	8.6	10.1
Gross Fixed Capital Formation	32.4	24.0	10.3	20.0	30.6	33.0	30.7	10.9
Public	-4.7	25.9	30.7	30.2	38.2	17.1	34.5	-11.3
Private	45.5	23.6	8.8	18.4	29.0	41.6	30.4	14.8
Total Final Domestic Demand	14.1	12.1	5.5	8.4	14.5	19.1	14.0	10.8
Total Domestic Demand	14.1	8.8	5.6	6.8	10.9	11.6	8.6	10.0
Exports of Goods and Services	12.5	8.5	14.0	6.7	3.9	10.9	3.5	4.3
Imports of Goods and Services	24.7	11.5	10.6	9.1	11.2	15.3	8.2	10.0

Source: TURKSTAT

High growth rates continued also during the first half of 2006 and an increase of 7 per cent was recorded in GDP, compared to the same period of the previous year. As in the previous years, increases in private consumption and private fixed capital investment were effective in the high growth rate in the mentioned period. During the first half of 2006, while the annual increase in the value-added of agricultural sector was 1.3 per cent, the increases in the value-added in industry and services sectors were 7.7 per cent and 7.2 per cent, respectively. The value-added of the construction sector, on the other hand, displayed a 19.3 per cent increase during the same period and maintained its substantial contribution to GDP growth.

While the increase in private consumption was 9.4 per cent in the first six months of 2006, the increase in private fixed capital investments was 21.5 per cent. During this period, public sector fixed capital investments displayed an increase of 1 per cent. The total domestic demand, on the other hand, increased by 9.4 per cent in the same period. While there was a 3.9 per cent increase in the exports of goods and services, the increase in the imports of goods and services was recorded as 9.2 per cent. Therefore, net exports of goods and services declined by 3.2 per cent.

Examining the industrial production data, it is observed that the upward trend recorded in industrial production since 2002 continued during the third quarter of 2006 as well. The manufacturing industry capacity utilization rate reached 81.3 per cent in the third quarter of 2006. Industrial production, on the other hand, increased by 5.8 per cent in the third quarter of 2006, compared to the same period of 2005. In the light of these developments, it is estimated that a GDP growth rate of 6 per cent will be realised in 2006.

Considering the labour market developments, it is noted that the transformation taking place in the sectoral structure of employment in recent years, continued in 2005 as well. In 2005, there was a 12.3 per cent decline in agricultural employment and 7.3 per cent and 8.4 per cent increases in industrial and services employments, respectively. Therefore, the transition from the agricultural sector to the other sectors continued. The employment increase of 13.7 per cent in the construction sector had a substantial impact on the employment increase of the services sector. As a result of this, total employment increased by 1.2 per cent in 2005 and 255 thousands of new jobs were created.

The unemployment rate was realised as 10.3 per cent in 2005, maintaining the same level of the previous year. During 2005, the unemployment rate in non-agricultural sectors dropped by 0.7 percentage points and went back to 13.6 per cent compared to the previous year, while the unemployment rate within the young population decreased by 0.4 percentage points from its level of the previous year, receding to 19.3 per cent.

Table. 1. 2: Developments in the Labour Market

(15+ Age, Thousands of Persons)

	Annual		2005			2006		
	2004	2005	Feb.	May	Aug.	Feb.	May	Aug.
Working Age Population	49,906	50,826	50,452	50,695	50,938	51,371	51,561	51,770
Labour Force Participation Rate (Per cent)	48.7	48.3	46.8	49.3	49.5	45.5	48.6	49.5
Female	25.4	24.8	23.3	26.2	25.6	22.2	25.8	26.5
Male	72.3	72.2	70.6	72.8	73.8	69.3	71.9	72.9
Labour Force	24,289	24,565	23,588	25,015	25,219	23,400	25,075	25,622
Employed	21,791	22,046	20,838	22,721	22,838	20,604	22,860	23,279
Unemployed	2,498	2,520	2,750	2,294	2,381	2,796	2,215	2,343
Unemployment Rate (Per cent)	10.3	10.3	11.7	9.2	9.4	11.9	8.8	9.1
Non-Agricultural Unemployment Rate	14.3	13.6	15.4	12.5	12.8	14.8	11.5	12.0
Employment Rate Among Young People	19.7	19.3	21.8	17.6	18.2	21.9	16.4	17.5
Employment by Sectors								
Agriculture	7,400	6,493	6,230	7,266	6,990	5,167	6,488	6,809
Industry	3,987	4,280	4,054	4,165	4,405	4,209	4,277	4,531
Services	10,404	11,273	10,553	11,290	11,442	11,229	12,095	11,939
Construction	1,030	1,171	924	1,252	1,294	971	1,336	1,382

Source: TURKSTAT

The labour force participation rate, on the other hand, declined to 48.3 per cent in 2005. Corresponding rates for male and female labour force were recorded as 72.2 per cent and 24.8 per cent, respectively. The overall employment rate in Turkey decreased by 0.3 percentage points to 43.4 per cent in 2005, while it declined by 0.4 percentage points to 22.3 per cent for female labour force, compared to the previous year.

During the three-month period covering July, August and September of the year 2006, the overall unemployment rate in Turkey decreased by 0.3 percentage points compared to the same period of the previous year and went back to 9.1 per cent. Non-agricultural unemployment rate decreased by 0.8 percentage points compared to the same period of the previous year and was recorded as 12 per cent, whereas the unemployment rate within the young population decreased by 0.7 percentage points from its rate of the previous year, receding to 17.5 per cent. The number of those employed increased by 441 thousand people during the three-month period covering July, August and September, compared to the same period of the previous year and increased to 23.3 million people.

During the three-month period covering July, August and September of the year 2006, the labour force participation rate, stayed at its previous year level and was realised as 49.5 per cent. During the same period, the employment rate increased by 0.2 percentage points, and was recorded as 45 per cent.

During the three-month period covering July, August and September of the year 2006, agricultural employment decreased by 181 thousand people as compared to the same period of the previous year. During the same period, the increase in industrial employment was 126 thousands while it was 497 thousands in the services sector. Employment in the construction sector, on the other hand, increased by 88 thousand people and the share of this sector within total employment was recorded as 5.6 per cent.

1.2. Balance of Payments

Current Account

Due to the high economic growth rates and increases in oil prices in the recent period, the deterioration in the current account balance accelerated. The current account deficit rose to 23.2 billion dollars in 2005 and its ratio to GDP was realised as 6.4 per cent. On the other hand, during January-September period of 2006, the current account deficit was recorded as 25.3 billion dollars.

In 2005, the high increases in world growth rate and world trade volume and a 5.7 per cent increase in world export prices compared to the previous year were the factors contributing to the export performance of Turkey. On the other hand, the sectoral diversity of exports increased and entrance to the new markets was achieved. Besides these, while the declining interest rates reduced the financing costs, the over-valued YTL decreased imported input costs. In addition, since the productivity increase in the manufacturing sector was higher than the real wage increase, unit labour costs declined. With the impact of all these factors, a high increase was achieved in exports despite the real appreciation of the domestic currency and exports increased by 16.3 per cent, reaching 73.5 billion dollars in 2005.

During the January-September period of 2006, exports increased by 13.4 per cent compared to the same period of the previous year and rose to 61 billion dollars. The

increase in the exports of motor vehicles and their parts and accessories, iron-steel and mineral fuels and oils contributed to this increase to a considerable extent.

In 2005, imports increased by 19.7 per cent compared to the previous year and reached 116.8 billion dollars. The demand of the industry for processed goods parallel to increasing activity in industry and the high rate of increase in machinery and equipment investments of the private sector due to high capacity utilization rates, were effective in the increase of imports. The real appreciation of YTL and the high rate of increase in crude oil prices can be considered as the other factors causing the increase in imports.

During the January-September period of 2006, imports continued to display their upward trend of 2005 and reached 100.5 billion dollars, rising by 17.8 per cent compared to the same period of the previous year.

The trade figures of Turkey with the European Union indicates that the exports to and imports from the EU countries, increased by 11.5 per cent and 8.3 per cent, respectively, in 2005, compared to the previous year.

As a result of these high increases in exports and imports in 2005, the share of Turkey in world trade increased. According to the International Monetary Fund (IMF) data, the share of Turkey in world exports, which was 0.71 per cent in 2004, was realised as 0.72 per cent in 2005 and its share in world imports increased from 1.09 per cent to 1.15 per cent.

Table. 1. 3: Foreign Trade by Countries

(In Million Dollars)

	Annual			January-September		
	2004	**2005**	**Percentage Change**	**2005**	**2006**	**Percentage Change**
Merchandise Exports	63,167	73,476	16.3	53,515	60,697	13.4
EU Countries	34,451	38,400	11.5	27,832	31,625	13.6
EU-15	32,589	35,872	10.1	26,070	29,502	13.2
New Member Countries	1,862	2,528	35.8	1,761	2,123	20.5
Other Countries	26,152	32,103	22.8	23,483	26,935	14.7
Turkish Free Zones	2,564	2,973	16.0	2,201	2,137	-2.9
Merchandise Imports*	97,540	116,774	19.7	85,329	100,540	17.8
EU Countries	45,444	49,220	8.3	35,973	39,694	10.3
EU-15	42,359	45,468	7.3	33,272	36,668	10.2
New Member Countries	3,084	3,752	21.6	2,701	3,026	12.0
Other Countries	51,285	66,794	30.2	48,803	60,192	23.3
Turkish Free Zones	811	760	-6.3	553	654	18.4

Source: TURKSTAT
* Excluding monetary gold, including non-monetary gold.

The balance on services, which traditionally yields surpluses, yielded a 14 billion dollar surplus in 2005 as well. Tourism revenues, which increased by 14.2 per cent in 2005 compared to the previous year, reached 18.2 billion dollars. During the January-September period of 2006, on the other hand, tourism revenues declined by 5.8 per cent compared to the same period of the previous year and were recorded as 13.7 billion dollars. The avian influenza, political tensions in the neighbouring countries and 2006 World Cup, which was organised in Germany, the most important country for Turkey in

terms of incoming tourists, played an important role in the decrease in tourism revenues.

In 2005, balance on income was realised at a level close to that of the previous year and yielded 5.7 billion dollars deficit. Interest payments, which is the largest item of the balance on income, was 5 billion dollars in 2005 and it increased by 19.5 per cent during the January-September period of 2006 compared to the same period of the previous year and was recorded as 4.4 billion dollars.

Table. 1. 4: Balance of Payments

(In Billion Dollars)

	Annual		January-September	
	2004	2005	2005	2006
Current Account	**-15.6**	**-23.2**	**-15.9**	**-25.3**
Balance on Goods	-23.9	-32.9	-24.3	-32.0
Exports	67.0	76.9	56.0	63.9
Imports	-90.9	-109.9	-80.2	-95.9
Balance on Services	12.8	14.0	11.6	10.1
Credit	22.9	25.8	20.1	18.5
Tourism	15.9	18.2	14.6	13.7
Debit	-10.1	-11.9	-8.5	-8.4
Balance on Income	-5.6	-5.7	-4.3	-4.6
Credit	2.7	3.7	2.9	3.5
Debit	-8.3	-9.3	-7.2	-8.1
Current Transfers	1.1	1.5	1.1	1.2
Capital and Financial Account	**13.4**	**20.9**	**13.2**	**26.0**
Financial Account	13.4	20.9	13.2	26.0
Foreign Direct Investment	2.0	8.7	3.1	12.4
Portfolio Investment	8.0	13.4	8.9	3.6
Other Investment	4.2	16.6	9.7	14.9
Assets	-7.0	0.2	-1.9	-5.6
Liabilities	11.1	16.4	11.7	20.5
Trade Credits	4.2	3.6	2.7	2.7
Credits	6.1	12.0	7.0	16.6
Monetary Authority	-4.4	-2.9	-2.6	0.0
General Government	-0.3	-4.6	-3.6	-3.6
Banks	5.7	9.2	6.8	5.7
Other Sectors	5.1	10.3	6.3	14.6
Currency and Deposits	0.6	0.5	1.6	0.9
Monetary Authority	-0.2	-0.8	-0.6	-0.9
Banks	0.9	1.3	2.2	1.8
Other Liabilities	0.2	0.3	0.3	0.3
Official Reserves	-0.8	-17.8	-8.6	-4.9
Net Errors and Omissions	**2.2**	**2.2**	**2.7**	**-0.7**

Source: CBRT

Workers' remittances and official transfers were realised as 0.9 billion dollars and 0.6 billion dollars, respectively in 2005 and the total current transfers were recorded as 1.5 billion dollars. On the other hand, current transfers were 1.2 billion dollars during the first three quarters of 2006.

Capital and Financial Account

The capital inflows realised in recent years due to the stability achieved in the economy and positive prospects for the future, continued in 2005 as well. While capital inflows were recorded as 20.9 billion dollars in 2005, this figure reached 26 billion dollars for the first nine months of 2006 and thereby, the increase in reserves were realised as 5 billion dollars during the same period. Therefore, the total increase in the official reserves since 2002 has reached 33.8 billion dollars.

Box. 1. 1: Developments in Foreign Direct Investments

The increase experienced in the global foreign direct capital flows based on the developments in cross border Mergers and Acquisitions (M&A) since the end of 1980s, reached a historical level of 1,400 billion dollars in 2000.

These capital flows, which displayed a relative contraction during the 2001-2003 period, displayed a considerable increase in 2004 and 2005 at the rates of 27 per cent and 29 per cent, respectively, with the impact of the revival in the world economy as well, and reached the level of 916 billion dollars at the end of 2005. During the recent period, the primary factor determining the vitality in global foreign direct capital flows was again cross border M&A. As a matter of fact, the share of global cross border M&A in the total global foreign direct capital flows, which was 53 per cent in 2003, reached 78 per cent at the end of 2005. The sector in which the M&A were more concentrated was notably the services sector. Within this context, it is observed that 63 per cent of the total cross border M&A were realised in the finance sector and this sector was followed by the transportation, storage and communication sector with a share of 14 per cent.

Considering the distribution of global foreign direct capital flows among economies, it is observed that these flows mostly occurred among the developed economies. In this context, the share of developing countries in the global foreign direct capital flows was 31 per cent in 2003, 39 per cent in 2004 and 36 per cent in 2005 and these flows were mostly directed towards South-eastern Asian economies.

Policies towards establishing stability and structural reform efforts, which have been implemented continuously in the Turkish economy since 2001, have started to display their positive impacts. The confidence environment achieved in the economy as a result of these efforts has positively affected the perceptions of foreign investors regarding the Turkish economy. As a result of these developments, the total foreign direct capital inflows to the Turkish economy, which was 5.1 billion dollars during the 1995-2000 period, rose to 18.9 billion dollars during the 2001-2005 period. During the first eight months period of 2006, on the other hand, the foreign direct capital inflows reached a historical level and became 12.4 billion dollars.

Examining the sectoral composition of foreign direct capital investments, it is observed that this composition shows similarities with global flows. Services was the sector in which foreign direct capital inflows were most intensively experienced. Considering the sub-sector details, on the other hand, finance and communication sectors became the top two sectors attracting foreign direct capital investments. As a matter of fact, while the share of finance sector in the foreign direct capital inflows was 47 per cent at the end of 2005, the share of communication sector was 38 per cent. During the January-September period of 2006, the shares obtained by these two sectors were 31 per cent and 43 per cent, respectively.

In spite of this significant development in foreign direct capital inflows, Turkey is still attracting a level of foreign direct capital below its potential. In this context, with the aim of utilizing this potential, reform activities, particularly towards improving the investment environment will be continued during the following period as well. Thus, the supporting role of foreign direct capital investment towards convergence to the EU economies will be benefited from to the greatest extent through achieving a permanent sustainable growth performance.

Table: Foreign Direct Investments (In Billion Dollars)

	1995-2000	2001-2005	2004	2005	2005 Jan-Sept	2006 Jan-Sept(1)
Total Foreign Direct Investments (Net)	5.1	18.9	2.9	9.8	3.9	12.8
- Foreign Direct Investments	5.1	14.7	1.5	8.0	2.8	10.5
- Capital (Net)	5.1	14.1	1.2	8.2	3.0	10.5
- Inflow	6.2	14.6	1.3	8.6	3.4	11.0
- Outflow	1.1	0.5	0.1	0.3	0.3	0.6
- Other Capital	--	0.6	0.3	0.2	0.2	0.0
- Reel Estates (Net)	--	4.2	1.3	1.8	1.0	2.3

Source: CBRT
(1) Provisional figures

Source: World Investment Report 2006, UNCTAD

Scrutinizing capital movements, the trends observed in 2004 continued in 2005 as well. The share of short-term capital flows in total continued to decrease in 2005. This share, which was 88.8 per cent in 2004, declined to 47.6 per cent in 2005. While the share of short-term loans borrowed from abroad by the domestic banks in total loans decreased, the amount of long-term loans increased during the same period.

While portfolio investments constituted 34.7 per cent of the net 38.8 billion dollars inflow recorded in the capital and finance account (excluding reserves) in 2005, this figure was realised as 11.6 per cent during the January-September period of 2006. This is the result of the increase experienced in the loans borrowed by the non-bank private sector from abroad and the realisation of the record level in foreign direct investments.

Excluding the reserve assets, a net capital inflow of 30.9 billion dollars was recorded during the January-September period of 2006. While the Treasury borrowed 2.5 billion dollars through the issuance of Eurobonds during the first nine months of the year, the government domestic borrowing bonds and equity purchases of foreigners were 0.7 billion dollars and 1.6 billion dollars, respectively.

Compared to the previous years, it is observed that weight of items originating from the private sector increased in the financing of current account deficit and that the public sector became a net debt payer in the first nine months of 2006. Private sector borrowing is mostly composed of long-term commercial and investment credits. The fact that private sector foreign debt mostly stems from imports of machinery, equipment and intermediary goods for production, is important in terms of enhancing debt repayment capacity.

The foreign direct investments in 2005 were more than the total of those realised between 2000 and 2004. Direct investments reached a net amount of 8.7 billion dollars in 2005 and became a significant source of financing. This increase in the direct investments continued during the January-September period of 2006 and net direct investments reached 12.4 billion dollars.

Other investments item of the capital and finance account, on the other hand, yielded a surplus of 16.6 billion dollars in 2005. The total loans borrowed by banking sector was realised as 9.2 billion dollars in 2005 and of this amount, 6.5 billion dollars were long-term loans and 2.7 billion dollars were short-term loans. The positive change in the maturity structure of the loans borrowed by the banking sector continued during the first nine months of 2006. As a matter of fact, in this period the total loans of 5.7 billion dollars were composed of 5.3 billion dollars of long-term loans and 0.4 billion dollars of short-term loans.

Decreasing uncertainties and the risk premium in the economy in recent years created the appropriate environment for investments and therefore domestic investment expenditures increased. As a result of this, the net amount of long-term loans borrowed by the non-bank private sector from abroad was 9.9 billion dollars in 2005. During the January-September period of 2006, on the other hand, this figure exceeded its 2005 level and reached 14.1 billion dollars.

While 5.4 billion dollars of repayment was made to the IMF during the January-September of 2006, 1.9 billion dollars were borrowed. Thus net repayments to the IMF amounted 3.5 billion dollars.

1.3. Monetary and Exchange Rate Policies

Monetary Policy

With the fulfilment of pre-conditions and completion of the necessary infrastructure, the Central Bank of the Republic of Turkey (CBRT) moved to the implementation of explicit inflation targeting regime starting with the beginning of 2006. Along with this regime, important arrangements were introduced into the monetary policy in terms of institutionalisation, transparency and accountability. While the interest decisions taken at the Monetary Policy Board were advisory during the previous period, they were equipped with a binding characteristic with the amendments made. In the same context, by publicising minutes of the board, policy implementation has become more institutionalised and transparent. On the other hand, the inflation itself was determined as the final target instead of monitoring monetary aggregates such as monetary base and net domestic assets. In addition, quarterly publication of the Inflation Report containing the future inflation estimations and the monthly publication of the Monetary Policy Board minutes can be listed as other basic arrangements.

In the framework of explicit inflation targeting, the point inflation targets for the end-year Consumer Prices Index were determined in collaboration with the government. The inflation path consistent with this target was announced as of quarterly periods and symmetric uncertainty bands around the inflation path were created as basis of the accountability mechanism. The uncertainty bands around the path created for 2006 were determined as 2 points in both directions and these bands constituted the performance criteria together with the Net International Reserves to be used in the quarterly reviews within the framework of the programme agreed with the IMF. Inflation targets determined for 2006, 2007 and 2008 are 5 per cent, 4 per cent and 4 per cent, respectively and the target for 2009 will be determined at the end of 2006.

Table. 1. 5: Performance Criteria for Monetary Policy in 2006

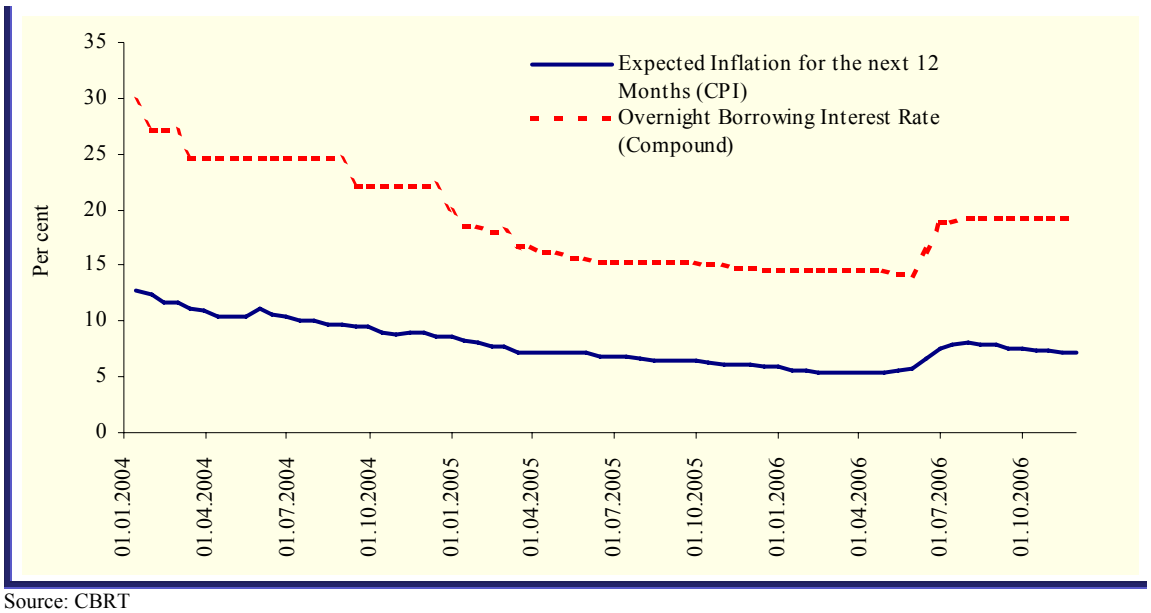
	Inflation (Annual, Per cent)		Net International Reserves (In Billion Dollars)	
	Target(1)	Realization	Target(2)	Realization
31 March 2006	5.4-9.4	8.16	17.2	32.4
30 June 2006	4.5-8.5	10.12	19.9	31.0
30 September 2006	3.8-7.8	10.55	20.3	31.0
31 December 2006	3.0-7.0	-	22.6	-

(1) Uncertainty bands in line with the target path.
(2) Lower limit.

While inflation remained within the determined uncertainty bands during the first quarter of 2006, due to the impact of the fluctuation arising from the contraction in the liquidity flow in the international markets during the months of May and June on prices, it exceeded the uncertainty bands determined for June and September. Particularly because of the primary impacts of the upward volatility experienced in the foreign exchange rates, rapid increases in the prices of some commodity groups were the primary determining factors in exceeding uncertainty bands. Within the framework of the accountability principle, two letters containing the deviations experienced in inflation during the second and third quarters of 2006, the reasons for such deviations and required measures to be taken in order to converge to the target again were submitted to the government by the Central Bank on 14 July and 30 October 2006, they

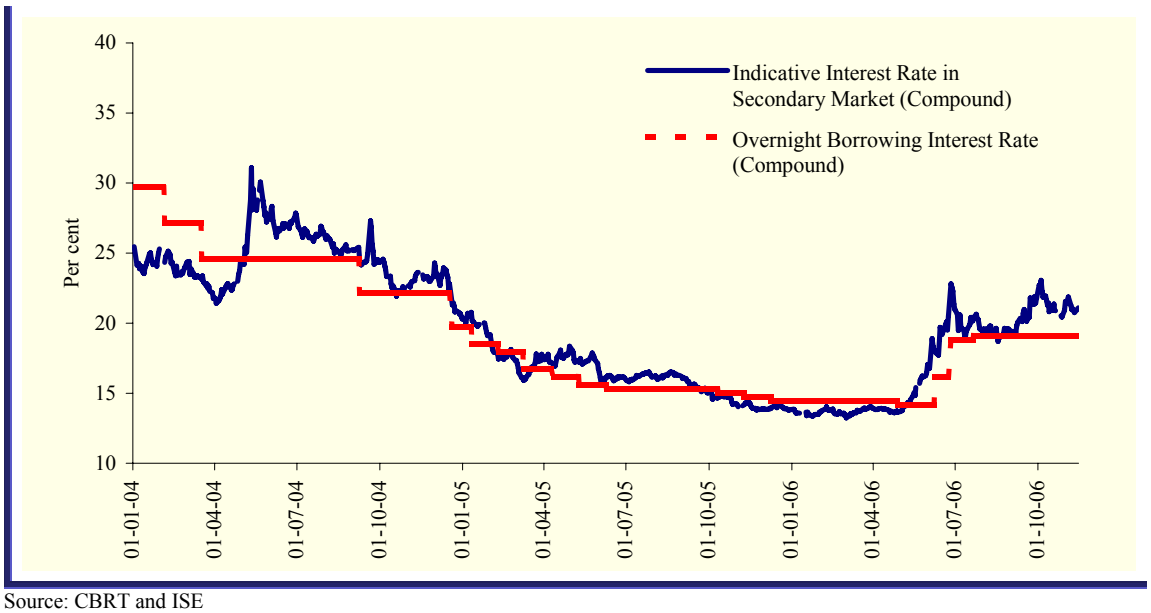
were publicised and also sent to the IMF within the framework of programme requirement. It was stated in these letters that it would not be possible to achieve the inflation target for 2006 due to the cost increases arising from the factors out of the control of the monetary policy, however, that the probability of convergence to the 2007 target was high and a certain amount of monetary tightening could be needed towards this end.

Figure. 1. 1: Monetary Policy and Expectations - 1



Source: CBRT

Figure. 1. 2: Monetary Policy and Expectations - 2



Source: CBRT and ISE

Within the framework of the implemented monetary policy strategy, short-term interest rates have also been used in 2006 as a primary policy instrument in order to direct expectations and affect funding cost. The Monetary Policy Board considers the consistency of inflation estimates and expectations with the target and takes interest rate decisions based on a medium-term perspective. The Central Bank reduced interest rates

nine times during 2005 and decreased overnight borrowing interest rates from 18 per cent to 13.5 per cent. The Central Bank pointed out factors such as increase in oil prices, possibility of changes in global liquidity conditions in favour of developed countries and price rigidity in the services sector despite the positive prospects at the beginning of 2006 and kept the policy interest rates fixed during the first three months of the year. In April, on the other hand, interest rates were reduced by 25 basis points in light of the existing information.

As a result of the changes in global liquidity conditions in favour of developed countries, capital outflows from developing countries, including Turkey, were experienced as of May. Capital outflows resulted in fluctuations in capital markets and YTL started to depreciate rapidly. In order to prevent the distortions that started in the inflation prospects due to these developments, the Board convened an extraordinary meeting on 7 June 2006 as a policy reaction and increased policy interest rates by 175 basis points. During the following days, restart of depreciation in YTL and the increase in the volatility in foreign exchange rates started to threaten the stability in the markets. In order to prevent the damages of these developments on medium-term inflation targets, the Board raised the interest rates by 225 basis points at its second extraordinary meeting held on 25 June 2006. In the ordinary meeting of the Monetary Policy Board on 20 July 2006, interest rates were increased by 25 basis points. In addition, since the interest rates determined in YTL Depo purchase auctions realised by the Central Bank with the aim of drawing the excess liquidity from the markets exceeded the interest rates for lending, the Central Bank made a technical arrangement in lending interest rates and increased them by 200 basis points. Thus, as of 10 November 2006, the borrowing interest rate of the Central Bank became 17.5 per cent, while the lending interest rate was realised as 22.5 per cent.

Exchange Rate Policy

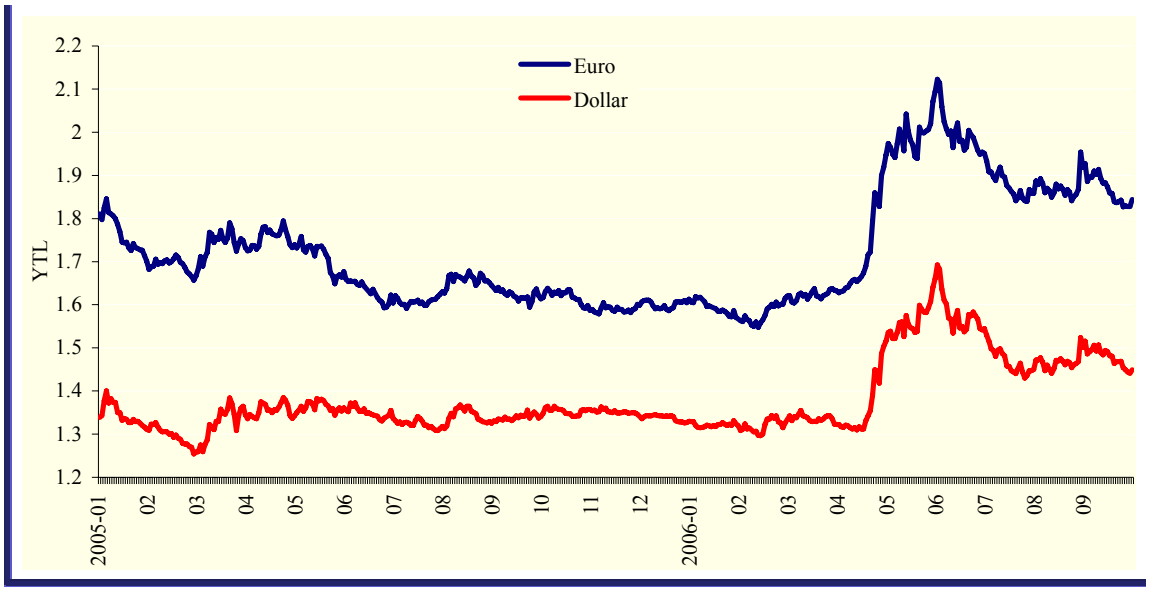
The floating exchange rate regime, which is an important component of the existing monetary policy, was continued during 2006 as well and foreign exchange rates were determined according to the supply-demand conditions in the market.

In addition, the Central Bank intervened in the exchange rate market in both directions to prevent actual and potential excess volatility in the exchange rates that could damage the inflation target. As a matter of fact, the foreign capital inflows directed towards developing countries at the beginning of 2006 and the reverse currency substitution resulting from the increasing confidence in the implemented policies, led to a rise in supply in the foreign exchange market. Within this framework, the Central Bank intervened in the foreign exchange market through direct purchases on 15 February 2006, with the aim of preventing the downward volatility in the exchange rates. With this intervention, the Central Bank bought 5.4 billion dollars from the foreign exchange market. On the other hand, as a result of the decrease in the risk appetite towards developing countries including Turkey, capital outflows increased the foreign currency demand and caused upward volatility in exchange rates. Consequently, the Central Bank intervened in the foreign exchange market through sales for three times on 13, 23, and 26 June and sold a total amount of 2.1 billion dollars to the market.

Taking into consideration the contribution of a strong foreign exchange reserve position to the confidence in the economic programme being implemented, in order to accumulate reserves, the Central Bank held foreign exchange auctions within a pre-announced schedule without affecting the medium and long-term equilibrium level of the foreign exchange rate. In this context, with the foreign exchange purchase auctions

held until 15 May 2006, 3.3 billion dollars were purchased. However, due to the liquidity shortage in the foreign exchange market fundamentally owing to external developments, foreign exchange auctions were suspended on 15 May 2006. On the other hand, with the aim of eliminating the liquidity shortage in the foreign exchange market resulting from the fluctuations observed in May and June, the Central Bank held foreign exchange sales auctions with a daily limit of 500 million dollars and sold 1 billion dollars in two auctions. With the relative stability provided in the foreign exchange markets, the Central Bank started foreign exchange purchase auctions again as of 10 November 2006.

Figure. 1. 3: Developments in Exchange Rates



Source: CBRT

Table. 1. 6: FX Purchases of the Central Bank

(In Million Dollars)

	FX Purchase Auctions	FX Sale Auctions	Direct FX Purchases	Direct FX Sales
2002	795	---	16	---
2003	5,653	---	4,808	---
2004	4,104	---	1,283	9
2005	7,443	---	14,565	---
2006 January - October	3,318	1,000	5,441	2,105
Total	21,313	1,000	26,113	2,114

Source: CBRT

1.4. Financial Sector

Banking Sector

The Turkish banking sector strengthened its position within the Turkish financial system as a result of the realization of a planned financial and operational restructuring and harmonization of the legal and institutional framework regulating the sector with international standards. The confidence environment, which became more definite particularly starting from 2003, and the macroeconomic stability achieved, facilitated

the sector's carrying out its intermediary function more efficiently. As a result of these developments, banking sector assets, which was 117.7 billion dollars at the end of 2001, reached 290 billion dollars in the first half of 2006 and displayed a significant growth performance. During the same period, banking sector credit stock increased from 23.4 billion dollars to 127.4 billion dollars. In spite of the considerable increase in loans, the share of non-performing loans in total loans, which is an important indicator in terms of the financial performance of the system, continued to decrease during the mentioned period as well.

The positive developments in the banking sector enabled stability in the profitability performance of the sector as well. As a matter of fact, while the average net profit of the sector was 3.5 billion dollars during the 2002-2005 period, it reached 3.6 billion dollars as of the first half of 2006.

The developments in the composition of bank assets in favour of loans since 2004 caused a change in the risk profile, which is taken into consideration in the calculation of capital adequacy ratios. With the impact of this development, a significant decline was observed in the capital adequacy ratios of the banking sector in 2005. During the financial fluctuation in May and June of 2006, and particularly, the leap displayed in the interest rates caused a significant corrosion in the capital adequacy ratios of the banking sector.

Table. 1. 7: Overview of the Banking Sector

	2001	2002	2003	2004	2005	2006 June
Main Aggregates						
Assets (In Billion Dollars)	117.7	130.1	178.9	228.3	295.9	290.0
Loans (In Billion Dollars)	23.4	30.0	47.4	74.0	113.7	127.4
Deposits (In Billion Dollars)	76.6	84.4	111.3	143.0	187.1	185.8
Number of Banks	61	54	50	48	47	47
Number of Employees (Thousands)	139.0	123.9	124.0	127.9	133.0	139.4
Performance Indicators						
Net Profit (In Billion Dollars)	-8.2	1.8	4.0	4.5	3.7	3.6
Return on Assets (Per cent)	-7.0	1.4	2.2	2.1	2.7	1.7
Rate of Return for Equity Capital (Per cent)	-77.0	9.2	15.8	14.0	18.6	12.5
Loans/Deposits (Per cent)	30.5	35.5	42.6	51.7	61.7	69.3
Risk Indicators						
Capital Adequacy Ratio (Per cent)	20.8	26.1	30.9	28.8	24.2	18.6
FX Position in the Balance Sheet (In Billion Dollars)	-1.6	-0.6	0.0	-1.4	-1.9	-5.8
Net General Position (In Billion Dollars)	-0.5	-0.4	0.3	-0.1	-0.1	-0.4
Non-Performing Loans/Gross Loans (Per cent)	29.3	17.6	11.5	6.0	5.0	3.9
Securities Portfolio/Assets (Per cent)	35.0	40.5	42.8	40.4	36.0	36.2

Source: BRSA

With the withdrawal of the insolvent banks from the system and encouragement of mergers and acquisitions of private banks in the following stage within the framework of the restructuring of the banking sector, the number of banks in the sector displayed a significant decline starting from 2001. In this context, the number of banks, which was 61 at the end of 2001, was recorded as 47 in June 2006. The banking sector employment, which showed a serious decline following the 2000 and 2001 crises,

started to recover, particularly starting from 2004, and reached its 2001 level during the first half of 2006.

Capital Market

While the weight of government bonds and bills in total equities continued, the share of private equities displayed an increase in recent years. While this rate was around 8 per cent in 2002, it increased to 12.5 per cent as of July 2006. While the number of companies quoted in the İstanbul Stock Exchange (ISE) was 4 in 2002, this figure went up to 9 in 2005 and to 13 as of September 2006.

The ISE National 100 Index, which has displayed an upward trend since 2002, started to follow a horizontal path after the fluctuations in the financial markets in May-June 2006 period. The ISE-100 Compound Dollar Index (1986=100), which was 1,726 dollars at the end of 2005, has been floating around 1,500 dollars since May 2006. As of the end of September 2006, on the other hand, the ISE-100 Compound Dollar Index was realised as 1,436 dollars. Market capitalization declined to 213.5 billion YTL as of the end of September 2006 from its level of 218.3 billion YTL at the end of 2005. When the transaction volume on YTL basis is examined, an increase at the rate of 34 per cent is observed with a transaction volume of 256.9 billion YTL during the first nine months of 2006 compared to the same period of 2005. The share of stocks held by foreign investors in the stock market reached 66.3 per cent at the end of 2005 from 55 per cent at the end of 2004 and even though it slightly declined in the May-June 2006 fluctuations, it preserved this level as of the end of September 2006.

The number of intermediary companies that perform in the capital market is 147 as of September 2006. As of the same period, there are 316 incorporated companies, the stocks of which are traded in the stock exchange market. In this period, the number of investment trusts registered in the Capital Market Board is 43, the number of mutual funds is 281 and their portfolio values are 2.8 billion YTL and 24 billion YTL, respectively. On the other hand, the number of private pension funds that were started to be established at the end of 2003, reached 81 in 2004 and 102 as of the end of September 2006. As of the same date, the number of participants in the private pension funds rose to 1,040,568 persons while the portfolio amount reached 2.4 billion YTL.

Insurance Sector

There were 46 companies in operation in the Turkish insurance and private pension sectors as of the end of 2005. 9 of these are life insurance companies, 10 of them are life insurance/pension companies, 1 of them is a pension company, 14 of them are non-life insurance companies, 11 of them are composite companies and 1 of them is a reinsurance company.

The insurance sector realised total premiums of 7.8 billion YTL at the end of 2005 with a growth rate of 18 per cent. The share of the total premiums in GDP reached 1.6 per cent. Thus, the insurance sector has been growing faster than the other fields of the financial sector. As a matter of fact, examining the developments regarding total premiums on YTL basis in the past decade, it is observed that growth rate was realised as 12,256 per cent. The share of non-life insurances in total premiums was realised as 84.1 per cent, while that of life insurances was 15.9 per cent.

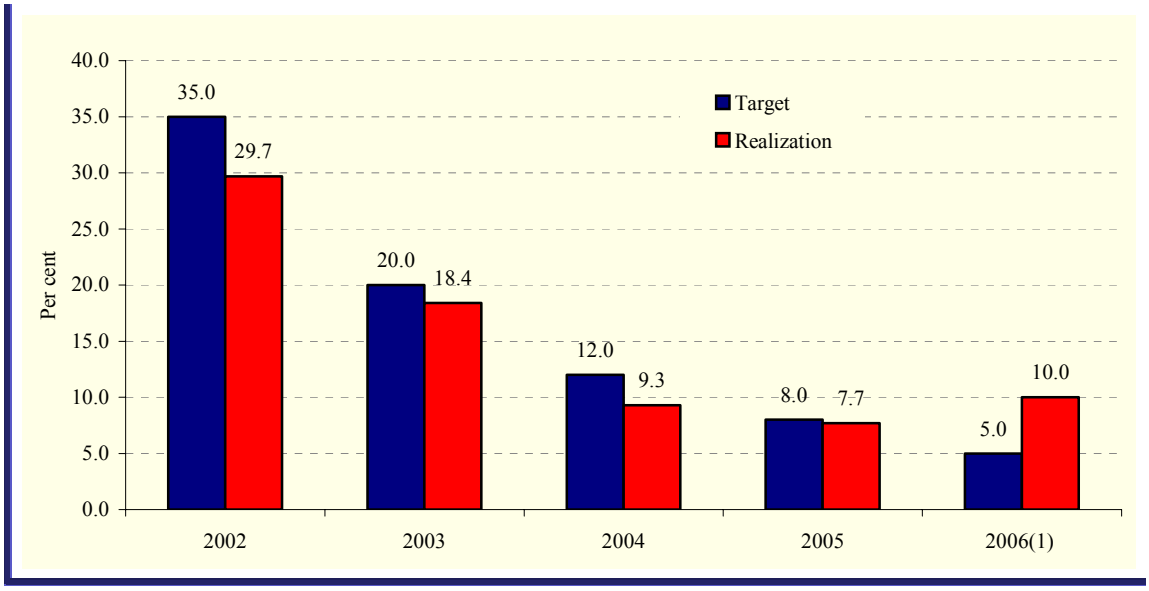
When the private pension system is examined, 672,696 participants were covered with 714,146 contracts concluded as of the end of 2005. The total amount of funds

directed to investment within the system, which was 276.3 million YTL as of the end of 2004, increased to 1,078.6 million YTL at the end of 2005.

1.5. Inflation

12-month inflation was 7.7 per cent in Consumer Prices Index (CPI) and was 2.7 per cent in Producer Prices Index (PPI) as of the end of 2005. The annual inflation in the consumer prices declined by 1.6 percentage points compared to its level in 2004. Therefore, the annual inflation was realised below the target also in 2005 as in the period of 2002-2004. During this period, despite the high increases in energy and raw material prices in international markets, the tight monetary policy as well as the decisive implementation of the fiscal discipline constituted the determining factors in meeting the inflation target. On the other hand, continuation of productivity increases, strong position of YTL and favourable developments regarding inflationary expectations in 2005 contributed to the realization of the inflation target.

Figure. 1. 4: CPI Targets and Realizations



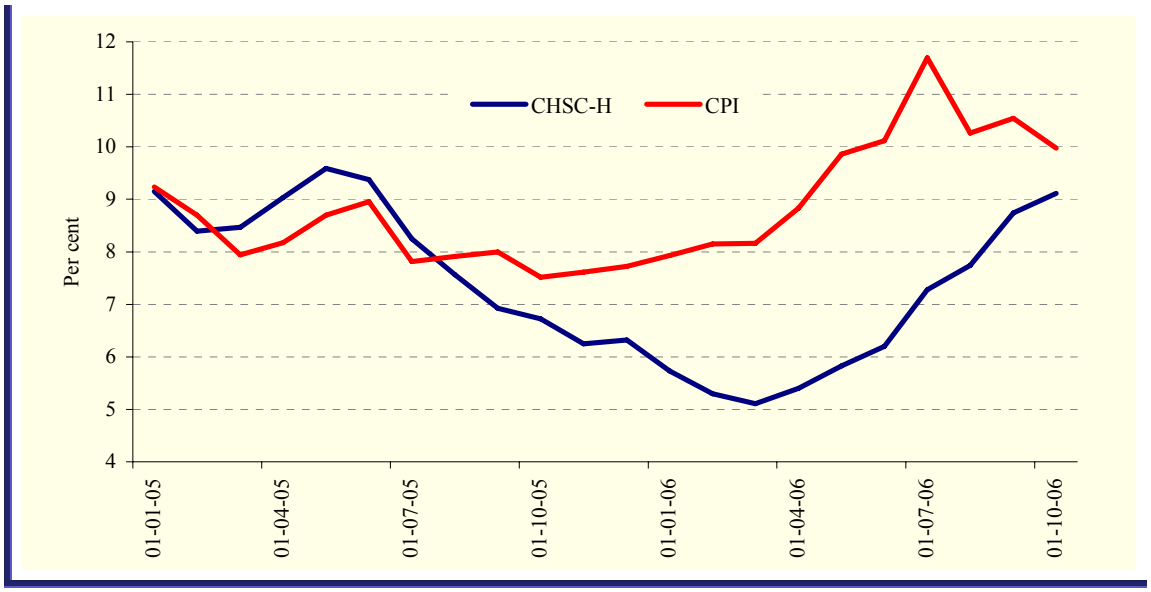
Source: TURKSTAT, CBRT
(1) 2006 realization figure is as of October.

The downward trend of inflation was replaced with an increase in 2006 and the upward trend in annual inflation continued until August. It was observed that rising commodity prices and high increases in the prices of unprocessed food products and tobacco products were the determinants in inflation increases during the first four months of the year. During the following period, the depreciation of YTL along with supply shocks caused an inflationary pressure. As a result of this depreciation and increases in the prices of tradable goods, consumer inflation displayed a significant deviation from the path consistent with the target. As a result of the recovery in YTL and positive developments regarding energy prices, the CPI inflation started to decline again starting from August. As a matter of fact, the annual CPI inflation, which was 8.2 per cent at the end of the first quarter of the year, declined to 10 per cent in October after increasing up to 11.7 per cent in July.

Examining the indicator having specified coverage with H code (CHSC-H), which excludes energy, unprocessed food, alcoholic beverages and tobacco product prices as well as gold prices, it is observed that the annual inflation receded back to 5

per cent in March and rose to 9.1 per cent as of October with the impact of the depreciation in YTL. (Figure 1.5). On the other hand, the ongoing rigidity in services prices preserves its importance even though this rigidity displayed a partial reduction compared to the previous year. In this context, the probability that the annual inflation will go beyond the target level at the end of 2006 has emerged.

Figure. 1. 5: CPI and CHSC-H Indicators



1.6. Public Finance

Developments in the Consolidated Budget/Central Government Budget Revenues and Expenditures

The 2005 budget was prepared in a way to yield a high primary surplus under the objective of maintaining sustainable public debt stock as a requirement of the economic programme being followed and it was implemented in line with the same purposes.

With the aim of achieving the objectives determined under the tight fiscal policy implemented in 2005, some income increasing measures were taken. In this context, the rate of tax on certain goods included in the Special Consumption Tax (SCT) IV list was raised from 6.7 per cent to 20 per cent.

In February 2005, the amounts of SCT imposed on alcoholic beverages and tobacco products were increased. SCT rates on alcoholic beverages and tobacco products were increased in February 2005. Taxation of cigarettes based on their oriental tobacco content, which prompted cigarette manufacturers to use different pricing and product diversification strategies in a way to cause loss of tax revenues, was abandoned in July and a single proportional SCT (58 per cent) was adopted for all products. In addition, it was stipulated that the tax to be computed by using proportional SCT rate could not be less than the minimum fixed tax (0.06 YTL per unit/gram).

In addition to the revenue increasing measures in 2005, precautions towards controlling expenditures were also taken. In this context, salaries and wages of public workers were determined according to inflation target and restrictions on new civil servant recruitment were introduced. New measures and regulations were put into force in order to keep public health expenditures and medicine expenses under control.

In addition to revenue raising and expenditure reducing measures, some arrangements for increasing employment, reducing regional development disparities and social purposes were introduced. In this context, the number of provinces covered within the scope of the Law No. 5084 on the Encouragement of Investments and Employment was raised from 36 to 49. The rate of value added tax (VAT) on certain education materials and services, medicine and health services and some basic food products was reduced. The income tax top tariff rate was reduced by 5 percentage points while the corporate tax rate was reduced by 3 percentage points.

Box. 1. 2: IMF-Defined Primary Budget Surplus

Primary consolidated budget surplus, which was defined under the IMF stand-by agreements, is obtained by making a series of adjustments to income and expenditure items. The adjusted items and IMF-defined primary budget surplus figures are presented in the following table.

Table: IMF-Defined Primary Budget Surplus

(Per cent of GDP)

	2002	2003	2004	2005
Primary Surplus	**3.67**	**5.12**	**6.08**	**7.71**
Profits of CBRT (-)	1.08	0.00	0.00	0.00
Interest Receipts (-)	0.56	0.35	0.82	1.74
Privatisation Revenues (-)	0.00	0.00	0.00	0.37
Tax Arrears (+)	0.10	0.00	0.00	0.07
Risk Account (+)	0.00	0.26	0.11	0.04
Revaluation Difference (-)	0.01	0.01	0.00	0.00
SSK and BAĞ-KUR Adjustment (Previous Year Debts) (-)	0.00	0.09	0.00	0.00
SSI Adjustment (Payments Credit to Budget) (+)	0.34	0.00	0.00	0.00
SSI Adjustment (Appropriation-Cash Difference) (+)	0.00	0.00	0.01	-0.01
Seniority Allowance (+)	0.07	0.00	0.00	0.00
Dividend Payments of State Banks (-)	0.00	0.00	0.26	0.26
Seigniorage Revenues from Coins (-)	0.00	0.00	0.00	0.11
IMF-Defined Primary Surplus	**2.53**	**4.93**	**5.13**	**5.34**

Source: SPO

As a result of these developments, while the ratio of consolidated budget expenditures to GDP was 32.1 per cent, the share of revenues was 30.5 per cent in 2005. The share of the consolidated budget deficit within GDP decreased by 5.3 percentage points compared to that of the previous year and became 1.7 per cent and the primary surplus was 7.7 per cent of GDP, which was above the targets.

As in 2005, contributing to the sustainability of the public debt stock through yielding a high rate of primary surplus was adopted as the basic objective in the 2006 budget. In addition, supporting development activities and the struggle against inflation are the other objectives of the budget.

The 2006 budget was prepared on the basis of the central government budget as required by the Public Financial Management and Control Law No. 5018. The 2006 Central Government Budget, which was prepared in line with main economic indicators and rules and principles specified in the Medium Term Program and Medium Term Financial Plan, also includes the revenue and expenditure estimates for the following two years in addition to the current year. Therefore, the year 2006 is characterized as being the first year of transition to multi-year budgeting in our country. 25

organizations, which were not included within the scope of the consolidated budget before 2006, 8 regulatory and supervisory agencies that transfer their revenue surpluses to the budget, health centers and cultural centers operating in connection with universities were included in the scope of the central government budget.

There is no significant revenue-raising measure was projected in 2006. In April, particularly to deal with the current account deficit, the SCT rates imposed on motorcycles were increased. During this period, the most important development affecting the budget revenues has been one-time revenues. The amounts transferred to the budget for the finalized tax, charge, fines, late payment penalty, arrears and the GSM treasury share liabilities of organizations, the management and supervision of which were taken over by the Savings Deposit Insurance Fund (SDIF), reached the level of 1.1 per cent of GDP. In addition, the cash at the rate of 0.2 per cent of GDP, which was decided to be transferred to the Treasury due to the privatisation of the Turkish Telecom, affected the budget revenues in a positive manner.

Table. 1. 8: Consolidated/Central Government Budget Balance

(Per cent of GDP)

	2002	2003	2004	2005	2006*
Expenditures	42.2	39.0	35.0	32.1	31.8
Non-Interest Expenditures	23.5	22.7	21.8	22.7	23.2
Current Expenditures	11.0	10.7	10.4	10.0	10.5
Personnel	8.3	8.4	8.5	8.2	8.0
Other	2.7	2.3	1.9	1.8	2.5
Investment	3.0	2.0	1.8	1.9	2.2
Transfer	28.2	26.3	22.8	20.2	19.1
Non-Interest Transfer	9.5	10.0	9.7	10.8	10.5
Interest Payments	18.7	16.3	13.1	9.4	8.5
Revenues	27.2	27.9	27.9	30.5	29.2
General Budget	26.9	27.4	27.5	30.0	29.2
Tax Revenues	21.5	23.4	23.1	24.0	24.0
Non-Tax Revenues	3.9	2.8	3.9	5.5	4.9
Special Revenues and Funds	1.5	1.1	0.5	0.4	0.3
Annexed Budget	0.4	0.5	0.4	0.5	-
Primary Surplus	3.7	5.1	6.1	7.7	6.0
IMF-Defined Primary Surplus	2.5	4.9	5.1	5.3	4.9
Budget Deficit	15.0	11.2	7.0	1.7	2.6

Source: SPO, Ministry of Finance
Note : The figures given for 2004, 2005 and 2006 are not based on analytical budget code system in order to make them comparable with the figures of the previous years.
* The figures are initial appropriates and prepared based on the central government budget

2006 was a year in which important reforms in the field of taxes were realised. Corporate Tax Law was rewritten taking into consideration such priorities as, simplifying the tax legislation, expanding the tax base and struggle against informal economy. With this regulation, the corporate tax rate was decreased from 30 per cent to 20 per cent. In this manner, the tax burden on corporate earnings was withdrawn to the level of 34 per cent. Institutions such as hidden capital, hidden earning distribution through transfer pricing, controlled foreign company and application of withholding tax against harmful tax competition, were added to the system parallel with international applications.

One of the important arrangements with regard to taxes was realised in the Income Tax Law in 2006. In this context, the number of revenue tariffs was decreased from 5 to 4. The implementation of different tax rates on wage and non-wage incomes was abandoned and the income tax rates imposed on the taxpayers other than wage earners were reduced by 5 percentage points. The implementation of investment allowances, the efficiency of which was subject to controversy, was ended in a 3 year transition process. In addition, the equity capital revenue taxation system, which was rearranged by the Law No. 5281, was put into force at the beginning of 2006. However, further amendments were made in the following period and the taxing of domestic and foreign investors were differentiated, and reductions were made in rates of withholding tax imposed on some equity capitals. In this framework, withholding tax rate on GDBI revenues was reduced to 0 per cent for foreign investors and 10 per cent for domestic investors.

A revenue of 493 million YTL was raised in 2006 from the instalments of the real estates belonging to the Civil Servants Pension Fund, which were sold over the previous years and within the year.

With the Law No. 5458 on Restructuring Social Security Premium Revenues and Amending Certain Law, the SSK and BAĞ-KUR, premium receivables were restructured and an opportunity was given for the restructured receivable to be paid by the insured in instalments distributed over a period of maximum 5 years. By this Law, restructuring revenue of 3,050 million YTL in BAĞ-KUR and 714 million YTL in SSK is expected in 2006.

As a requirement of the tight fiscal policy implemented in 2006, important measures were taken to keep budget expenditures under control. Within this scope;

- Salaries and wages in the public sector were determined according to the inflation target,
- The limitation on recruitment of new personnel was maximum 80 per cent of positions vacated due to such reasons as retirement, resignation, or death,
- The additional increase in revenues to be saved, to contribute to primary surplus, except for prioritised investment projects.
- An upper limit was introduced in central government primary budget expenditures and social security expenditures except for the transfers made to social security institutions.

In spite of the measures taken related to expenditures in 2006, implementations such as reflecting the difference between the actual inflation rate in the first half of the year and the salary increase rate to civil servant salaries during the second half of the year, additional increases and improvements in the salaries and other personnel rights of some public personnel, green card and agricultural support expenditures exceeding the targets, played a significant role in increasing the budget expenditures.

With the Budget Implementation Directive effective from the beginning of 2006, no increases were made on average in treatment prices compared to those of 2005 and a positive list, which would be used jointly by all institutions, was set up. Again to be effective from the beginning of 2006, the term of the protocol signed between the Ministry of Finance, the Ministry of Labour and Social Security and the Turkish Pharmaceutical Association in 2005, which provided approximately 10 per cent reduction in pharmaceutical prices on average, was extended for one year. In addition,

while payments were used to be made up to 30 per cent more than the price of the most inexpensive medicine within equivalent medicine groups, this rate was decreased to 22 per cent starting from May 2006 and the number of medicines included in the positive list was reduced and transition to the system of payment per case was started to be implemented in outpatient treatment. However, execution of this system of payment per case was stopped by the Council of State in October 2006. Moreover, based on the developments in the foreign exchange rates, pharmaceutical prices were increased by 5 per cent in the months of July, August and September.

The ratio of budget transfers to social security institutions in GDP is expected to be 4.1 per cent in 2006. The revenue obtained from the restructuring of SSK and BAĞ-KUR premium receivables and the increase of current premium revenues in SSK contributed to the 0.7 percentage points decrease in this ratio compared to the previous year. When the revenue obtained from the restructuring of premium receivables are excluded, it is observed that the ratio of budget transfers to social security institutions in GDP preserved its level of 2005.

As a result of these developments, during the January-October period of 2006, central government budget revenues and expenditures were realised as 140.5 billion YTL and 144.3 billion YTL, respectively. During the same period, the central budget deficit became 3.8 billion YTL and the primary surplus 37 billion YTL.

Box. 1. 3: Central Government Budget

By the central government budget, the scope of the budget has been expanded both in respect of the number of institutions and organizations and the details of revenues and expenses, thus the right of the Turkish Grand National Assembly (TGNA) in budget has been strengthened. Further, the principle of transparency and accountability has enhanced in the public.

The central government budget includes the budgets of the following:

I. General budget: public administrations included in the legal personality of the state (TGNA, Prime Ministry, Ministries, Higher Judiciary Bodies etc.)

II. Special budget: public administrations which are established under a ministry or to perform a specific public service, to which revenues are allocated, which is authorized to make expenditure out of such revenues, and for which the organization and working principles are laid out in a special law (Council of Higher Education, Universities, Student Selection and Placement Center etc.),

III. Budgets of regulatory and supervisory agencies: agencies which are organized as board, authority, or higher board by special laws (CMB, Radio and Television Supreme Council, Energy Market Regulatory Authority etc).

The central government budget which is prepared within the framework of principles and basic sizes indicated in the Medium Term Program and Medium Term Financial Plan, has included, for coming two years in addition to the current year, revenue and expense estimates, the amount of budget deficit or surplus if any, how the deficit will be made up or the surplus will be utilized, and the information related to revenues waived due to such practices as tax exemption, exception and discounts and similar practices, and introduces the multi-year budgeting approach to our country.

The central government budget differs from the consolidated budget in respect of fiscal size in that it has a wider scope than that of the consolidated budget and also the fund shares are indicated in the revenues and expenses.

Table: Central Government Budget Balance

(Per cent of GDP)

	2006*
Total Revenues	29.6
Total Expenditures	32.2
Total Non-Interest Revenues	23.6
Primary Surplus	6.0
Budget Balance	-2.6

* Initial appropriate.

Developments in the General Government Revenues and Expenditures

General government balance is obtained through consolidation of the revenues and expenditures of the consolidated budget/central government budget, local administrations, extra-budgetary funds, social security institutions, the unemployment insurance fund, universal health insurance and revolving funds.

The ratio of government revenues to GDP, which was 40.9 per cent in 2004, was realised as 43.9 per cent in 2005. The ratio of general government tax revenues to GDP, on the other hand, exceeded the previous year level by 1.3 percentage points. The increase in indirect tax collection played an important role in this increase. During the same period, the share of general government tax revenues in the general government total revenues receded back from 57.6 per cent to 56.7 per cent, compared to the previous year. The share of indirect taxes in the total taxes increased from 66.4 per cent to 66.9 per cent and the share of direct taxes in GDP, on the other hand, preserved its level of 2004. While as a ratio of GDP, a limited increase was observed in the general government non-tax revenues compared to the previous year, factor revenues rose by 1.1 percentage points due to the increase in interest revenues.

Table. 1. 9: Revenues and Expenditures of the General Government

(Per cent of GDP)

	2002	2003	2004	2005
Taxes	22.2	23.6	23.6	24.9
Direct	7.8	7.6	7.3	7.4
Indirect	14.0	15.1	15.6	16.6
Wealth	0.4	0.9	0.6	0.8
Non-Tax Revenues	3.2	3.1	3.1	3.3
Factor Incomes	7.4	6.4	6.9	8.0
Social Funds	6.1	6.6	7.0	6.9
Total	38.9	39.8	40.5	43.0
Privatisation Revenues	0.2	0.1	0.4	0.8
Total Revenues	39.1	39.9	40.9	43.9
Current Expenditures	17.6	17.5	17.7	17.5
Investment Expenditures	4.6	3.6	3.1	3.8
Fixed Investment	4.6	3.6	3.1	3.8
Change in Stocks	0.0	0.0	0.0	0.0
Transfer Expenditures	30.5	28.8	25.4	22.3
Current Transfers	29.4	28.1	24.6	21.8
Capital Transfers	1.0	0.6	0.8	0.5
Stock Revaluation Fund	0.0	0.0	0.0	0.0
Non-Interest Expenditure	33.4	33.1	32.8	34.0
Total Expenditures	52.7	49.9	46.2	43.6
Primary Surplus	5.7	6.8	8.1	9.8
Borrowing Requirement	13.6	10.0	5.3	-0.2
IMF-defined Primary Surplus	3.0	5.5	6.0	6.2
Borrowing Requirement Compatible with Fiscal Notification	12.9	11.3	5.8	0.7

Source: SPO
Note: Tax rebates are not included in the figures for revenues and expenditures.

The ratio of general government to total expenditures, which was realised as 46.2 per cent in 2004, went back to 43.6 per cent in 2005. While non-interest expenditures

increased by 1.2 percentage points during this period, the decrease in interest expenditures was realised as 3.8 percentage points. During the same period, an increase by 0.7 per cent of GDP was observed in investment expenditures.

As a result of these developments, the ratio of the general government borrowing requirement to GDP turned to a 0.2 per cent surplus from a 5.3 per cent deficit in 2004. During the same period, the ratio of the primary surplus to GDP, on the other hand, was realised as 9.8 per cent, with a 1.7 percentage points increase. As a percentage of GDP, the borrowing requirement harmonized with fiscal notification receded from 5.8 per cent in 2004, to 0.7 per cent in 2005.

Box. 1. 4: Adjustments in General Government Balance in the Context of Fiscal Notification

Through various adjustments, the deficit of the general government and the scope of the debt stock and accounting records are being harmonized with the budget deficit and debt definitions of the European Union and every year on 1 April, these are communicated to the relevant units of the European Union in the form of fiscal notification tables.

During preparation of fiscal reporting tables;

- Revenues and expenditures (duty losses of the state banks, etc.) which are defined as such in the ESA 95 rules but not included in the consolidated budget deficit are added to the budget; and accounts which do not comply with the definition of revenue (privatisation, revaluation differences, revenue of issuing coins, etc.) or expenditure (risk account, etc.) but which are included in the consolidated budget are eliminated from the budget,
- Revenues and expenditures, which are reported in the consolidated budget on a cash basis, are changed to the required values on an accrual basis. Interest expenditures on the public debt stock are calculated on an accrual basis and allocated to the year to which they belong.

The differences between the two definitions at the end of these adjustments are presented below.

Table.1: General Government Borrowing Requirement Compatible with Fiscal Notification

(Per cent of GDP)

	2002	2003	2004	2005
General Government Borrowing Requirement	**13.6**	**10.0**	**5.3**	**-0.2**
Privatisation Revenues	0.2	0.1	0.4	0.8
Risk Account	0.0	-0.3	-0.1	0.0
Claims and Credits (Net)	-0.9	-0.4	-0.4	-0.2
Paid and Accrued Interest Rate Differences	0.2	1.6	0.6	-0.1
Duty Loss of State Banks	0.0	0.2	0.0	0.0
Other	-0.2	0.1	0.0	0.5
General Government Borrowing Requirement (Compatible with Fiscal Notification)	**12.9**	**11.3**	**5.8**	**0.7**

Source: SPO, Ministry of Finance, Undersecretariat of Treasury

Table.2: General Government Debt Stock Compatible with Fiscal Notification

(Per cent of GDP)

	2002	2003	2004	2005
General Government Debt Stock	**88.7**	**79.3**	**74.0**	**68.2**
Adjustment Items	**4.4**	**5.8**	**2.9**	**1.4**
Adjustment Items for Central Government	6.0	8.3	6.1	4.8
Adjustment Items for Local Administrations	0.0	0.0	0.1	0.1
Adjustment Items for Social Security Institutions	-1.6	-2.5	-3.3	-3.5
General Government Debt Stock (Compatible with Fiscal Notification)	**93.0**	**85.1**	**76.9**	**69.6**

Source: SPO, Ministry of Finance, Undersecretariat of Treasury

General Government Debt Stock Compatible with Fiscal Notification is calculated in nominal terms by making necessary consolidations in and among sectors.

Public Debt Stock

The economic programme being implemented since 2002, fiscal discipline and political stability have increased the efficiency of debt management. In this context, the ratio of the general government gross debt stock to GDP continued to display its downward trend and went back to 69.2 per cent at the end of 2005, from 74.7 per cent in 2004.

Table. 1. 10: General Government Gross Debt Stock

(Per cent of GDP)

	2002	2003	2004	2005
Domestic Debt	54.7	54.8	52.9	51.0
External Debt	34.7	25.3	21.9	18.1
Total	89.3	80.1	74.7	69.2

Source: SPO, Undersecretariat of Treasury
Note: Debt stock includes gross debt of general government (total public sector excluding SEEs). Therefore, the definitional difference should be taken into account when comparing these figures with the net public debt stock including SEEs, which is announced by Undersecretariat of Treasury.

The central government domestic debt stock rose from 224.5 billion YTL as of the end of 2004 to 244.8 billion YTL at the end of 2005. When it is considered in terms of its ratio to GDP, on the other hand, it is observed that the central government domestic debt stock receded from 52.1 per cent in 2004, to 50.2 per cent in 2005. As of the end of September 2006, the central government domestic debt stock realised as 250.9 billion YTL.

Table. 1. 11: Composition of Central Government Domestic Debt Stock

	2002	2003	2004	2005	2006 Sep.	2002	2003	2004	2005	2006 Sep.
	At Current Prices, In Billion YTL					Percentage Distribution				
Cash	89.3	130.5	165.6	194.2	203.8	59.6	67.1	73.8	79.3	81.3
Fixed Rate	37.6	68.6	94.9	101.4	110.8	25.1	35.3	42.3	41.4	44.2
Floating Rate	17.4	29.1	36.3	57.9	59.0	11.6	15.0	16.2	23.7	23.5
FX Denominated	16.5	16.8	26.6	30.8	34.0	11.0	8.7	11.9	12.6	13.6
FX Indexed	17.8	16.0	7.7	4.0	0.0	11.9	8.2	3.4	1.7	0.0
IMF Credits	9.7	8.5	3.7	0.0	0.0	6.5	4.4	1.6	0.0	0.0
Swap	7.6	7.5	4.0	4.0	0.0	5.1	3.8	1.8	1.7	0.0
Others	0.5	0.0	0.0	0.0	0.0	0.3	0.0	0.0	0.0	0.0
Non-Cash	60.6	63.9	58.9	50.6	47.0	40.4	32.9	26.2	20.7	18.7
Fixed Rate	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Floating Rate	46.7	54.1	53.8	47.5	45.2	31.2	27.8	24.0	19.4	18.0
FX Denominated	11.9	7.9	3.4	1.6	0.0	7.9	4.1	1.5	0.7	0.0
FX Indexed	2.0	1.9	1.7	1.5	1.8	1.3	1.0	0.8	0.6	0.7
Total Stock	149.9	194.4	224.5	244.8	250.9	100.0	100.0	100.0	100.0	100.0

Source: Undersecretariat of Treasury

In the scope of the borrowing strategies followed towards alleviating foreign exchange currency risks, the borrowing was continued to be made mostly in YTL. The share of YTL denominated debt stock in the central government domestic debt stock

rose from its 2005 end-year level of 84.5 per cent to 85.7 per cent as of the end of September 2006.

While borrowing was mostly realised through fixed rate bonds, issuance of floating rate notes was also included with the aim of extending the maturity. While the share of fixed rate bonds in the central government domestic debt stock was 45.4 per cent for 2005, this ratio was realised as 47.9 per cent as of the end of September in 2006.

Table. 1. 12: Interest Composition of Central Government Domestic Debt Stock

	2003	2004	2005	2006 Sept.	2003	2004	2005	2006 Sept.
	At Current Prices, In Billion YTL				Percentage Distribution			
Fixed Rate	85.0	115.6	111.1	120.1	43.7	51.5	45.4	47.9
Floating Rate	109.4	108.9	133.7	130.8	56.3	48.5	54.6	52.1
Total	194.4	224.5	244.8	250.9	100.0	100.0	100.0	100.0

Source: Undersecretariat of Treasury

Realization of the amortizations of an important part of non-cash bonds issued in 2001 within the recent years led to a decrease in the average maturity of the debt stock. In spite of this, with the fixed and floating rate bonds with 5 years maturity, which were started to be issued in 2005, the average maturity of the central government domestic debt stock increased gradually. The average maturity of the central government domestic debt stock was 20.6 months in 2004, 23.5 months in 2005, and 24.2 months as of September 2006.

Table. 1. 13: Maturity Structure of the Central Government Domestic Debt Stock

	2002	2003	2004	2005	2006 Sep.
	Average Maturity (Month)				
Cash	12.8	12.4	11.8	19.6	22.3
Non-Cash	60.4	51.2	45.5	38.7	32.4
Total	32.1	25.1	20.6	23.5	24.2

Source: Undersecretariat of Treasury

The share of the public sector in central government total domestic debt stock, which reached the level of 66 per cent due to the bonds issued for duty losses and capital injection to public banks in 2001 and those issued to the Savings Deposit Insurance Fund for the restructuring in the banking sector, continued to decrease and declined to 30.8 per cent in 2005 and 30 per cent as of September 2006.

The cost of discounted borrowing in YTL, which was realised as 23.1 per cent during December 2004, continued its rapid downward trend during the first quarter of 2004. However, it displayed a slight increase with the withdrawal of foreign investors from the developing markets during April and May, in the framework of the prospects that the US Federal Reserve Bank would continue to increase the interest rates. With the impacts of the fluctuations arising from foreign markets alleviated following the month of June, and especially with the decision to start the full membership negotiations with the EU during October, the borrowing interest rates reentered the

stage of a downward trend. The cost of discounted borrowing in YTL realised as 14.2 per cent in December 2005.

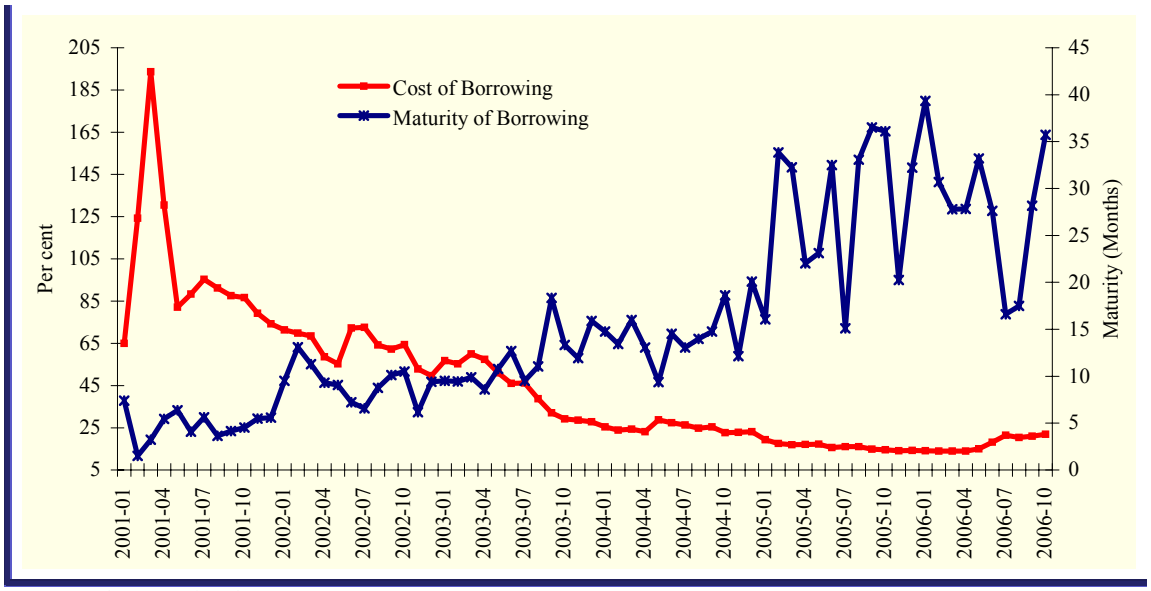
Table. 1. 14: Domestic Debt Stock Composition by Lenders

	2002	2003	2004	2005	2006 Sep.	2002	2003	2004	2005	2006 Sep.
	At Current Prices, In Billion YTL					Percentage Distribution				
Total	149.9	194.4	224.5	244.8	250.9	100.0	100.0	100.0	100.0	100.0
Public	79.1	92.6	88.3	75.5	75.2	52.8	47.7	37.1	30.8	30.0
CBRT	18.4	18.4	18.4	18.4	17.9	12.3	9.5	8.2	7.5	7.1
State Banks	24.3	27.2	27.5	25.0	23.4	16.2	14.0	12.2	10.2	9.3
SDIF Banks	11.0	15.1	8.3	4.5	4.8	7.4	7.7	3.7	1.8	1.9
IMF Credits	9.7	8.5	3.7	-	-	6.5	4.4	1.6	-	-
Other	15.7	23.4	25.4	27.5	29.1	10.5	12.1	11.3	11.2	11.6
Market*	70.8	101.8	141.1	169.3	175.6	47.2	52.3	62.9	69.2	70.2

Source: Undersecretariat of Treasury
* The figure which indicates market includes SDIF Banks' deposit transfers (4.4 billion of YTL) for December 2001.

In the framework of the structural reforms continued in the scope of the economic programme being implemented and developments in the area of privatisation, the positive atmosphere in the markets continued during the January-April 2006 period as well. However, along with the fluctuation in foreign markets starting with May, increasing hesitations concerning the inflation target and current account deficit, an increase was observed in the borrowing interest rates and in this framework, secondary market interest rates exceeded 22 per cent in June. In this period, with the suspension of fixed coupon auctions, increasing the share of floating rate notes and keeping the debt conversion rates low, the increase of borrowing costs were limited and as a result of the fiscal and monetary measures taken, the secondary market interest rates receded back to 19 per cent in September.

Figure. 1. 6: Maturity and Cost of Treasury's Borrowing



Source: Undersecretariat of Treasury

The average real interest of the domestic debt stock, which was 9.5 per cent at the end of December 2004, was realised as 8 per cent at the end of 2005 and as 7.7 per cent as of August in 2006.

The average maturity of the cash domestic borrowing, which was 14.6 months in 2004, was realised as 27.4 months in 2005 and exceeded 30 months during the January-April period of 2006. On the other hand, as a result of the shortening of maturities with the fluctuations in the market starting in May, the average maturity of domestic borrowing went back to 27 months during the January-September period of 2006.

Since 2001, general government foreign debt stock is composed of medium and long-term foreign debts.

The share of loans obtained from international organizations in the general government foreign debt stock which approximately doubled as a result of 2001 crisis was 35.7 per cent in 2002, 36.7 per cent in 2003 and 38.1 per cent in 2004. The share of loans obtained from international organizations in the foreign debt stock decreased by 4 percentage points during the second quarter of 2006 compared to the end of 2005, and realised as 30.1 per cent. In addition, the share of loans obtained from commercial banks and other private creditors in the general government foreign debt stock, which was 57.9 per cent in 2005, became 62.2 per cent during the second quarter of 2006.

The share of dollar denominated loans in general government foreign debt stock, which was approximately 41 per cent between 2002-2004, rose to 48.6 per cent in 2005 and 51.6 per cent during the second quarter of 2006. The share of SDR denominated loans, which remained at 25 per cent during the years of 2002-2004, on the other hand, went back to 17.4 per cent during the second quarter of 2006. The share of euro denominated loans, which was in a downward trend until the end of 2005, increased to 26.5 per cent during the second quarter of 2006, with an increase by 2.1 percentage points.

Table. 1. 15: The Structure of General Government External Debt Stock

	In Million Euros					Percentage Distribution				
	2002	2003	2004	2005	2006 June	2002	2003	2004	2005	2006 June
By Maturity	56,472	52,123	51,502	55,674	52,150	100.0	100.0	100.0	100.0	100.0
Short-Term	0	0	0	0	0	0.0	0.0	0.0	0.0	0.0
Medium and Long-Term	56,472	52,123	51,502	55,674	52,150	100.0	100.0	100.0	100.0	100.0
By Lender	56,472	52,123	51,502	55,674	52,150	100.0	100.0	100.0	100.0	100.0
International Organizations	20,153	19,121	19,602	18,974	15,671	35.7	36.7	38.1	34.1	30.1
Government Institutions	6,772	5,712	4,882	4,450	4,049	12.0	11.0	9.5	8.0	7.8
Commercial Banks	17,051	15,428	15,868	18,169	18,258	30.2	29.6	30.8	32.6	35.0
Other Private Creditors	12,497	11,862	11,151	14,081	14,172	22.1	22.8	21.7	25.3	27.2
By Currency	56,472	52,123	51,502	55,674	52,150	100.0	100.0	100.0	100.0	100.0
USD	22,755	21,103	21,805	27,074	26,912	40.3	40.5	42.3	48.6	51.6
JPY	4,203	2,993	2,110	1,949	1,723	7.4	5.7	4.1	3.5	3.3
EUR	14,493	13,603	13,237	13,584	13,810	25.7	26.1	25.7	24.4	26.5
SDR	13,385	13,389	13,557	12,386	9,096	23.7	25.7	26.3	22.2	17.4
Other	1,636	1,035	794	682	609	2.9	2.0	1.5	1.2	1.2

Source: Undersecretariat of Treasury

The main reasons for the change in the structure of the debt stock are the net payer position of Turkey regarding foreign credits, IMF credits in particular during the recent years, and net borrower position within international bond markets.

2. MACROECONOMIC FRAMEWORK

Main Objectives of the Macroeconomic Policy

The objectives economic policies to be implemented during the 2007-2009 period will be increasing the welfare of the society in harmony with the *Turkey, growing with stability, sharing her income more equitably, having competitiveness at the global scale, being in the process of transforming into the information society and having completed her coherence process for EU membership* vision of the Ninth Development Plan (2007-2013)[2]. In this respect, along with the implementations towards continuing and strengthening the macroeconomic stability achieved during the recent period, efforts will be continued to diversify the social policy implementations within the budgetary constraints.

Following the official commencement of the negotiation process for full membership to the EU on 3 October 2005, screening in 35 chapters were started and they were finalized as of the end of October 2006. Within the continuing membership process, economy policies will be implemented with the fundamental perspective of developing the existing market economy and providing the economy with a more dynamic and highly competitive structure in harmony with the Copenhagen economic criteria. As a matter of fact, increasing competitiveness has been determined as one of the development axes of the Ninth Development Plan.

During the 2006 PEP period, the fundamental priority of Turkey's macroeconomic policies is ensuring the sustainability of growth, and thus continuation of per capita income convergence with the EU average. In this context, ensuring price stability, decreasing the ratios of public deficit and public debt stock to GDP and hence fulfilling the Maastricht criteria in this respect and continuing the structural reforms, are among the fundamental goals of the policies to be implemented. In this context, the economic policies to be implemented will contribute to the process of convergence to the Maastricht criteria, where a remarkable progress has been achieved especially in the recent years.

During the 2006 PEP period, in order to strengthen the market economy and increase competitiveness; continuing to reduce the weight of the public sector in the economy through privatisation, strengthening regulatory and supervisory roles of regulatory and supervisory institutions, encouraging private entrepreneurship and eliminating the legal and economic uncertainties that adversely affect the functioning of the free market have specific importance in the Turkish economy. In addition, reducing the deficiencies and imbalances in the areas of education and health, improving the quality of the labour force, strengthening the relationship between the labour market and the educational system and decreasing inter-regional development gaps are the other prior topics of the ongoing economic and social policies.

Fiscal Policy

The current fiscal policy, which brought about a significant improvement in fiscal balances, will be continued during the 2006 PEP period. In this context, permanently decreasing the ratio of the public debt stock to national income and public deficits, achieving a balanced budget structure, contributing to the sustainable growth environment and supporting the struggle against inflation will be the main goals.

[2] Detailed information about the Ninth Development Plan is presented in Box 2.1.

Box. 2. 1: Ninth Development Plan (2007-2013)

Development Plans, which have been prepared since the 1960's with the aim of ensuring economic and social development through efficient utilization of resources, are binding on the public sector and guiding for the private sector.

Taking the 9th Development Plan Strategy adopted by the Council of Ministers as basis, The Ninth Development Plan, covering the period of 2007-2013, was prepared with the contributions of all public institutions and organizations under the coordination of the State Planning Organization and accepted by the Turkish Grand National Assembly on 28 June 2006. In this Plan, a strategic approach that would increase predictability through considering macroeconomic balances, bring forth the institutional and structural regulations to allow for a more efficient functioning of markets, prioritise problems, and concentrate on main objective and priorities, was adopted.

The vision of the Ninth Development Plan has been determined as *"Turkey, growing with stability, sharing her income more equitably, having competitiveness at the global scale, being in the process of transforming into the information society and having completed her coherence process for EU membership"*. In the framework of this vision, with the aim of sustaining economic growth and social development in a stable structure, five development axes focused on the fundamental problematic areas have been determined. Under each development axis, prioritised policy areas have been identified in order to achieve the main objective of the development axis in question. In addition, sectoral and thematic policies and priorities have been taken up under these axes and made correlated with each other in a way to serve the same strategic goal.

The first axis, which will be prioritised in all policies, is *Increasing Competitiveness*. According to this, the main objective is to provide the economy with a stable and highly productive structure, which has a high technological capability and a qualified labour force, which rapidly adapts to changing conditions, and which is competitive in national and international markets. To this end, making macroeconomic stability permanent, improving the business environment, reducing informality in the economy, improving the financial sector, improving the energy and transportation infrastructure, protecting the environment and improving the urban infrastructure, developing R&D and innovativeness, spreading information and communication technologies, rendering the agricultural infrastructure more efficient and ensuring transition to a high value added production structure in industry and services will constitute the prioritised areas.

The second development axis has been determined to be I*ncreasing Employment*. In the framework of sustainable employment-focused growth, improving employment opportunities by improving the quality of the labour force as required by a competitive economy and knowledge society, decreasing unemployment, strengthening the relationship between education and employment and making the labour market more effective are the goals to be achieved under this axis.

Strengthening Human Development and Social Solidarity is the third development axis. The main objective of the policies to be implemented within this scope will be to raise the quality of life and prosperity through ensuring that all segments of the population particularly women, children, handicapped and poor people sufficiently benefit from the basic public services such as education and health and from a multidimensional social protection. Ensuring an inclusive and sustainable health and social security system, increasing efficiency of social services, improving income distribution, social inclusion and fighting against poverty, protecting and improving culture and strengthening social dialogue will be the fundamental priority areas.

The fourth development axis is *Ensuring Regional Development*. The main objective in regional development policies is to increase contribution to national development, competitiveness and employment through triggering the potential and thereby increasing productivity of regions and to decrease the development differences among regions and between rural and urban areas. In this context, activities towards increasing the coherence and effectiveness of policies at the central level, ensuring development based on local dynamics and internal potential, increasing institutional capacity at the local level and accelerating rural development will be emphasized.

The main purpose of the last development axis, which has been determined as *Increasing Quality and Efficiency in Public Services*, is to provide public administration with a structure that respects human rights and that is citizen-oriented and that can provide services with high quality in an effective and rapid manner, in the framework of rule of law, flexibility, transparency, participation and accountability. With the aim of increasing quality and effectiveness in public services; duties, authorities and functions of public institutions and organizations will be reviewed, repetitions in this area will be eliminated, policy making, cost accounting and implementation capacities of institutions and organizations will be increased, human resources will be developed, information and communication technologies will be efficiently benefited from in the provision of public services to citizens and effective provision of justice and security systems will be ensured.

Participation was shown due diligence during the preparation of the Plan. With this aim, various Special Ad hoc Committees (SAC) covering a wide range of areas were established and persons from the pubic sector, the private sector, universities and non-governmental organisations participated in the these commissions. Along with the institutional knowledge and experience, SAC reports were also benefited from in the preparing process of the Plan.

In an era where globalisation is pervasive in all areas, competition is intense and uncertainties increase, the Ninth Development Plan has been prepared as a fundamental policy document that sets forth the transformations Turkey will realize in economic, social, and cultural areas in an integrated approach. With this understanding, the period covered by the Plan, which was designed as the fundamental document to contribute to the EU membership process has been determined as 7 years, in a way to cover the years between 2007-2013, taking the EU financial programming into consideration as well. In addition, the Plan will also form the basis for the Pre-Accession Economic Plan and the Strategic Coherence Framework as well as other national and regional plans and programs, and sectoral and institutional strategy documents and by ensuring coherence among the these mentioned documents with different functions, the Plan will play an important role in directing all planning activities.

Note: Full text of the Ninth Development Plan will be available in SPO's web address, http://www.dpt.gov.tr.

In this context, efforts towards increasing tax revenues through expanding the tax base and reducing informal economy and ensuring efficiency in public expenditures will be continued as in the previous years. Therefore, implementation of the tight fiscal policy to meet the primary surplus targets will be continued in 2007-2009 period.

Monetary and Exchange Rate Policy

Within the framework of the main objective of price stability, the Central Bank started to implement implicit inflation targeting in 2002 and shifted to explicit inflation targeting at the beginning of 2006 upon the completion of the necessary preparations and provision of the appropriate economic environment. In this period, a significant progress has been made in reducing the high inflation rates. Single digit medium-term inflation targets confirm the decisiveness for ensuring price stability and fulfilling the related Maastricht criterion. Monetary policy will be continued in the same framework during the 2006 PEP period as well.

Foreign exchange rates are determined by the supply and demand conditions in the market within the scope of the floating exchange rate regime; however, the Central Bank could intervene in the foreign exchange market to prevent existing and potential excess volatility in the foreign exchange rates. Additionally, in order to accumulate reserves, the Central Bank could hold foreign exchange purchase auctions in a pre-announced schedule considering the developments regarding balance of payments and currency substitution.

Incomes Policy

Determination of the incomes policy in line with the inflation targets has great importance to make the success achieved in the struggle against inflation, permanent. Therefore, incomes policy will be determined considering the inflation targets in the short-term and price stability, productivity and profitability in the medium-term. In the framework of the ongoing economic programme, implementation of forward-looking indexation will be continued in the public sector wage policy.

Structural Reform Policies

Structural reforms have played an important role in the recent improvements obtained towards achieving a highly competitive economic structure, which is based on market principles and allows for sustainable growth. Together with the commencement of the membership negotiations, structural reforms have also gained importance in terms of integration with the EU.

In this scope, strengthening the market mechanism, increasing the role of the private sector in the economy through decreasing the share of the state, developing the intermediary capacity of the financial sector in a way to meet the funding needs of the real sector and improving the qualifications of the labour force as required by the contemporary world, are the main goals of structural reforms. In addition to these, with the aim of increasing efficiency in public services administrative reforms will be continued. Furthermore in the agricultural sector, reform activities for increasing productivity and competitiveness and ensuring efficient utilization of resources, will be continued as well.

External Factors

Assumptions about the world economy used in macroeconomic analyses and forecasts of the Pre-Accession Economic Programme are based on the most recent forecasts of institutions like the European Commission and the IMF.

The crude oil barrel price, which floated around 34 dollars in 2004, rose to 53 dollars in 2005 with an increase beyond expectations. However, in spite of this increase, the world growth rate decreased only by 0.4 percentage points compared to 2004 and was realised as 4.8 per cent. The world output growth is expected to be 5.1 per cent in 2006 and around 4.7 per cent on average during the 2007-2009 period[3].

It is expected that the increase in oil prices will continue in 2006 and the crude oil barrel price will be 65.6 dollars. This figure is expected to be 66.3 dollars in 2007 and maintain this level during the 2008-2009 period.

The growth rate of EU-25, which is important in terms of the export performance of Turkey, is expected to increase by 1.1 percentage points compared to 2005 and to realise as 2.8 per cent in 2006. It is assumed that the growth rate will slow down slightly and realize around 2.4 per cent during the 2007-2009 period.

In 2005, the US economy entered into an inflationary period and CPI (Consumer Prices Index) inflation, which was 2.7 in 2004, was realised as 3.4 per cent. This rate is expected to increase slightly and reach 3.6 per cent in 2006. On the other hand, it is assumed that CPI inflation will decline significantly during the 2007-2009 period and realize around 2.3 per cent annually on average[4].

2.1. Growth and Employment

The Turkish economy displayed a high growth performance with the help of the decisively implemented structural reforms and macroeconomic policies following the 2001 crisis as well as of a favourable international environment and became one of the fastest growing countries among the OECD countries in 2005. The high growth performance also continued in the first half of 2006. In addition, with the impact of the fluctuations in the second quarter of 2006, a decrease in the risk appetite of the financial capital was observed. As a result of this, as in other emerging markets, financing costs increased in Turkey as well, based on the increasing risk premium. Thus, while an increase was experienced in real interest rates and inflation rates during the second half of 2006, a slowdown emerged in growth indicators. However, this slowdown is expected to be limited and the GDP growth rate is estimated to realize as 6 per cent in 2006. As the necessary interventions have been made by the economy management, the long-term impact of the fluctuations and the risk premium increase experienced in 2006 is expected to be limited.

An important change in the framework and priorities of the economic policy is not expected during the 2007-2009 period. In this scope, the macroeconomic forecasts for the 2007-2009 period have been made under the assumption that the existing economic policy will be sustained.

As known, the Turkish economy displayed an important performance in terms of exports during the 2001-2005 period and increased its export level more than two-fold. Labour productivity increase, competitive wage levels, access to new markets and

[3] European Commission DG ECFIN 2006 Fall Estimates.
[4] IMF World Economic Outlook Report, September 2006.

product diversification were the factors behind this success. In the 2006 Pre-Accession Economic Program period, economic growth is projected to be driven mainly by exports.

Average GDP growth rate is expected to be 5.5 per cent during the 2007-2009 period. In order to bring the inflation, which diverged from the target path during the second half of 2006 with the impact of international fluctuations, back to its target path, the Central Bank will maintain its cautious stance in the interest rate policy in 2007 as well. In this context, with the impact of the interest rates that are expected to stay relatively high, the slowdown in growth that started in the second half of 2006 is expected to continue in 2007 as well and the growth rate is estimated to decline to 5 per cent. During the 2008-2009 period, on the other hand, it is projected that interest rates will decline as inflation returns to its target path and therefore the growth rate will increase slightly.

Demand Components of Growth

GDP growth rate for 2005 was projected to be 5 per cent in the 2005 Pre-Accession Economic Programme. However, the economy displayed a high performance beyond expectations and the growth rate was realised as 7.4 per cent. Examining the composition of the growth rate of 2005, it is observed that an increase was experienced in almost all demand components of growth. Contrary to the expectations that the implemented tight fiscal and monetary policies would restrict growth, private investment and consumption expenditures were realised well over the 2005 PEP estimates. As a result of this, imports of goods and services were realised higher than the 2005 PEP projection. Moreover, the realization of exports of goods and services over the forecasts alleviated the negative impact of the increase in imports on trade deficit to some extent.

Table. 2. 1: Demand Components of Growth

(Percentage Change at 1987 Prices)

		Forecast			
	2005	**2006**	**2007**	**2008**	**2009**
Total Consumption Expenditures	8.1	7.9	3.6	5.3	5.7
Private	8.8	7.6	3.3	5.3	5.8
Public	2.4	10.0	6.0	5.1	4.6
Total Investment Expenditures	10.3	4.9	5.3	5.4	7.3
Gross Fixed Capital Formation	24.0	11.6	6.0	6.0	8.1
Private Fixed Investment	23.6	14.0	6.0	6.5	8.2
Public Fixed Investment	25.9	1.2	5.8	3.8	7.8
Changes in Inventories (1)	-2.5	-1.6	0.0	0.0	0.0
Exports of Goods and Services	8.5	6.7	11.0	11.8	10.9
Imports of Goods and Services	11.5	9.3	7.9	10.6	11.1
Gross Domestic Product	7.4	6.0	5.0	5.6	5.9
Gross National Product	7.6	6.0	5.0	5.7	6.0

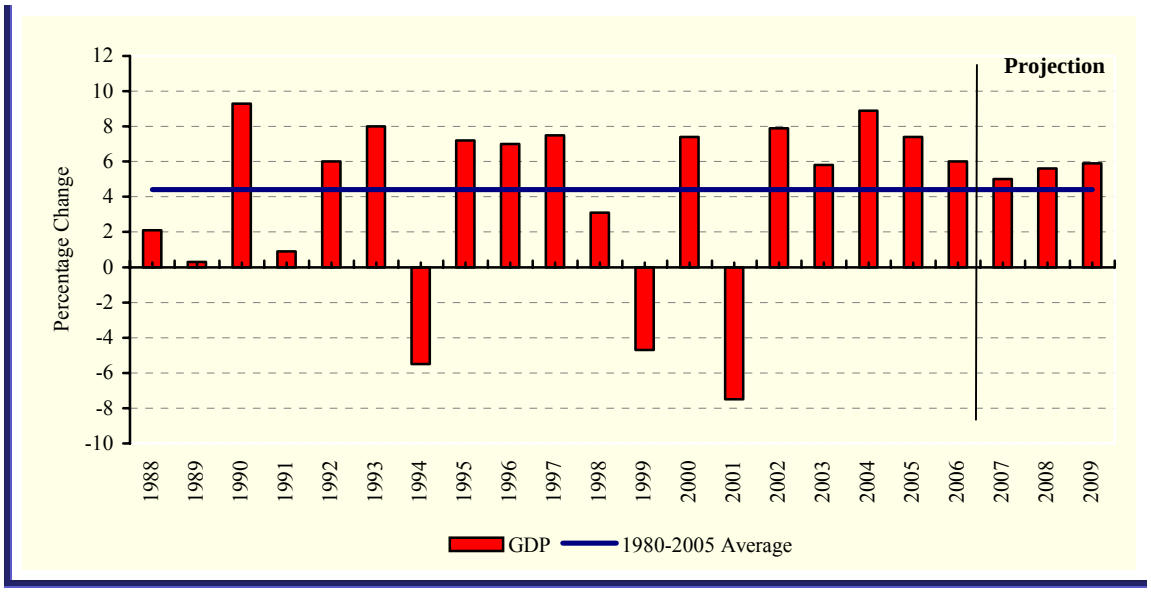
Source: SPO, TURKSTAT
(1) Reported as the contribution to GDP growth.

It is estimated that the growth rate of the economy will slow down in 2006 and the GDP growth will be 6 per cent. The reasons for this slowdown are the deviation of inflation from the target path as a result of the fluctuations experienced in the

international financial markets and thereby the increase in the short-term interest rates used as the policy instrument. In this context, it is expected that the growth rate of private investment expenditures will decline significantly in 2006, compared to 2005, and recede to 14 per cent. On the other hand, it is estimated that the private consumption expenditures will increase by 7.6 per cent in 2006. Public investment, which displayed a significant increase in real terms in 2005, is expected to sustain its previous year level. Public consumption expenditures displayed an increase beyond expectations in the first half of 2006. One of the most important reasons behind this is the substantial increase in health expenditures owing to the transformations realised in the health sector. Therefore, public consumption expenditure is expected to increase by 10 per cent throughout 2006.

Exports of goods and services constituted the driving factor behind high growth in the 2002-2004 period by an average annual increase rate of 13.2 per cent. However, growth rate of exports decreased in 2005 and this trend continued in 2006. Thus, the growth rate of exports is estimated to remain below the 2002-2004 average and to realize as 6.7 per cent in 2006. Along with this, growth rate of imports is also expected to decline as a result of the slowdown in economic growth and realize as 9.3 per cent.

Figure. 2. 1: GDP Growth Rate

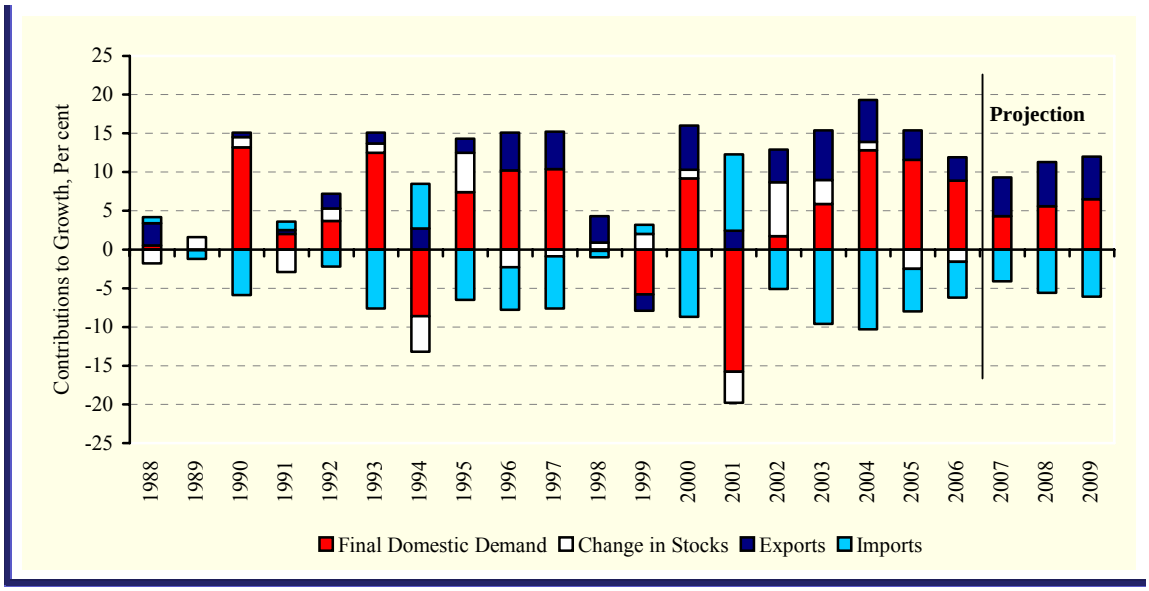


The Turkish economy is expected to grow around an annual average rate of 5.5 per cent during the 2007-2009 period. Decisive implementation of tight monetary and fiscal policies will continue during the 2006 Pre-Accession Economic Programme period. In addition, it is expected that economic growth will be driven by investments and exports.

During the 2007-2009 period, the growth in private consumption expenditures is expected to realize below the GDP growth and realize at an annual average rate of 4.8 per cent. On the other hand, public consumption expenditures are projected to increase approximately around the growth rate. During the same period, private and public fixed capital investments are estimated to increase by 6.9 per cent and 5.8 per cent annually on average, respectively. In the 2006 Pre-Accession Economic Programme period, exports are expected to regain momentum and exports of goods and services are

expected to increase by 11.2 per cent annually on average. On the other hand, imports of goods and services are projected to increase by 9.9 per cent.

Figure. 2. 2: Contributions to GDP Growth



Savings-Investment Balance

The share of private fixed capital investments in GDP was realised as 15.5 per cent in 2005. Since private sector fixed capital investments grew faster than GDP during the 2006-2009 period, the share of private fixed capital investments in GDP is expected to reach 17.2 per cent at the end of the period.

The share of public investments in GDP was realised as 4.3 per cent, consistent with the 2005 PEP estimates. The share of public investments in GDP is projected to increase slightly and realize around 5 per cent during the 2006 PEP period.

Table. 2. 2: Total Savings-Investment Balance

(Per cent of GDP)

		Forecast			
	2005	**2006**	**2007**	**2008**	**2009**
Total Investment	25.1	24.8	24.8	24.7	25.0
Fixed Capital Formation	19.8	21.5	21.7	21.8	22.2
Public	4.3	4.9	5.0	4.9	5.0
Private	15.5	16.6	16.7	16.9	17.2
Change in Stocks	5.3	3.3	3.1	2.9	2.8
Total Savings	25.1	24.8	24.8	24.7	25.0
Domestic Savings	18.4	16.7	17.2	17.9	19.0
Public	4.0	5.3	3.5	4.5	5.0
Private	14.4	11.4	13.7	13.4	14.0
Foreign Savings	6.7	8.1	7.6	6.8	6.0

Note: The savings-investment balance is based on the TURKSTAT figures of GDP by expenditures. Public investments in the table include the investments of the SEEs in addition to those of the general government.

Due to the implemented tight fiscal policy, the public disposable income increased significantly during 2005 and the ratio of public savings to GDP was realised as 4 per cent. It is projected that this structure will also continue during the 2006 PEP period. As a result of this, the ratio of public savings to GDP is expected to realize around 4.5 per cent during the 2006-2009 period.

Sources of Growth

As a result of the speeding up of the contraction in agricultural employment starting from 2005, the desired increase in total employment could not be achieved. Hence, it was observed that the driving force of the high growth in 2005 was the total factor productivity (TFP). Transformation of the employment structure in favour of the sectors with higher productivity levels may be shown as the main reason of this high TFP increase. In this context, while the contribution of TFP to growth was 74.7 per cent in 2005, the contributions of capital accumulation and employment to growth were calculated as 15.8 and 9.5 per cent, respectively.

Table. 2. 3: Growth Rates of Factors of Production

(Per cent)

Period	GDP	Capital Stock	Employment	TFP
2004	8.9	3.3	3.0	5.6
2005	7.4	2.7	1.2	5.5
2006	6.0	4.1	0.3	4.0
2007	5.0	4.8	1.5	2.1
2008	5.6	4.6	1.7	2.6
2009	5.9	4.3	1.9	2.9
2006-2009	5.5	4.6	1.7	2.5

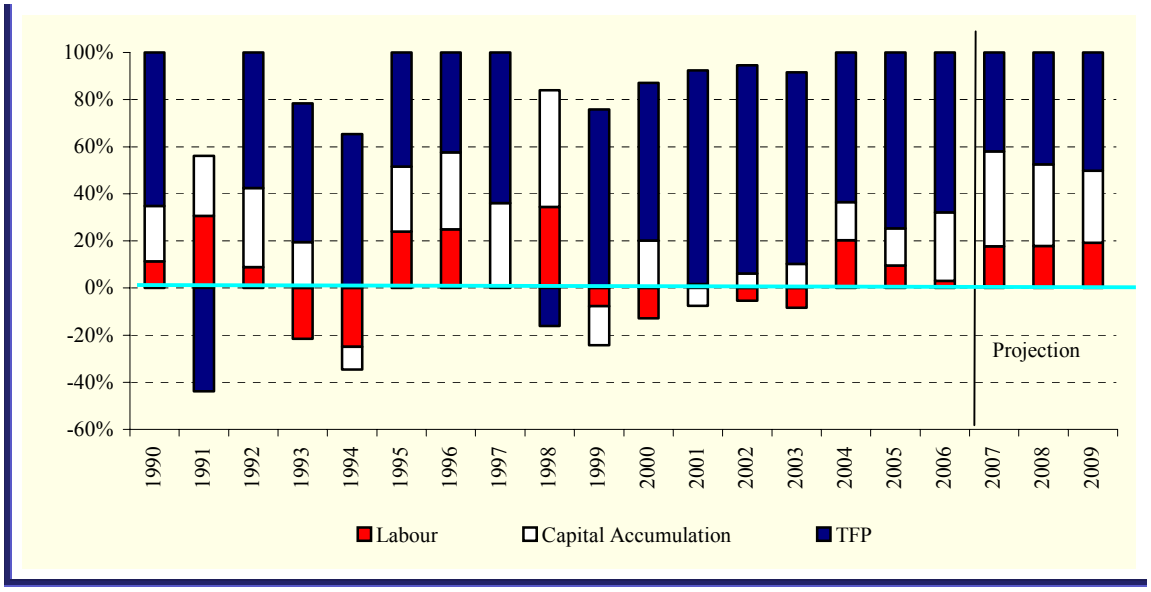
The growth rates projected for the 2006-2009 period are expected to be backed by the productivity increase, and the capital accumulation in particular. It is estimated that the contribution of total factor productivity to growth will be 46.9 per cent on average, and the contribution of capital accumulation will be 34.9 per cent on average during this period.

Table. 2. 4: Contribution to Growth by Factors of Production

(Per cent)

Period	Capital Accumulation	Employment Increase	TFP Increase
2005	15.8	9.5	74.7
2006	29.2	3.0	67.8
2007	40.3	17.7	42.0
2008	34.6	17.8	47.6
2009	30.7	19.1	50.2
2006-2009	34.9	18.2	46.9

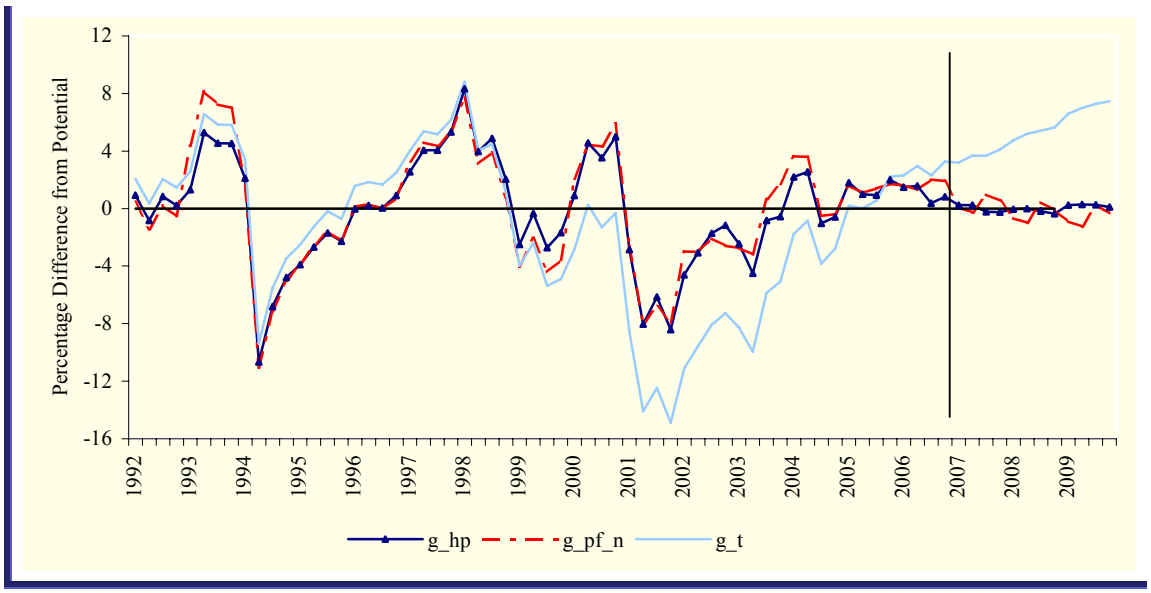
Figure. 2. 3: Contribution to Growth by Factors of Production



Potential Output

The level of production is expected to realize around the potential output during the 2006 PEP period. Figure 2.4 shows calculated output gap series based on three different methods, namely the linear method, the Hodrick-Prescott method and the production function method.

Figure. 2. 4: Output Gap



g_hp : Output gap calculated by Hodrick-Prescott method.
g_pf_n : Output gap calculated by using production function and variable NAIRU assumption.
g_t : Output gap calculated by linear method.

It is seen in this figure that the output gap calculated by the linear method points out to a warming up starting from 2005. The main reason for this situation is that the average growth rate was pulled down by the low growth rates recorded throughout the 1990s. However, it is considered that the Turkish economy has experienced a structural

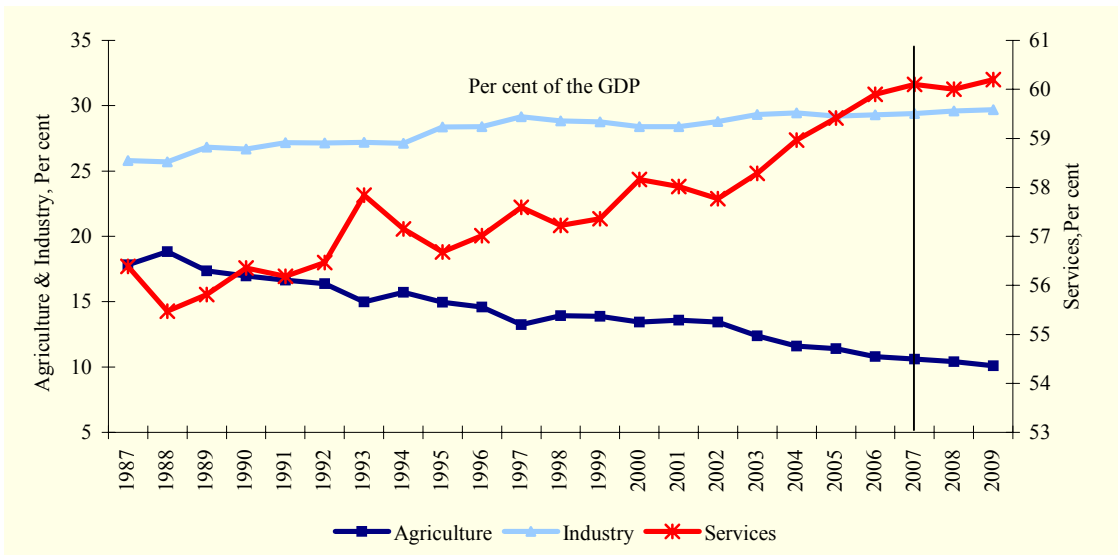
break following the year 2000 and the potential growth level rose in this period. When this analysis is replicated with the segmented trend assumption for post 2000, it is observed that the warming up indications disappear.

On the other hand, output gap values calculated according to the production function and Hodrick-Prescott methods do not indicate warming up in the economy and support the view that the growth potential has increased. Depending on the estimated increases in investment and employment, it is expected that the projected growth path will not have an inflationary impact during the 2006 Pre-Accession Economic Programme period.

GDP Growth by Sectors

The share of the agricultural sector is quite low in developed countries. For instance, the share of agriculture in total production was 1.9 per cent in the European Union (EU-25) countries in 2005. The Turkish economy has also been transforming into a structure based on industry and services. The share of agriculture in total production, which was around 17 per cent in 1987, receded back to 11.4 per cent in 2005.

Figure. 2. 5: Production by Sectors



The share of agriculture in total production is expected to decline to 10.1 per cent by the end of the 2006 PEP period. It is estimated that the growth rates of the industry and services sectors would be higher than that of GDP during the same period, and in this context the sectoral composition of production will be transformed in favour of the industry and services sectors. Figure 2.5 shows the realizations for the 1987-2005 period and the projections for the 2006-2009 period.

Table. 2. 5: Value Added by Sectors

(At 1987 Prices, Per cent)

	Realization			Forecast			
	2003	2004	2005	2006	2007	2008	2009
	Growth Rates						
Agriculture	-2.5	2.0	5.6	0.5	2.5	3.7	3.5
Industry	7.8	9.4	6.5	6.5	5.2	6.4	6.2
Services	6.7	10.2	8.2	6.8	5.4	5.6	6.1
GDP	5.8	8.9	7.4	6.0	5.0	5.6	5.9
	Shares in GDP						
Agriculture	12.4	11.6	11.4	10.8	10.6	10.4	10.1
Industry	29.3	29.4	29.2	29.3	29.4	29.6	29.7
Services	58.3	59.0	59.4	59.9	60.1	60.0	60.2
GDP	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Developments in the Labour Market

Despite the high growth rate recorded in 2005, the employment increased by 1.2 per cent. Even though the industrial sector and the services sector employments increased by 7.3 per cent and 8.4 per cent in the same year, the contraction in agricultural employment at a high rate of 12.3 per cent, restricted the increase in employment to a great extent. Therefore, even though 1.2 million new jobs were created in non-agricultural sectors, the increase in total employment was limited to 255 thousand people. It is observed that a similar structure continued during the first half of 2006 as well. While an average contraction of 880 thousand persons was observed in agricultural employment during the first six months of 2006, an increase of 930 thousand people was recorded in non-agricultural employment. Therefore, although a high growth rate was recorded, the increase in total employment was quite limited. This tendency is expected to continue during the second half of 2006 and no significant employment increase is expected to take place throughout the year.

The transformation process in the agricultural sector will continue to be one of the main determinants of developments in employment during the 2007-2009 period as well. As of 2006, it is expected that the share of agricultural employment in total employment will be 26.5 per cent and this ratio will continue to decline more gradually over the coming years. In this context, it is considered that moderate increases will be recorded in total employment starting from 2007. As a result of this, it is projected that 1.1 million new jobs will be created during the 2006 PEP period and the unemployment rate will slightly decrease.

Table. 2. 6: Developments in the Labour Market

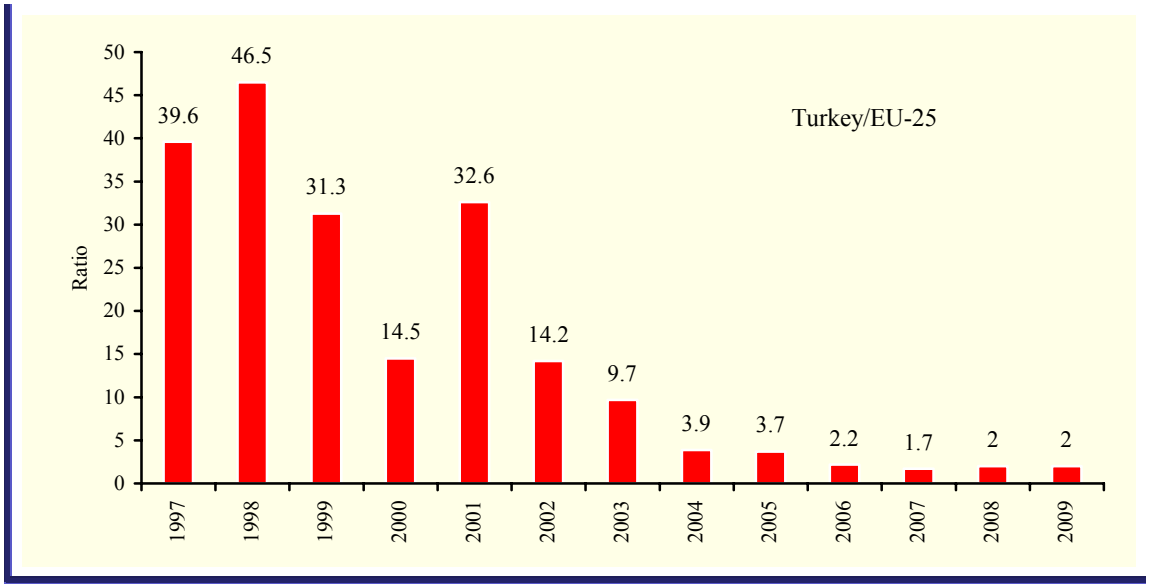
	Realization	Forecast			
	2005	2006	2007	2008	2009
Working Age Population (Thousand Persons)	50,826	51,728	52,632	53,549	54,467
Labour Force (Thousand Persons)	24,565	24,597	24,895	25,307	25,741
Labour Force Participation Rate (Per cent)	48.3	47.6	47.3	47.3	47.3
Employment Level (Thousand Persons)	22,046	22,112	22,444	22,823	23,255
Employment (Percentage Change)	1.2	0.3	1.5	1.7	1.9
Unemployment Rate (Per cent)	10.3	10.1	9.8	9.8	9.7

The fact that no increase is expected in the unemployment rate, despite limited employment growth, basically results from the developments regarding labour force participation. The contraction in agricultural employment brings along the incident of migration from rural to urban areas. It is known that the women, who actively participate in the labour force in rural areas, withdraw from the labour market to a great extent upon their migration to urban areas. For instance, female labour force participation rate, which was 33.7 per cent in rural areas in 2005, was realised as 19.3 per cent in urban areas. This fact restricts participation in the labour force during the agricultural transformation process.

2.2. Inflation

In terms of ensuring a sustainable growth environment in the economy and a fair income distribution, struggle against inflation constitutes one of the prior objectives of the economic policy. At the same time, decreasing inflation to the EU average has importance in the convergence process of the Turkish economy to the EU. In this framework, the achievements obtained in the struggle against inflation during the 2002-2005 period enabled a progress in the convergence of inflation in Turkey to the EU-25 average (Figure 2.6). However, supply shocks and the depreciation in YTL that were experienced in 2006, strengthened the probability of inflation to realize above the target. In spite of this, the measures taken by the Central Bank in June as well as the decisive attitude in the monetary policy towards inflation will make it possible for inflation to converge to the targets in the medium-term. In this context, the targets for CPI inflation were preserved at the level of 4 per cent, without any modifications for the years of 2007 and 2008.

Figure. 2. 6: The Ratio of Turkish Inflation to EU-25 Inflation



Source: TURKSTAT, EUROSTAT
Note: 12-month end-year inflation figures are used. CBRT targets are taken for 2006-2008 period.

In addition to tight monetary policy, sustaining the fiscal discipline will also be crucial in the struggle against inflation in the coming period. Continuation of incomes policy in harmony with the inflation target and not deviating from the primary surplus targets are important in terms of directing the inflationary expectations and reducing the risk premium during the following period. In addition to these, it is considered that the

decisive implementation of structural reforms will contribute to fighting against inflation and ensuring price stability.

Fundamental risks that create uncertainties in achieving inflation targets in the coming period are considered to be the potential changes in the global risk appetite and the new fluctuations that might arise in the financial markets consequently, as well as the high level of medium-term inflationary expectations and the inflation inertia that can not be broken in the services sector. In addition, developments in the energy prices are also considered as a risk factor that should be monitored in terms of inflation dynamics.

Table. 2. 7: Price Targets and Projections

(Percentage Change)

	2006	2007	2008	2009
CPI (1)	5.0	4.0	4.0	---(2)
GDP Deflator (3)	8.6	7.0	4.0	4.0

(1) End-year target.
(2) CBRT has not set the target for 2009 yet.
(3) Projections for average annual increase.

2.3. Monetary and Exchange Rate Policies

The Central Bank continues with the inflation targeting regime that has been implemented since the beginning of 2006 based on the determined operational framework. In monetary policy decisions, the Central Bank follows an attitude that is focused on the consistency of the medium-term outlook of inflation with the targets. In this context, a cautious-optimistic stance was displayed during first three months following the transition to the inflation targeting regime. Despite the inflation figures that turned out to be higher than expectations in April, this stance was preserved determining that this was a temporary increase arising from factors out of the control of the monetary policy. Due to the fluctuations experienced in financial markets as a result of the changing international liquidity conditions during May, the Central Bank took a tighter stance in the monetary policy starting from June. At the same time, the Central Bank was able to take the fluctuations in YTL and foreign exchange markets under control in a short time with additional measures and therefore proved its decisiveness regarding inflation targeting.

The Central Bank determines the monetary policy targets with a medium-term perspective. In this framework, what is important for the Central Bank is the convergence of inflation to the target in the medium-term rather than temporary fluctuations that occur in inflation. At the beginning of 2006, when the inflation targeting regime was introduced, the Central Bank determined its inflation targets, in a way to cover the 2006-2008 period.

The Central Bank estimates that the inflation rate would realize between 1.7 per cent and 5.2 per cent with a 70 per cent probability in the first quarter of 2008 and therefore the convergence to the target path would be achieved within a time frame of one and a half year, according to the existing information set and under the scenario that the tight monetary stance is preserved until the beginning of the last quarter of 2007 and a moderate interest rate reduction is introduced afterwards.

With the shift to explicit inflation targeting in 2006, the Central Bank introduced an important institutional change in the decision-making process concerning the interest

rates. In this context, decisions concerning the interest rates are voted at the Monetary Policy Board and the minutes are announced. Additionally, in order to increase predictability in monetary policy implementation, Inflation Reports including quantitative estimates of inflation rates started to be published as of the first quarter of 2006 on a quarterly basis.

The Central Bank continues to monitor the credit developments in the banking sector, with a medium-term perspective. Intermediary activities of the banking sector displayed a significant slowdown following the fluctuations during the second quarter of 2006. Particularly the fast growth in the loans offered by banks to households, slowed down considerably due to the increases in interest rates. The Central Bank will continue to closely monitor the credit developments in the banking sector, due to its information content regarding the total demand and the soundness of the financial system, in the future as well.

Potential changes in the global risk appetite and the new fluctuations, which might arise in the financial markets as a result of this, will continue to constitute a fundamental risk in terms of the outlook of inflation within the coming period as well.

Another risk factor that creates uncertainty in terms of the inflation target, on the other hand, is the high level of medium-term inflationary expectations and the inflation inertia that cannot be broken in the services sector.

The Central Bank will continue to monitor the impacts of the tight monetary policy on the economy during the coming period as well and in case the improvement in the outlook of inflation in the medium-term is slower than expectations due to the realizations of risk factors, it will not hesitate to further tighten the monetary policy.

The Central Bank will continue the implementation of the floating exchange rates regime during 2007, as well. According to the moderate reserve accumulation policy that the Central Bank carries out under the floating exchange rate regime, the Central Bank will continue the foreign exchange purchase auctions in 2007, as well, in a way to affect the foreign exchange rate level to the minimum extent and to ensure that the fundamental principles and operation of the floating exchange rates regime are adhered to. In addition, in case the depth of the foreign exchange market decreases as a result of a serious external shock or extraordinary developments; extreme volatility in foreign exchange rates and unhealthy price formation that might emerge in consequence, the Central Bank might suspend the foreign exchange purchase auctions for a short or long period after announcing to the public in advance.

While the inflation targeting regime will be continued with a medium-term perspective in the coming period as well, continuation of the structural reform process, preserving the independence of the Central Bank and decisive implementation of fiscal discipline will play an important role in formation of expectations, which is one of the most important explanatory variables of inflation, in line with targets.

2.4. Balance of Payments

Current Account

The exports in 2005, which were estimated to be 72.4 billion dollars in the 2005 PEP, were slightly above the estimates, as 73.5 billion dollars. Even though the increase in exports was 16.3 per cent in 2005, it remained below the rate of increase in 2004. Main reasons for this slowdown, as mentioned in the 2005 PEP, were the pass-through

of the increases in the world energy prices to production costs, the increase of competition in the world textile and clothing sector due to the removal of the quotas on China, and the continuation of the real appreciation in YTL.

Following the fluctuation experienced in the exchange rate market during the May-June period of 2006, YTL depreciated considerably in nominal terms. However, the impact of this depreciation on exports growth remained limited both because this depreciation was eliminated to a great extent starting from July and impacts of the afore-mentioned factors continued in 2006 as well. As a matter of fact, the export growth rate in 2006 is expected to decrease to a certain extent compared to that of 2005. Realizations for the first nine months of 2006 verify this expectation.

On the other hand, imports, which were estimated to be 115 billion dollars for 2005, displayed a 19.7 per cent increase compared to the previous year and reached 116.8 billion dollars, in line with the estimates. Data concerning the January-September period of 2006 show that imports move in parallel with the economic growth and it is estimated that the growth rate of imports will decrease to a certain extent in 2006 compared to 2005 with the slowdown in the economy.

Tourism revenues, on the other hand, reached 18.2 billion dollars in 2005 in line with the estimates. However, due to the factors such as conflicts in the Middle East and the avian influenza, tourism revenues remained below the expectations in the first nine months of 2006. During the 2000-2005 period, the number of tourists visiting Turkey increased by 19.4 per cent annually on average and the tourism revenues increased by 23.2 per cent annually on average. However, during the January-September period of 2006, the number of tourists visiting Turkey declined by 5.1 per cent. Comparing to the same period of the previous year, the 7 per cent decrease in the number of tourists coming from the European countries, which constitute approximately 85 per cent of total tourists visiting Turkey, was effective in this decrease. As a result of this, tourism revenues in the January-September period of 2006 declined by 5.8 per cent compared to the same period of the previous year.

As a result of these developments, the current account deficit of 2005, which was estimated to be 21.3 billion dollars in the 2005 PEP, was realised as 23.2 billion dollars due to the above-mentioned factors as well as the fact that services balance excluding tourism remained below expectations.

Systematic advertising and marketing activities are being carried out in recent years to increase the performance of exports. In addition, the share of goods with high value-added, such as machinery and transportation vehicles, in exports is also increasing. As a matter of fact, the share of exports of automotive, other transportation vehicles, office machinery and communication devices and electrical and non-electrical machinery sectors in total exports, which was around 21 per cent in 2000, increased over the years and reached 30 per cent in 2005. It is considered that export volume of Turkey will continue to increase based on the expectations that the world economic growth will continue and especially that the growth rate of the EU, which constitutes the largest exports market of Turkey, will stay high in the future, in addition to the continuation of the performance achieved in aforementioned sectors. As a result, it is estimated that the exports, which are expected to be 83.5 billion dollars in 2006, will reach 121.2 billion dollars in 2009.

When the realisations are examined, it is observed that the energy imports of 2006 will be higher than that is projected in the 2005 PEP. In addition, depending on the increases expected in the growth rates, it turned out that, in the 2006 PEP period,

imports would remain above the 2005 PEP estimates. In this context, it is estimated that imports will reach 135.5 billion dollars in 2006 and 176.8 billion dollars in 2009.

The recent decline in the number of tourists visiting Turkey required the revision of tourism revenues in the 2006 PEP compared to 2005 PEP figures. In this context, tourism revenues for 2006 are expected to be 18.1 billion dollars. However, it is also projected that this decline will not be permanent and tourism revenues will reach around 23 billion dollars by the end of the PEP period.

In this framework, it is estimated that the current account deficit, which is expected to be 30.8 billion dollars in 2006, will decline to 27.4 billion dollars in 2009, as a result of the expected improvement in balance on services during the Pre-Accession Economic Programme period. It is also estimated that the ratio of current account deficit to GDP will realize as 7.9 per cent in 2006 and 5.7 per cent in 2009.

Capital and Financial Account

The net capital inflow that increased to a considerable extent in recent years and that finances the current account deficit was estimated to be 16.4 billion dollars for 2005, in the 2005 PEP. However, net capital inflow was at a higher level than estimated and reached 20.9 billion dollars. Large amounts of capital inflows are expected to continue in 2006 and in the following years.

It is projected that the composition of capital inflows will change over the years. Foreign direct investments are expected to be at higher levels in 2006 and 2007 compared to realizations in 2005; however, they are projected to decrease slightly in the following years. In addition, it is estimated that the portfolio investments will continue to preserve the level of 2006 estimate during the course of the PEP period. Other investments, on the other hand, are expected to move around the 2005 realization during the 2006 PEP period.

Foreign direct investments reached to a record level in 2005 with a three-digit rate of increase. In 2006, foreign direct investments are expected to realize at higher levels particularly due to privatisations and cross-border merger and acquisitions in banking sector. However, it is also projected that the foreign direct capital inflows will be below the level of 2005 starting from 2008, in spite of this, they will reach an annual average amount of 10.3 billion dollars during the 2007-2009 period.

Net portfolio investments, which were estimated to be 11.1 billion dollars in the 2005 PEP, were recorded as 13.4 billion dollars in 2005 due to the increasing demand for the government domestic borrowing instruments (GDBI). Along with this, it is projected that the portfolio investment inflows will realize at a relatively lower level during the 2006 PEP period especially as a result of decreasing need of the Treasury for foreign borrowing. Thus, it is estimated that the net portfolio investments, which are expected to be 5.6 billion dollars in 2006, will increase slightly in 2009 and realize as 6 billion dollars.

In this context, it is foreseen that no problems will be encountered in the financing of the current account deficit, even though a net amount of 5.6 billion dollars will be repaid to the IMF during the 2007-2009 period. Parallel to the developments in capital inflows, an increase in official reserves is expected in 2007. With the impact of the termination of credit claims from the IMF, limited increase in official reserves is projected in 2008 and 2009.

Table. 2. 8: Balance of Payments Forecasts

(In Billion Dollars)

	Realization			Forecast			
	2003	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**
Current Account	-8.0	-15.6	-23.2	-30.8	-30.4	-28.7	-27.4
Balance on Goods	-14.0	-23.9	-32.9	-39.4	-40.8	-40.0	-40.0
Exports	51.2	67.0	76.9	88.0	99.9	111.9	126.3
Exports (fob)	47.3	63.2	73.5	83.5	95.0	106.9	121.2
Imports	-65.2	-90.9	-109.9	-127.4	-140.7	-151.9	-166.3
Imports (cif)	-69.3	-97.5	-116.8	-135.5	-149.7	-161.5	-176.8
Balance on Services	10.5	12.8	14.0	13.5	15.5	16.7	18.1
Credit	17.9	22.9	25.8	24.6	27.4	29.9	32.4
Tourism	13.2	15.9	18.2	18.1	19.8	21.3	23.1
Debit	-7.4	-10.1	-11.9	-11.1	-11.8	-13.1	-14.3
Balance on Income	-5.6	-5.6	-5.7	-6.3	-7.0	-7.3	-7.4
Credit	2.2	2.7	3.7	4.7	5.4	5.4	5.5
Debit	-7.8	-8.3	-9.3	-11.1	-12.4	-12.7	-12.8
Current Transfers	1.0	1.1	1.5	1.5	1.8	1.8	1.8
Workers' Remittances	0.7	0.8	0.9	1.0	1.2	1.2	1.2
Capital and Financial Account							
Financial Account (Including Reserves)	3.1	13.4	20.9	31.9	30.4	28.7	27.4
Foreign Direct Investment	1.3	2.0	8.7	18.3	13.2	7.2	6.8
Direct Investment Abroad	-0.5	-0.9	-1.1	-0.7	-1.0	-1.3	-1.4
Direct Investment in Turkey	1.8	2.9	9.8	19.0	14.2	8.5	8.2
Portfolio Investments	2.5	8.0	13.4	5.6	5.6	5.8	6.0
Assets	-1.4	-1.4	-1.2	-0.9	-1.0	-1.0	-1.0
Liabilities	3.9	9.4	14.7	6.5	6.6	6.8	7.0
Equity Securities	1.0	1.4	5.7	2.0	2.0	3.0	3.3
Debt Securities	2.9	8.0	9.0	4.5	4.6	3.8	3.7
Other Investments	3.4	4.2	16.6	10.8	16.9	15.9	15.3
Assets	-1.0	-7.0	0.2	-8.5	-0.1	-1.0	-1.0
Liabilities	4.4	11.1	16.4	19.3	17.0	16.9	16.3
Monetary Authority	-1.0	-4.6	-3.7	0.0	0.0	0.0	0.0
General Government	-0.8	-0.3	-4.6	-4.2	-0.9	-1.4	-3.7
Banks and Other Sectors	6.2	16.0	24.7	23.5	17.9	18.3	20.0
Official Reserves	-4.0	-0.8	-17.8	-2.8	-5.3	-0.2	-0.8
Net Errors and Omissions	5.0	2.2	2.2	-1.1	0.0	0.0	0.0

Source: SPO, CBRT

The commercial loan claims of the non-bank private sector from abroad is expected to be correlated with the expansion in the trade volume; whereas the long-term loan claims is expected to be correlated with domestic investment. It is projected that long-term loan claims of the non-banking private sector will be 13.1 billion dollars and 6.5 billion dollars, respectively, whereas short-term loan claims will be 0.3 billion dollars and 0.2 billion dollars, in 2006 and 2007, respectively.

3. PUBLIC FINANCE

The 2007 budget was prepared in a way to yield a primary surplus in line with the economic programme targets with the purpose of reducing the ratio of the public debt stock to national income, just as in the previous years. In addition, contributing to the process of decreasing inflation and maintaining the current growth environment are among the criteria taken in consideration in the preparation of the 2007 budget.

3.1. Objectives of Fiscal Policy

Fiscal Policy

The basic objectives of the fiscal policy in practice are to contribute to the process of sustaining macroeconomic stability, to support the fight against inflation and the current account deficit and to yield a significant public primary surplus as a share of GDP with the aim of continuing the process of reducing the ratio of the public debt stock to national income. During the 2007-2009 period, public revenues, expenditure and borrowing policies will effectively be implemented in harmony with the afore mentioned basic objectives.

Public Revenues Policy

The objectives that will be pursued while implementing the public revenues policy are;

- To determine and carry out public revenue policies in a way that they are consistent with the primary surplus target,
- To take informal economy under control through strengthening the implementation, monitoring and supervisory functions of the revenue administration, rationalizing the tax system and improving inter-institutional cooperation,
- To consider the investment and employment impact of tax policies during their implementation, to develop policies towards this end, to increase predictability in tax policies,
- To continue with the works concerning the reevaluation of exception, exemption, tax discount and similar provisions included in tax laws within the framework of economic and social policies and with the simplification of the tax legislation,
- To use the income surpluses that will be created in reducing the tax burden, transaction taxes and payroll taxes in particular, to the extent allowed by the public fiscal balances,
- To increase the self-revenues of local administrations.

Some important regulations realised in line with these purposes, on the other hand, are as follows. The Corporate Tax Law was rewritten and legislated considering such priorities as simplifying the tax legislation, expanding the tax base, and fighting with informality. With this regulation, the corporate tax rate was decreased from 30 per cent to 20 per cent. Thus, the tax burden on corporate earnings was withdrawn from 44 per cent to 34 per cent. In line with international practices, tax safety institutions such as revenue of controlled foreign company, hidden capital, hidden earning distribution through transfer pricing, fighting against tax heavens were developed and incorporated

in our tax system. Provisions about full and limited liability were undertaken separately and purity and simplicity was achieved. Some exceptions and exemptions were abolished.

The number of income tariff rates was decreased from 5 to 4. The implementation of imposing different tax rates on wage and non-wage incomes was abandoned. The implementation of investment allowance was ended with a 3-year transition period.

The works for the functional restructuring of the revenue administration so as to enable efficient management of the tax system were completed in 2005. Within this scope;

- The General Directorate of Revenues was restructured under the name of the Revenue Administration taking its functions as basis, as a semi-independent organization reporting to the Ministry of Finance.
- It was ensured that the Revenue Administration has become more independent and efficient in implementing revenue policies.
- Tax Offices were established in 29 provinces and a Large Taxpayers Office was set up in Istanbul so as to allow for direct relations between the central and provincial units. The Large Taxpayers Tax Office is projected to start its activities as of the beginning of 2007.

Furthermore, in the framework of the restructuring of the revenue administration, beside the Revenue Administration responsible for the implementation of revenue policies, the General Directorate of Revenue Policies, assigned with the duty of working on the creation government revenues policies, was established under Ministry of Finance.

Within the framework of the Tax Office Automation Project (VEDOP), which was initiated with the aim of reducing the work burden of tax offices through the realization of their transactions in electronic environment, increasing productivity and efficiency in the operation and transactions of tax offices and setting up a sound decision support and management information system infrastructure, a total of 448 tax offices were included within the scope of automation.

e-statement implementation was started as of 1 October 2004. As of 31 August 2006, 37,069 taxpayers and 31,742 professionals obtained passwords for e-statement and as of 27 September, they submitted a total of 38,164,676 e-statements to the revenue administration in electronic environment. A Call Center providing continuous services to assist taxpayers was established.

With the aim of rationalization and simplification of the tax system, works for rewriting the Income Tax Law and rearranging its systematic structure, just as in the Corporate Tax Law, are continuing.

With the aim of enhancing the tax inspection capacity, recruitment of large numbers of tax inspection personnel and efforts towards strengthening the tax inspection units technologically are continuing.

The implementation for the use of the T.R. Citizenship numbers instead of the tax identification number will be started in 2007.

Public Expenditures Policy

The main objective of the expenditure policy in practice is to keep the financing requirement at a reasonable level by increasing efficiency in public expenditures and ensuring the continuity of discipline in expenditures.

Policies to be implemented regarding expenditures have been specified below.

- The reform efforts in the public financial administration system will be completed.
- Realization of a comprehensive personnel regime reform and rearrangement of the public personnel system is envisaged. Efforts in this subject are continuing.
- With the aim of increasing the efficiency of personnel expenditures in the public sector, the restriction related to new personnel recruitment in the public sector included in the budget laws of previous years, is also included within the Draft Law on 2007 Central Government Budget.
- The inflation target, the public financing balance and ensuring equity of wages among employees will be considered while determining the wages and salaries in the public sector.
- Works related to increasing the effectiveness of the health expenditures in the public sector will be continued. Efforts towards increasing premium collection rates and reducing health expenditures in the social security system will be continued.
- Works on strategic planning and performance-based budgeting will be accelerated.
- Works towards the rationalization of public expenditures will be continued.
- Law on Agriculture will be taken as basis in determining the share allocated from the budget for agricultural support and distribution of this share among agricultural support instruments.
- Notions of multi-year budgeting and prioritisation of expenditures will be considered in the determination of appropriations to public expenditures.

Public Finance Projections (2007-2009)

General government balance is obtained by the consolidating the revenues and expenses of the central government budget, local administrations, extra budgetary funds, social security institution, unemployment insurance fund, general health insurance and revolving funds.

In the estimation of general government accounts, the following assumptions were taken in account in addition to the general macroeconomic assumptions such as economic growth, inflation, interest rates, balance of payments, terms of trade, wage increases and foreign exchange rates projected for the 2007-2009 period.

Assumptions related to revenues:

- It was assumed that the Special Provincial Administration and Municipality Revenues Law, which constitutes one of the components of the local administrations reform, would be implemented starting from 2008 and its financial impact was reflected on balances.

- It was assumed that a reduction would take place in the shares allocated to the budget from the revenues of State Economic Enterprises and dividend incomes due to privatisations.
- It was assumed that possible price changes in international energy prices would not affect the amounts of SCT on energy products.
- It was estimated that additional increases would take place in the collection of income tax and SCT in particular, within the framework of fighting against informality effectively.
- A premium structuring revenue was projected in BAĞ-KUR and SSK during the 2007-2009 period as a result of premium debt restructuring.
- A revenue of 200 million YTL is expected from the sales of real estate that belongs to the Social Security Institution in 2007-2009 period.
- A total privatisation revenue of 9 billion dollars is targeted for the 2007-2009 period, 5 billion dollars of which is in the privatisation fund and approximately 4 billion dollars is in the budget. On the other hand, since no projections could be made regarding the privatisation schedules and the privatisation revenues of Halkbank and energy SEEs, and the collection form of these revenues, no privatisation revenue was projected related to these organizations.

Under these assumptions, general government total revenues, which are expected to be around 46.3 per cent of GDP in 2006, are estimated to realize as 44.9 per cent of GDP in 2007.

Assumptions regarding expenditures are as follows:

- It was assumed that the reform concerning the personnel regime would be implemented in 2009.
- It was assumed that the restriction policy related to the recruitment of new public personnel would be continued and wages and pensions would be determined in line with the targeted inflation.
- No changes were projected in the rights and obligations related to the conditions of benefiting from unemployment insurance.
- The financial impact that would occur within the scope of the Universal Health Insurance and the Retirement Insurance, which will be effective in 2007, was reflected to balances. Although a significant increase will occur in health expenditures due to the expansion of the scope and facilitation of access to health services, the additional revenue that will particularly arise from incorporating all wage elements of civil servants within the scope of premiums will compensate for a significant part of these expenditures.
- Due to the social security reform and incorporation of all wage elements of civil servants within the scope of premiums, there will be an increase in the premium expenditures made from the central government budget for civil servants. A separate appropriation is to be allocated to the budget in order to compensate for this reduction in the salaries of civil servants.

As a result of the projections made by taking these assumptions into consideration, it is estimated that the share of general government expenditures in GDP, which is estimated to be 43.6 per cent in 2006, is expected to increase by 1.5 percentage

points in 2009 and realize as 45.1 per cent. During this period, an increase of 3.2 percentage points is expected to take place in the share of primary expenditures in GDP. Therefore, it is projected that the expected decline in interest payments will restrict the increase in general government expenditures.

General Government Borrowing Requirement

It is projected that the share of tax revenues within GDP, which constitutes 54.8 per cent of general government revenues, will become 25.5 per cent in 2007, with an increase of 0.6 percentage points compared to 2006. General government revenues, which are programmed to be 45.7 per cent of GDP excluding privatisation revenues, rises to 46.5 per cent of GDP, with an increase of 0.2 percentage points compared to the previous year, including privatisation revenues.

It is projected that the 2007 general government expenditures would increase by 3.5 percentage points as a share of GDP and become 47.1 per cent and primary expenditures would increase by 3.4 percentage points and reach 38.6 per cent compared to the previous year levels. The share of general government fixed capital investments in GDP is expected to increase by 0.1 percentage points compared to 2006 and rise to 3.9 per cent in 2007.

The ratio of the general government primary surplus in GDP, which is estimated to be 11.1 per cent in 2006, is expected to become 7.9 per cent, 7.2 per cent and 6.5 per cent, respectively, during the 2007-2009 period.

The general government balance, which is expected to yield a 2.7 per cent surplus as a share of GDP in 2006, is projected to yield a 0.6 per cent deficit in 2007. This arises mainly from the decrease in privatisation revenues and the increase in personnel, other current, health and social assistance expenditures.

The general government balance is estimated to be in equilibrium 2008 and yield a deficit of 0.3 per cent of GDP in 2009.

A certain amount of decrease is expected in the revenues of the central government budget, which constitutes the major element of general government, both in 2008 and 2009 compared to the previous year, however, it is also estimated that the central government budget balance will be positively affected as a result of a higher amount of decrease expected in its expenditures, particularly in interest expenditures. In this framework, the central government budget is expected to affect the general government balance positively, especially in 2008. Another reason for the improvement expected in the general government balance in 2008 is the local administrations. With the assumption that the Draft Law on Special Provincial Administration and Municipality Revenues will be put into force in 2008, an increase is projected in the self-revenues of Municipalities.

In the 0.3 percentage points deterioration projected for the general government balance as a share of GDP in 2009 compared to the previous year, it is considered that the fall in privatisation revenues, the decline in the SSK and BAĞ-KUR premium structuring revenues and the drop in the interest revenues of unemployment insurance fund will be effective.

Table. 3. 1: General Government Revenues and Expenditures

(Per cent of GDP)

	2006	2007	2008	2009
Taxes	24.9	25.5	25.4	25.1
Direct	6.9	7.2	7.3	7.2
Indirect	17.2	17.4	17.0	16.8
Wealth	0.9	0.9	1.1	1.1
Non-Tax Revenues	3.5	2.9	2.6	2.6
Factor Incomes	7.9	6.8	6.4	6.2
Social Funds	7.8	10.5	10.7	10.6
Total	44.1	45.7	45.1	44.4
Privatisation Revenues and Asset Sales	2.2	0.8	0.8	0.5
Total Revenues	46.3	46.5	45.9	44.9
Current Expenditures	18.7	19.7	19.7	19.5
Investments	3.9	4.0	3.9	4.0
Fixed Investment	3.8	3.9	3.9	3.9
Change in Stocks	0.0	0.0	0.0	0.0
Transfers	21.0	23.4	22.3	21.7
Current Transfers (net)	19.8	22.5	21.4	20.8
Capital Transfers	1.2	0.9	1.0	0.9
Stock Revaluation Fund	0.0	0.0	0.0	0.0
Non-interest Expenditure	35.2	38.6	38.7	38.4
Total Expenditures	43.6	47.1	45.9	45.1
Primary Surplus	11.1	7.9	7.2	6.5
Borrowing Requirement	-2.7	0.6	0.0	0.3
IMF-defined Borrowing Requirement	7.0	5.9	5.5	5.2

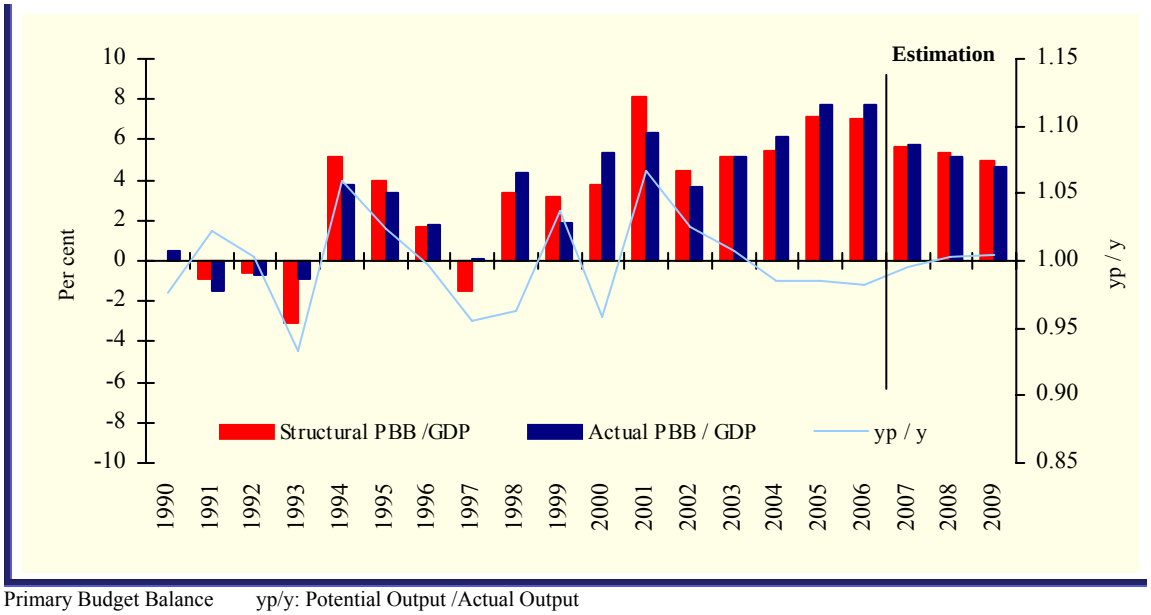
Source: SPO
Note: Tax refunds are not included in revenue and expenditure figures.

Structural and Cyclical Consolidated/Central Government Budget Balance

With the help of the methodology used by the European Commission and OECD, structural and cyclical budget figures for Turkish economy were obtained and cyclical effects on the budget were examined.

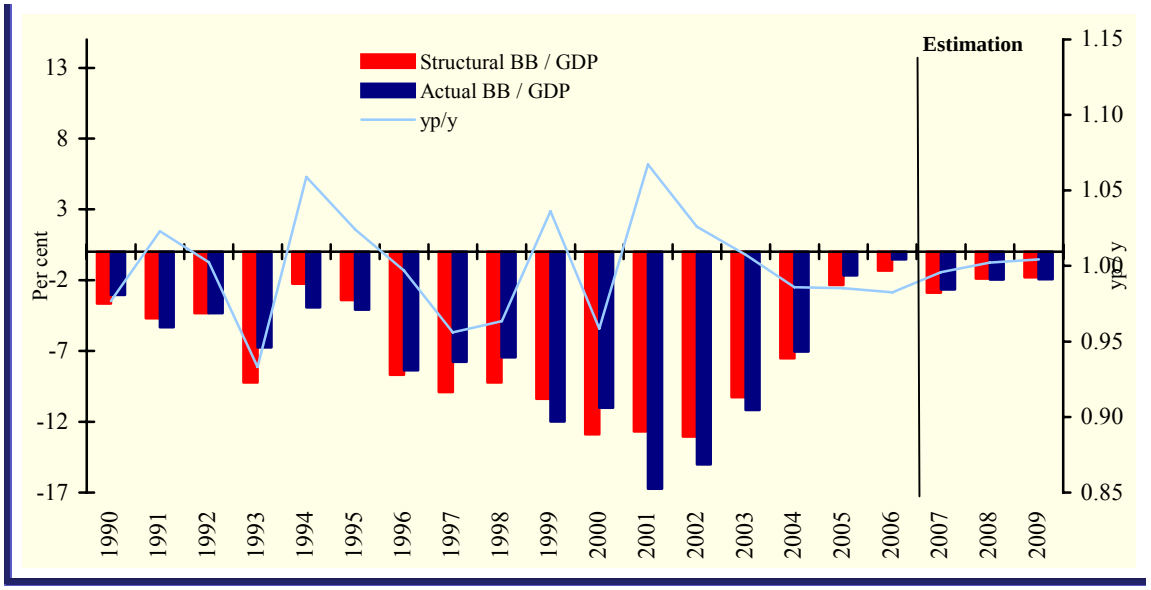
Structural primary budget balance and actual primary budget balance are presented in Figure 3.1. According to this, the ratio of structural primary budget balance to GDP, which was 5 per cent in 2004, increased considerably as a result of decisively implemented tight fiscal policy and was realised as 7.1 per cent in 2005. It is foreseen that the similar tendency will continue in 2006 as well. It is envisaged that tight fiscal policy will be continued in 2007; however, the ratio of structural primary budget surplus to GDP will be slightly below the 2005-2006 average. This situation particularly stems from the expectation of increasing health expenditures with the effect of the realised structural transformation. In this context, the ratio of structural primary budget balance to GDP is estimated to be 5.5 per cent in 2007. It is envisaged that this ratio will approximately maintain this level in 2008-2009 period.

Figure. 3. 1: Actual and Structural Primary Budget Balances



Primary Budget Balance yp/y: Potential Output /Actual Output

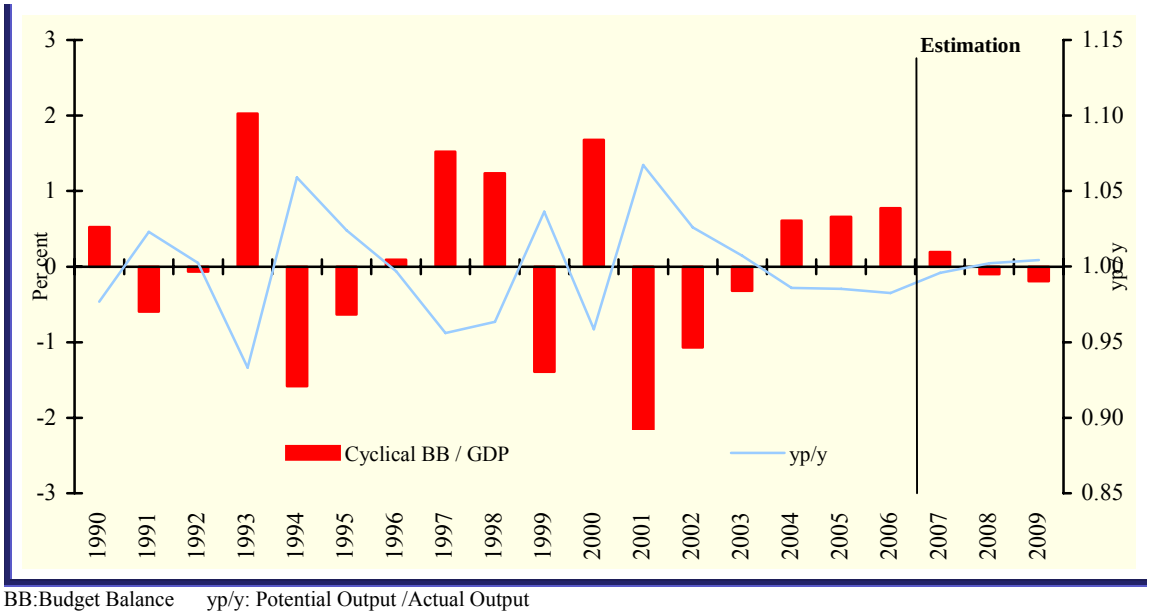
Figure. 3. 2: Actual and Structural Budget Balances



BB:Budget Balance yp/y: Potential Output /Actual Output

As presented in Figure 3.2, structural budget balance moved in the positive direction and deficit gradually declined from 2002 to 2005. Decline in interest rates and high primary surpluses were considerably influential in this favourable development. This tendency is expected to continue in 2006 as well. With the effect of fluctuations experienced in international markets in the second quarter of 2006, an increase in interest rates was observed. Due to the maturity structure of government domestic borrowing instruments, the impact of this increase on interest payments is not reflected in 2006. However, it is predicted that the increase in interest rates will affect interest payments of budget in 2007 and that downward trend of interest payments to GDP ratio observed in recent years will not continue and this ratio will maintain its level in 2007. Depending on these reasons, structural budget deficit is expected to increase in 2007. In 2008-2009 period, it is envisaged that the ratio of interest payments to GDP will show a downward tendency again and thereby budget deficit will decline.

Figure. 3. 3: Cyclical Budget Balance



BB:Budget Balance yp/y: Potential Output /Actual Output

Cyclical budget balance is obtained by subtracting structural budget balance from the actual budget balance. In 2004-2006 period, with the contribution of implemented structural reforms as well, Turkish economy grew above its potential. It is estimated that the economy will grow around its potential starting from 2007 as can be seen in Figure 3.3. Therefore, it is foreseen that there will be no cyclical effects on budget in 2007-2009 period.

3.2. Public Debt Management

Institutional Responsibilities For Debt Management and Borrowing Limits

Debt management is carried out within the framework of the borrowing limit determined as required by Article 5 of the Law No. 4749 on Regulating Public Finance and Debt Management promulgated on 9 April 2002.

The basic principles of public debt and risk management in this Law were determined as:

- Following a sustainable, transparent and accountable borrowing policy that is in line with monetary and fiscal policies by considering macroeconomic balances,
- Meeting financing requirements at the lowest possible cost in the medium and long-run, within the framework of the risk level determined by considering domestic and foreign market conditions and cost elements.

The borrowing limit is defined as the amount of the difference between the total commencement appropriations that are specified in the budget law of a certain fiscal year and estimated revenues. Within the framework of Article 5 of the Law No. 4749, the net borrowing limit may be increased by 5 per cent taking the requirements and development of debt management in account and if this amount is not sufficient, an additional 5 per cent increase may be realised with the decree of the Council of Ministers.

Debt Management Strategy

The practice of strategic benchmark has been continued since 2004 in order to ensure that transparency is increased in debt management and efficient borrowing based on performance is realised at the minimum cost and a reasonable risk level. In the framework of the strategic benchmarks determined according to cost and risk calculations, implementations such as;

- Increasing the weight of fixed interest rate and YTL denominated bonds in borrowing with the aim of alleviating the interest rate and foreign exchange rate risks that might be encountered in the implementation of the borrowing policy,
- Not using foreign exchange denominated borrowing,
- Extending the maturity in domestic borrowing by taking the market conditions into consideration,
- Keeping reserves at a sufficient level throughout the year with the aim of mitigating the liquidity risk that might arise in cash and debt management,

are being continued as the main components of the borrowing policy in 2006. Following borrowing strategies that are consistent with strategic benchmarks will be continued within the framework of risk and cost objectives during the period following 2006 as well.

The high amount of primary surplus projected within the framework of the economic programme being implemented during the 2007-2009 period will result in sustaining the confidence environment created in the markets and continuance of the decrease in debt requirement. It is projected that, with the positive impact of the decreasing borrowing requirements and of the confidence environment in domestic and foreign markets on the expectations, borrowing costs will preserve their downward trend; and in line with all these developments, the ratio of the public debt stock in GDP will continue to decrease during the coming period as well.

Within the framework of these benchmarks that are taken as basis in debt management, the risks to which the Treasury debt stock is exposed are being eliminated gradually and the sensitivity of the debt stock to fluctuations in foreign exchange and interest rates are being alleviated. The share of debts in/indexed to foreign exchange within the domestic debt stock of the central government budget, which was 17.6 per cent as of the end of 2004, receded back to the level of 14.3 per cent as of September 2006. While the share of fixed interest rate debt stock in the domestic debt stock was 51.5 per cent in 2004, it withdrew back to 47.9 per cent as of September 2006.

It is also projected for the coming period that the investor base of the Government Domestic Borrowing Instruments will be enhanced and policies towards ensuring efficiency in the issuance of GDBI and secondary markets will be continued. Within this context, Primary Dealer System implementation will be continued. On the other hand, continuing with the benchmark bond implementation is planned towards creating a healthy yield curve in secondary markets and providing liquidity in GDBI buying-selling transactions.

In addition, within the scope of sustaining transparency in debt management, regular announcement of the financing programs, the monthly procurement programme and debt information will also be continued in the coming period. Related to domestic borrowings, which constitute a major part of the annual financing requirement, it is

projected that the repurchasing and clearing transactions being currently implemented as active debt management instruments will be continued in a manner consistent with strategic benchmarks with the aim of making the current amortizations more organized. Enhancing the GDBI investor base through the diversification of borrowing instruments to be issued according to the preferences of different investors is included among the priorities of the coming period.

Contingent Liabilities

Contingent liabilities are those liabilities, which are not government debts in nature at the moment they are created, however, which bear payment obligations and create costs by transforming into government debts if the risk of debt undertaking occurs. While contractual liabilities as well as those determined by law are called as explicit contingent liabilities, those falling out of this scope are expressed as implicit contingent liabilities.

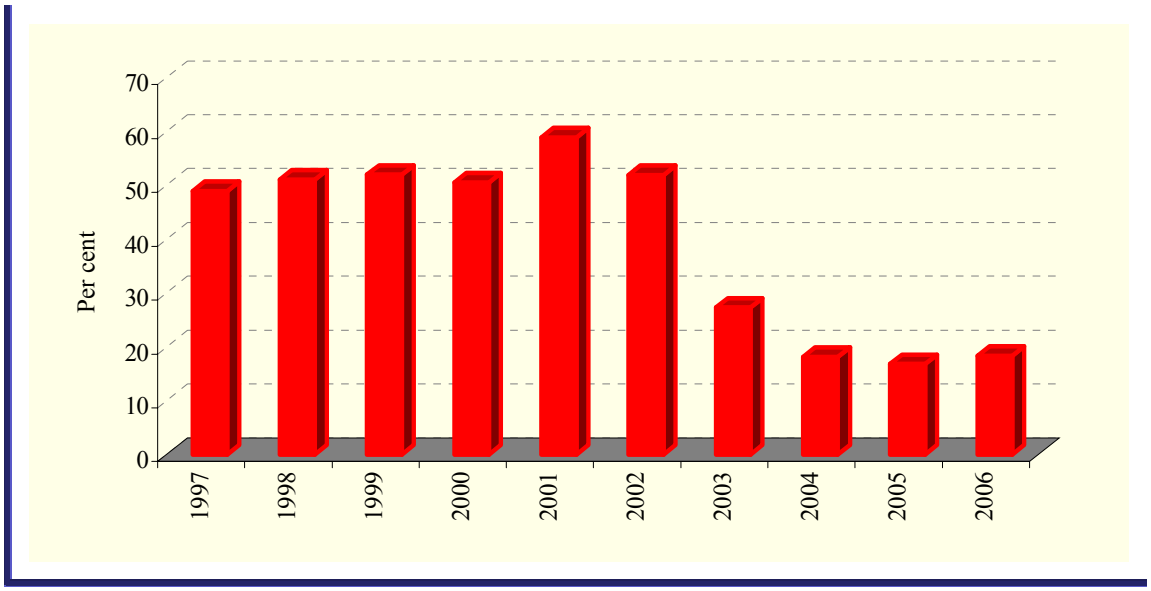
Risks such as falling in default by public institutions and local administrations in their debts that are not guaranteed by the Treasury constitute implicit contingent liabilities that should be taken in consideration in the example of Turkey. In addition, the third person limited guarantee that is currently given to the civil aviation sector and the deposit guarantee in the banking sector, which is limited with 50 thousand YTL per client, are explicit contingent liabilities that should be taken in account.

Undersecretariat of Treasury provides repayment guarantees for purposes such as keeping the investment financing requirements of administrations and institutions that remain outside those included in schedule (I) attached to the Public Financial Management and Control Law No. 5018 at the minimum level, ensuring the sustainability of growth and meeting the funding requirements of investments spread over the years. In addition, within the scope financing projects realised with the Build-Operate-Transfer (BOT) and Build-Operate (BO) models, those administrations that remain outside those included in schedule (I) attached to the Public Financial Management and Control Law No. 5018, which have buy-or-pay agreements signed with the BOT/BO companies, are also provided with investment guarantees by the Treasury. Obligations covered by these guarantees constitute a major part of the financial risks with a possibility of being compensated by the Treasury.

Repayment Guarantee

Repayment guarantees provided by the Treasury for project financing purposes, which were monitored outside the budget until 2003 and incorporated in the budget through the determination of their potential risk amounts after 2003, have been used for years for keeping financing costs at the minimum level and ensuring the sustainability of economic growth. Since from the total amount of Treasury guaranteed loans provided between the years 1996 and 2001, which is 10.3 billion dollars, 54.2 per cent was used by the SEEs and 22.3 per cent was used by local administrations, shares of SEEs and local administrations within the total guaranteed debt stock are relatively large.

Figure. 3. 4: Undertaken Ratios of Treasury Guaranteed Debt



Note: Figure for 2006 belongs to the first half of the year.
Source: Undersecretariat of Treasury

The first undertaking request was placed in 1992 and from the foreign debt repayment guarantees given on behalf of organizations; an approximate payment amount of 9.3 billion dollars was realised between the years 1992-2006 (2nd quarter). The largest share in these payments that were undertaken belongs to local administrations, followed by SEEs.

The most important development realised within the scope of repayment guarantees is the Law on Public Finance and Regulation of Debt Management and through this Law, monitoring of financial transactions carried out within the scope of public financial management easily and creation of an active risk management strategy in terms of contingent liabilities have been achieved.

With the Law on Public Finance and Regulation of Debt Management and legal regulations introduced within this context, a significant increase has been achieved in the collection of Treasury receivables and sharp decreases have been recorded in undertaking rates since 2002.

Table. 3. 2: Treasury Guaranteed External Debt Service Projections

(Million Euros)

	Principal	Interest	Total
2006 (III.-IV. Quarter)	272	85	357
2007	449	145	594
2008	413	122	535
2009	393	101	494
2010-2015+	1,810	319	2,129

Note: Projections are based on debt stock.

While, the Treasury guaranteed debt stock decreased by 2.1 billion dollars as of June 2006 period, compared to 2002 and became 4.2 billion dollars, the undertaking rate fell from 52 per cent to 18 per cent.

When the repayment projection of Treasury guaranteed foreign debt stock is examined in the medium-term, it is observed that the repayment amounts entered in a downward trend as well.

Investment Guarantees

Apart from repayment guarantees, investment guarantees provided to 11 electricity power plants established with the BOT and 5 with the BO model and one energy SEE with a buy-or-pay agreement constitute important explicit contingent liabilities as well. Even though there has not been any payment obligation arising from the subject guarantees until now, these financial risks must also be taken into consideration while calculating the burdens that might arise from these contingent liabilities.

In addition to these, an investment guarantee was provided to a municipality within the scope of a BOT project in 1995 for its water invoice payment obligation. Within the scope of the subject investment, a total undertaking of 1.3 billion euros was realised from 1999 until August 2006.

Treasury Receivables

When the Treasury receivable stock as of the end of October 2006 is examined, it is observed that, within the total, the share of funds, local administrations, SEEs and other receivables are 79 per cent, 13.1 per cent, 5.3 per cent and 2.6 per cent, respectively. Receivables from the SDIF constitute 97.8 per cent of funds.

When the distribution of realised collections is examined according to their sources, payments made in cash by organizations constitute 88.1 per cent of actual collections during the January-October period. While the collections consisting of the deductions made from the tax revenue shares of municipalities by the Ministry of Finance constitute 9.9 per cent, those made by the İller Bank cover 0.3 per cent of the total collections realised during this period. Collections made within the scope of the Law No. 6183, on the other hand, are equal to 1.03 per cent of the total collections realised during the same period.

When the collections made through deductions are compared with those of the previous year, it is observed that there is a decline in such collections. Reconciliation works carried out according to the Laws No. 5393 and 5216 and the increase in the tendency of the relevant organizations to pay their own debts were effective in this.

Risk Account

With the Law on Public Finance and Regulation of Debt Management accepted in 2002, a Risk Account was created under the Central Bank with the aim of eliminating the problems caused in cash and debt management by the amounts paid by the Undersecretariat of Treasury within the scope of Treasury guarantees. The funds for the risk account consist of the loans and guarantee fees received, the repayments made by the relevant organizations in return for the payments made, the interests received on a daily basis for the amounts held in the account and the appropriations projected to be transferred to this account with budget laws. Increasingly less amounts of budgetary funds were transferred to this account, both because the undertakings arising from the guarantees provided decreased and the collections realised increased and utilization of such appropriations were realised as 924.8 million YTL in 2003, 484.3 million YTL in 2004 and 199.8 million YTL in 2005.

2006-2009 General Government Gross Debt Stock Projections

A significant recovery is projected in the share of the general government gross debt stock in GDP as a result of the stable growth environment to be achieved with the tight fiscal policy and efficient debt management that will be implemented during the 2006 Pre-Accession Economic Programme period. It is estimated that this rate, which was 69.2 per cent in 2005, will recede back to 48.4 per cent in 2009.

Within this context, the ratio of general government gross debt stock to GDP estimated for the 2006-2009 period is presented in the Table 3.3.

Table. 3. 3. General Government Gross Debt Stock Projections

(Per cent of GDP)

	Realization	Estimation			
	2005	2006	2007	2008	2009
Domestic Debt Stock	51.0	45.7	41.0	38.0	34.8
Foreign Debt Stock	18.1	17.7	16.6	15.1	13.6
Total Debt Stock	69.2	63.4	57.7	53.1	48.4
Decrease in Total Debt Stock	---	5.7	5.8	4.5	4.7

3.3. Risks Associated with Public Finance

The tight fiscal policy implementation with the aim of achieving the sustainability of debt stock through yielding high primary surpluses will also be continued during the 2007-2009 period. Potential risks that might be encountered in the implementation of revenue, expenditure and borrowing policies to be carried out in compliance with this objective are given below.

- Bonds in/indexed to foreign exchange and with floating interest rates within the existing domestic debt stock might be adversely affected by the unexpected increases that might arise in foreign exchange rates or interest rates.
- Negative developments that would adversely affect the premium collection in social security institutions and inability to discipline health expenditures will result in an increase in the amount of transfers from the budget to social security institutions.
- Treasury guaranteed loans and product purchase and input guarantees given to BOT projects constitute a risk on the Treasury due to the possibility of their being undertaken by the Undersecretariat.
- In case the privatisations, the tender processes of which were completed in 2005, are cancelled during the processes of administrative actions and judicial inspection, a significant amount of revenue loss will occur.
- In case central government revenues are reduced in order to increase local administration revenues, a requirement for additional measures might arise.
- Even though wages and salaries are planned to be increased in compliance with the inflation target, requests towards increasing the prosperity levels of employees by compensating for the corrosion in their real wages that realised during crises constitute a significant risk element on personnel expenditures.

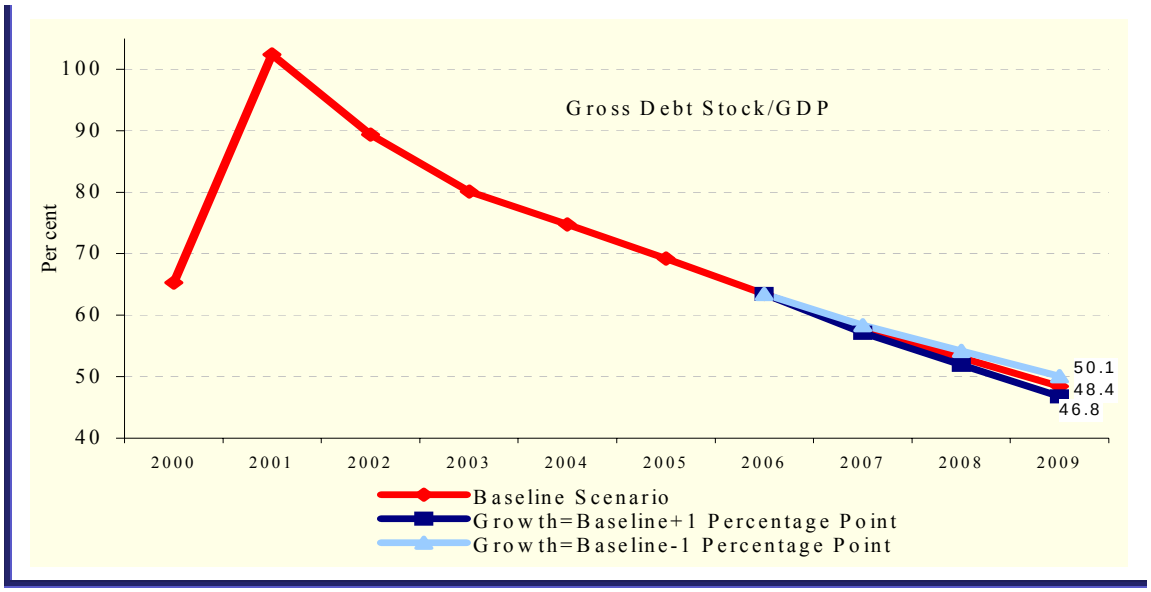
- The global liquidity, which moves in response to the interest rates of the Federal Reserve Bank of US, might continue to be an element of pressure on developing country economies.
- An unexpected rate of increase in energy prices might adversely affect the world payments system and terms of trade.

3.4. Sensitivity Analyses

Analyses of Accounting Approach

Within the scope of sensitivity analysis, impacts of the changes in the growth rate, real interest rate, primary surplus and real exchange rate on the general government gross debt stock were analysed separately for the 2006-2009 period, within the framework of the accounting approach[5]. The ratio of the general government gross debt stock in GDP realised at the level of 69.2 per cent as of the end of 2005. The subject rate is expected to decline by 5.8 percentage points at the end of 2006 compared to the previous year and realize as 63.4 per cent. Within the framework of sensitivity analyses, the gross debt stock, which is divided into two as YTL and foreign currency, drops to the level of 48.4 per cent in 2009 under the baseline scenario.

Figure. 3. 5: Analysis of Sensitivity to Growth Rate



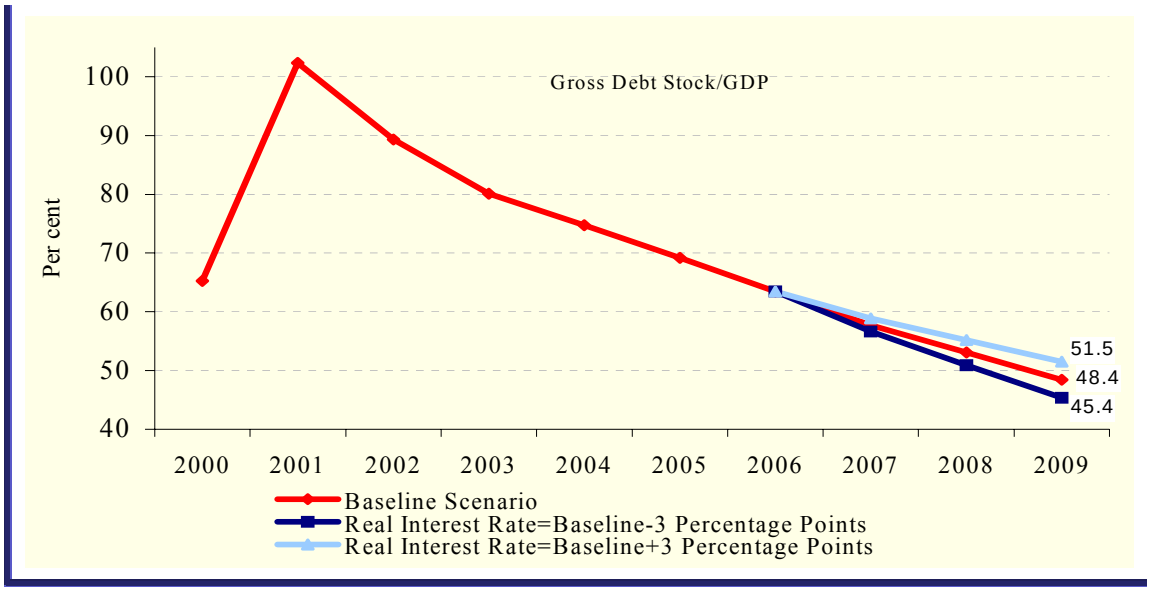
Firstly, with the aim of analysing the sensitivity of the debt burden to growth, two scenarios were created where the GDP growth rate was assumed to realize 1 point above or below the baseline scenario each year starting from 2006. According to the results of the baseline scenario, under the assumptions that the growth would realize 1 point above or below the base scenario, the ratio of the gross debt stock to GDP realizes 1.7 percentage points above and 1.6 percentage points below the baseline scenario in 2009 (Figure 3.5).

Secondly, impacts of changes in the real interest rate of the debt denominated in YTL on the debt stock were analysed and two scenarios were created where the real interest rate of the debt in YTL was assumed to realize 3 percentage points above or

[5] Detailed information concerning accounting approach is included in the 2003 PEP under the Public Finance chapter.

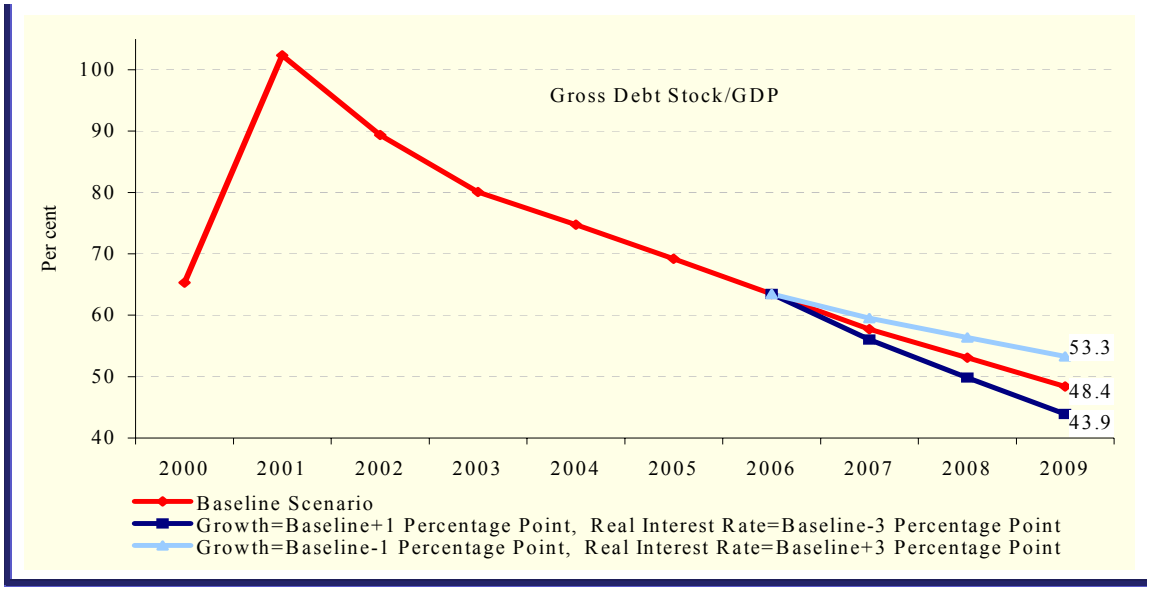
below the base scenario over the years. According to this, under the assumptions that real interest rates would realize 3 points above or below the base scenario, the percentage of the gross debt stock in GDP will be 3.1 percentage points above and 3 percentage points below the base scenario in 2009 (Figure 3.6).

Figure. 3. 6: Analysis of Sensitivity to Real Interest Rate on YTL Denominated Debt



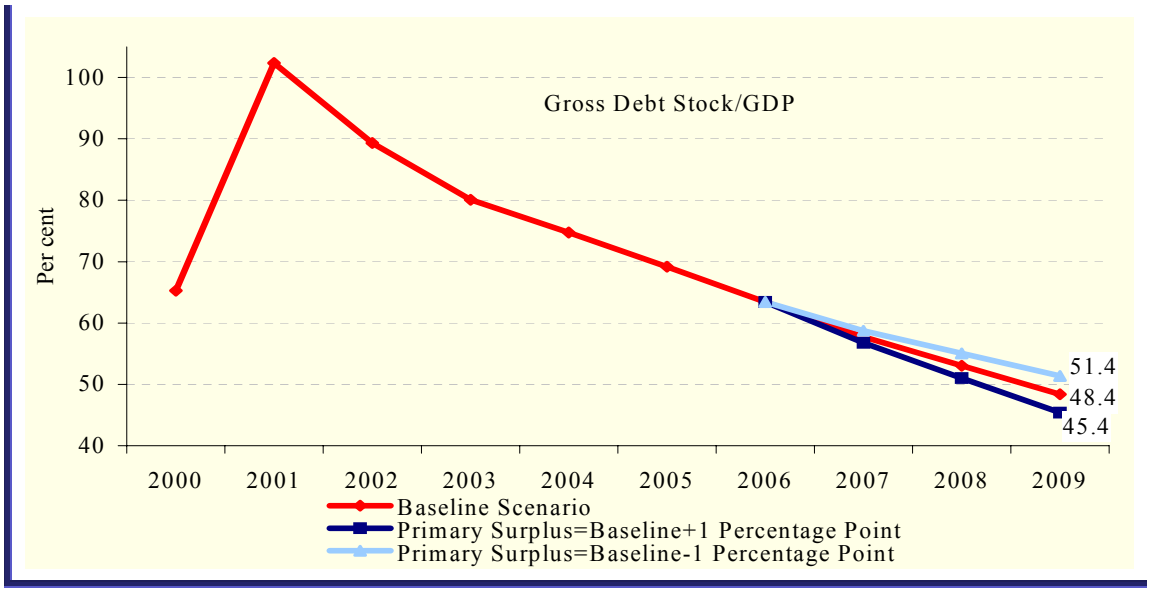
In the third analysis, impacts of the changes that might occur simultaneously in growth and real interest rates on the debt stock were analysed and two scenarios, one being optimistic and the other being pessimistic, were created with this aim. In the optimistic scenario, it was assumed that the real interest rate of the debt in YTL would realize 3 percentage points below the base scenario every year starting from 2006 and at the same time, growth would be 1 percentage point above the baseline scenario. As opposed to this, in the pessimistic scenario, it was assumed that the real interest rate of the debt in YTL would realize 3 percentage points above the baseline scenario every year starting from 2006 and at the same time, growth would be 1 percentage point below the baseline scenario. According to this, while the ratio of the gross debt stock to GDP remains 4.5 percentage points below the baseline scenario in 2009 under the optimistic scenario, the ratio of the gross debt stock to GDP remains 4.9 percentage points above the baseline scenario in 2009 under the pessimistic scenario (Figure 3.7).

Figure. 3. 7: Analysis of Sensitivity to Growth and Real Interest Rates



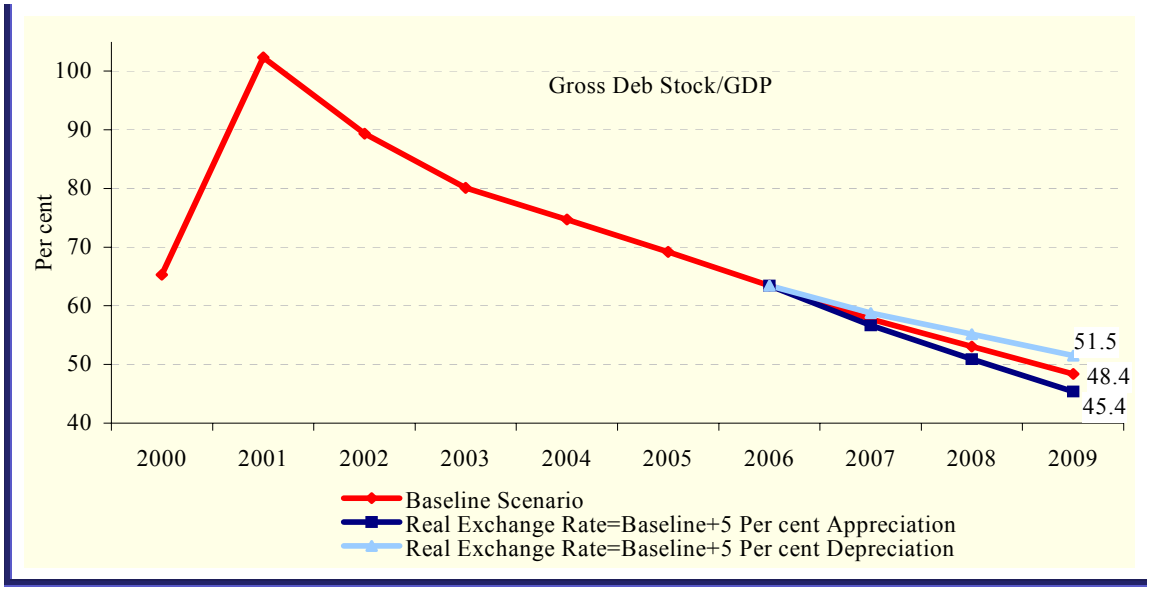
In the analysis, where the sensitivity of the debt stock to the primary surplus, which is the most important indicator of fiscal discipline, is tested, on the other hand, it was assumed that the primary surplus would realize 1 percentage point above or below the baseline scenario every year starting from 2006. Under these scenarios, it is estimated that the ratio of the gross debt stock to GDP will realize 3 percentage points above and below the baseline scenario in 2009 (Figure 3.8).

Figure. 3. 8: Analysis of Sensitivity to Primary Surplus



Finally, the sensitivity of the debt ratio to the changes in the real exchange rate is analysed. According to the results of this analysis, under the scenario where the real exchange rate depreciates at a rate of 5 per cent every year starting from 2006 compared to the baseline scenario, the ratio of the gross debt stock to GDP is found to be 3.1 percentage points above the baseline scenario. On the other hand, under the scenario where the real exchange rate appreciates at a rate of 5 per cent over the years, the debt ratio descends 3 percentage points below the base scenario (Figure 3.9).

Figure. 3. 9: Analysis of Sensitivity to Real Exchange Rate



To sum up, analyses made within the scope of the accounting approach show that in 2009, the ratio of the general government gross debt stock, which is estimated to realize at the level of 63.4 per cent at the end of 2006, will realize at a,

- 1.6 percentage points lower level if the growth rate is 1 percentage point above the baseline scenario,
- 3 percentage points lower level if the real interest rate is 3 percentage points above the baseline scenario,
- 4.5 percentage point lower level if the growth rate is 1 point above and at the same time, the real interest rate is 3 percentage points below the baseline scenario,
- 3 percentage points lower level if the ratio of the primary surplus to GDP is 1 percentage point above the baseline scenario and
- 3 percentage points lower level if the real exchange rate appreciates at a rate of 5 per cent compared to the baseline scenario.

4. STRUCTURAL REFORMS

4.1. Strengthening Market Economy and Entrepreneurship

4.1.1. Privatisation

Privatisation where considerable progresses have been made in recent years has been continued as a government policy. The state completely withdrew from the sectors of fertilizers and mining (electro metallurgy, chromium, aluminium, salt, silver, and copper), iron-steel and oil refinery between 2004 and 2006 and state transferred its leading position in the telecommunications market to the private sector. In line with the Strategy for Restructuring and Privatisation of Public Banks regarding the privatisation of the public banks, which was announced in July 2004, it is planned to privatise such public banks as Vakıflar Bank, Ziraat Bank, and Halkbank. To this end, Supreme Board of Privatisation has decided on the inclusion of Treasury's shares in Halkbank in the privatisation programme and on the sales of all those shares through block sale. Efforts are continuing to prepare a schedule to gradually remove the privileges and obligations specific to public banks.

Table. 4. 1: Privatisation Implementations, 1985-2006 *

Covered under the scope of Privatisation **	Privatised	Current Situation (October 2006)	
		Under the Scope of Privatisation	Under the Programme of Privatisations
244 companies, 22 incomplete plants, 376 real estate holdings, 6 highways, 2 suspension bridges over Bosphorus, 97 plants, 6 ports, games of chance/ transfer of operating rights, vehicle inspection stations/transfer of service rights	Privatisation of 173 companies, dissolving of the legal entity in 14 companies, transfer of 8 companies to other public enterprises have been realised.	3 companies, 6 highways, 2 suspension bridges over Bosphorus, 80 plants	12 companies, 111 real estate holdings, 2 plants, 6 ports, games of chance and vehicle inspection station services

Note: In 11 companies the public shares are still above 50 per cent.
* As of October 2006.
**23 institutions have been excluded from the scope of privatisation.

The year of 2005 can be considered as a very important year in terms of success of privatisation in Turkey. As a matter of fact, while total revenues of the privatisation operations for which sale/transfer operations was completed, was 1.3 billion dollars in 2004, it increased to 12.5 billion dollars in 2005 and to 8.2 billion dollars as of October 2006. Total revenues from all privatisations realised between 1985 and 2006 (until October) reached 25.8 billion dollars. Figures about privatised entities of which transfer/acquisition took place between 2005 and 2006 are presented in the table below.

Table. 4. 2: Privatisation Revenues and Expenditures, 1985-2006 *

Revenues			Expenditures
Privatisation Proceeds	Dividends and Other	Total	
20.1 billion dollars	3.1 billion dollars	23.2 billion dollars	23.1 billion dollars

*As of October 2006

Privatisation transactions completed between 2005 and 2006 are presented in the below table.

Table. 4. 3: Privatisation Transactions, 2005-2006 *

Company	Privatisation Transaction	Sales Price (In Dollars)
Privatisation Transactions Completed in 2005		
Türk Telekom	Block Sales of 55 per cent of Public Shares	6,550,000,000
DHMİ	Leasing of Ataturk Airport for 15.5 years	3,000,740,000
Vakıflar Bank	Public offering of 25.18 per cent of Public Stake	1,274,000,000
TÜPRAŞ	Sales of 14.76 per cent of Public Shares in ISE	453,977,633
Eti Alüminyum	Block Sales	305,000,000
PETKİM	Public offering of 34.5 per cent of Public Shares	279,976,836
Emekli Sandığı	Istanbul Hilton Hotel	255,500,000
Ataköy Otelcilik	Block Sales	62,796,764
Adapazarı Şeker Fab.	Block Sales 95.37 per cent of Public Shares	45,750,000
Samsun Gübre	Block Sales	41,000,000
Ataköy Turizm	Block Sales	33,697,808
Kıbrıs Türk Hava Yolları	Block Sales 50 per cent of Public Shares	33,000,000
Emekli Sandığı	Kuşadası Holiday Village	34,500,000
Ataköy Marina	Block Sales	23,755,428
Other	Sales and Transfer of Various Assets and Plants	103,285,762
Total		**12,496,980,231**
Privatisation Transactions Completed in 2006*		
TÜPRAŞ	Block Sales 51 per cent of Public Shares	4,140,000,000
ERDEMİR	Block Sales 49.29 per cent of Public Shares	2,960,200,000
THY	Public offering of 26.18 per cent of Public Shares	207,820,151
Başak Sigorta A.Ş.	Block Sales 56.67 per cent of Public Shares	204,376,800
Emekli Sandığı	Büyük Tarabya Hotel	145,300,000
Emekli Sandığı	Büyük Efes Hotel	121,500,000
TEKEL	Ankara Headquarter Buildings (Bilkent Twin Towers)	100,000,000
Başak Emeklilik A.Ş.	Block Sales of 41 per cent of Privatisation	63,623,200
Emekli Sandığı	Kızılay Emek Office and Shopping Building	55,500,000
TEKEL	Kayacık Salt Quarry	42,200,000
TEKEL	Kaldırım Salt Quarry	40,700,000
Karadeniz Bakır İşletmeleri	Murgul Plant/HPP/Assets	37,600,000
TEKEL	Yavşan Salt Quarry	37,300,000
Emekli Sandığı	Büyük Ankara Hotel	36,830,000
Other	Sale and Transfer of Various Assets and Plants	11,824,009
Total		**8,204,774,160**

* As of October 2006

Simultaneous tenders were held for the below three subsidiaries of Turkish Electricity Distribution Inc. as of 31 August 2006, which were included under scope of privatisation on 2 April 2004 and which are operating in below operation areas. Decisions were taken to start privatisation procedures of the Turkish electricity distribution sector.

- Region 9: Başkent Electricity Distribution Inc. (BAŞKENT)
- Region 14: İstanbul Anatolian Side Electricity Distribution Inc. (AYEDAŞ)
- Region 15: Sakarya Electricity Distribution Inc. (SEDAŞ)

Privatisation of the distribution companies will be through transfer of operation rights (TOR). According to the TOR model, an investor will acquire all shares of a distribution company, which is the single company holding electricity distribution license in one region. However, current assets and new assets to be generated upon investment of the investor will belong to TEDAŞ.

Basic objective of a liberal structure aimed in the electricity market is to lower tariffs by improving efficiency of the system. In this context, the tariffs were specified on a cost basis and within the framework of the pre-determined objectives, which are intended to be improved, about loss/illegal use and operational efficiency.

In the framework of Electricity Energy Sector Reform and Privatisation Strategy Document, privatisation of Electricity Generation Portfolio Companies of EÜAŞ will be initiated.

Privatisation of games of chance will begin after adoption of the bill specifying market regulatory mechanisms and rules.

Processes related to the privatisation of Vehicle Inspection Stations for which tender procedures were conducted in 2004, could not be completed in 2006 due to pending litigations.

In the process of privatisation of large ports belonging to Turkish State Railways (TCDD), tender procedures pertaining to Mersin and İskenderun ports were finalized and tender procedures for İzmir Port began in 2005. The deadline for submission of bids for the port, which is to be privatised through transfer of operating rights for a period of 49 years, was specified as 30 March 2007. It is planned that Bandırma, Derince, and Samsun Ports will also be tendered in 2006-2007 period.

Procedures for the privatisation of public shares in Bor, Ereğli, and Ilgın Sugar Factories and State's stake in Kayseri Sugar Factory have been ongoing and efforts about the privatisation schedule of plants and assets belonging to Turkish Sugar Factories Inc. still continue.

Considering the conjectural situation, it is planned to initiate privatisation procedures for PETKIM and TEKEL and/or their assets in shortest time, once privatisation strategy has been specified and negotiations with potential buyers have been completed.

Amount of cash transferred from the Privatisation Fund to the Treasury in the first 9 months of 2006 is 5.3 billion dollars. Current and future transfers will be used in Treasury's debt repayments and will contribute significantly to reducing the public debt stock.

4.1.2. Competition Law and Policies

As is stated in the PEP 2005, amendments aimed at ruling out problems encountered in practice were made to the Law on the Protection of Competition No. 4054 within 2005. And in 2006, the secondary legislation was amended in line with the amendments to the Law. With the amendment to the Law made in 2005, the obligation for notifying agreements, concerted practices and decisions of associations of undertakings to the Competition Board was eliminated, and a voluntary exemption notification system was introduced. With the aim of presenting explanations regarding the procedure to be followed by undertakings and associations of undertakings in voluntary exemption notifications, the Guideline Concerning the Voluntary Notification

of Agreements, Concerted Practices and Decisions of Associations of Undertakings was issued in 2006. In addition to the Guideline, with the Communiqué No. 2006/2 issued by it in 2006, the Competition Board abolished those Communiqués that had been issued during the period when the obligation for notification was effective. On the other hand, arrangements were also made in the Communiqué No. 1997/1 on Mergers and Acquisitions Calling for the Authorization of the Competition Board, parallel to the amendments to the Law made in 2005, and particularly included were provisions that a fine would be in question in case merger and acquisition transactions subject to authorization were realised without being subject to the authorization of the Competition Board.

The Block Exemption Communiqué No. 2005/4 on Vertical Agreements and Concerted Practices in the Motor Vehicle Sector which was prepared with a view to ensuring harmonization with the EU regulations and which replaced the Communiqué No. 1998/3 on Group Exemption Regarding Distribution and Servicing Agreements in relation to Motor Vehicles was published in the Official Gazette dated 12 November 2005 and was put into force on 1 January 2006. Having regard to the innovations introduced by the Commission Regulation No. 1400/2002 and the distresses observed in the market, the new Communiqué provides an automotive sector which enables manufacturers and importers to be able to apply different distribution systems, supports competitive behaviour of dealers that are strengthened vis-à-vis the provider, allows that alternative channels be included in competition in terms of spare parts and services that are briefly called as after-sales services and where, consequently, consumers can benefit from increased competition.

In the Law on the Protection of Competition No. 4054, the number of the Board members was reduced from 11 to 7, with a view to increasing efficiency in the works of the Competition Board. However, since the membership of the existing members continued, the Council of State overruled the decisions taken by the Board with the participation of 8 members on procedural grounds. With the amendment made to the Law No. 4054, the Chairman has been empowered to determine which member would be made not to participate in a meeting in turn in case the number of the Board members at the time of the meeting was more than seven.

In terms of both enhancing enforcement efficiency and harmonizing with the EU legislation, certain amendments are also required to be made to the Law on the Protection of Competition No. 4054. It is considered that following such amendments, harmonization of the Turkish legislation in the field of antitrust with the effective legislation in the EU, in the form of regulations and notices would be increased.

On the other hand, for ensuring harmonization with the EU legislation in the field of competition law and policies, the bill providing for the creation of a unit within the State Planning Organization with a view to forming a supervision mechanism for state aid that distorts competition and supervising and monitoring state aid was submitted to the Prime Ministry.

4.1.3. Improvement of the Investment Environment

Technical committees, which were formed in the scope of Reform Programme for Improvement of the Investment Environment, have been carrying on their activities. In this context, in order to include corporate governance issue into these activities, a new technical committee on corporate governance under the coordination of the Capital Market Board was established in September 2005. Additionally, a Steering Committee,

composed of ten organizations representing public and private sectors, was established in May 2005 to determine agenda of the Coordination Council for the Improvement of the Investment Environment (YOİKK), and to monitor, coordinate, and improve effectiveness of works of technical committees.

As a result of works of these committees, the following progresses have been achieved since 2005:

In relation to sectoral licensing, with the Regulation on Opening a Business Place and Work License, which was enacted in August 2005, it is aimed to extend authorities of local governments in terms of new business openings and operation licensing to reduce red tape in related procedures. Upon enforcement of the mentioned Regulation, number of documents required for the licensing sanitary business places, has been decreased from 52 to 6 and as for non-hygienic establishments, it has been decreased from 43 to 7.

With this arrangement, location selection and plant construction report was substituted with the Environmental Impact Assessment (EIA) approval certificate and report, which is prepared for plants requiring an EIA, thereby reducing the number of documents required.

Also, with the Law on Establishment, Coordination, and Duties of Development Agencies No. 5449 enforced on 25 January 2006, the arrangements on establishment of Investment Support Offices were undertaken with the aim of monitoring and coordinating the sectoral permissions required in investment and operation phases by a single authority. Regulation setting the principles and procedures for operation of these offices came into force on 25 July 2006.

In the context of works of the Technical Committee on Investment Location, the Draft Bill Amending the Coastal Act, which was prepared by Ministry of Public Works and Settlement, has been submitted to the Prime Ministry in May 2006.

Regarding the establishment of companies, with the Draft Bill Amending Turkish Commercial Law submitted to the TGNA, the liquidation process of non-problematic companies will be shortened and made easier, the requirement for being of the same type company will be repealed in company mergers and the requirement to have a government commissar in the General Assemblies of the companies will be repealed except for special companies. In addition, Technical Committee on Company Establishment has started to work on reducing cost of company establishments.

The Law on the Establishment of the Investment Support and Promotion Agency of Turkey No. 5523, which was prepared to specify and implement the investment assistance and promotion strategies to encourage foreign direct investment in Turkey, was put into force on 4 July 2006. It is envisaged that the Agency, which will be designated to ensure enforcement of the Law and perform the duties specified by the Law, will be a public legal person entity, which will have administrative and financial autonomy and be an affiliate of the Prime Ministry. Also, an investment portal (www.investinturkey.gov.tr) has been activated in May 2006 to provide the investors with on-line information.

The Law on Inserting A Provision into the Law on Organization and Duties of Ministry of Industry and Trade No. 5331 was put into force on 16 April 2005, in order to have a common SME definition in Turkey in compliance with the EU regulations. As a result of the works in the scope of the mentioned Law, the Regulation on Definition, Characteristics, and Classification of Small and Medium Sized Enterprises, which was

prepared and promulgated through the Official Gazette on 18 November 2005, provides a common SME definition in compliance with the Community acquis. This Regulation came into force 6 months after it was published in the Official Gazette. By this way, a common definition, which will be referred to in all related practices, is provided for all agencies and institutions to overcome difficulties encountered in respect to SME-related incentives and to improve effectiveness of such incentives. With this Regulation, by harmonizing the definitions and criteria used in classification of enterprise with the Community acquis, enterprises have been classified as micro enterprise, small-scale enterprise, and medium-scale enterprise. Also, the Regulation specifies independency criteria for enterprises.

With the same arrangement, it is aimed to ensure unification in definitions included in the legislation and the programs of agencies and institutions involving in SMEs-related activities, in the process of developing SMEs-related policies and planning the programs to be implemented in line with such policies and carrying out researches. A SMEs Information Web Site (URL: http://www.kobi.org.tr) project has been initiated to provide SMEs with necessary information in collaboration with related institutions. With the project, which is under the responsibility of Ministry of Industry and Trade, correct and up-to-date information on the EU funds and projects are provided to the institutions and organizations offering services, licenses, incentives, and assistances to SMEs.

On the other hand, works related to revising the SME Strategy and Action Plan, which was adopted upon decision of the High Planning Board in November 2003, have been going on and it will be ensured that the plan will be in harmony with changing conditions and that its implementation pace and effectiveness will be improved.

Regarding works initiated to deal with the institutional capacity shortages and difficulties in foreign personnel work permits, it is now possible that formalities related to applications for the permits may be finalized in 12 to 13 days, provided that all required documentations are available. The Draft Bill, which has been prepared by Ministry of Labour and Social Security to address implementation problems related to foreign personnel work permit procedures, is on the agenda of the TGNA.

The National Qualification System Law No. 5544 was put into force on 21 September 2006, to arrange the issues regarding the national competency framework, to determine the principles for national competencies in technical and vocational areas based on national and international applicable vocational standards and to establish the National Qualification Institution, which will be responsible for establishing and operating the required national competency system to carry out activities of supervision, measurement, assessment, licensing, and certification related activities.

The twinning project, which was initiated under 2003 EU-Turkey Financial Cooperation Program, aiming to support works for improving effectiveness of promotional activities to increase foreign direct investment and enhancing the investment environment in Turkey, was completed in 2006.

4.2. Financial Sector

4.2.1. Banking Sector

In the framework of privatisation strategy of public banks, preliminary works for privatisation of Halkbank have been started. In this context, in order to ensure that the privatisation process is continued in coordination among the Bank, Treasury, and

Privatisation Administration (PA) and to allow the PA to receive consultancy services, a legal arrangement has been put into effect in November 2005. In this scope, selection of the technical and legal consultancy firms has been completed in April 2006 and the firms have initiated related works. Upon submission of the reports by the consultancy firms in June 2006, privatisation of Treasury shares in Halkbank has been taken into the privatisation agenda and programme in August 2006.

Additionally, for the removal of the privileges of public banks, the schedule for re-arranging of public treasurership practices has been announced in a press release, dated 27 July 2006.

As a part of the strategy for building a robust finance system by discarding insolvent banks from the system, the works for liquidation of İmar Bank, which bankrupted in June 2005, have been ongoing. It was decided in July 2006 that the shares of Adabank, which was under the control of the Saving Deposit Insurance Fund (SDIF), would be sold to a foreign company.

The works have still been in progress to minimize the burden that the public should assume during the process of resolving of the banks under SDIF. In this scope, a total amount of 12.6 billion dollars was collected in the period between date of transfer to SDIF and June 2006, from the claims under prosecution, claims established under agreed repayment plans, sales of participations and affiliates, property, security and bank sales. In addition, 8 billion dollars of revenue is expected from the resolution of assets of banks transferred to SDIF.

The Banking Law No. 5411, which is prepared in harmony with the EU directives and internationally accepted guidelines and standards, has been put into effect on 1 November 2005. In this context, the Banking Law ensures that:

- Markets will have an effective, regular, and transparent structure,
- Rights of customers using financial services will be protected,
- Organizational structure, duties and responsibilities of Banking Regulation and Supervision Agency (BRSA) are responsive to the market requirements and BRSA has a resilient structure,
- BRSA will be responsible for regulating and supervising activities of the banks, financial holding companies, financial leasing companies, factoring companies, consumer finance institutions and the entities, which provide support services for the mentioned institutions,
- Management and organizational structure of institutions covered by the Banking Law will be responsive, resilient, and on a dialogue basis,
- Corporate governance principles will be put into effect to establish good governance,
- Turkish banking system will be integrated with international markets,
- Permits required for establishment and operation of banks will become part of prudent supervision,
- General principles, such as transparency and fairness will be maintained among the actors in the financial system,
- Financial markets will be reliable and stable,

- Any development, which may create a risk for financial markets, will be envisaged,
- Transaction and intermediation costs in banking system will be reduced,
- The strategies and policies of BRSA will be in line with the financial markets-related road maps, and
- Procedures for sharing of information by BRSA with related authorities will be governed with specific guidelines.

Secondary legislations related with the Banking Law No. 5411 have been completed as of 1 November 2006.

The Bank Cards and Credit Cards Law No. 5464 has been put into effect on 1 March 2006. In line with the Recommendation of EU Commission dated November 1998, the Law regulates relations among institutions establishing card systems, card issuing institutions, institutions contracting with businesses and member businesses and cardholders.

The Strategic Plan for 2006-2008 promulgated by BRSA on 20 July 2006, envisages strengthening of trust and stability and improvement of effectiveness and competition in financial markets, and building an effective and efficient supervision system. In this framework, it is planned to introduce a risk-based supervision approach, which determines the content, scope, form, and timing of its supervision procedures and resource allocation on the basis of risk profiles of banks. Additionally, it is aimed to effectively pursue the preparations for Basel II/Capital Adequacy Directive. BRSA has announced its Road Map for Transition to Basel II on 30 May 2005. Works to improve and update this road map have been in progress.

Results of the first Quantitative Impact Study aiming at identifying the possible impacts of the new capital adequacy directive realised by the participation of 23 banks representing 95 per cent of the entire banking sector, were announced in December 2004. Additionally, works related with the second Quantitative Impact Study for determining possible impacts of new capital adequacy directive have been initiated.

In addition to these works, the Basel II Guidance Committee comprising BRSA officials and top managers of banks in charge of risk management was established. The Basel II Coordination Committee comprising representatives from the Treasury, the Central Bank, Capital Markets Board (CMB) and Banks Association of Turkey, which will act in coordination with BRSA, was designated to provide coordination and take advisory decisions about matters pertaining to the Basel II. Furthermore, the Basel II Project Committee comprising representatives from departments of BRSA was established.

Works about the implementation of the Basel II, which were left to the initiative of national supervision authorities, have been completed. In addition, works aiming to resolve issues about SMEs, which are considered as the stakeholders that might encounter problems in adaptation to new practices introduced under the Basel II, are undertaken. Detailed studies have been conducted on the role of SMEs in the economy, financial resources of SMEs, and comparison between the current and the new system in terms of SMEs.

Banks were asked to submit their internal road maps on works related with the Basel II. Furthermore, periodic progress questionnaires for the banks have been

conducting. Upon the results obtained from these questionnaires, the Banking Sector Basel II Progress Report was published on 19 June 2006.

4.2.2. Capital Market

In order to ensure the protection of investors and creating a stable and effective market, following improvement have been made at the end of 2005 and in 2006 considering the EU Directives.

- Registration of securities and mutual funds listed in the stock exchange has been completed as of the end of 2005. The registration system, which was once operated by Takasbank (Clearing and Settlement Bank) on basis of immobilization principle, started to be operated by Central Registration System following the establishment of the legal framework.
- Preliminary works about the incorporation of the company, which is planned to be in charge of setting up the organization and infrastructure of SME-specific market, were completed as of December 2005. Among the founders of the company are The Association of Capital Market Intermediary Institutions of Turkey, the Union of Chambers and Commodity Exchanges of Turkey, and Small and Medium Industry Development Organization (KOSGEB) as well as 7 banks and 45 intermediary institutions.
- Legal arrangement requiring intermediary institutions to ask for its clients to sign risk notification form prior to any security transactions was published in the Official Gazette in December 2005. Arrangements pertaining to participation limits and institutions eligible for participation were promulgated in the Official Gazette on March 2006.
- Upon promulgation of the amendment on the related communiqué in January 2006, mutual funds and their partnerships are also allowed to include option agreements into their portfolio.
- As part of efforts towards harmonization with International Valuation Standards, Communiqué on International Valuation Standards in Capital Market was promulgated in March 2006. The mentioned communiqué was updated in August 2006 in line with the changes in the International Valuation Standards.
- Communiqué Amending the Communiqué on Principles Regarding Licensing and Registration of Those Operating in the Capital Market were promulgated in March 2006 and May 2006, setting the guidelines for the examination and the licensing of rating experts.
- Amendment on the communiqué promulgated in the Official Gazette in April 2006 expanded scope of the Communiqué on Stock Exchange Mutual Funds. This amendment allowed that the said Communiqué will also cover those stock exchange mutual funds, which are to be established to keep track of indices related with precious metals and assets based on such materials as well as capital market instruments to be specified by the Board.
- CMB's Communiqué Serial X No. 22 on Independent Auditing Standards in the Capital Market, which is fully compliant with the International Auditing Standards, was put into effect on 12 June 2006. In order to ensure harmony of practices with the said communiqué, amendments on other communiqués

about equity, bonds, other debt instruments and the exemption conditions for the issuers were also made.

- The amending Communiqué that permits existing portfolio management companies to provide portfolio management services in the field of venture capital only to qualified investors and permits incorporation of portfolio management companies solely engaged in the field of venture capital, was published in July 2006.
- The regulation on Real Estate Investment Trusts has been revised by the communiqué published in July 2006. The revision aims to create new fields of activities for the real estate investment trusts in line with world practices, to liberalise incorporation conditions of such trusts, and enhance corporate investor base in the country.
- The mortgage bill has been prepared and submitted to the TGNA. It is planned that secondary legislation on the mortgage system will be completed until December 2006.

The following are the list of actions to be carried out between 2006 and 2009 for increasing level of supply and demand in capital markets, for ensuring trust and stability in the market, for adopting the legislations in line with the community acquis and for building up the infrastructure that will allow the implementation of these legislations.

- In the context of harmonization with the EU legislation, the project, which was prepared to benefit from the PHARE programme under the Pre-Accession Financial Assistance being provided to Turkey by the EU, was initiated in February 2006. In the scope of this project, the works on market abuse, prospects, protection of investors, independent auditing, clearing and collaterals, remote provision of financial services and share acquisition were started. Within scope of the project, issues such as mutual funds, investment services, capital adequacy requirements of intermediary institutions, disclosure to public, commercial law, and other issues related to the capital market will be addressed between the last quarter of 2006 and in 2007. As a result of the process, which will take almost 2 years, the bill on Turkish Capital Market fully harmonised with the Community acquis, and the secondary regulations will be prepared and upon completion of the works about strengthening the administrative capacity, regulatory impact analysis, and training of and disclosure to the public, the project will be completed in November 2007. Furthermore, international experts will be asked to provide technical assistance in identifying the IT infrastructure requirements necessary for the implementation of the EU harmonised legislation.
- Efforts will be made to establish a registry system to ensure timely fulfilment of notification requirements and effective supervision as required under the Communiqué on Independent Auditing Standards in the Capital Market, which is harmonised with international auditing standards.
- In the context of the implementation of inflation accounting and increasing the minimum capital requirement, the criteria for redefining total assets and capital exemptions, and cancellation of the registration from the Board will be revised and necessary amendments on the related communiqué will be made.
- Secondary legislations on the mortgage system will be finalized.

- Principles and guidelines for maintaining assets covered in portfolios management by portfolio management companies will be specified.
- Actions will be undertaken to revise the Communiqué about operation, valuation, and reporting standards of valuation companies; establishment of guaranteed funds, protected funds, and fund of funds; establishment of venture capital and real-estate investment trusts; and investment trusts.
- The CMB-ISE surveillance system, aiming at compilation of data on ISE's session transactions, performing real-time oversight both via reports and screens, and detection of manipulative transactions in particular, will be in effect starting from the end of this year after the completion of the testing phase.

4.2.3. Insurance Sector

The Insurance Bill, which was prepared with consideration of requirement for adapting the insurance regulations to the community acquis and international standards, has been submitted to the TGNA on 26 May 2006.

Main purpose of the bill is to develop insurance sector in the country and to protect rights and benefits of those covered under an insurance contract. Furthermore, in order to create a reliable and stable environment in which insurance sector can effectively function, the bill also aims to revise the principles and procedures related with establishment, organization, management, operation, dissolution and auditing of persons and institutions covered under the Law, in line with EU regulations and international standards. In addition, the bill introduces new provisions about professional organizations of agents and experts and about insurance arbitration system for settlement of disputes arising from insurance contracts.

In addition, Bill on Regulating the Public Debt Management and Amending Certain Laws and Decrees has been submitted to the TGNA on 14 April 2006. The bill aims to improve regulations on pension schemes linked with employment contracts in our country and ensure harmonization with the EU regulations in respect of entitlement of employees to such pension schemes, provided that employers should contribute to such schemes in part or whole.

Secondary legislations were made in the fields of new accounting system, informing of the insurance holders and capital adequacy in order to protect the rights of the insured and to ensure a stable and effective insurance sector in 2005 and 2006, taking into consideration EU regulations and international standards.

Depending on the enactment of the draft bill, works on the secondary legislation in parallel with the Community acquis will continue in the coming period.

4.3. Labour Market

A healthy and effectively functioning labour market is the key to well functioning of a country's economy. Among the main problems hindering transition to an economic structure, which is highly competitive and has high employment creation capability, are significant unemployment rates and, rapid contraction of employment in agriculture, which accounts for one third of total employment in Turkey, low labour market participation and employment rates, low level of training and qualification of the workforce, weak linkage between education and employment, and common informal employment.

Another important factor in terms of labour market developments is the demographic trends. Demographic analysis in Turkey reveals that ratio of population at ages between 0 and 14 to total population has decreased, while the ratio of working-age population and senior citizens to total population have increased. This situation necessitates development of new policies especially for employment and education. It is expected that such change in characteristics of total population would support development if appropriate and effective education and employment policies were implemented.

No significant progress has been attained in 2005 with regard to labour market participation and employment rates, which are the most problematic issues of Turkish labour market. Compared to the EU averages, these lower rates can be basically attributed to the fact that labour market participation rate of women is very low. In 2005 labour market participation rate of women in Turkey was 26,5 per cent whereas it was around 63,5 per cent in the EU-15 countries. Therefore, a similar structure exists for employment rate of women

Table. 4. 4: Share of Age Groups in Total Population

(Per cent)

	0-14 Age Group		15-64 Age Group	
	2000	**2006**	**2000**	**2006**
EU-15	16.7	15.7	66.9	66.8
Turkey	30.0	28.1	64.7	66.0

Source: EUROSTAT

In Turkey, problems such as insufficient quality of the vocational education and lack of lifelong learning practices in particular, as well as deficiencies in capital accumulation and technological renovation processes, lead to degradation in labour efficiency.

Lack of effective interaction between employment and education in Turkey results in a disequilibrium between demanded and supplied skills in the labour market. This situation leads to both unemployment and vacant positions at the same time. There are problems as regards the supply of employees for middle level posts required in the economy. On the other hand, unemployment rate of vocational education graduates is high. Among the reasons for this are that vocational education is not in line with requirements of the labour market, and that employers cannot find labour force as skilful as they desire. This situation necessitates that vocational education should be shaped in line with labour market demands and establishment of a national vocational qualification system.

In this direction, Law on Vocational Qualification Agency has been put into effect on 21 September 2006 to establish and operate the required national qualification system in order to improve the level of technical and vocational education, through specifying principles of national qualifications in technical and vocational fields based on national and international vocational standards and carrying out supervision, measurement, assessment, and certification activities in this field.

Duration of education in vocational and technical high schools as well as general high schools increased to 4 years, applicable on the 9th grade starting from 2005-2006 semester to make vocational education at secondary education level harmonised with

labour market requirements. To this end, 250 professional standards specified by the Professional Standards Board were reviewed. The curriculum, which will allow students to transfer between education programs and provide them with modular educational system that offers 42 areas of education, developed on the basis of International Standard Classification of Education (ISCED), has been effective since the start of 2006-2007 semester throughout the country. The Project on Strengthening Vocational Education and Learning System funded through a Europe-Mediterranean Programme (MEDA) grant has had a significant role in carrying out the foregoing activities.

In Turkey, individuals who are graduated from a primary school and illiterate individuals constitute 67.3 per cent of total labour force, 68 per cent of total employment, and 60.5 per cent of total unemployed in 2005. Lower qualifications of existing labour force reduce productivity of the labour force, create mismatch between demand and supply of labour thereby degrading effectiveness of the labour market.

Table. 4. 5: Education Level of the Labour Force in 2005

(Per cent)

	Labour Force	Employed	Unemployed	Labour Force Participation Rate	Employment Rate	Unemployment Rate
Total	**100.0**	**100.0**	**100.0**	**48.3**	**43.4**	**10.3**
Illiterate	5.4	5.7	2.4	21.9	20.9	4.5
Pre-High School	61.9	62.3	58.1	47.4	42.8	9.1
High Schools and Equivalents	21.2	20.5	28.1	57.1	49.3	13.6
- Vocational and Technical High Schools	---	---	---	66.6	57.7	13.3
Higher Education	11.5	11.5	11.4	79.1	70.7	10.2

Source: TURKSTAT

When labour force is analysed according to educational levels, for the primary and high school graduates group, unemployment rate increases as the level of education increases. The main reason for this situation is that as the level of education increases labour market participation rates increase.

Informal employment, which leads to a reduction in tax revenues and insurance premium collection, unfair competition between companies, unfavourable working conditions and lack of social security for the employed, constitutes one of the most important problems of the labour market. It is estimated that 50 per cent of total employment is unregistered in 2005. On the other hand, problems in terms of labour market accession for women, the disabled, long-term unemployed and youth still continue.

Along with the non-wage labour costs, employers in Turkey also have obligations arising from the persons they have to employ and the units they must open in accordance with the number of their workers. In order to increase the employment and reduce unemployment, the necessity for reviewing the afore-mentioned obligations of employers in connection with employment and for making new arrangements with this regard, still continues to exist. Therefore; the burden on the employment will be gradually reduced by taking actuarial balances into consideration as well, in a way to

encourage the development of new employment opportunities, to increase the number of proper jobs and to reduce informal employment.

In the framework of employment-focused and sustainable growth, it will be ensured that the labour force be educated and trained with the competencies and skills required by a competitive economy and knowledge society, employment opportunities be broaden, and unemployment be reduced. To this end, the labour market will be made more functional, an effective link will be established between education and employment, necessary actions will be taken to employ the labour force coming from the agricultural sector in other sectors, active labour policies will be made effective and promoted, and resources allocated for such policies will be increased.

Towards accession to the EU, Employment Background Study was prepared in 2003 within scope of harmonisation with the European Employment Strategy. It is expected that the Joint Assessment Paper, which specifies priorities and the policies to be followed in relation with employment, will be completed by the end of 2006.

Turkish Employment Agency (İŞKUR) has carried out the Active Labour Market Programmes Project, which was jointly funded by Turkey and the EU, between 2003 and 2006 within the scope of developing active labour market policies. Within the framework of this project, almost 50,000 individuals were trained and more than 9,000 of them are employed now.

The Privatisation Social Support Project (PSSP) was completed as of the end of 2005. And, second PSSP will be carried out between 2006 and 2008, as privatisations still continue.

In the context of supporting investment and employment, the number of total individuals that benefited from an investment or employment incentive according to the Laws No. 5084 and 5350 is 141.415 as of December 2006.

Within scope of the Loan Programme for Employment of Qualified Workers, which was initiated in September 2005 in cooperation with KOSGEB, İŞKUR and Vakıflar Bank to promote employment of qualified labour force in the formal sector, 88.7 million YTL was provided to 3692 SMEs. The programme was completed as of May 2006.

It is very important that an integrated approach be adopted to address educational policies in order to overcome low education level and low education quality problems that are among the main problems of the labour market. Many initiatives have been taken to address such problems in the last couple of years, and, outcomes of such initiatives have started to be observed in education specified quantitative indicators as well.

Significant progress has been attained in terms of level of education of the population of Turkey in the last decade. Important steps have been taken in terms of objectives pertaining to the utilization of information and communication technologies and renovation of the entire curriculum to keep up with developments in the education and improve the quality of education. Within scope of projects undertaken, 23.540 schools and institutions have been provided with broadband internet access, approximately 22.000 IT classrooms have been set up 14.500 of which are for primary schools, and teachers have been provided with in-service-training on IT and communications, as of September 2006. On the other hand, the new curriculum, which was prepared in accordance with requirements of modern education, was put into effect for grades one to five of primary education in 2005-2006 semester and for the 6th grade

in 2006-2007. New course books, student study books, and teachers' manuals were prepared in line with the new curriculum and in-service-training activities provided to teachers to ensure that teachers highly adopt themselves to the new curriculum have been ongoing.

Easy access to education and higher education quality are the basic factors for quality and productivity of the labour force. Education reforms have been ongoing accordingly. With an increase in the duration of mandatory primary education to eight years and improvement of physical infrastructure of secondary education institutions, and increased importance of mass education, gross rate of schooling in primary education has risen to 95.6 per cent from 94.3 per cent, in secondary education to 85.2 per cent from 57.1 per cent, and tertiary education to 43.4 from 25.3 in the last nine years.

Table. 4. 6: Trends in Gross Schooling Rates, 1998-2006 *

(Per cent)

Level of Education	1998-99	2005-06
Pre-School	10.2	19.9
Primary Education (1)	94.3	95.6
Secondary Education (1)	57.1	85.2
Standard High Schools	32.2	54.3
Vocational-Technical High Schools	24.9	30.9
Higher Education(2)	25.3	43.4
Formal	16.3	27.5
Non-Formal	9.0	15.9

* The figures for schooling rates given in previous PEPs were net schooling rates
(1) Air-correspondence primary and high school students are included.
(2) These figures include students in universities and other education institutions but exclude graduate students for 17-20 age group.

The Basic Education Project, which is funded by a 600 million dollar loan granted by the World Bank to support the Basic Education Programme initiated in 1998, is in the final phase. Besides, the Secondary Education Project aiming to restructure our general, vocational, and technical secondary education system, to improve quality thereof, to develop related programs, to provide training to teachers in line with renovated programs, and to equip education institutions accordingly, has been initiated in 2006 with a loan worth 80 million euros granted by the World Bank.

Demand for tertiary education is still very high since no effective orientation has been provided for vocational training, no interlink has been maintained between vocational training and labour market, and capacity of tertiary education institutions has not been improved. In order to meet demand for tertiary education, 15 new state universities have been established in 2006. Thus, the number of total universities has risen to 93, including 68 state universities and 25 foundation universities.

The Regulation on Academic Evaluation and Quality Improvement in Tertiary Educational Institutions was prepared and put into force within scope of efforts to evaluate and improve the quality of tertiary educational institutions. The Regulation specified general guidelines for and obligations of tertiary educational institutions in respect to the improvement and evaluation of quality of activities and services of tertiary educational institutions and for approval and definition of level of quality of such institutions by means of independent external audit.

The Regulation on Students' Councils of Tertiary Educational Institutions and National Tertiary Educational Institutions Students' Council aiming at establishing

student associations to ensure involvement of students in university administration, has been put into effect. Works aiming to develop a regulation, which will allow national tertiary educational institutions to execute joint diploma programs with other tertiary educational institutions abroad, have been ongoing.

Within scope of the EU Education and Youth Programs, 900 students have visited Turkey in 2005 under the Erasmus Programme while 2,900 Turkish students have been sent to the EU member states. 450 European instructors have visited Turkey during the same period while 700 Turkish instructors have visited the EU member states. Within scope of the Leonardo da Vinci Programme approximately total 3,400 students, new graduates, or young workers were provided with hands-on training in various EU member states and instructors conducted study visits. Within scope of the Youth programme, on the other hand, projects of total 347 youth institutions or groups were provided financial assistance in 2005. Amount of total funds allocated for these programmes was 30.9 million euros in 2005 and 39.1 million euros in 2006.

It is very important to enhance social dialogue to ensure that arrangements in the EU harmonisation process are based on common agreement among all stakeholders. In order to attain this, existing social dialogue mechanisms in Turkey should be strengthened at national, sectoral, and bilateral levels, in particular. To this end, the Social Dialogue Project, which is financed jointly by EU and Turkey and undertaken by Ministry of Labour and Social Security, has been initiated on 1 February 2006. The project aims at strengthening social dialogue at any level, achieving harmonisation with the related EU regulations and accelerating acquis implementation process, and taking necessary actions to assume obligations specified by the EU social policies, including the post accession period as well.

The Law Regarding Assent on Approval of the Reviewed European Social Charter has been put into force on 3 October 2006.

Table. 4. 7: Matrix of Policy Commitments: Labour Market

(In 1000 Euros)

	2005	2006	2007	2008	2009
1. Privatisation Social Support Project II					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-9,500	-25,779	-27,750	-26,971	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-9,500	-25,779	-27,750	-26,971	---
2. Active Labour Market Programs Project					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-6,626	---	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-6,626	---	---	---	---
3. Project for Strengthening Social Dialogue for Innovation and Change					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-125	---	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-125	---	---	---	---
4. Basic Education Programme					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	---	-820,806	-688,997	-700,000	-640,000

B.1. Direct Effect on Budgetary Revenues (1)	---	165,850	200,000	220,000	260,000
B.2. Direct Effect on Budgetary Expenditures (2)	---	-986,656	-888,997	-920,000	-900,000
Total Net Budgetary Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-16,251	-846,585	-716,747	-726,971	-640,000
B.1. Direct Effect on Budgetary Revenues	---	165,850	200,000	220,000	260,000
B.2. Direct Effect on Budgetary Expenditures	-16,251	-1,012,435	-916,747	-946,971	-900,000

(1) It represents the difference between the cost of additional capacity acquired as a result of the tax concession provided as part of the Campaign for 100 per cent Support for Education and the loss arising from the tax concession. Tax losses were included in budgetary expenditure.

(2) The Fundamental Education Project and the projects funded by European Investment Bank were included. Expenditure funded by provincial special administrations, MEDA grants and the Social Solidarity Fund were not considered since they are not included in the budget.

4.4. Administrative Reform

Public Financial Management and Control Law

The Law No. 5428 Amending Some Articles of the Constitution of the Republic of Turkey, published in the Official Gazette dated 9 November 2005, has amended budget-related provisions of the Constitution in the context of the Public Financial Management and Control Law No. 5018. These amendments ensure uniformity and consistency between the Law No. 5018 and related provisions of the Constitution.

After promulgation of the Law No. 5018, in the context of the discussions with the EU officials, issues detected during secondary legislation preparation phase required by the Law, and remarks and recommendations received from related public agencies, it was realised that an amendment was necessary on the Law. To this end, the Law No. 5436 Amending the Public Financial Management and Control Law and Certain Laws and Decrees was prepared and published in the Official Gazette on 24 December 2005.

By the Law No. 5436,

- To improve enforcement of the Law No. 5018 all provisions of the Law will become effective on 1 January 2006. Along with this, some expressions were corrected, the internal control system was re-defined and made more comprehensive, in order to accelerate the transaction process and increase efficiency in expenditures financial control officer was discarded from the system and provisions were made for performing ex ante financial control function by the financial services department and by spending units, and duties, authorities, and responsibilities of the financial services department as well as attached charts were revised.
- Budget Departments, Finance Departments, and Research, Planning, and Coordination Boards associated of public agencies have been abolished and the Financial Services Departments in all public agencies were established as of 1 January 2006. Total 1,200 financial services expert positions were provided for the Financial Services Departments and 400 individuals, who succeeded in the qualification examination, were appointed as financial services expert to Financial Services Departments. Furthermore, total 1,200 internal auditor positions have been created for internal auditing purposes in the public agencies.

Table. 4. 8: Secondary and Tertiary Legislation List of Law No. 5018

Name of the Arrangement	Legal Basis	Situation
By-Law on the Structure and Working Procedures and Principles of State Accounting Standards Board	5018 Art. 49	Published in Official Gazette dated 13.5.2005 No. 25814.
By-Law on General Government Accounting	5018 Art. 49	Published in Official Gazette dated 8.6.2005 No. 25839.
Communiqué on Public Administrations Detailed Account Plans and Joint Auxiliary Accounts	5018 Art. 49, Provisional Art.3	Published in Official Gazette dated 17.7.2005 No. 25878.
By-Law on Working Principles and Procedures of Internal Audit Coordination Board	5018 Art. 66	Published in Official Gazette dated 8.10.2005 No. 25960.
By-Law on Selection, Training and Certification of Internal Auditor Candidates	5018 Art. 65	Published in Official Gazette dated 8.10.2005 No. 25960.
General Communiqué on Authorizing Officers (Serial No:1)	5018 Art. 31	Published in 4. repeated Official Gazette dated 31.12.2005 No. 26040.
Principles and Procedures on Internal Control and Ex ante Control	5018 Art. 55, 56, 57, 58	Published in 3. repeated Official Gazette dated 31.12.2005 No. 26040.
By-Law on General Budget Accounting	5018 Art. 49	Published in 3. repeated Official Gazette dated 31.12.2005 No. 26040.
By-Law on Central Government Expenditure Documents	5018 Art. 33	Published in Official Gazette dated 31.12.2005 No. 26040 and came to force.
By-Law on the Assignment, Auditing, Authorities and Working Procedures and Principles of Accounting Officer's Paymasters	5018 Art. 61	Published in 3. repeated Official Gazette dated 31.12.2005 No. 26040.
By-Law on the training of the accounting officers, their certification and working procedures and principles.	5018 Art. 62	Published in Official Gazette dated 21.01.2006 No. 26056.
By-Law on the Procedures and Principles of Prepayment	5018 Art. 35	Published in Official Gazette dated 21.01.2006 No. 26056.
Principles and Procedures on Preparation, Visaing, Implementation and Monitoring of Detailed Expenditure and Financing Programmes.	5018 Art. 20	Budget implementation order no (2) was published in Official Gazette dated 7.2.2006 No. 26073.
By-Law on the Working Procedures and Principles of Strategy Development Units.	5018 Art. 60 5436 Art. 15	Published in Official Gazette dated 18.02.2006 No. 26084.
By-Law on Local Administrations Budget and Accounting	5018 Art. 49	Published in Official Gazette dated 10.3.2006 No. 26104.
By-Law on Accountability Reports to be Prepared by Public Administrations	5018 Art. 41	Published in Official Gazette dated 17.3.2006 No. 26111.
Principles and Procedures on Dispatching Appropriations to Public Administration Within the Scope of Central Government	5018 Art. 22	Budget Implementation Communiqué (Serial No.5) was published in Official Gazette dated 28.3.2006 No. 26122.
By-Law on the Procedures and Principles with regard to the Arrangement of Final Accounts of Public Administrations within the scope of Central Government	5018 Art. 42	Published in Official Gazette dated 26.4.2006 No. 26150.
General Communiqué on Authorizing Officers (Serial No:2)	5018 Art. 31	Published in Official Gazette dated 28.4.2006 No. 26152.
By-Law on Principles and Procedures with regard to Strategic Planning in Public Administrations	5018 Art. 9	Published in Official Gazette dated 26.5.2006 No. 26179.
By-Law on Working Principles and Procedures of Internal Auditors	5018 Art. 65	Published in Official Gazette dated 12.7.2006 No. 26226.
Strategic Planning Guide	5018 Art. 9	Included in the web site of State Planning Organization.
Performance Based Budgeting Guide	5018 Art. 9	Included in the web site of Ministry of Finance on December 2004.
Communiqué on Principles and Procedures to be implemented in Internal Auditor Appointments	5018 Art. 65	Published in Official Gazette dated 8.9.2006 No. 26283.

Source: Ministry of Finance

- Necessary arrangements have been made to restructure the revolving funds established in the public administrations until 31 December 2007 and to

determine procedures related with preparation, implementation, finalisation, accounting as well as control and auditing of budgets of such revolving funds under a regulation to be issued by the Ministry of Finance until they are restructured. Accordingly, works on the Draft Regulation on Budgeting and Accounting of Revolving Fund Enterprises prepared by the Ministry of Finance have been ongoing.

State Accounting Standards Board and Internal Audit Coordination Board to be established according to the Law No. 5018 have been established, members of these boards have been selected and these boards have started to carry out their activities. Secondary legislation necessary for implementation of the Law No. 5018 have been prepared and put into effect on 1 January 2006.

On the other hand, in the context of the Law No. 5018, starting from 2006 fiscal year the central government budget has been prepared on basis of the Medium Term Program and Medium Term Financial Plan in line with multiyear budgeting approach.

Budget Accounting Code System and Fiscal Transparency

Under the works carried out to restructure the public financial management, the Analytical Budget Classification has been put into effect in all public agencies under the general government, starting from 2006. This system strengthened transparency and accountability principles in public financial management. Furthermore, this system enables consolidation and comparison of budgets of different public administrations, which had different budgeting practices prior to introduction of the system.

An accrual based government accounting system has been introduced in all public agencies under the general government, in order to build an accounting and reporting system, which is in compliance with international standards and which will improve transparency and accountability in the public financial management and will cover all financial actions, assets, and liabilities resulting from public activities, and to generate reliable data on public finance.

The Regulation on General Government Accounting, which is an accrual based regulation enacted to regulate the guidelines pertaining to the framework chart of accounts, accounting standards, and reporting, which is compliant with the IMF's Government Financial Statistics Manual (GFSM 2001), and which covers all general-budget public agencies, special-budget administrations, regulatory and supervisory agencies, and local administrations and social security institutions has been published in the Official Gazette on 8 June 2005 and put into effect on 1 January 2006.

The Regulation on General Budget Accounting was put into effect on 1 January 2006, after promulgation in the Official Gazette on 31 December 2005. The special-budget administrations, regulatory and supervisory agencies, social security agencies, and local administrations have started to implement their respective accounting regulations and detailed chart of accounts prepared by these institutions in accordance with the General Government Accounting Regulation upon approval of the Ministry of Finance, starting from 1 January 2006.

Local Administration Reform

Local Administration Reform has been initiated so as to strengthen and restructure local administrations within the framework of Public Administration Reform that has been launched recently. In this context, Metropolitan Municipality Law No.

5216, Municipality Law No. 5393, Special Provinces Law No. 5302 and Local Administration Associations Law No. 5355 have been enacted. However, deficiencies regarding financial and managerial efficiency and qualified human resources continue in local administration units. Works to build up a financial structure in which local administration units can perform their increasing duties and responsibilities resulting from the new legislation efficiently have not been completed yet. In this context, a draft law regulating the revenues of municipalities and special provinces has been prepared but has not been enacted yet.

Ombudsman

Designation of Office of Ombudsman Law No. 5548, which proposes designation of an office of ombudsman to inspect and investigate complaints of real persons or legal persons about operation of the administration, to inspect and investigate all actions and acts as well as attitudes and behaviours of the administration, and to propose suggestions to the administration, was enacted on 28 September 2006.

Strategy Development Units

With the Law No. 5436 Amending the Public Financial Management and Control Law and Certain Laws and Decrees dated 22 December 2006, strategy development units were established in the Prime Ministry, ministries, and central units of the public agencies and institutions. Duties of these units are as follows; To carry out the necessary works in order to determine medium and long-term strategies and policies and objectives of the institution in the framework of national development strategy and policies, annual programmes and government programmes; to develop performance and quality indicators for the issues within the administration's field of duty; to collect, analyse and interpret information and data related to the management of administration, improvement of its services and performance; to examine the external factors that might affect the services in institution's field of duty; to conduct a study on the intra-institutional capacity; to analyse effectiveness and satisfaction level of services; to make general researches on the issues within the administration's field of duty, and to carry out the services pertaining to the management information systems.

Regulatory Impact Analysis

Article 24 of the Regulation on Procedures and Principles Regarding Legislation Preparation enforced on 17 February 2006 upon promulgation in the Official Gazette, introduces the regulatory impact analysis. The Article stipulates that starting from February 2007, a regulatory impact analysis should be prepared for any bills and decrees which may have financial impacts exceeding 10 million YTL when they are enforced. Besides, the Prime Ministry may also require regulatory impact analysis for any laws and decrees with financial impacts below 10 million YTL and for other regulations regardless of their financial impacts.

4.5. Agriculture and Rural Development

4.5.1. Agriculture

The basic objectives of agricultural policies are; to ensure balanced and adequate nutrition, and to access quality and safe food of the increasing population by taking food security principle into account; to build an agricultural structure, which is economically, socially and environmentally sustainable, well-organized, highly

competitive and in line with the EU; to ensure the effective use and development of natural resources.

In this regard, in the pre-accession process to the EU, while emphasis is given to raising and ensuring stability in the income level of producers, ensuring production increase using policy tools not distorting the market operation and preserving and effectively using soil and water resources both in terms of quality and quantity. By accelerating rural development efforts, it is aimed to alleviate the pressure of employment and migration from the rural to the urban areas caused by the transformation of agricultural structure. In this context, implementation of measures towards improving human resources, diversifying rural economy and enhancing rural infrastructure is important.

Plant Production

Increasing value-added in agriculture sector is mainly attributable to crop production and changes in yield directly affect growth of the sector. Structural problems, such as small and fragmented agricultural holdings, marketing problems, and insufficiency in organization of producers, hinder the increase of productivity and producers' income in the sector. In this context, in order to improve productivity and quality in plant production, it is aimed to improve quality of crops by supplying all types of reproduction materials related to the crops with high quality and higher genetic potential in line with standards, on time and with affordable prices.

The Seed Law, which was prepared to amend the Law on Registration, Control, and Certification of the Seeds (No.308 and dated 1963) in line with the EU harmonisation process and by taking into account international seed systems and advanced technologies, was enacted in 2006.

Parallel to the developments in the world, for preservation of the ecologic balance, decreasing the negative impacts of agriculture on the environment, and improving socio-economic level of producers, organic agriculture practices in Turkey have become more important. In Turkey, starting from mid 1980's, number of exported organic crops produced increased to 205 in 2005, which was 8 at the beginning. According to 2005 figures, total area used for organic agriculture in Turkey is approximately 204 thousand hectares.

The Extension and Control of Organic Agriculture Project, in order to develop training, dissemination and building institutional capacity in the field of organic agriculture, has been implemented since 1997. In the framework of the EU Financial Cooperation, the Project for Development of the Organic Agriculture and Harmonisation of Turkish Legislation with the Community acquis was initiated in 2005 as a sub-component of this project in order to develop legislative harmonisation and the data infrastructure. While total project cost of the EU harmonisation project is 1,3 million euros, all tender transactions related to the project have been completed and in the context of the project, implementation of the activities have been commenced in 2006.

Livestock Sector

In order to create a competitive structure in the livestock sector, intensive effort are being made to improve animal species, increase production of concentrated feed and fodder crops of high quality, organize animal breeders, eradicate animal diseases and pests, and diversify publications.

The Decree No. 2005/8503 of the Council of Ministers on Supporting Animal Husbandry aims at increasing of production of roughage, promotion of breeding of studs, spreading of artificial insemination, and creating regions free of animal diseases.

In addition, works on the alignment of national legislation on livestock with the related EU regulations are underway. In this context, to build an animal identity system almost entire livestock population is included in the system. Starting from 2005, works, regarding the operation and healthy functioning of the system, have been continued through the inclusion of new borns into the system and removal of those animals, which died or slaughtered from the system. Works were commenced to identify sheep and goat population.

Developments in Agricultural Subsidies

Desired progress could not be attained in especially some components of the Agricultural Reform Implementation Project (ARIP), which was initiated in 2000, to contribute to agriculture reform process and building of technical infrastructure. After the revision in 2005, the project has been extended to 2007. In this context, with the aim of accelerating works, administrative measures have been introduced for implementation of every component of the project under the responsibility of concerned institutions. The revision gives priority especially to the cadastral works supporting Farmer Registration System (NFRS), land consolidation, agricultural investment support, preservation of agricultural areas for environmental purposes, and licensed warehousing. Extension of the project to the end of 2008 is on the agenda, since some tendering procedures and expenditure items have not been completed so far.

In order to meet needs other than income stability, which is attempted to be ensured by the Direct Income Support (DIS) programme in the sector, the Law on Agriculture No. 5488 was put into force in 2006, in line with the foresights of the Agriculture Strategy Document (2006-2010) initiated in 2004. The Law basically specifies subjects and purposes of the agricultural policies, principles and priorities of agricultural support policies, and the programs through which such incentives are to be provided. In this respect, it is aimed to create a stable environment where producers are able to plan their production activities and an environment, which is not considerably affected by short-term preferences. To this end, agricultural support tools are being restructured and DIS payments are handled with other policy tools regarding production.

Proportion of DIS payments in agricultural support budget was recorded as 55 per cent, in 2006. Within scope of this tool, total area covered by the scheme increased to 17 million hectares in 2005 from 12.2 million hectares in 2001, which is the starting year of the programme, and total number of eligible farmers has increased to 2.8 million in 2005 from 2.2 million in 2001. In addition to DIS payment practice per hectare, which was introduced in 2005, additional DIS payment implementation will continue for producers, who have their soil analysed, use certificated seed, and engage in organic farming activities. An eligibility condition for producers to benefit from all agricultural supports is to be registered to the NFRS.

Decree on Supports for Rural Development Investments, which will be implemented between 2006 and 2010 and is expected to contribute to the competitiveness of the sector substantially, was put into force in 2006. With this, it is aimed to support the investments towards processing, using and marketing of agricultural products of both real and legal persons.

Implementation of Agriculture Insurance Mechanism Assisted by State has been started in 2006, pursuant to the Agriculture Insurance Law No. 5363, which was enacted in 2005 to compensate damages of farmers and breeders as a result of risks and uncertainties threatening the crop production and animal husbandry in Turkey.

Agricultural Information Infrastructure

The Project on Preparation for Implementation of the EU's Common Agriculture Policy, which is included in the EU-Turkey Financial Cooperation 2004 Programme and which includes the IACS and Land Parcel Identification System, was initiated in 2005. In this regard, within the Ministry of Agriculture and Rural Affairs, works are emphasized in order to provide support on creating basic elements of IACS at EU norms and create an operational integrated administration and control system in the medium-term.

Farm Accounting Data Network project, which will be supported in the framework of EU-Turkey Financial Cooperation, will be initiated in 2007.

Works regarding NFRS, which is a precondition for effective implementation of DIS and for farmers to be eligible to receive other agricultural supports, has come to the final phase. Works are being conducted in the scope of ARIP in order to strengthen the land registration and cadastral infrastructure, as the system is based on the land information, and in order to check whether the payments are being made to land actually being cultivated and to the right persons. Additionally, it is expected that, required hardware infrastructure will be completed in 2006 and software infrastructure will be completed at the beginning of 2007 for the establishment of Farmer Registration System.

Food Safety, Phytosanitary and Veterinary

The Law on Amendment of the Decree Law on Production, Consumption and Control of Foods No. 5179 aims at centralised execution of permission and control activities of food and food companies by Ministry of Agriculture and Rural Affairs. Nevertheless, local administration have been granted certain authorities in terms of implementation of the food legislation such as, operation permits for food producers and food registration formalities under the Greater Municipalities Law No. 5216 and the Municipalities Law No. 5393, which were enforced in 2004 and 2005 respectively. However, this amendment has created problems in maintaining a structure for centralised monitoring and intervention, in order to ensure effectiveness in control and monitoring food safety.

Law No. 5179 has been reviewed on basis of critiques received from the EU Commission and it is expected that the problems encountered in food safety control system will be eliminated. The necessary arrangements in related legislation is planned to be done to ensure production and control of animal feeds in compliance with the Community acquis.

Provincial Control Laboratory Directorates in Ankara, İzmir, İstanbul, Mersin, Samsun, Ordu, Giresun, and Antalya and Bursa Food Control and Central Research Institute Directorate have been accredited by Turkish Accreditation Agency (TURKAK) for certain types of analysis. Provincial Control Laboratory Directorates in Trabzon, Konya, Kocaeli, Gaziantep, and Tekirdağ have applied to the TURKAK for accreditation. In addition, efforts to expand scope of Provincial Control Laboratories in

Ankara, İzmir, İstanbul, and Mersin and Bursa Food Control and Central Research Institute have been in progress.

The Project for Restructuring and Strengthening of the Food Safety and Control System in Turkey, which is supported by the EU and expected to be completed in 2008, aims at ensuring food safety in Turkey, improving effectiveness in food control system and ensuring functioning of this system through assessing duties and responsibilities and institutional framework of central and regional organization of the Ministry of Agriculture and Rural Affairs and improving cooperation with the private sector in this regard. Total project cost is 11 million euros and 2 million euros of this amount is financed by Turkey. It has been scheduled to complete construction of the National Food Reference Laboratory in Ankara by 2007 and procurement of necessary tools, equipment, and devices by 2008. Works have been ongoing on the plan and project of this laboratory construction and it is expected that construction procurement process will be finalised on time. Also, it is expected that works related with procurement of food inspection equipment and setting up an information network for the Food Safety Control System to build a food control and inspection system compliant with the EU regulations, will be continued as planned.

It is noted that initiation of works related with improving technical and hygienic qualifications in food enterprises where necessary, acceleration of accreditation processes of food control laboratories, and addressing infrastructure deficiencies in the control and inspection services through the entire production chain from growers to consumers are the main priority areas in the coming period.

As part of the Project to Ensure Alignment of Turkish Legislation in the Field of Plant Health with the Community acquis, which was initiated in 2003 under the EU Financial Cooperation, four agricultural quarantine laboratories were established in Antalya, Mersin, İzmir, and İstanbul. Turkey financed 1.1 million euros of total project cost of 5.3 million euros. The project was completed at the end of 2005. In addition to that, works are ongoing to comply with Community acquis pertaining to plant health.

Regarding animal health, in order to ensure harmonisation with the Community acquis the Project for Creating an Animal Health Information System and Border Check Points, a project with cost of total 17 million euros co-funded by the EU and Turkey which provided 13.3 million euros and 3.7 million euros respectively, was initiated in 2003. Within that scope, it has been planned to set up a selected veterinary border check point in accordance with EU norms as a pilot example. To this end, a border check point has been started to operate in İstanbul Sabiha Gökçen Airport. Moreover, another project, which has been designed to set up additional 6 border check points in İzmir, Mersin (port border check point), Hatay (Cilvegözü), Habur, Gürbulak, and Sarp (land border check points) in accordance with EU norms, will be initiated in 2007 with EU grant. Also, the Avian Influenza Fight Project, which is a project financed partly through a loan by the World Bank, a grant by USA, and a grant by EU to fight with the avian influenza, has been initiated in 2006. In addition to the foregoing, projects to be financed through funds granted by the EU for controlling of foot-and-mouth disease and rabies will be initiated in 2007.

In the field of animal health, Emergency Plans were formed for avian influenza, PPR, and foot-and-mouth diseases. Control and Eradication Plans were also prepared for foot-and-mouth disease, sheep-goat pox, tuberculosis and brucellosis. Furthermore, 20 analyses being used by 9 different laboratories in the Central Veterinary and Control Research Institutes were accredited by TURKAK. The preparatory works for legislation

in compliance with the Community acquis regarding the meat and meat product plants are underway.

Fisheries

In the fisheries sector, effective utilization of the resources by ensuring conservation is essential and to this end the priority is given to the activities related to reinforcement of the administrative structure, improving the effectiveness of protection and control system and ensuring aquaculture production in harmony with the environment and supplying high quality products to the markets.

In line with this aim, the Project for Institutional Strengthening and Development of Fishery Sector covering the 2004-2006 period has been initiated in order to ensure compliance with the EU Common Fishery Policy. In the context of this project, it is planned to strengthen institutional capacity, to create legal and structural policies, to ensure protection, control and resource management and to make necessary regulations for common market organizations and for setting up of fishery vessels registration and information system to ensure efficient execution of the mentioned activities.

In the scope of this project, which is composed of twinning and technical assistance components, offices have been constructed in 30 fishery harbours to conduct controls at the landing points and to establish a sound functioning system for data collection. Setting up of the physical properties of the mentioned offices have been completed and works related with personnel training and establishment of the fisheries information system, which will provide the information flow from the offices to the center, have been going on. In addition, it is expected that works related with the installation of vessel monitoring system for controlling fishery activities, will be finalized in 2007. The Bill on the Amendment of Fisheries Law, which has been prepared in line with the EU regulations, has been submitted to the TGNA for the purposes of creating the legal foundation for implementation of the mentioned systems, enabling the establishment of fishery producers' organizations and their participation to the development of market policies, supplying healthy and high quality product to domestic and international markets, and enhancing resources through conservation.

Besides, in the scope of technical assistance component of the project, activities related to setting up the vessel registration system and designing of wholesale markets have been carried out and various training programs have been organized for the purpose of harmonization with the EU system.

4.5.2. Rural Development

In the process of the full membership to the EU, and in the context of increasing the alignment of Turkey to the acquis about rural development, solving the problems on adjustment emerged in rural areas resulted from the rapid transformation in agricultural structure, contribution to the implementation of national regional development policies, which aim to decrease development disparities among urban-rural and among regions during the period of Ninth Development Plan (2007-2013), the rural development goals of Turkey is increasing the competitiveness of rural economy, ensuring the economic and social development through increasing the income level and life quality of the rural population, extending the training and participatory organization, and protecting rural environment.

In addition to the arrangements on the building of European Agricultural Fund for Rural Development (EAFRD), this year the Council Regulation on the Instrument for

Pre-Accession (IPA) has been adopted. Therefore, the basic legal foundation for granting the rural development funds (IPARD) to Turkey by the EU during 2007 to 2013 period has been created.

In Turkey, while agricultural activities have an important role in rural development, non-agricultural activities are also emphasized more in rural development policies due to the underdevelopment of rural areas in terms of economic and social aspects, and the decline of agricultural employment.

The activities for development of rural areas will have been realised in order to contribute to the goals of Development Plan on the following principles: to ensure the harmony of rural development policies with sectoral and spatial policies, to perceive the rural development and agricultural development as a whole, to accord with the agricultural and rural policies of the EU, to consider the differing characteristics, needs and potential of the rural areas in the country, to ensure coordination and cooperation among the relevant organizations responsible for the implementations of all rural development projects, to include local administrations, the non-governmental organizations and beneficiaries in the decision making and the implementation processes.

In order to align with the EU's Common Agriculture Policy and the EU rural development policies that have become more important in terms of both cohesion and environmental policies and to design a framework for the rural development activities in our country, the National Rural Development Strategy has been endorsed in 2006. Preliminary works related with the Rural Development Plan, which will be prepared in line with the strategy document, have been ongoing. Within the scope of the Plan, for the programming of IPA rural development component, consistency and alignment with other IPA components will be ensured considering economic and social cohesion with the EU. Preliminary works on the Rural Development Plan will be supported with a technical assistance project to be initiated under the EU-Turkey Financial Cooperation. The Rural Development Plan will be designed not only to align with the EU but also to include all rural development, in terms of its coverage, activities and in a way to ensure close cooperation and division of labour between agencies.

The endeavours on capacity building are continuing regarding the management of EU rural development funds to be used by Turkey in the 2007-2013 period. The Strategy Development Division of Ministry of Agriculture and Rural Affairs has been assigned as the Managing Authority for the IPA rural development component. The Draft Law on the establishment of Agriculture and Rural Development Support Institution, which is expected to act as the IPARD Agency, was submitted to the TGNA.

In this context, technical support has been provided by a twinning project in order to strengthen the institutional capacity for the implementation of the Rural Development Plan under Turkey-EU Financial Cooperation. The project prepared to provide support for the establishment of IPARD Agency is included in the Turkey-EU 2005 Financial Cooperation Programming.

Many rural development projects, mostly funded by foreign loans and grants, have been carried out in Turkey and some of them are currently being implemented. In addition, the Village-Based Participatory Investment Programme was put into practice in 16 pilot provinces in the context of ARIP. Thus, investment projects of the civil society organizations, private sector and public sector, which are consistent with the determined criteria, are financed at certain rates. Furthermore, the Programme on

Supporting the Rural Development Investment, which is the successor of this programme, financed through domestic funds has been launched in the rest 65 provinces.

On the other hand, Anatolian Watershed Rehabilitation Project, which is planned to comprise 28 micro-basins, where poverty is widespread, in 6 provinces located in central Turkey, was started. The project aims to contribute to capacity building in compliance with EU standards and similar activities. Implementation of rehabilitation activities and income generating activities was started in micro-basins with completed plans, and it is foreseen that the implementation will be extended further.

On the other hand, in accordance with the policies of activating agricultural potential, supporting entrepreneurship and accelerating socio-economic development in rural areas, technical assistance and financial supports have been provided to more than 300 cooperatives engaged in greenhouses and livestock production activities in the rural areas in 2006.

Electrification, communication and stabilized-road infrastructure services have been largely completed in the rural areas. However, this infrastructure need to be modernized and works are continuing in this respect. Efforts are underway to extend and improve the standards of water networks, sewerage, and wastewater treatment facilities in rural areas. After the closing down of the General Directorate of Rural Services in 2005, funds have been allocated from the central government budget for village infrastructure investments of special provincial administrations in 79 provinces. In addition, it is planned that funds will be allocated to meet infrastructure needs of small-scale municipalities.

Table. 4. 9: Matrix of Policy Commitments: Agriculture

(In 1000 Euros)

	2005	2006	2007	2008	2009
Significant Developments in Agriculture Support					
1. Agricultural Reform Implementation Project (1)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-45,043	-55,525	-47,464	---	---
B.1. Direct Effect on Budgetary Revenues	0	0	0	---	---
B.2. Direct Effect on Budgetary Expenditures	-45,043	-55,525	-47,464	---	---
2. Direct Income Support (2)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-1,408,805	-1,449,905	-1,429,871	---	---
B.1. Direct Effect on Budgetary Revenues	0	0	0	---	---
B.2. Direct Effect on Budgetary Expenditures	-1,408,805	-1,449,905	-1,429,871	---	---
3. Pursuant to the Decree 2005/8503 on Supporting Livestock Sector					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-206,649	-358,403	-395,793	---	---
B.1. Direct Effect on Budgetary Revenues	0	0	0	---	---
B.2. Direct Effect on Budgetary Expenditures	-206,649	-358,403	-395,793	---	---
4. Support for Rural Development Investments					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	-27,152	-50,171	---	---
B.1. Direct Effect on Budgetary Revenues	---	0	0	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-27,152	-50,171	---	---
5. Agriculture Insurance					
A. Implementation Profile	---	---	---	---	---

B. Net Effect on Budget	---	-10,861	-27,873	---	---
B.1. Direct Effect on Budgetary Revenues	---	0	0	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-10,861	-27,873	---	---
Total Net Effect on Budget					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-1,660,497	-1,901,846	-1,951,172	---	---
B.1. Direct Effect on Budgetary Revenues	0	0	0	---	---
B.2. Direct Effect on Budgetary Expenditures	-1,660,497	-1,901,846	-1,951,172	---	---
Projects under Turkey-EU Financial Cooperation (3)					
1. Plant Health–Project to Eradicate Plant Diseases and Pests (4)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-1,168	-1,575	-1,700	-1,771	-1,941
B.1. Direct Effect on Budgetary Revenues	0	0	0	0	0
B.2. Direct Effect on Budgetary Expenditures	-1,168	-1,575	-1,700	-1,771	-1,941
2. Animal Health–Project to Eradicate Plant Animal Diseases and Pests					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-10,213	-2,715	-13,100	-13,004	-13,033
B.1. Direct Effect on Budgetary Revenues	0	8,146	0	0	0
B.2. Direct Effect on Budgetary Expenditures	-10,213	-10,861	-13,100	-13,004	-13,033
3. Restructuring the Border Check Points Project					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	---	3,375	3,375	---
B.1. Direct Effect on Budgetary Revenues	---	---	5,000	5,000	---
B.2. Direct Effect on Budgetary Expenditures	---	---	-1,625	-1,625	---
4. Controlling of Rabies Project					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	---	3,162	3,162	---
B.1. Direct Effect on Budgetary Revenues	---	---	4,552	4,552	---
B.2. Direct Effect on Budgetary Expenditures	---	---	-1,390	-1,390	---
5. Controlling of foot-and-mouth Diseases Project					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	---	10,906	10,906	10,906
B.1. Direct Effect on Budgetary Revenues	---	---	16,359	16,359	16,359
B.2. Direct Effect on Budgetary Expenditures	---	---	-5,453	-5,453	-5,453
6. Avian Influenza and Preparation for and Fight against Epidemics					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	238	-7,769	-8,100	-9,268
B.1. Direct Effect on Budgetary Revenues	---	1,650	1,095	1,095	270
B.2. Direct Effect on Budgetary Expenditures	---	-1,412	-8,864	-9,195	-9,538
7. Spread and Control of Organic Agriculture Project					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	475	610	---	---
B.1. Direct Effect on Budgetary Revenues	---	563	610	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-88	0	---	---
8. Institutionally Strengthening, Improving Fisheries Sector Project-Alignment to the Community acquis					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	1,083	3,588	-230	-230	-230
B.1. Direct Effect on Budgetary Revenues	1,293	3,812	0	0	
B.2. Direct Effect on Budgetary Expenditures	-210	-224	-230	-230	-230
9. Restructuring and Strengthening of Food Safety and Control Management in Turkey					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	0	-28	2,799	4,122	---
B.1. Direct Effect on Budgetary Revenues	0	265	3,969	4,700	---
B.2. Direct Effect on Budgetary Expenditures	0	-293	-1,170	-578	---

Total Net Effect on Budget					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-10,298	-17	-1,947	-1,539	-13,566
B.1. Direct Effect on Budgetary Revenues	1,293	14,436	31,585	31,706	16,629
B.2. Direct Effect on Budgetary Expenditures	-11,591	-14,452	-33,532	-33,246	-30,195

(1) It includes all spending under the Agricultural Reform Implementation Project including investments and transfer (excluding cadastral works).
(2) They represent spending from the budget in the current year and exclude payments related to the respective year. The amount is the projected value for 2007.
(3) In EU-funded projects, impact on budgetary revenues result from EU contributions with grant and investment component in the related projects.
(4) No amount was spent by the EU and Turkey under the projects as the bidding process related to the EU project has yet to be completed. Figures recorded as budgetary spending represent spending related to the national project, which is being implemented under the National Investment Programme and also comprises the EU Projects.
(5) The amount belongs sub-component of Improvement of Organic Agriculture and Cohesion of Turkish Acquis to EU Project, which has been initiated by EU contribution in 2005 and implemented since 1997 by financing from national budget, however the Project was activated in September 2006. The implementation period of the Project is 15 months.

4.6. Other Reform Areas

4.6.1. Regional Development

One of the five development axes defined in the Ninth Development Plan of Turkey for 2007-2013 period is to ensure the regional development. As mentioned in the Plan, basic objectives of regional development policies are to increase the harmonization and effectiveness of policies at central level, to increase institutional capacity at local level, to distribute economic development and social welfare in a balanced manner throughout the country, to keep the inter-regional migration tendencies within the region, to ensure balanced distribution of population in space and to reduce the socio-economic development disparities in rural and urban areas by ensuring a healthy structure of urbanization and increasing the welfare in the rural areas, in the framework of a development approach based on local dynamics and internal potential.

In this framework, in the scope of the Twinning Project: Support to the State Planning Organization General Directorate of Regional Development and Structural Adjustment for Strengthening Institutional and Administrative Capacity which provides a basis for sharing important experiences about improving institutional and administrative infrastructure for more effective use of resources allocated for local/regional development and development and institutionalisation of joint decision-making processes in the field of regional development; many technical studies and training activities have been carried out and also study visits to Italy and Poland have been conducted.

As for the regional level, the Draft Law on the Establishment, Coordination and Duties of Development Agencies aiming to accelerate regional development and to ensure its sustainability by means of determining and activating the potentials of the regions in cooperation among the public sector, private sector and civil society and ensuring the use of EU funds provided for regional development through an effective coordination, was enacted by Turkish Grand National Assembly on 25 January 2006.

In this scope, Development Agencies were established on 6 July 2006 in TR62 NUTS II Region (comprising the provinces of Adana and Mersin), for which the province of Adana is the center and TR31 NUTS II Region (comprising the province of İzmir), for which İzmir is the center; secretaries general of established agencies have taken office; development councils have been designated and first meetings were

realised; and administrative boards have started their regular works. The establishment of Development Agencies will go on in the course of 2007 in priority NUTS II regions where need exists. Furthermore, it is planned to arrange various training programs for improving the capacities of personnel working in the Development Agencies established and to be established and as well as to improve technical infrastructure of the Programme Coordination and Implementation Units, which coordinate the EU supported regional programmes in the regions at present.

Out of the projects received through call for proposals within the context of Cultural Heritage Development Programme under the South-eastern Anatolia Project Regional Development Programme being implemented in coordination of South-eastern Anatolia Project (SAP) Administration, 29 projects amounting 9.6 million euros were deemed successful and the implementation of projects have been started. In the scope of the Rural Development component of the Programme, contracts for 83 projects were signed as of August 2006 and 81 projects out of these have been initiated. Amount of grant provided for realization of the projects in the context of the Programme is 20 million euros.

While the evaluation process within the scope of call for proposals in Eastern Anatolia Development Programme (covering the provinces of Bitlis, Hakkari, Muş and Van) was completed, total 309 projects were deemed successful to receive funds from the grant budget of the Programme and grant contracts were signed with successful project owners. In this context, 87 per cent (29,1 million euros) of total budget allocated for grant programmes have been contracted and the implementation of the projects started. Tatvan Waste Water Treatment Project, which was initially included in the same Programme, has been rejected by the European Commission and discarded from the Programme.

Evaluation process for the projects in Local Development Initiatives, SMEs and Small Scale Infrastructure priority areas within the context of TR82 (provinces of Çankırı, Kastamonu and Sinop), TR83 (provinces of Amasya, Çorum, Samsun and Tokat) and TRA1 (provinces of Bayburt, Erzincan and Erzurum) NUTS II Regions Development Programme belonging to 2003 Financial Cooperation Programme, was completed; and as of 31 May 2006, total 396 projects were deemed successful to receive funds from the grant budget of the Programme and grant contracts were signed with successful project owners.

Within the context of the mentioned Programme, 98 per cent (48.3 million euros) of the budget allocated for grant programmes in amount of 49.3 million euros, have been contracted and become disbursable. Advances have been paid under the Programme in 2006 and also transfer of the national co-finance for the advances (9.7 million euros) has been made in 2006. Besides, transfer of national co-finance for final payments (2.4 million euros) to the grant beneficiaries will be made in 2007.

In the context of TRA2 (provinces of Ağrı, Ardahan, Iğdır and Kars), TR72 (provinces of Kayseri, Sivas and Yozgat), TR52 (provinces of Karaman and Konya) and TRB1 (provinces of Bingöl, Elazığ, Malatya and Tunceli) NUTS II Regions Development Programme under the 2004 Financial Cooperation Programme, calls for proposals were launched in April 2006 and the process for evaluating the project proposals gathered in Central Finance and Contracts Unit is ongoing. It is planned that grant contracts will be signed with successful project owners and the implementation of projects will be initiated until the end of 2006. It is planned for the Programme that 80

per cent of payments will be made in 2006 and remaining 20 per cent will be made in 2007.

In addition, it is planned that calls for proposals for TR90 (provinces of Artvin, Giresun, Gümüşhane, Ordu, Rize, Trabzon) NUTS II Region Development Programme, which was proposed under the 2005 Financial Cooperation Programme and approved by the European Commission, will be launched at the beginning of 2007. The budget of the Programme is 24 million euros in total, with 18 million euros EU contribution and 6 million euros Turkey's contribution. Local Development Initiatives, SMEs, and Tourism and Environmental Infrastructure are the priority areas to be considered in the context of the Programme. In the Programme, it is planned that 80 per cent of the payments will be made in 2007 and remaining 20 per cent will be made in 2008.

In the context of the Turkey-Bulgaria Cross-Border Cooperation Programme, implementation of 9 projects financed from 2003 Joint Small Projects Fund Programme, which costs 500 thousand euros and was supported in the framework of 2003 Financial Cooperation Programme have been in progress. Final reports for these projects have been started to prepare and no serious problem has been encountered during the programme implementation. Evaluation process for the projects received in the context of 2004 Joint Small Projects Fund with a budget of 500 thousand euros under the 2004 Financial Cooperation Programme has been completed and approval of the Delegation of the European Commission to Turkey for the short-listed projects has not been yet received. And, in scope of Edirne Ekmekçizade Kervansaray Restoration Project, another qualified project with a budget of 3.3 million euros under the 2004 Financial Cooperation Programme, restoration works have been started in March 2006 following the finalisation of contract award process. In the context of 2005 Joint Small Projects Fund with a budget of 500 thousand euros under the 2005 Financial Cooperation Programme, the guideline for applicants and application package have been submitted to the Central Finance and Contracts Unit to enable launching of the call for proposals. On the other hand, 4 projects amounting 12 million euros on environment and infrastructure priorities, prepared by various public agencies and institutions under the coordination of SPO, have been proposed for 2006 Financial Cooperation Programme.

Furthermore, as agreed with Bulgaria, the 2006 Joint Small Project Funds with a total budget of 700 thousand euros have been submitted for review under 2006 Financial Cooperation Programme.

The Interreg III/A Turkey-Greece Programme, on the other hand, has been suspended, as it has become impossible to implement the programme since political agreement, which was once obtained at the initial stage of the programme, could not be maintained.

Moreover, by means of the Project for procurement of services and goods, which was proposed in the scope of the 2005 Financial Cooperation Programme and approved by the European Commission, it is foreseen to prepare regional development strategies and operational programmes in a participatory approach and to support the prioritisation of infrastructure investment project ideas; to support enhancement of the project management and monitoring capacity, in the centre and region as a preparation for Structural Funds, as well as to provide technical consultancy, material and equipment for the establishment and operation of Development Agencies. The budget of the programme is 19.5 million euros, with 18.5 million euros EU contribution and 1 million euros Turkey's contribution. Implementation of the project will begin in 2007.

Furthermore, the works of the Yeşilırmak Basin Development Project, which has been an example of regional development plans financed from the public budget, are planned to be completed at the end of 2006 and the project implementation will begin in 2007.

It is thought that the contribution of regional programmes to economic development will be limited particularly in the pre-accession period considering the implementation period of Regional Development Programmes prepared and started to be implemented, amount of funds allocated to the programs and the capacity of regional and central agencies to draw up and implement projects. However, it is expected that project development, implementation and monitoring capacity at regional and central level will be enhanced through efficient use of pre-accession funds and capacity building activities at regional and central levels and that income and employment effects will be observed in the regions where programmes are implemented even at a limited scale.

Table. 4. 10: Matrix of Policy Commitments: Regional Development

(In 1000 Euros)

	2005	2006	2007	2008	2009
1. Regional Development in TR82, TR83 and TRA1 NUTS II Regions Programme					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	-9,655	-2,414	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-9,655	-2,414	---	---
2. Turkey-Bulgaria Cross-Border Cooperation Programme					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	-648	-2,439	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-648	-2,439	---	---
3. Regional Development in TRA2, TR72, TR52 and TRB1 NUTS II Regions Programme					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	-8,369	-12,301	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-8,369	-12,301	---	---
4. Regional Development in TR90 NUTS II Regions Programme					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	---	-4,800	-1,200	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	---	-4,800	-1,200	---
5. Technical Assistance for Programming and Management of Regional Development Programs and Support to the Establishment and Functioning of Development Agencies Project (1)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	---	-1,000	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	---	-1,000	---	---
6. EU Regional Programs (2)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	-213	-1,672	-1,735	-1,780
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---

B.2. Direct Effect on Budgetary Expenditures	---	-213	-1,672	-1,735	-1,780
7. Regional Development Project (3)					
A. Implementation Profile	---	---	X	X	X
B. Net Effect on Budget	---	-145	-279	-289	-300
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-145	-279	-289	-300
8. Allocations for Local Administrations					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	-4,973	-4,460	-3,818	-3,961
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-4,973	-4,460	-3,818	-3,961
9. Development Agencies (4)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	-5,288	-105,914	-285,540	-296,551
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-5,288	-105,914	-285,540	-296,551
Total Net Effect on Budget					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	-29,291	-135,279	-292,582	-302,592
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-29,291	-135,279	-292,582	-302,592

Note: Spending related to the programs being implemented take place in the following year due to the approval procedure under Decentralized Implementation System.

(1) In the context of the project, this amount shows the national co-finance contribution of supply tenders in order to support the establishment of Development Agencies.

(2) For the regional development projects under this project, in case of necessary circumstances, transfers will be made to the budgets of local administrations and their enterprises directly or via Ministry of Internal Affairs' budget.

(3) Yeşilırmak Project prepared by strategic planning approach.

(4) In 2006, the Draft Law on the Establishment, Coordination and Duties of Development Agencies was enacted and Development Agencies in two NUTS II regions were established. Until the end of 2006, only the displayed amount in the table could be transferred because of the delays in works of establishment.

4.6.2. Health, Social Security and Improvement of Income Distribution

The Transformation in Health Programme, which was initiated with the aim of realizing structural changes in the field of health, aims to restructure the Ministry of Health to strengthen its regulating, planning and supervising roles, create the general health insurance system, spread and facilitate access to health services, ensure rational use of medicine and medical devices and make the health information system effective. Main components of the Health Transition Project, which was initiated to support the execution of this programme are; restructuring the Ministry of Health for effective management, building the institutional capacity of the health insurance fund, reorganising the provision of health services, strengthening the human resources capacity, and building the infrastructure for health and social security. These components cover the provision of the training required for the implementation of the Transformation in Health Programme and execution of pilot implementations.

In the framework of the Transformation in Health Programme, pilot implementation of Family Medicine was started in one province in 2005 and the number of provinces was increased to three in 2006 in the scope of restructuring the provision of health services. Increasing the number of pilot provinces in 2007 and spreading the implementation to cover the whole country by the end of 2008 are aimed. With the implementation of family medicine, strengthening of the basic health services

and efficient use of the referral chain will be ensured. In addition, within the scope of restructuring the provision of health services, health units belonging to Social Insurance Institution and some public institutions were transferred to the Ministry of Health with all kinds of duties, rights and obligations, movable and immovable properties as well as vehicles, thus a centralized execution of public health services and increasing their efficiency were achieved.

In the scope of the Health Transition Project, works towards the collection, analysis and evaluation of data from health institutions in line with the determined standards are continuing. In addition, Family Medicine Information System has been developed and started to be implemented in pilot provinces.

Establishing the universal health insurance, strengthening the institutional capacity of social security system and establishing health and social security infrastructure are the common components of the social security and health reforms.

With the laws enacted in 2006 in order to solve the structural problems of the social security system, the works carried out within the scope of the social security reform have been completed to a significant extent.

The social security reform, apart from the reform implemented in 1999, is a much more comprehensive reform mostly focused on institutional structuring. With the present social security reform, which has a fundamental purpose of reaching an equitable, easily accessible and financially sustainable social security system, quite a comprehensive including a unique retirement and health system covering the whole population, and combining the social security institutions under one single organization has been achieved. Within the scope of this reform, a significant improvement was recorded through the legislation of the Social Insurances and Universal Health Insurance Law No. 5510 and the Social Security Institution Law No. 5502 in 2006 in the social security system, where in people covered benefit from the social security rights with different criteria and they were subject to the norms, which were in a dispersed structure, provision and financing of the health services were carried out within the same structure, and short and long-term insurance branches existed together.

With the Social Insurances and Universal Health Insurance Law No. 5510, five different social insurance regimes were combined and therefore the implementation, where by people benefited from social insurance rights according to different criteria, was ended. With the same law, health services were also provided with a common standard and the compulsory Universal Health Insurance system covering the whole population was established. In the health component of the mentioned Law, the scope and financing of health services were combined for all the citizens and the principles were introduced so as to collect the premiums according to the payment abilities of people and payment of health insurance premiums by the government for those who do not have the ability to pay. In addition, rules that require obedience to the referral chain and imply collection of co-payment for outpatient treatments were included with the aim of ensuring financial sustainability of the health system.

With the aim of ensuring financial sustainability and achieving long-term actuarial balances of the retirement system, amendments were made in basic parameters related to retirement with the Law No. 5510. For those who will start to work after 1 January 2007, the retirement age was increased on a gradual basis, replacement rates were reduced, retirement salaries were linked to the premiums paid, all income elements were included in the premium base, especially for civil servants, the number of premium payment days for workers was increased from 7,000 days to 9,000 days on

a gradual basis following a transition period of 20 years, and in the calculation of the premium base for the self-employed and farmers consideration of the income statement rather than income levels was introduced. In addition, the principle of government contribution to disability, old age and death insurance premium and health insurance premium was established.

With the Social Security Institution Law No. 5502, General Directorates of SSK, Social Insurance Institution for Self-Employer (BAĞ-KUR) and Pension Fund for Government Employees were abolished and combined under the new Social Security Institution. The new institution comprises the General Directorate of Social Insurances, the General Directorate of Universal Health Insurance, the General Directorate of Non-Premium Payments and the General Directorate of Service Provision. In the Law No. 5502, it is aimed to accelerate the provision of retirement and health services through establishment of social security centers with full automation at the local level in line with the single point service approach.

Box. 4. 1: Poverty and Social Inclusion in the Ninth Development Plan

Poverty and income distribution issues have been considered also in development plans and annual programs in Turkey. In this context, the title Improving Income Distribution and Fighting Against Poverty was included in the Eighth Five Year Development Plan. Even though, social inclusion, which is a relatively new concept, was not mentioned in the Eighth Five Year Development Plan on a conceptual basis, fundamental elements of social inclusion were included among the goals, principles and policies. Social inclusion, however, has been one of the issues, which have gained importance within the recent years, especially in the process of EU accession. Turkey participated in the European Union Community Programme for Fighting Against Social Exclusion as required by the Framework Agreement dated 26 February 2002 and articles 2-4 of the Memorandum of Understanding dated 3 February 2003. With the title of Improving Income Distribution, Social Inclusion and Fighting Against Poverty in the Ninth Development Plan, the concept of social inclusion was used in a development plan for the first time. Besides income distribution and poverty, there are some policies focused on some social segments, which are subject to social exclusion in terms of benefiting from education, health services, cultural opportunities, information and communication technologies, taking part in production activities and participating in the decision process under this title.

Segments that are exposed to social exclusion are concurrently the segments carrying the highest risk of poverty. When the figures concerning poverty are examined in Turkey, it is observed that food poverty is low, however, the population under the poverty line, which includes both food and non-food expenditures is still high, despite its declining trend. When the food expenditure cost is taken as the poverty line in Turkey, 1.29 per cent of the population was below the hunger line in 2004 while this ratio was 1.35 per cent in 2002. When the cost of food and non-food expenditures is considered as the poverty line, the population below this line has declined to 25.6 per cent in 2004 from its 26.96 per cent level in 2002. Poverty is most widespread in the segments of people working in the agricultural sector, people working temporarily and without social security, uneducated individuals, women, children, the old-aged and the disabled.

Table: The Poorest Segments in Terms of Food and Non-Food Expenditures

(Per cent)

	Poverty Rate		
	2002	**2003**	**2004**
Rural	34.5	37.1	40.0
Women	27.2	28.3	26.0
Illiterate	41.1	42.4	45.1
Patriarchal or Big Family	34.3	32.7	32.0
Employed in Agriculture	36.4	39.9	40.9
General Poverty Rate (Food and Non-Food Poverty)	27.0	28.1	25.6

Source: TURKSTAT Household Labour Surveys

Establishment of an efficient information processing system is also foreseen with the social security reform. Works concerning the information processing system, which will be used in eligibility inquiry, provision of health services and allowances, are carried on within the Social Security Institution.

Since 1994, improvements have been observed in the indicators of income distribution. While the Gini coefficient, which indicates the income distribution inequality, was 0.49 in 1994, it declined to 0.4 in 2004. Starting from 1994, while the share of the first four quintile from the total income increased, the share of the fifth quintile displayed a continuous trend of decrease. While the share of the first quintile, which receives the smallest share from the total income, was 4.9 per cent in 1994, it rose to 6 per cent in 2004. The share of the fifth quintile, which receives the largest share from the total income, on the other hand, dropped from 54.9 per cent in 1994 to 46.2 per cent in 2004. In addition, the GDP per capita, which was 2,598 dollars in 2002, rose to 5,008 dollars in 2005. Regulations made within the framework of health and social security reforms are also expected to positively affect these developments in the income per capita and income distribution.

Facilitating the access for the poor to basic public services and the social security system, is very important in terms of improving income distribution and fighting against poverty. The poor segment is generally supported through the social services and assistance rather than social insurance within the context of accessing health services and social security. However, the lack of common norms and standards, and a mutual database within the system of social services and assistance system, decrease the effectiveness of the system. Particularly, with the universal health insurance, premiums of those who do not have ability to pay will be compensated by the government starting from 1 January 2007, and the whole poor population will be covered within the scope of social security in terms of health services. Studies concerning social assistance and non-premium payments aiming to increase the efficiency of the social services and assistance system, which is an important component of the social security reform, have been continued. On the other hand, with the aim of improving the health indicators of the poor in priority, concerning the field of public health, programs such as the General Immunization Programme, the Programme for Controlling Diarrheali Diseases, the Programme for Controlling Acute Respiratory Infections, the National Programme on the Screening of the Newborn, the Promotion of Breastfeeding and Baby Friendly Hospitals and the Sexual Health / Reproductive Health Programme, are being carried out by the Ministry of Health.

Table. 4. 11: Matrix of Policy Commitments: Health Care-Social Security

(In 1000 Euros)

	2005	2006	2007	2008	2009
1. Neonatal Screening Programme (Phenylketonoury, Hypothyroid)					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-420	-1,200	-1,672	-1,660	-1,220
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-420	-1,200	-1,672	-1,660	-1,220
2. Ministry of Health / EU Healthy Reproduction Programme					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-1,000	-2,000	-2,000	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-1,000	-2,000	-2,000	---	---
3. Life Free of Cancer Project (1)					

A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	---	---	-300	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	---	-300	---	---
4. Application of Good Laboratory					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	---	-108	-150	-155	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-108	-150	-155	---
5. Eradication of Epidemics (2)					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	---	-1,000	-1,390	-265	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-1,000	-1,390	-265	---
6. Health Transformation Project in Health Care (3)					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-900	-11,150	28,315	84,290	100,000
B.1. Direct Effect on Budgetary Revenues	---	---	50,000	100,000	100,000
B.2. Direct Effect on Budgetary Expenditures	-900	-11,150	-21,685	-15,710	---
7. Avian Influenza Project (4)					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	---	---	-5,370	-3,229	-2,597
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	---	-5,370	-3,229	-2,597
8. Other (Medication, Biocidal project, etc.)					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-220	-1,800	-1,500	-1,000	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-220	-1,800	-1,500	-1,000	---
Total Net Budgetary Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-2,540	-17,258	16,233	77,981	96,183
B.1. Direct Effect on Budgetary Revenues	---	---	50,000	100,000	100,000
B.2. Direct Effect on Budgetary Expenditures	-2,540	-17,258	-33,767	-22,019	-3,817

(1) It is the continuation of Cancer Screening and Research Centers Project.
(2) Establishment of Surveillance System Project is included.
(3) Establishment of institutional and database infrastructure of universal health insurance and social security is included.
(4) The project has two components, one of which will be funded by the World Bank and the other by the European Union.

4.6.3. Information and Communication Technologies

One of the basic goals set out in the Ninth Development Plan for 2007-2013 is transforming Turkey to an information society.

The e-Transformation Turkey Project 2005 Action Plan, which has been prepared as a transition period plan in cooperation with related public agencies and NGO's, by the time Information Society Strategy had been in preparation within the framework of the e-Transformation Turkey Project which aims to implement this transformation vision, mainly covers the actions related with the implementation. 20 of these actions (40 per cent of total actions) have been completed and remaining 19 actions (38 per cent) have been included into the Information Society Strategy directly or after revision. Other actions, which have been carried out on continuous basis, are ensured to be monitored.

The Information Society Strategy and annexed Action Plan, which sets out main targets and policies required to be adhered by Turkey in transforming to an information society, and covers methods and tools as well as required funds to attain policy targets, were approved by the High Planning Council on 11 July 2006 and was put into force after published in the Official Gazette on 28 July 2006. The Strategy includes social transformation, information and communication technologies adoption by businesses, citizen-focused service transformation, modernisation of the public administration, globally competitive information technologies sector, competitive, widespread, and affordable communication infrastructure and services, and improvement of R&D activities and innovation. To realize the strategy, institutional organisation and governance model as well as communication strategy are involved in this Strategy.

Pursuant to the protocols executed between the Ministry of National Education and Turkish Telecom Inc. in the context of developing human resources required by the information society, 24,600 schools and institutions under Ministry of National Education were connected to Internet over Asymmetric Digital Subscriber Line (ADSL) as of November 2006. These connections enable 11 million students, 85 per cent of primary education students and 97 per cent of secondary education students, to access to the Internet. Internet connections for approximately 3,500 schools and institutions will be completed until December 2006 by Turkish Telecom, thereby making number of schools and institutions with Internet access 28,100 in total. However, remaining 11,230 schools and institutions covered under the project could not be provided with the Internet access with ADSL broad-band connection due to technical capability problems of Turkish Telecom. For these schools and institutions, necessary works were initiated in 26 pilot schools to find solutions using the satellite Internet connection under the protocol between the Ministry of National Education and Ministry of Transportation.

In the context of Education Portal works which will provide services to public, to enable communication among school administrations, students, and parents, implementation pilot project for 120 primary schools in 9 provinces has been completed by the Ministry of National Education and works related to extend the implementation of the project were initiated.

After privatisation of Turkish Telecom, the duty and responsibility to set the technical infrastructure for the e-Government Gateway where citizens and businesses would access integrated public services from a single point, was assigned to TURKSAT, Inc. by a Decree of Council of Ministers in 2006. It is expected that e-Government Gateway will be available through pilot services by the beginning of 2007.

The Identification Data Sharing System (KPS) aiming at sharing of identity information between public agencies and institutions, Central Demographic Administration System (MERNIS) that provides access to citizen identity information by a single and a unique number, Tax Offices Automation (VEDOP I-II), National Judiciary Network project (UYAP), Customs Administration Modernisation (GIMOP), Police Forces Information Network (POLNET), Accounting Office Automation System (Say2000i), and Social Security Agency (SSK) e-Declaration and Prime Ministry Legislation Information System are the major widely implemented e-Government applications. In addition, works related to the address information system, land registry and cadastre information system (TAKBIS), and assignment of single unique number for legal entities have been going on.

Regulatory works on cyber crimes have been carried out in harmony with the EU regulations. The Draft Bill on Protection of Personal Data has been submitted to the Prime Ministry. The Ministry of Justice has been reviewing the Draft Bill on Regulating the Cyber Network Services and on Cyber Crimes by taking remarks received from public agencies and institutions into account.

The memorandum of understanding regarding Turkey's participation in the Interoperable Delivery of pan-European e-Government Services to Public Administrations, Businesses and Citizens (IDABC) has been approved.

Turkey was included in the e-Government country review of OECD, which aimed to assess the level of preparation for e-Government, and the works in this scope have been completed in November 2006.

Efforts are continuing for liberalization and compliance with the Community acquis in the telecommunications sector which aim at providing low-cost and widespread telecommunications services in quality for Turkey's transformation into an information society. In this regard, the Draft Bill for the Electronic Communications Law, which aims to eliminate the disorganized structure of legislation in the field of telecommunications and make arrangements required by the sector in line with new developments, has been on the agenda of the TGNA. The Draft Bill specifies the general framework for regulations required by the sector, simplifies the authorisation process, and defines functions for policy development and regulation. The Regulation Specifying the Procedures and Guidelines for Enforcement of the Law on Universal Service, which was enacted in June 2005, was put into implementation in June 2006.

After the full liberalization, authorizations were issued for long distance telephone services starting from May 2004, and as of September 2005, 41 operators were authorized. In addition, the numbers of operators authorized by service types are given below:

1. National Telecommunications Services: 1
2. Global System for Mobile Communications (GSM) Mobile Phone Services: 3
3. Satellite Platform Services: 1
4. Satellite Telecommunications Services: 22
5. Global Mobile Personal Communications by Satellite (GMPCS) Mobile Phone Services: 5
6. Wired and Wireless Internet Service Providers: 74
7. Data Communications Services over Land Lines: 20
8. Joint Use Radio (PMR/PAMR) Services: 48
9. Infrastructure Operation Services: 5
10. Cable Platform Service: 4

In the context of compliance with the EU legislation, developments regarding secondary regulations in the field of telecommunications are given in Table 4.12.

In the context of 2002 Turkey-EU Financial Cooperation Programming, Project for Institutional Organisation of the Telecommunication Authority, which aims at developing telecommunication legislation in alignment with the Community acquis, improving current Turkish telecommunication legislation in harmony with the Community acquis, and improving capacity of the Authority by reinforcing its capability to enforce the legislation, was completed as of 10 February 2006. In addition to the related laws, in the context of the project, existing and draft secondary legislation of the Authority have been reviewed by experts for compliance with the Community

acquis and reports have been drawn up, and draft regulations on number portability, significant market power, and monitoring and supervision of license holders have been prepared.

Table. 4. 12: Legislation in the Framework of Adaptation to the Community Acquis

Date	No	Title	Remarks
15/11/2005	Official Gazette No. 25994	Regulation on Amending the Regulation of Authorization for Telecommunications Service and Infrastructure	It is an amendment to the authorization regulation, which is adding an appendix related to wired and wireless Internet service providers.
02/05/2006	Official Gazette No. 26156	Regulation on Right-of-Way in Telecommunication Service Execution	It specifies the procedures and principles related wit the right-of-way of operators enabling them to access to and use the infrastructure facilities required for execution of telecommunication services.
06/07/2006	Official Gazette No. 26220	Regulation on Amending the Regulation of Authorization for Telecommunications Service and Infrastructure	It is an amendment to the authorization regulation, which is adding an appendix related to directory services.
---	---	Right-of-Way regulations	Works are underway to comply with Full Competition Directive No. 96/19/EC.
---	---	Number Portability Regulation	The Draft Regulation aiming at alignment with the Directive 2002/22/EC of the European Parliament and of the Council on universal service and users' rights relating to electronic communications networks and services, has been submitted to the Telecommunication Board for final approval.
---	---	Amendment on the Access and Interconnection Regulation	Works are underway to conform to Directive 2002/19/EC of the European Parliament and of the Council 2 on access to, and interconnection of, electronic communications networks and associated facilities
---	---	Regulation on Procedures and Principles Regarding Identification of the Operators with Significant Market Power	Works are underway to conform to the Access Directive 2002/21/EC and the Regulation will be promulgated after enactment of the Electronic Communications Law.
---	---	Amendment on the Regulation on the Authorisation in Electronic Communications Sector	Works are underway to conform to the Authorisation Directive 2002/20/EC and the Regulation will be promulgated after enactment of the Electronic Communications Law.
---	---	Regulation on processing of personal data and the protection of privacy in the electronic communications sector	Works are underway to conform to the Directive 2002/58/EC of the European Parliament and of the Council concerning the processing of personal data and the protection of privacy in the electronic communications sector and the Directive 2006/24/EC on the retention of data generated or processed in connection with the provision of publicly available electronic communications services or of public communications networks.

Furthermore, in order to implement the Regulation on Market Monitoring and Supervision, works related with the project titled Strengthening Physical Infrastructure

for Market Monitoring in Telecommunications Sector with 4.8 million euros budget in the context of 2003 Turkey-EU Financial Cooperation Programming, aiming at the strengthening of the existing laboratory in which the Telecommunications Authority will conduct its market monitoring activities, have been in progress. The tender process for this project was completed and works related to construction of testing rooms, accreditation of laboratories, and training for laboratory personnel has been continuing. The national contribution share of 714 thousand euros in 2005 and remaining 432 thousand euros in 2006 were transferred to the main account of the National Fund National Contribution Share.

Table. 4. 13: Matrix of Policy Commitments: ICT

(In 1000 Euros)

	2005	2006	2007	2008	2009
1. Project of Enhancement of Physical Infrastructure of Telecommunication Authority					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	-714	-432	---	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	-714	-432	---	---	---
Total Net Budget Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	-714	-432	---	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	-714	-432	---	---	---

4.6.4. Transportation

Measures for increasing the efficiency of the transportation system and providing a balance between the modes of transportation were continued after 2005 and insufficiency of traffic safety, especially on highways, continued to constitute an important problem. In the framework of the European Union Accession Negotiations, screening meetings were held under two separate titles as the Transport Policy and Trans-European Networks in 2006.

Transport Infrastructure Needs Assessment (TINA) Project, which aims to determine the arteries, connections and transfer points that will constitute the extensions of the Trans-European transport network (TEN-T) to Turkey and to integrate Turkey in TEN-T, was commenced with the kick-off meeting held on 2 December 2005. The closing date of this project, the last quarter of which is reached, was set to be 30 November 2006.

In line with the action plan on railway transportation prepared by the Turkish State Railways (TCDD), a total amount of 4.3 million euros, comprising of 3.8 million euros of grant from the EU and 0.5 million euros from national sources, was obtained for the Project for Restructuring and Strengthening the Railway Sector aiming to create the legal and institutional framework of the railway sector within the scope of the Community acquis. Main components of this project are; the Organization of the Railway Sector (Twinning Project), the New Organization of TCDD, Financial Management Information System and Financial Relations with the Government.

In the scope of sub-project of the Organization of the Railway Sector; a general railway draft law regulating the railway sector, a separate draft law for the TCDD and

draft secondary legislations on Operating License, Safety Certificate, Infrastructure Access and Pricing and Passenger Rights, as well, are being prepared and expected to be completed as of November 2006. This project is being carried out in collaboration with the German Railways.

In the scope of sub-project of the New Organization of TCDD and Financial Relations with the Government, it is aimed to establish a financial information system for measuring and monitoring the financial performance of the TCDD, to develop the managerial knowledge and skills of the TCDD executives, to define the public sector obligations and regarding this to progress in the contracts to be made with the government.

In addition to this, following the negotiations held with the World Bank, an agreement was reached to support the Project for the Restructuring of the TCDD with a two-phase Applicable Programme Loan (APL) in the 2005-2010 period. This project will consist of two components, which are the supporting of the signalisation projects for increasing the line capacity on the selected TCDD lines and the restructuring of the labour force. In the scope of the first phase of this project named as APL1, 184.7 million dollars of the total loan of 221 million dollars, which is projected to be provided by the World Bank, was approved with the decision of the Council of Ministers in March 2006. In the context of this project, the tender process for the Boğazköprü-Ulukışla-Yenice, Mersin-Adana-Toprakkale Signalisation, Telecommunication Project has been continuing. Negotiations for APL2, the second phase of the project, will be started depending on the progress to be achieved under APL1. In the scope of APL2, approximately 230 million dollars of financing is expected to be obtained. 115 million dollars of this amount is planned to be provided by the World Bank.

In the framework of maritime transportation, harmonization with the Community acquis has been achieved to a great extent with 10 regulations that were put into effect regarding maritime safety and efforts for putting into effect other regulations, the drafts of which have been prepared, are still continuing. In the scope of the EU Twinning Project called Support for Strengthening Maritime Safety in Turkey and with the works carried out and measures taken in addition to this project, efficient implementation of country obligations regarding flag state implementations and port state control has been achieved. With the aim of monitoring maritime traffic in Turkish sea areas, the establishment of Automatic Identification System (AIS) and Vessel Traffic Services (VTS) will be completed. Planned works regarding port security will be realised in the framework of the EU Twinning Project, which is named Increasing Maritime Safety in the Ports and Coastal Areas of Turkey and is expected to start at the end of 2006. The process of Turkey's becoming a party to certain important international maritime contracts will be continued in the framework of the previously prepared programme.

In the context of highway transportation, 5.5 million euros portion of Highways Sector Support Project covering personnel training, machinery and equipment procurement and automation, which includes regulations for the EU harmonization process, shall be financed by the EU. For the twinning component of the project, the joint proposal by Netherlands and Germany has been selected. The contract was signed following the completion of the necessary preparations and the twinning component of the project was initiated in May 2006.

Necessary pre-conditions for the second leg of the Highways Sector Support Project, which is procurement of services, have been fulfilled. In this context, the Terms of Reference, prepared on the basis of the Report on the Assessment of the Training

Needs and the Quality of Training Facilities of the Highways Transportation Sector, has been approved by the Central Finance and Procurement Unit. The preparation of the short list from the proposals submitted to the project has been completed.

In the field of civil aviation, a growth that is beyond expectations has been achieved through the liberalization of the domestic lines market in the framework of the regional aviation policy started in Turkey in 2003. Along with the reductions in airplane ticket prices in this industry where free market conditions are in force, the number of passengers carried until the beginning of 2006 increased by 136 per cent and 40 per cent in domestic and international lines, respectively compared to 2003. The figure for the traffic growth projected by the International Air Transport Association (IATA) for Turkey for 2015 was reached in 2005. The increase in the number of the destination points where the Turkish airline companies fly in domestic and international lines has enabled the aircraft fleet and air traffic to increase as well as the sector to grow.

With the Law No. 5431 on the Organization and Duties of the General Directorate of Civil Aviation (SHGM), that was put into effect in order for strengthening the structure of the General Directorate of Civil Aviation which is in the position of the Turkish Civil Aviation authority and the first priority of which is ensuring flight safety and aviation security, General Directorate of Civil Aviation has been provided with administrative and financial autonomy. A total of 5 regulations as complementary to this Law, were prepared and in the context of these regulations, establishment of representative offices was planned in Istanbul and Antalya, which are among important aviation centers. The office in Istanbul started to operate following the necessary arrangements.

Harmonization with the Council Directive numbered 91/670/EEC, dated 16 December 1991 regarding the mutual acceptance of license certificates of personnel in order to perform activities in the Civil Aviation Field was realised with the Airplane Pilot License Regulation SHY-1 published in the Official Gazette in June 2006.

In addition, in the framework of harmonization with the Community acquis and as specified in the Council Directive numbered 94/56/EC, under Article 18 of the Regulation on the Duties, Authorities and Responsibilities of the Technical Inspectors of the General Directorate of Civil Aviation and their Working Procedures and Principles, published in the Official Gazette dated 15 April 2006, an Accident Investigation Board was set up which would be functionally independent from the General Directorate of Civil Aviation and report to the Minister.

The purpose of the Slot Application Principles Directive issued regarding the slot allocation, is to realize the necessary arrangements to ensure the most efficient use of airports in compliance with the IATA standards by all local and foreign airline companies organizing flights in scheduled or unscheduled domestic and international lines on the condition that the apron, parking area and air field capacities of Turkey's airports are included in the scope of coordination and tariff preparation.

Table. 4. 14: Matrix of Policy Commitments: Transportation

(In 1000 Euros)

	2005	2006	2007	2008	2009
1. Reconstruction of TCDD and Turkish Railway Sector					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	-477	---	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	-477	---	---	---
2. Project on Support to Road Sector					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	-1,500	-1,500	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	-1,500	-1,500	---	---
3. Increasing Maritime Safety in Ports and Coastal Areas of Turkey					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	---	-162.5	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	---	-162.5	---	---
Total Net Budget Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	-1,977	-1,662.5	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	-1,977	-1,662.5	---	---

4.6.5. Energy

Turkey attaches great importance to realizing energy market reforms and fully harmonizing the national energy legislation with the EU legislation. Important reforms have been realised in recent years and a significant progress has been made in opening the sector for competition.

The Energy Market Regulation Authority (EMRA), which was established in the framework of the Electricity Market Law that was put into force on 3 March 2001, is assigned with the duty of ensuring that the sector operates in a healthy manner. Secondary legislation works being carried out by the EMRA have been completed to a large extent. Works on the regulations required by the amendments made to the Law are currently continuing.

On the other hand, certain amendments were made to the Electricity Market Law with the Law No. 5496 dated May 2006. In this framework, regulations were made in the subjects of;

- Preparation of Transfer of Operating Rights (TOR) contracts between TEDAŞ and electricity distribution companies established to perform activities in distribution regions,
- Implementation of a price equalization mechanism until 31 December 2010,
- Conclusion of transition period contracts for energy sales and purchases among TETAŞ, EÜAŞ, distribution companies with retail sales license, groups created as a result of the restructuring of EÜAŞ or public generation companies, provided that their terms do not exceed five years.

In this framework, TEDAŞ was restructured and 20 electricity distribution regions were created, companies to perform activities in each of these regions were established and transfer of operation rights contracts were signed between TEDAŞ and these companies. Licensing the 20 distribution companies created as a result of the restructuring of TEDAŞ and approving tariffs were completed as of 1 September 2006. Works related to the licensing of Kayseri ve Civarı Elektrik Dağıtım T.A.Ş, which is currently the only private sector company, and the approval of its tariffs are continuing.

Following the determination of the hydroelectric power plants that will remain at state's ownership, works for setting up generation portfolio groups were completed. In this framework, the privatisation of generation assets is expected to start in 2007.

Transition period contracts envisioned in the Law No. 5496 were signed and the in cash implementation of the balancing and settlement mechanism, which enables the price to be formed in a competitive environment, was started in 1 August 2006, with the EMRA decision dated 20 July 2006.

With these activities realised, significant progress has been made in restructuring the electricity sector. However, the actual completion of the reforms will only be possible with the completion of the privatisation process regarding generation and distribution assets and creation of a market structure where many actors compete one another. Reforms are expected to be completed to a large extent by the end of 2009.

In the framework of the Natural Gas Market Law, which became effective in May 2001, numerous regulations in the areas of licensing, facilities, transmission, distribution and customer services, certificates, internal installation, tariffs and inspection were put in force within the past five years in the natural gas sector. Natural gas distribution tenders are being held by the EMRA to create the market structure envisioned by the Law.

All the natural gas import agreements are held by the Petroleum Pipeline Corporation (BOTAŞ). As required by the Natural Gas Market Law No. 4646, BOTAŞ will not sign any new purchase contracts until its share in the imports drops below 20 per cent of the national consumption. In addition, BOTAŞ is obliged to transfer the existing sales and purchase agreements to independent supply companies by 2009. In line with the amendment made by the second article of Law No. 5367 in the related article of Natural Gas Market Law, tender was held on 30 November 2005. Of the 16 billion sm^3 (64 lot) of tender, bid for the whole 4 billion sm^3 of Russia-Turusgaz contract was taken. The tendering process is about to complete.

Important progress has also been achieved in liberalizing the oil market, which is another component of the energy sector. Following the Oil Market Law's being into effect, important progress has been achieved in the secondary legislation works carried out with the aim of liberalizing market activities related to crude oil, fuel oil and other oil products (Table 4.15). The new market structure defined in the Oil Market Law started activities as of January 2005. In this framework, licensing activities are being continued by the EMRA. In the framework of the Oil Market Law and secondary legislation; fuel oil prices are started to be determined in the market, some regulations concerning official naming, technical arrangement and circulation were realised within the scope of the Works towards increasing the free circulation possibility and capability of oil and a market monitoring system was established.

After the Liquefied Petroleum Gas (LPG) Law dated March 2005 was put into force, secondary legislation works towards the related market were intensified. Within

this scope, By-Law on Liquefied Petroleum Gas (LPG) Market Licenses, By-Law on Liquefied Petroleum Gas (LPG) Market Authorized Manager, By-Law on Liquefied Petroleum Gas (LPG) Market Training, and By-Law on the Procedures and Principles to be followed in the Inspections and Preliminary Examinations and Investigations to be realised in the Liquefied Petroleum Gas (LPG) Market were put into force.

Draft Law on Energy Efficiency has been submitted to the TGNA. Manifold benefits, such as ensuring the rational use of energy and energy resources, providing the country economy with the savings potential, reduction of environmental pollution caused by energy use and creation of new job opportunities, are expected to be obtained with this Law, which is expected to become effective in 2007.

Projects towards the physical integration of Turkey with the EU market in the fields of electricity and gas are continuing. In this framework, Turkey–Greece gas pipeline is planned to be operational at the end of 2006. Works concerning the Turkey–Bulgaria–Romania–Hungary-Austria (Nabucco) Project are continuing. With the implementation of these projects, Turkey will become a new route in the gas supply to the EU. These projects will have important contributions for the EU, both in terms of diversifying resources and increasing competition. On the other hand, works for the UCTE (Union for the Coordination of Transmission of Electricity) membership, which will allow for the Turkish electricity system to work synchronously with UCTE are continuing.

Table. 4. 15: Legislation Realised in 2006 in Energy Market

Date	No	Name	Description
		Electricity	
24/05/2006	Official Gazette No. 26177	Law On Amending Electricity Market Law	In the context of Strategy Paper, the law defines the transition period mechanisms.
24/12/2005	Official Gazette No. 26033	By-Law on Electricity Market Import and Export	This is the latest version of the By-Law which sets forth the principles and procedures pertaining to the activities of import and/or export of electricity and principles pertaining to allocation and use of interconnection capacity for cross border trade in the electricity market.
19/03/2006	Official Gazette No. 26054	Communiqué Revoking The Communiqué Regarding Wind and Solar Measurements	Based on Provisional Article 7 of By-Law on Electricity Market Licensing, the Communique setting forth the principles and procedures regarding wind and solar measurements, which is the basis to set up electricity generation plants based on wind and solar energy, is revoked.
04/04/2006	Official Gazette No. 26129	By-Law on Concerning Electricity Demand Forecasts	This regulation sets forth the principles and procedures regarding formation of electricity demand forecasts which constitute the basis for preparation of generation capacity projection together with transmission system 10 year statement, and distribution companies' investment plans together with distribution system 10 year statement.
26/04/2006	Official Gazette No. 26150	By-Law on Electricity Market Licensing	This is the latest version of the regulation, which came into force in 2002, setting forth the principles and procedures regarding the licenses to be granted to the legal entities who shall be

			acting in electricity market.
24/06/2006	Official Gazette No. 26208	By-Law on Electricity Market Customer Services	This regulation sets forth the standards, procedures and principles that will be applied for the customers that are connected to or that seek connection to the distribution system and the parties that provide service to these customers in accordance with the connection agreements, retail agreements or bilateral agreements.
26/07/2006	Official Gazette No. 26240	Communiqué Revoking The Communiqué Regarding The Standards, Procedures and Principles To Be Applied Within The Electricity Market For Balancing and Settlement Purposes.	The subject Communiqué is revoked in the context of the start of the in cash implementation of the balancing and settlement mechanism as of 1 August 2006.
01/08/2006	Official Gazette No. 26246	By-Law on Electricity Market Grid	This is the latest version of the regulation setting forth the principles and procedures regarding the standards applicable for reliable and low-cost operation of the transmission system and ensuring system stability and energy quality in order to establish the market model envisaged in Law no. 4628.
12/08/2006	Official Gazette No. 26257	By-Law on Electricity Market Tariffs	This is the latest version of the regulation setting forth the principles and procedures governing the preparation, examination, evaluation, modification and approval of the regulated tariffs in the electricity market.
12/09/2006	Official Gazette No. 26287	By-Law on Ensuring Availability, Technical and Commercial Quality Of The Electricity In Distribution System In Electricity Market	This regulation sets forth the rules and implementation procedures and principles for the distribution companies to ensure the availability, technical and commercial quality of the electricity.
Natural Gas			
26/07/2006	Official Gazette No. 26240	By-Law Amending By-Law on The Natural Gas Market Certificate Regulation	This is the latest version of the regulation setting forth the principles and procedures regarding the certificates to be granted by the Authority to real persons or legal entities, who will perform the internal installations and service lines construction and service activities in the natural gas market.
Petroleum			
09/12/2005	Official Gazette No. 26018	By-Law on Petroleum Market Information System	This regulation sets out the principles for the collection of the information regarding the market structure and its development and defines the responsibilities of the legal entities acting in the market regarding the subject.

12/09/2006	Official Gazette No. 26287	By-Law Amending The By-Law on The Procedures and Principles To Be Followed In The Inspections, Preliminary Examinations and Investigations To Be Realized In The Petroleum Market	This is the latest version of the regulation setting forth the principles and procedures regarding the surveillance, inspection and the sanctions regarding the market activities pertaining to the delivery of petroleum and mineral oil supplied from domestic and foreign resources to consumers, directly or after processing, in a reliable, cost-effective manner within a competitive environment.
10/10/2006	Official Gazette No. 26315	By-Law Amending The By-Law on The Procedures and Principles Regarding National Marker Practice in Petroleum Market	This is the latest version of the regulation setting forth the procedures and principles regarding the affixing of national marker to fuel marketed domestically.
20/10/2006	Official Gazette No. 26325	By-Law Amending The By-Law on Petroleum Market Licensing	This is the latest version of the by-law on Petroleum Market setting forth the principles and procedures regarding licensing the real and legal entities, the declarations to be made to EMRA and the registration mechanism in order to ensure the transparent, non-discriminatory and stable performance of the market activities pertaining to the sale of petroleum supplied from domestic and foreign resources to consumers, directly or after processing, in a reliable, cost-effective manner within a competitive environment.
Liquefied Petroleum Gases (LPG)			
01/11/2006	Official Gazette No. 26333	By-Law Amending The By- Law on Liquefied Petroleum Gases (LPG) Market Licensing	This is the latest version of the regulation setting forth the principles and procedures regarding licensing the real and legal entities, the declarations to be made to EMRA and the registration mechanism in order to ensure the transparent, non-discriminatory and stable performance of the market activities pertaining to the sale of Liquefied Petroleum Gases (LPG) supplied from domestic and foreign resources to consumers in a reliable, cost-effective manner within a competitive environment.
10/05/2006	Official Gazette No. 26164	By-Law Amending The By-Law on the Procedures and Principles To Be Followed In The Inspections, Preliminary Examinations and Investigations To Be Realized In The Liquefied Petroleum Gases (LPG) Market	This is the latest version of the regulation setting forth the principles and procedures regarding the surveillance, inspection and the sanctions regarding the market activities pertaining to the delivery of Liquefied Petroleum Gases (LPG) supplied from domestic and foreign resources to consumers in a reliable, cost-effective manner within a competitive environment.

6 different projects are being implemented with the EU and EU member countries in the context of reforms in energy sector;

1. With the aim of developing energy efficiency in Turkey, the Twinning Project towards Increasing the Energy Efficiency in Turkey, which aims to strengthen the administrative capacity of the Electrical Power Resources Survey and Development Administration – National Energy Savings Center (EİEİ/UETM), which is an affiliate of the Ministry of Energy and Natural

Resources that is assigned with the duty of executing energy saving projects and contributing to the development of relevant policies, started on 13 July 2005. The general purpose of the project is the creation of an energy efficiency framework in Turkey, which is similar to those in Europe in order to increase efficiency in the use of energy in Turkey. The project also covers the activities of strengthening the legal and institutional structure and determining energy savings potential. The project is being supported by the EU, within the scope of financial cooperation programs. EU support to the subject project is 1.3 million euros.

2. In line with the purpose of creating public awareness on the efficient use of energy in buildings, preparation studies for the Creating Public Awareness on Efficient Use of Energy in Buildings Project with a budget of 1.1 million euros within the scope of the EU 2005 Financial Cooperation Programming, to be started in 2007, are currently continuing.
3. The UN-UNDP Project for Capacity-Building for the Removal of Barriers to the Implementation of Energy Efficiency Standards and Labelling in EU Candidate Member Countries with the purpose of creating public awareness on the efficient implementation of energy efficiency standards and labelling in the household appliances sector and developing the capacities of the relevant actors within the sector is expected to start in 2007. Half of the project budget, which is around 3 million dollars, will be met by the UNDP/GEF and the other half will be provided by the Turkish project stakeholders. Bulgaria, Romania, Croatia and Turkey are included in this regional project towards EU Candidate Member Countries. Activities of the subject project concerning Turkey will be carried out under the coordination of the General Directorate of the Electrical Power Resources Survey and Development Administration, with the cooperation of the Ministry of Industry and Trade, relevant institutions and sectors.
4. Technical works and trainings being carried out within the scope of the Project on Providing Legal and Know-How Support to BOTAŞ in Natural Gas Transmission and Transit are continuing and the project is expected to be completed in March 2007.
5. In the framework of the goal of fully integrating the national electricity market with the EU electricity market, the project on the Feasibility Study for Turkey's Integration to UCTE System related to the determination of the technical conditions on which the national electricity network will be connected with fully synchronization to the UCTE system, is being carried out by TEİAŞ. The budget of the project is 1.5 million euros and of this amount, 12,500 euros is national contribution.
6. The Regulatory Board Information System Project being carried out by EMRA envisages the creation of a regulatory information system structure with the aim of supporting the efficient regulation and supervision of energy markets by EMRA. The tender regarding the project was concluded as of November 2005, the contract was signed and the implementation of the project was started.

Table. 4. 16: Matrix of Policy Commitments: Energy

(In 1000 Euros)

	2005	2006	2007	2008	2009
1. Project for Feasibility Study for Turkey's Integration to UCTE Electricity System					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	-12.5	---	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditure	---	-12.5	---	---	---
Total Net Budget Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	-12.5	---	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditure	---	-12.5	---	---	---

ANNEX TABLES

Table.1: Growth and Related Indicators

Percentages unless otherwise indicated	ESA	2005	2006	2007	2008	2009
1. GDP Growth at 1987 Prices (14+15+16)	B 1 g	7.4	6.0	5.0	5.6	5.9
2. GDP at Current Prices (Billion YTL)	B 1 g	487	561	630	692	762
3. Change in GDP Deflator		5.4	8.6	7.0	4.0	4.0
4. CPI Change (Annual Average)		8.2	9.5	7.1	4.0	4.0
5. Employment Growth*		1.2	0.3	1.5	1.7	1.9
6. Labour Productivity Growth**		6.1	5.7	3.4	3.9	3.9
7. Investment Expenditures (Per cent of GDP)		25.1	24.8	24.8	24.7	25.0
Sources of Growth: Percentage Changes at 1987 Prices						
8. Private Consumption Expenditures	P3	8.8	7.6	3.3	5.3	5.8
9. Government Consumption Expenditures	P3	2.4	10.0	6.0	5.1	4.6
10. Gross Fixed Capital Formation	P51	24.0	11.6	6.0	6.0	8.1
11. Changes in Inventories and Net Acquisition of Valuables (Per cent)***	P52+P53	-2.5	-1.6	0.0	0.0	0.0
12. Exports of Goods and Services	P6	8.5	6.7	11.0	11.8	10.9
13. Imports of Goods and Services	P7	11.5	9.3	7.9	10.6	11.1
Contributions to GDP Growth						
14. Final Domestic Demand		11.6	8.9	4.3	5.6	6.5
15. Changes in Inventories and Net Acquisition of Valuables	P52+P53	-2.5	-1.6	0.0	0.0	0.0
16. External Balance of Goods and Services	P11	-1.7	-1.6	0.9	0.1	-0.6
Growth of Gross Value Added						
17. Agriculture		5.6	0.5	2.5	3.7	3.5
18. Industry		6.5	6.5	5.2	6.4	6.2
19. Construction		21.5	13.1	5.0	5.6	5.9
20. Services		8.2	6.8	5.4	5.6	6.1

* Occupied population, domestic concept, persons, national account definition.
** Growth of GDP at constant prices per person employed.
*** Contribution to growth.

Table.2: Labour Markets Developments

	2005	2006	2007	2008	2009
1.Population (Thousand Persons, Mid-year)	72,065	72,974	73,875	74,766	75,643
2.Population Growth Rate (Per cent)	1.28	1.26	1.23	1.21	1.17
3.Working Age Population (Thousand Persons)*	50,826	51,728	52,632	53,549	54,467
4.Labour-Force Participation Rate (Per cent)*	48.3	47.6	47.3	47.3	47.3
5.Employment Level (Thousand Persons)*	22,046	22,112	22,444	22,823	23,255
6. Employment Growth Rate (Per Cent)	1.2	0.3	1.5	1.7	1.9
7. Public Sector Employment (General Government, Thousand Persons)	2.391	---	---	---	---
8. Public Sector Employment Growth Rate (Per cent)	-4.5	---	---	---	---
9.Unemployment Rate (ILO Definition, Per cent)	10.3	10.1	9.8	9.8	9.7
10. Labour Cost Growth Rate (Per cent)					
Public	6.6	---	---	---	---
Private	4.5	---	---	---	---
11.Average Real Wage Growth Rate (Per cent)					
Public	7.6	---	---	---	---
Private	0.5	---	---	---	---

* +15 years-old

Table.3: Balance of Payments

Billion Dollars, Unless Otherwise Indicated	2005	2006	2007	2008	2009
1. Current Account (Per cent of GDP)	-6.4	-7.9	-7.4	-6.5	-5.7
2. Total Exports of Goods	76.9	88.0	99.9	111.9	126.3
3. Total Imports of Goods	-109.9	-127.4	-140.7	-151.9	-166.3
4. Balance on Goods	-32.9	-39.4	-40.8	-40.0	-40.0
5. Services: Credit	25.8	24.6	27.4	29.9	32.4
6. Services: Debit	-11.9	-11.1	-11.8	-13.1	-14.3
7. Balance on Services	14.0	13.5	15.5	16.7	18.1
8. Net Interest Payments From Abroad	-4.0	-5.0	-5.7	-5.4	-5.1
9. Other Net Factor Income From Abroad	-1.7	-1.3	-1.2	-1.9	-2.2
10. Current Transfers	1.5	1.5	1.8	1.8	1.8
11. *of which* from EU (Billion Euros)	---	0.3	0.5	0.5	0.5
12. Current Account Balance	-23.2	-30.8	-30.4	-28.7	-27.4
13. Foreign Direct Investment (Net)	8.7	18.3	13.2	7.2	6.8
14. Change in Official Reserves	-17.8	-2.8	-5.3	-0.2	-0.8
15. Foreign Debt (Total)	171.1	192.1	210.9	229.2	247.2
16. *of which*: Public	68.1	70.0	72.4	72.7	72.5
17. *of which*: Foreign Currency Denominated	---	---	---	---	---
18. Exchange rate vis-à-vis EURO (end-year)	1.5904	1.9100	---	---	---
19. Exchange rate vis-à-vis EURO (annual average)	1.6695	1.8036	---	---	---
20. Net Foreign Saving (Per cent of GDP) (1)	6.7	8.1	7.6	6.8	6.0
21. Domestic Private Saving (Per cent of GDP) (1)	14.4	11.4	13.7	13.4	14.0
22. Domestic Private Investment (Per cent of GDP) (1)	15.5	16.6	16.7	16.9	17.2
23. Domestic Public Saving (Per cent of GDP) (1)	4.0	5.3	3.5	4.5	5.0
24. Domestic Public Investment (Per cent of GDP) (1)	4.3	4.9	5.0	4.9	5.0

(1) Savings-investment balance calculations are based on the GDP by expenditure figures of TURKSAT. The public investment figures in the table also include SEEs investments in addition to general government.

Table.4: General Government Budgetary Developments

Per cent of GDP	ESA	2005	2006	2007	2008	2009
Net Lending by Sub-Sectors *						
1. General Government	S13	0.2	-2.7	0.6	0.0	0.3
2. Consolidated Budget	S1311	-3.0	-3.2	0.3	-0.1	-0.2
3. Funds	S1311	-0.4	-1.6	-0.5	-0.5	-0.3
4. Local Government	S1313	0.4	0.5	0.5	0.1	0.1
5. Social Security Fund	S1314	4.1	3.2	1.8	1.7	1.8
6. Revolving Funds	S1311	-0.4	-0.6	-0.6	-0.6	-0.6
7. Unemployment Fund		-1.0	-1.0	-1.0	-0.9	-0.8
8. Universal Health Insurance		0.0	0.0	0.3	0.4	0.4
General Government (S13)						
9.Total Receipts	ESA	43.9	46.3	46.5	45.9	44.9
10.Total Expenditures	ESA	43.6	43.6	47.1	45.9	45.1
11. Budget Balance*	B9	0.2	-2.7	0.6	0.0	0.3
12.Interest Payments	D41	9.5	8.4	8.5	7.2	6.7
13.Primary Balance*		-9.8	-11.1	-7.9	-7.2	-6.5
Components of Revenues						
14. Taxes	D2+D5	24.9	24.9	25.5	25.4	25.1
15. Social Funds	D61	6.9	7.8	10.5	10.7	10.6
16. Other		12.1	13.6	10.5	9.8	9.2
17. Total Receipts	ESA	43.9	46.3	46.5	45.9	44.9
Components of Expenditures						
18. Total Consumption	P3+D1	17.5	18.7	19.7	19.7	19.5
19. Social Security Transfers		8.1	8.0	8.3	8.2	8.2
20. Interest Payments	D41	9.5	8.4	8.5	7.2	6.7
21. Subsidies (1)	D3	0.9	1.1	1.0	1.0	1.1
22. Gross Fixed Capital Formation	P51	3.8	3.9	4.0	3.9	4.0
23. Other		3.7	3.6	5.6	5.8	5.7
24. Total Expenditure	ESA	43.6	43.6	47.1	45.9	45.1

(1) Includes agricultural support, duty losses of SEEs and Support and Price Stability Fund.
* (+) refers to deficit, (-) refers to surplus.

Table.5: General Government Debt Developments

	ESA	2005	2006	2007	2008	2009
Per cent of GDP						
1. Gross Debt Level		69.2	63.4	57.7	53.1	48.4
2. *Of which*: Repayments Due		29.8	23.1	20.5	13.4	10.7
3. Change in Gross Debt		-5.5	-5.8	-5.7	-4.6	-4.7
Contributions to Change in Gross Debt						
4. Primary Balance (Per cent) (*)	B9	-9.8	-11.1	-7.9	-7.2	-6.5
5. Interest Payments (Per cent) (*)	D41	9.5	8.4	8.5	7.2	6.7
6. Nominal GDP Growth (Per cent)	B1g	-13.2	-15.2	-12.3	-9.8	-10.1
7. Other Factors Influencing The Debt Ratio		8.0	12.1	6.0	5.2	5.2
8. Other Factors Influencing The Debt Ratio: Exchange Rate Change etc.		8.8	14.3	6.8	6.0	5.7
9. Other Factors Influencing The Debt Ratio: Privatisation Receipts		-0.8	-2.2	-0.8	-0.8	-0.5

(*) There is no estimated data in the framework of ESA-95 criteria.

Table.6: Divergence From Previous Update

	2005	2006	2007	2008	2009
1. GDP Growth (Per cent)					
Previous Update	5.0	5.0	5.0	5.0	---
Latest Update	7.4	6.0	5.0	5.6	5.9
Difference	2.4	1.0	0.0	0.6	---
2. Current Account Balance (Million Euros)					
Previous Update	-16,368	-17,483	-18,027	-18,421	---
Latest Update	-18,596	-24,585	-24,152	-22,629	-21,558
Difference	-2,228	-7,102	-6,125	-4,208	---
3. Total Foreign Debt Level (Million Euros)					
Previous Update	132,800	140,952	149,365	158,333	---
Latest Update	137,391	153,596	167,377	180,497	194,649
Difference	4,591	12,644	18,012	22,164	---
4. Actual General Government Balance (Per cent of GDP)					
Previous Update	-1.3	0.2	-0.9	0.0	---
Latest Update	-0.2	2.7	-0.6	0.0	-0.3
Difference	1.1	2.5	0.3	0.0	---
5. Actual General Government Primary Balance (Per cent of GDP)					
Previous Update	8.4	8.9	6.1	6.0	---
Latest Update	9.8	11.1	7.9	7.2	6.5
Difference	1.4	2.2	1.8	1.2	---
6. General Government Gross Debt Level (Per cent of GDP)					
Previous Update	70.0	65.6	61.4	56.7	---
Latest Update	69.2	63.4	57.7	53.1	48.4
Difference	-0.8	-2.2	-3.7	-3.6	---

Table.7: Assumptions on the External Economic Environment Underlying the PEP 2006 Framework

	2005	2006	2007	2008	2009
Interest Rates (Per cent)					
Domestic Interest Rate (Treasury Bill Rate, Simple)	16.6	18.0	---	---	---
Short-Term Domestic Interest Rate (Treasury Bill Rate, Simple)	---	---	---	---	---
Long-Term Domestic Interest Rate (Treasury Bill Rate, Simple)	---	---	---	---	---
Euro Area: Short-Term (3-months Money Market)	2.2	---	---	---	---
Euro Area: Long-Term (10-years Govt. Bonds)	3.4	---	---	---	---
USA: Short-Term (3-months Money Market)	3.6	---	---	---	---
USA: Long-Term (10-years Govt. Bonds)	4.3	---	---	---	---
Exchange Rates				---	---
Exchange Rate vis-à-vis € (YTL / €)	1.6695	1.8036	---	---	---
Change in Annual Average ("-" depreciation)	-5.6	8.0	---	---	---
Parity (USD/ €)	1.25	1.25	1.26	1.27	1.27
Percentage Change in Real Exchange Rate ("+" depreciation)	-11.0	1.4	2.2	0.0	0.0
Real GDP Growth					
World (excluding EU)	5.6	5.7	5.2	5.2	5.2
USA	3.2	3.4	2.3	2.8	2.8
Japan	2.6	2.7	2.3	2.1	2.1
EU-25	1.7	2.8	2.4	2.4	2.4
World Trade (In Real Terms)					
EU Export Market (Extra-EU-25)	9.0	9.6	8.6	7.8	7.8
EU Imports (Excluding intra-EU-25)	---	---	---	---	---
World Import (Excluding EU-25)	8.2	9.1	8.3	7.9	7.9
International Prices					
World Import Prices (Percentage Change)	5.2	0.7	0.4	---	---
Non-Oil Commodity Prices	8.9	23.5	1.4	-0.9	---
Oil Prices (USD per Barrel)	53.0	65.6	66.3	68.0	68.0

Table.8: Cyclical Developments *

	2005	2006	2007	2008	2009
1. GDP Growth (1987 Prices)	7.4	6.0	5.0	5.6	5.9
2. Actual Balance	-3.0	-3.2	0.3	-0.1	-0.2
3. Net Interest Payments	9.4	8.2	8.4	7.1	6.6
4. Potential GDP Growth	7.3	5.7	6.4	6.3	6.1
5. Output Gap (percentage difference from the potential)	1.5	1.8	0.4	-0.2	-0.4
6. Cyclical Budget Component	-0.7	-0.8	-0.2	0.1	0.2
7. Cyclically Adjusted Balance	2.3	1.3	2.9	1.9	1.8
8. Cyclically Adjusted Primary Balance	-7.1	-7.0	-5.6	-5.3	-5.0

* Consolidated/Central Government budget, (+) refers to deficit, (-) refers to surplus.

Table.9: Structural Reform Agenda and Developments

Measures Taken in the Last Year's PEP	Realization Status (Y/N)	Date[6]	Comments
Privatisation			
Initiation of the privatisation process for electricity distribution companies by the end of 2005	N	---	The tender process has started in August 2006 for 3 companies (AYEDAŞ, Başkent EDAŞ, SEDAŞ) The tender for these companies will be realised in January 2007.
Initiation of the privatisation process for lottery games	N	---	Waiting for the Draft Law, which includes the mechanism and the rules that regulate the market after privatisation, to be enacted.
Privatisation of public banks	N	---	Halkbank was taken into Privatisation Programme in August 2006. It is planned to be privatised via block sale within 2 years.
Privatisation of seaports of TCDD	N	---	The tenders for Mersin and İskenderun Ports could not be finalized yet. The tender for İzmir Port was declared. The last bidding date for the tender is 30 March 2007.
Privatisation of Başak Sigorta A.Ş. and Başak Emeklilik A.Ş. insurance companies.	Y	2006	Transfer transactions were completed in May 2006.
Privatisation of Tarabya and Çelik Palas Hotels of Emekli Sandığı.	Y	2006	Transfer of Tarabya was realised in June 2006. The tender opened for Çelik Palas was cancelled.
Privatisation of sugar factories	N	---	The tender process for Bor, Ereğli and Ilgın sugar factories and the public shares in Kayseri Sugar Factory has started in March 2006. The last bidding date for the tender is 30 November 2007.
Competition Law and Policies			
In respect of the Act on the Protection of Competition No. 4054; for purposes of both enhancing enforcement efficiency and ensuring harmonization with the effective legislation in the EU, in the form of Regulations and Notices.	N	---	The text of the Draft Law for which the opinions of the institutions concerned have been obtained is on the agenda of the Competition Board.
Works for aligning the Communiqué No. 1998/3 on Group Exemption Regarding Distribution and Servicing Agreements in relation to Motor Vehicles with the European Commission Regulation No. 1400/2002 on Categories of Vertical Agreements and Concerted Practices in the Motor Vehicle Sector.	Y	2006	The Block Exemption Communiqué No. 2005/4 on Vertical Agreements and Concerted Practices in the Motor Vehicle Sector which replaced the Communiqué No. 1998/3 entered into force on 1 January 2006.
Works aimed at the creation of a functionally independent state aid monitorization and supervision unit under the SPO.	N	---	The Draft Bill has been submitted to the Prime Ministry.

[6] The date or foreseen date of realization.

Improvement of the Investment Environment			
The Law on the Establishment of Development Agencies	Y	2006	The Law on Establishment, Coordination, and Duties of Development Agencies (No. 5449) enforced on 25 January 2006 sets the rules for establishment of Investment Support Offices designated for centralized tracking and coordination of sectoral permissions required in investment and commissioning phases. Principles and procedures for operation of such offices are determined by a Regulation enforced on 25 July 2006.
The regulation for SME's definition and hence, acceptation of SME's definition in line with the community acquis	Y	2005	The Regulation for Definition, Characteristics and Classification of The Small and Medium Size Enterprises was promulgated in the Official Gazette on 18 November 2005 and this regulation was put into effect six month later from its promulgation. Thus, a common SME definition in compliance with the community acquis was introduced.
Investment Promotion Activities	Y	2006	The Law on the Establishment of the Investment Support and Promotion Agency of Turkey (No. 5523), which was prepared to specify and implement the investment assistance and publicity strategies to promote foreign direct investment in Turkey, was put into force on 4 July 2006. It is envisaged that the Agency, which will be designated to ensure enforcement of the Law and perform the duties specified by the Law, will be a public legal person entity, which will have administrative and financial autonomy and be an affiliate of the Prime Ministry.
The Coastal Act	N	2007	Bill Amending the Coastal Act prepared by Ministry of Public Works and Settlement was submitted to the Prime Ministry in April 2006.
Turkish Commercial Law	N	2007	The bill amending Turkish Commercial Law, which aims to shorten the time required for liquidation of non-problematic firms and facilitate the processes and to abolish the condition requiring that both companies should be of the same type in mergers, was submitted to the TGNA.
Financial Sector			
Privatisation of public banks	N	---	Works are continuing along the Strategy Report, which aims to privatise Ziraat Bank and Halkbank by public offering and the other methods. Works for privatisation of Halkbank have been started. In this context, a legal arrangement has been put into effect in November 2005 to ensure coordinated actions among the Bank, Treasury, and the PA and to allow the PA for holding a consultancy firm. The selection of technical and legal consultancy firms was completed in April 2006 and related works were initiated by these firms. Upon submission of the related reports by the consultancy firms in June 2006, privatisation of Treasury's stakes in Halkbank was included into privatisation agenda and programme in August 2006. Furthermore, 21.89 per cent of shares of Vakıflar Bank were offered to public.

Legislation on the Banking Cards and Credit Cards Law which includes provisions that specify the establishment principles of card issuing organizations	Y	2006	Banking Cards and Credit Cards Law No.5464 was promulgated in the Official Gazette dated 1 March 2006.
According to the provisional Article No.1 of the Banking Law No. 5411, the completion of secondary legislation until 1 November 2006.	Y	2006	Secondary legislations related with the Banking Law No. 5411 were completed as of 1 November 2006.
Disclosure of the results of quantitative impact study regarding New Capital Adequacy Framework (Basel II) and determining associated roadmap and announcing to public	Y	2005	Results of the quantitative impact analysis realised by the participation of 23 banks, which represented 95 per cent of the sector, were announced in December 2004. In May 2005, the Roadmap to Basel II, which sets the timing of the necessary steps that will be implemented, was announced to the public in transition to Basel II.
Completion of the establishment of a company to lay down the organization and infrastructure of an organized market where capital market instruments issued by SMEs will be traded and commencement of operations in the market in 2005.	N	2007	The company (Emerging Enterprises Markets) which would create and develop a transaction platform where trading transactions could be made in this market and which would make the organization required by such platform is established as of the end of the year 2005. The technical and legal works have been completed. Works for the commencement of the operations in the market are continued by the shareholders of the company.
Works on the registration of participation certifications of investment funds at Central Registry Agency.	Y	2005	Works on the dematerialization of all mutual fund certificates apart from those of liquid mutual funds were realised on 31 December 2005. Liquid mutual fund certificates were dematerialised on 31 March 2006.
Completing works on the dematerialization of stock certificates and associated rights of listed companies by the beginning of 2005.	Y	2005	Works on the dematerialization of stock certificates and associated rights of listed companies were completed as of November 2005.
Continuing works on restructuring custody and clearing system.	N	2007	Dematerialization works took significant time in the work plan of Takasbank and kept its priority. Besides, the fact that the subject is a part of Twinning Project held within CMB to comply with the Community acquis affected the timing of the work. The completion of works within 2007 is targeted.
Legal and technical works for creating mortgage financing system.	Y	2006	Draft bill prepared and submitted to the TGNA. Secondary regulations are planned to be completed by December 2006 on creating mortgage financing system.
Initiating the project to benefit from the Pre-Accession Financial Fund in the context of 2004 Programming for Candidate Countries in Central and Eastern Europe (PHARE) programme under the Pre-Accession Financial Assistance being provided to Turkey by the European Union.	Y	2006-2007	The works of EU Twinning Project between the Capital Markets Board and the German Ministry of Finance on Support of Harmonization of Capital Markets Board to EU Capital Markets has been initiated following the kick of meeting held on 1 February 2006. Within the scope of the project the works on compliance with the Community acquis as well as training and regulatory impact analysis works are continued.
Making existing auditing standards compliant with International Auditing Standards.	Y	2005-2008	International Auditing Standards fully compliant Communiqué Series X No. 22 of Independent Auditing Standards in Capital Markets has been effective as of 12 June 2006.

Capital markets compliance with the Community acquis dealing with the intermediary institutions' capital adequacy following the acceptance of Basel II criteria by EU.	N	2005-2008	New Capital Adequacy Directive formed within the framework of Basel II criteria promulgated in June 2006 and the effective date for the most part of the said Directive was determined as 31 December 2006. The compliance with the Community acquis on the capital adequacy is one of the subjects of Twinning Project as well. For this reason, compliance works will be completed within 2007 and the compliance that includes many changes on the existing structure is foreseen to be fully ensured in 2008.
Establishing specialty courts for capital markets.	N	---	No progress made due to the need for coordinated work with other institutions.
Dematerialization of Government Domestic Borrowing Instruments (GDBI) at the Central Registry Agency and custody and monitor on customer basis.	N	2007	In the scope of continued works, GDBI's outright purchases and sales and repo reverse repo transactions are decided to be handled separately. Primarily principles on the dematerialization of GDBI's outright purchases and sales transactions are determined and submitted to the State Ministry in February 2006. Within these principles, the works on system development and software initiated by Central Registry Agency (CRA) was completed and training and testing period continues. The dematerialised system on GDBI's outright purchases and sales at CRA is foreseen to be in effective in 2007, unless there aren't any troubles due to delays stem from especially banks that are unable to finish necessary harmonization works. On the other hand, the works on setting the principles on the dematerialization of GDBIs subject to repo transactions are completed following the review of the repo legislation.
Legislation of the draft bill for Law on the Regulation and Supervision of the Insurance Transactions	N	2006	The draft bill was submitted to the TGNA on 26 May 2006.
Labour Market			
Privatisation Social Support Project II	N	2006-2008	Privatisation Social Support Project II was started as the implementations of privatisation continue.
Administrative Reform			
Public Financial Management and Control Law	Y	2005-2007	The Law No. 5428 has ensured uniformity and consistency between the Law No. 5018 and related provisions of the Constitution. With the Law No. 5436 enforcement of the Law No. 5018 has been improved and it is ensured that all provisions of the Law to become effective on 1 January 2006. Secondary legislation necessary for the implementation of the Law No. 5018 have been prepared and put into effect on 1 January 2006.
Spreading analytical budget code classification	Y	2005-2007	As of 2006, analytical budget code classification has started to be implemented in local governments, social security institutions and the public administrations that are included in the central government with the Law No. 5018.
Local Administration Reform	Y	2005	Metropolitan Municipality Law No. 5216 dated 10 July 2004, Municipality Law No. 5393, Special Provinces Law No. 5197 dated 10 July

			2004, which was prepared in the context of the local administration reform, came into force.
Office of Ombudsman	Y	2006	The Law on Designation of Office of Ombudsman No. 5548 was enacted on 28 September 2006.
Agriculture			
Law on Agriculture	Y	2006	The policy framework laid down in the Agriculture Strategy Document (2006-2010) gained an institutional and legal framework with the Law on Agriculture. The Law basically specifies: subjects and purposes of the agricultural policies, principles and priorities of agricultural support policies, the programs through which such supports are to be provided; and aims to create a stable climate which is not very much affected by short-term preferences, so that producers are able to plan their production activities.
Start of the implementations pursuant to the Agriculture Insurance Law	Y	2006	Implementation of Agriculture Insurance Mechanism Assisted by State has been started in 2006, pursuant to the Agriculture Insurance Law No. 5363 which was promulgated in June 2005 in order to compensate the damages that farmers may suffer due to risks and uncertainties exposed in the agricultural production.
Seed Law	Y	2006	The Seed Law, which was prepared to amend the Law on Registration, Control, and Certification of the Seeds No. 308 and dated 1963, has been enacted in 2006.
Privatisation of sugar factories	N	2006	Ereğli, Bor and Ilgın Sugar Factories are expected to be privatised till the end of 2006. Works on the privatisation of other sugar factories will be continued in the coming period.
Preparation of Rural Development Strategy	Y	2006	National Rural Development Strategy (NRDS) was adopted in February 2006 by the decision of High Planning Council.
Preparation of Rural Development Plan	N	2006-2007	The initiatives for the preparation of the plan has already started, and the technical support will be provided by the project no. TR0402.08 subject to 2004 financial cooperation programming.
Strengthening the Institutional Capacity	N	2005-2008	The twinning component of the project no. TR0402.08 subject to 2004 financial cooperation programming is expected to be finalized in the first quarter of 2007. The Draft Law on the Establishment of Agriculture and Rural Development Support Institution, which is expected to function as an IPARD Agency, building of the steering committee and management of the EU rural development funds was sent to Turkish Parliament. The endeavours both on achieving of the national accreditation and making the EU to take the decision of conferral management of the funds will be supported by the project no. TR0503.05.
Regional Development			
The Law No. 5449 on the Establishment, Coordination and Duties of Development Agencies	Y	2006	The Law, which allows the establishment of Development Agencies in the determined NUTS II Regions and regulates the related principles

			and procedures, has been enacted on 8 February 2006 by Law No. 5449 upon the adoption of the TGNA.
The Decision of the Counsel of Ministers on the Establishment of Development Agencies in certain NUTS II Regions.	Y	2006	Development Agencies have been established in TR62 NUTS II Region (comprising the provinces of Adana and Mersin), of which the province of Adana is the center and TR31 NUTS II Region (comprising the province of İzmir), of which İzmir is the center.
Regulation on the Working Principles and Procedures of Development Agencies	Y	2006	Provisions on structure and bodies of Development Agencies, duties and authorities of these bodies, and the functioning of Development Agencies have been regulated.
Regulation on the Personnel Regime of Development Agencies	Y	2006	Human resources policy, procedures for the personnel recruitment and other related provisions for personnel of Development Agencies have been regulated.
Regulation on the Budget and Accounting of Development Agencies	Y	2006	Authorities and responsibilities of the personnel who will serve in the budget and accounting system of Development Agencies, preparation and implementation process of the budget of Development Agencies and the provisions for accounting system of Development Agencies have been regulated.
Principles and Procedures for determining wages, daily allowances and other social and financial rights of personnel of Development Agencies, and for the determination of amount of allowances to be transferred to Development Agencies in 2006 and 2007.	Y	2006	Maximum and minimum level of wages, daily allowances and other social and financial rights of the personnel to be recruited in Development Agencies and allowances to be transferred from General Budget to Development Agencies established in TR62 NUTS II Region (comprising the provinces of Adana and Mersin), and TR31 NUTS II Region (comprising the province of İzmir) for the 2006 Provisional Budget and 2007 Budget were determined.
Twinning Project of Support to the State Planning Organization General Directorate of Regional Development and Structural Adjustment for Strengthening Institutional and Administrative Capacity	Y	2006	18 month-period project was initiated on 1 June 2005. The project is planned to be completed by November 2006.
Health, Social Security and Improvement of Income Distribution			
Spreading the pilot implementation of Family Medicine	Y	2006	The pilot implementation of Family Medicine is carried on at 3 cities.
Establishing the health information system	N	2007	Studies on establishing a standard information system continue.
Combining the social security institutions under a single organization, separating the long-term and short-term insurance branches and establishing universal health insurance	Y	2005-2006	The Social Insurances and General Health Insurance Law was published in the Official Gazette on 16 June 2006, and it will come into force on 1 January 2007.
	Y	2005-2006	The Social Security Institution Law was published in the Official Gazette and came into force on 20 May 2006.
	N	2006-2007	Works on the provision system, which is related to improving the social security information infrastructure, are carried on.

Information and Communication Technologies			
Information Society Strategy and its Annexed Action Plan	Y	2006	Implemented by the Decision No. 2006/38 of the High Planning Council.
Electronic Communications Law	N	2006	The Draft Law was sent to the TGNA.
Law on Protection of Personal Information	N	2007	The Draft Bill for the Law has been submitted to Prime Ministry.
Law on Regulating the Cyber Network Services and on Cyber Crimes	N	2007	The evaluation process of the Draft Bill is continuing.
Regulation on Amending the Regulation of Authorization for Telecommunications Service and Infrastructure	Y	2006	Regulation on the wired and wireless Internet service providers was put into effect on 15 November 2005.
Regulation on Right-of-Way in Telecommunication Service Execution	Y	2006	It was put into effect on 2 May 2006.
Regulation on Amending the Regulation of Authorization for Telecommunications Service and Infrastructure	Y	2006	Regulation on guidance service was put into effect on 6 July 2006.
Right-of-Way regulations	N	---	Works are underway to comply with Perfect Competition Directive No. 96/19/EC.
Number Portability Regulation	N	2006	The Draft Regulation aiming at alignment with the Directive 2002/22/EC on universal service and users' rights relating to electronic communications networks and services, has been submitted to the Telecommunication Board for final approval.
Amendment on the Access and Interconnection Regulation	N	2006	Works are underway to conform to Directive 2002/19/EC on access to, and interconnection of, electronic communications networks and associated facilities.
Regulation on Procedures and Principles Regarding Identification of the Operators with Significant Market Power	N	2006	Works are underway to conform to the Access Directive 2002/21/EC and the Regulation will be promulgated after enactment of the Electronic Communications Law.
Amendment on the Regulation on the Authorisation in Electronic Communications Sector	N	2007	Works are underway to conform to the Authorisation Directive 2002/20/EC and the Regulation will be promulgated after enactment of the Electronic Communications Law.
Regulation on processing of personal data and the protection of privacy in the electronic communications sector	N	2007	Works are underway to conform to the Directive 2002/58/EC concerning the processing of personal data and the protection of privacy in the electronic communications sector and the Directive 2006/24/EC on the retention of data generated or processed in connection with the provision of publicly available electronic communications services or of public communications networks.
Transportation			
Restructuring of Turkish State Railways	Y	2006	In the framework of Turkey-EU Financial Programming, a twinning project was initiated in 2003 to harmonize the Turkish railways legislation with the EU directives. The project, whose contactor was the German Airways, was completed in 2006.

Energy			
Works for privatising electricity sector	N	2004-2009	To start distribution privatisations, electricity distribution system has been restructured and corporatized as 21 regions and, these companies are turned over to the Privatisation Administration and their privatisation is going on. Privatisation of generation assets will be considered after distribution privatisations have come to a certain stage. It is anticipated that privatisations will be, to a great extent, completed by 2009.
Regulatory Board Information System Project	N	2004-2006	As of November 2005, the tender process for the project was completed, contract signed, and the implementation of the project has started. With the kick-off meeting on 7 February 2006, draft reports of start and need assessment were prepared. Technical equipment was procured and brought to EMRA on 24 July 2006. However, as a result of problems, the contractor suspended the project unilaterally. Regarding the subject, information is expected from the Central Finance And Contracts Unit (CFCU). Due to the problems with the contractor the anticipated completion date of the project, originally November 2006, is unknown.
Project for Feasibility Study for Turkey's Integration to UCTE Electricity System	N	2005-2007	TEIAS carries out the project for Feasibility Study for Turkey's Integration to UCTE Electricity System for determining under what technical conditions the national electricity network will be connected to the UCTE system in a fully synchronized manner in the framework of the purpose of fully integrating the national electricity market with the EU electricity market.
Project on Providing BOTAŞ Know-How Support in Natural Gas Transmission and Transit	N	2005-2007	The project was started on 1 September 2005 to enable BOTAŞ to perform its obligations to transmit and transit natural gas in parallel with EU standards and practices. In the context of the project, World Conference on Gas in Amsterdam was participated and training programs on liberal gas market applications in the EU countries, tariffs and transmission network operation regulations were arranged. Technical training activities are ongoing. The contractor is about to submit the reports on activities in the scope of the project. The project is estimated to finish in March 2007.
Project for Increasing Energy Efficiency in Turkey	N	2005-2007	In the context of harmonization with Community acquis and EU experiences, the project aiming to implement the energy efficiency programs to improve energy efficiency performance of our country is wholly financed under the financial cooperation programs and the project is expected to finish in 2007.
Development of Conditions for the Functioning of Cross-Border Electricity Trade of Turkey in line with the Best Practises in the EU	N	2006-2008	The project, aiming to integrate the technical infrastructure of Turkish electricity system with the EU electricity system in order to enable the cross-border trading and to establish the relevant legal framework, is carried out with a twinning approach under Financial Cooperation 2006 Fiscal Program.