REPUBLIC OF TURKEY

PRE-ACCESSION ECONOMIC PROGRAMME 2013 - 2015

ANKARA
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The Pre-Accession Economic Programme (2013-2015) has been adopted by High Planning Council Decision No. 2012/36.

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TABLES

FIGURES

BOXES

ABBREVIATIONS

BASEL-II	International Recommendations on Banking Laws and Regulations Issued by Basel Committee on Banking Supervision
BOTAŞ	Petroleum Pipeline Corporation
BRSA	Banking Regulation and Supervision Agency
CBRT	Central Bank of the Republic of Turkey
CMB	Capital Markets Board
CPI	Consumer Price Index
CRA	Central Registry Agency
ÇATAK	Environmentally Based Agricultural Land Protection
DAMS	Development Agencies Management System
DIS	Direct Income Support
ECOFIN	Economic and Financial Affairs Council
EDAŞ	Electricity Distribution Company
EFSF	European Financial Stability Fund
EMRA	Energy Market Regulatory Agency
ENTSO-E	European Network of Transmission System Operators for Electricity
ESA	European System of Accounts
EU	European Union
EU-27	The EU Member Countries After Enlargement on 1 January 2007
EUROSTAT	Statistical Office of the European Communities
EÜAŞ	Turkish Electricity Production Company Inc.
FATİH	Education and Technology Improvement Action to Increase Opportunities
FED	Federal Reserve System
FTE	Full-time Equivalent
GAP	Southeastern Anatolian Project
GDBI	Government Domestic Borrowing Instrument
GDP	Gross Domestic Product
GSM	Global System for Mobile Communications
HPC	High Planning Council
IFS	International Financial Statistics
ILO	International Labor Organization
IMF	International Monetary Fund
IOSCO	International Organization of Securities Commissions
IPA	Instrument for Pre-Accession Assistance
IPARD	IPA Rural Development Funds
ISE	İstanbul Stock Exchange
IT	Information Technology
ITCA	Information Technologies and Communications Authority
İŞKUR	Turkish Employment Organization
KASDEP	Social Support Project in Rural Areas
KKYDP	Rural Development Investments Support Programme
KOSGEB	Small and Medium Industry Development Organization
KÖY-DES	Project for Supporting Infrastructure of Villages
LNG	Liquefied Natural Gas
MENA	Middle East and North Africa
MERSİS	Central Registry System For Legal Persons Project
MTP	Medium Term Programme
OECD	Organization for Economic Co-operation and Development
PCMS	Province Coordination and Monitoring System
PEP	Pre-Accession Economic Programme
PMC	Portfolio Management Companies
PPI	Producer Price Index

PPP	Public-Private Partnership
ROC	Reserve Option Coefficient
ROM	Reserve Option Mechanism
SCT	Special Consumption Tax
SDIF	Savings Deposit Insurance Fund
SDR	Special Drawing Right
SEEs	State Economic Enterprises
SHÇEK	Social Services and Child Protection Agency
SII	Social Insurance Institution
SMEs	Small and Medium Sized Enterprises
SODES	Social Support Program
SPO	State Planning Organization
SSI	Social Security Institution
SUKAP	Water and Sewerage Infrastructure Project
SYDTF	Social Assistance and Solidarity Fund
TAEA	Turkish Atomic Energy Authority
TAKBİS	Land Registry and Cadastre Information System
TGNA	Turkish Grand National Assembly
TCDD	Turkish State Railways
TDZ	Technology Development Zones
TEDAŞ	Turkish Electricity Distribution Company
TEİAŞ	Turkish Electricity Transmission Company
TFP	Total Factor Productivity
TL	Turkish Lira
TOBB	Union of Chambers and Commodity Exchanges of Turkey
TŞFAŞ	Sugar Factories Company
TURKSTAT	Turkish Statistical Institute
TÜBİTAK	Scientific and Technological Research Council of Turkey
UCTE	Union for the Coordination of Transmission of Electricity
UKKS	National Rural Development Strategy
USA	The United States of America
VAT	Value Added Tax
VEDOP	Tax Office Full Automation Project
YOİKK	Coordination Council for the Improvement for the Investment Environment

1. POLICY FRAMEWORK AND OBJECTIVES

Turkey, as an acceding country for European Union (EU) membership, has prepared the Pre-Accession Economic Programme (PEP) and has submitted to the European Commission since 2001, responding to the request of the Economic and Financial Affairs Council (ECOFIN Council) dated 26/27 November 2000. The PEP (2013-2015) has been prepared under the coordination of Ministry of Development (State Planning Organization) with the contributions of relevant ministries and institutions, and adopted by the decision of the High Planning Council (HPC)[1] No. 2012/36.

Pre-Accession Economic Programme is prepared within the scope of the Ninth Development Plan (2007-2013), based on Medium Term Programme (2013-2015), which provided a basis for economic and social policies for the following three years, and 2013 Annual Programme, which is a detailed reflection of the first year of MTP. Developments occurred in the short period between Medium Term Programme (MTP) publication and PEP preparation are not evaluated as developments that will change the medium term trends. Thereby, the framework of MTP for medium-term outlook and projections has been kept in PEP.

In an environment of weakening recovery and ongoing uncertainties in world economy, Turkey became one of the fastest growing countries in the world with a growth rate of 8.5 percent in 2011. As a matter of fact, the 2012 Progress Report announced by the European Commission in October 2012 mentioned that Turkey has successfully carried out monetary and fiscal policy mix following the crisis. In the Report, it was underlined that fiscal consolidation and structural reform process, which were put into practice in previous periods, contributed to this strong growth performance.

Rapid recovery of domestic demand together with weak external demand in post-crisis period led to an expansion in current account deficit. In response, a new policy set has been put into practice towards rebalancing demand components. As a result of these policies, economic slowdown beginning from the last quarter of 2011 has also continued in 2012. Therefore, the contribution of external demand to growth has increased and a sound growth composition has been achieved. In parallel to these developments, current account balance has improved gradually since last year. Turkey’s policies towards rebalancing the domestic and external demand were indicated as important for economic stability in the 2012 Progress Report. On the other hand, it was stated that current account deficit, still maintaining its high levels, leaves Turkey fragile against global financial shocks. However, current account deficit has narrowed beyond the forecasts of MTP and the Commission in 2012. Moreover, policies taking into account the balance between domestic and external demand will be continued in the medium term. In this framework, it is foreseen that the contribution of net goods and services exports to growth will be neutral and domestic demand will recover relatively in the following period. Therefore, Turkish economy which has achieved soft landing in 2012 is expected to reach a balanced growth path around its potential levels in the medium term.

The Pre-Accession Economic Programme (2013-2015) has been prepared in an environment that downside risks in world economy has been continuing, global economic recovery loses its momentum and concerns about economic problems and political developments especially in the Euro Area are still prevalent.

In the following period, implementation of necessary policy adjustments in a coordinated, rapid, decisive and effective manner against global risks stemming from developed economies are essential for stable growth. In this framework, the main objectives of the Pre-Accession Economic Programme (2013-2015) in the direction of strengthening macroeconomic and financial stability are; to reach potential growth rate, to decrease current account deficit further, to reduce inflation and to improve public fiscal balances. In the PEP (2013-2015) period, sound fiscal frame, financial stability environment and strong banking system will provide favorable environment for balanced growth path.

[1] High Planning Council is composed of one Deputy Prime Minister and seven Ministers under the presidency of Prime Minister.

Despite measures taken in recent period, developed economies based global uncertainty environment keep concerns about financial stability and growth on the agenda, and this situation necessitates a flexible and effective policy understanding. Monitoring and evaluating developments with regard to economic stability and also coordinating plans and programs with regard to monetary, credit, finance, debt and other economic issues, Economy Coordination Board has met several times in order to discuss a wide range of issues including informal economy, social security and employment, new commercial law, incentive schemes and foreign trade policies. Unique position of the Board in terms of providing coordination between ministries and institutions results in effective policy making and implementation. In this context, respective authorities in our country will continue policy implementations cooperatively to manage macro financial risks under the coordination of various platforms, particularly Economic Coordination Committee and Financial Stability Committee. In the PEP (2013-2015) period, fiscal, monetary and income policies and macro prudential measures will be implemented in a framework that will strengthen confidence, stability and predictability and will increase resilience of the economy to external shocks.

In this direction, inflation targeting regime will be continued in compliance with the main objective of achieving price stability. The ultimate target is to decrease inflation rate to levels complying with the Maastricht criteria. Moreover, the floating exchange rate regime will continue in the forthcoming period. In PEP (2013-2015) period, as a supportive objective, financial stability will also continue to be taken into consideration. In this regard, the operational framework of monetary policy which enables flexible and effective liquidity management will be continued in the following period.

Fiscal policy will be carried out with an approach that will contribute to strengthen macroeconomic stability, to promote private sector-led growth process and to fight against current account deficit and inflation. In this period, in order to maintain fiscal discipline, necessary policy measures will be taken if significant indications for deviation from fiscal targets of the Programme are observed.

In the PEP (2013-2015) period, towards the main objective of increasing employment, policies to improve quality of labor force, to increase flexibility of labor market and participation rate will be given priority, in addition to the policies which will ensure stable growth environment. Furthermore, the competitiveness of the economy, the efficiency of the public expenditures, good governance, education system, juridical system, tax system, informality, and the continuation of structural transformation in the fields of local administration, regional development and sustainable development, the realization of urban transformation are among the main priorities of the Programme.

In the second chapter of the Pre-Accession Economic Programme (2013-2015), which consists of four main chapters, recent economic developments in the Turkish economy are evaluated by considering the developments in the world economy, and then the macroeconomic forecasts for the 2013-2015 period are presented. In the third chapter, fiscal policies for the PEP (2013-2015) period are put forward together with forecasts and analyses regarding budget and debt management. In the fourth chapter, assessments on developments in structural reforms, budgetary impacts and reform agenda are included.

2. MACROECONOMIC OUTLOOK

The negative effects of global crisis on the world economy carry on although measures have been taken, and slowdown tendency in economies still continues. Global economy has started to weaken again, due to the contagion of problems, especially in the Euro Area, to other regions via trade and confidence channels. Economic and political developments in the Euro Area continue to be determining factors on the global outlook.

In the context of enhancing international cooperation and coordination to establish global confidence and thereby overcome global crisis, effective working of multinational bodies like G-20 in which weight of developing countries is increasing, is still important. Parallel to its increasing economic and political power, Turkey gives utmost importance to coordinated action in international area and supports relative efforts. In this framework, Turkey will be in G-20 Troika for three years starting from 2014 and will undertake G-20 Presidency in 2015.

Global economic recovery experienced in 2010 could not be sustained in 2011. Banking and debt problems in some EU countries particularly in Greece, Spain and Italy caused a loss of confidence. Financial turbulence in the Euro Area and its repercussions to the banking sector and uncertainties in decision-making processes about economic policy caused lower than expected growth performance in advanced countries. This situation adversely affected growth in developing and emerging economies. Moreover, the uncertainty caused by fluctuations in energy, commodity and food prices had negative impacts on global growth. As a result of these developments, the world growth rate that was 5.1 percent in 2010, declined to 3.8 percent in 2011. The growth rate of advanced economies which was 3 percent in 2010, declined to 1.6 percent in 2011. In the same period, the growth rate of emerging and developing economies declined from 7.4 percent to 6.2 percent[2].

As a result of these developments in the world economy, international organizations have revised their growth forecasts downward. The world growth rate forecast for 2012 was reduced to 3.3 percent in October 2012, which was estimated as 4 percent in September 2011 by IMF. As for the years 2013, 2014 and 2015, it is estimated that world growth rate will be 3.6 percent, 4.1 percent and 4.4 percent, respectively.

Euro Area leaders took important decisions in order to fight against the crisis including; strengthening of institutional structure, establishment of banking union roadmap, forming of joint supervision mechanism, giving elasticity to the rescue funds, assigning the European Stability Mechanism for direct capitalization authority to banks. However, uncertainties about implementation details of decisions taken still exist and pose significant risk to the global economy. In addition, recently European Central Bank announced that it can buy troubled countries sovereign bonds in secondary markets without limitation on basis of conditionality clause in the framework of Outright Monetary Transaction (OMT) program. Despite measures taken, a significant progress could not be achieved towards stimulating economy and improving fiscal balances remarkably. Euro Area economy, as an important trade partner of Turkey, is projected to contract by 0.4 percent in 2012 and grows by 0.2 percent in 2013.

Despite the recovery tendency, weak growth performance was observed in US economy currently, which grew by 1.8 percent in 2011. U.S. Federal Reserve Bank (FED) announced third-round financial support program (Quantitative Easing 3) to stimulate the economy in September of 2012. In the first half of 2012, negative repercussions of the crisis in the Euro Area, weakness in consumer spending, lack of consumer confidence and inadequate employment creation point to a lower than expected growth in the U.S. economy at the end of the year. In addition to these, developments such as the risk of fiscal cliff in 2013 and the absence of medium term fiscal plan point to a moderate growth in the U.S. economy in next period. The US economy is expected to grow by 2.2 percent and 2.1 percent in 2012 and 2013, respectively.

Growth rate of developing countries has slowed down in parallel with the growth performance of developed countries since 2011. The developed economies are expected to grow by

[2] IMF, World Economic Outlook, October 2012

1.3 percent and 1.5 percent in 2012 and 2013, respectively, whereas the emerging and developing economies are expected to grow by 5.3 percent and 5.6 percent, successively over the same period.

World trade volume is projected to grow by 3.2 percent in 2012 and 4.5 percent in 2013. It is expected to increase by 5.8 percent and 6.1 percent in 2014 and 2015.

Oil prices increased by political developments in the Middle East region, in the first months of 2012 and then declined in the second quarter of 2012 because of the positive developments in the supply side and reduced demand pressure by the slowdown in global economic activity, but started to increase again in the second half of the year. Oil prices are expected to follow a stable trend around 110 dollars in the medium term.

In recent months, as a result of drought in some regions especially in the USA, the problems of agricultural production and inventory levels continue to remain below the historical average, have led to increase in food prices. Increases in agricultural commodity prices pose a risk to upward pressure on inflation and processed food prices in developing countries. Fluctuating trend in commodity prices have increased uncertainties.

In addition to fluctuations in energy and commodity prices, as a result of the easing monetary policies of the US and European central banks, the global inflation rate which realized as 4.9 percent in 2011 is expected to decline to 4 percent in 2012 and to 3.7 percent in 2013, due to weak global demand effect. In this context, inflation in both developed and developing countries tends to decrease gradually. Inflation rate in Euro Area, which was recorded as 2.7 percent in 2011, is estimated to be 2.3 percent in 2012, and 1.6 percent in 2013, respectively.

Because of the weak economic recovery on global scale in 2011, the lack of adequate employment growth in many countries has continued to be a major problem. While the unemployment rates in the EU countries, especially in Greece, Portugal, Ireland and Spain have increased to substantial levels, youth unemployment has reached worrying levels. In 2011, unemployment rate realized as 10.2 percent in Euro Area, 9 percent in the U.S. and 8 percent in total OECD, respectively. In 2012, in parallel with the slowdown in global economic activity, a significant improvement in employment is not expected. Unemployment rates in the U.S. and Euro Area is estimated to be 8.2 percent and 11.2 percent in 2012, respectively. The unemployment rate in Euro Area is expected to rise slightly to 11.5 percent while the unemployment rate in the U.S. is expected to remain at the same level in 2013.

In Euro Area, general government budget deficit to GDP ratio is expected to decline in the coming period with the effects of the fiscal measures taken in the problematic EU countries. This ratio which was 4.1 percent in 2011 is expected to decline to 3.3 percent in 2012 and to 2.6 percent in 2013. The general government gross debt stock to GDP ratio in Euro Area which was 85.4 percent at the end of 2010, increased to 88 percent at the end of 2011. Although there are differences among the EU countries, general government gross debt stock to GDP ratio is expected to continue the upward trend, and is expected to be 93.6 percent in 2012 and 94.9 percent in 2013.

A significant reduction in the US budget deficit is not expected because of the slow economic recovery and general government budget deficit to GDP ratio which was 10.1 percent in 2011 is expected to be 8.7 percent and 7.3 percent in 2012 and 2013, respectively. By keeping the increasing trend, the general government gross debt stock to GDP ratio is expected to increase to 107.2 percent in 2012 and to 111.7 percent in 2013.

In recent years, international capital inflows have directed from advanced economies which have fiscal problems and implement expansionary monetary policies to developing economies which recovered quickly from the crisis and have high growth potential. However, due to negative developments in global economy, net foreign capital inflows to emerging and developing countries decreased significantly and declined to 503 billion dollars in 2011 compared to 2010. In addition to weak banking structure, balance sheet reduction process in the financial sector in developed economies and increased global risk perception, the total amount of net foreign capital inflows to developing countries where the economic outlook was worsen, are expected to be affected significantly. The net foreign capital inflows are expected to return to the levels in the first period of the crisis and projected to be 268.3 billion dollars and 399.6 billion dollars in 2012 and in 2013, respectively.

Pre–Accession Economic Programme (2013-2015) has been prepared by closely monitoring the recent developments in the world economy, especially in the European Union which is the Turkey's largest trading partner, in an environment in which the global risks still continue. The assumptions about all exogenous variables used in PEP forecasts are presented in Annex Table 6.

2.1. Recent Economic Developments

2.1.1. Real Sector

2.1.1.1. Growth

Turkish economy recorded a high growth rate of 9.2 percent in 2010 due to strong domestic demand. With the continuing contribution of strong domestic demand in the first half of 2011, Turkish economy maintained its high growth performance. In the second half of the year, the contribution of final domestic demand to growth has decreased significantly as a result of measures taken to rebalance domestic and external demand. On the other hand, due to the diversification in export markets and the impact of the depreciation of the Turkish Lira, the contribution of net exports to growth was positive in the second half of the year. Throughout the year, Turkish economy showed a successful performance and grew by 8.5 percent.

Table 2.1: Growth Rates and Demand Components

(Annual Percentage Change, at 1998 Prices)

	Annual		Quarterly							
			2011				2012			
	2010	2011	I	II	III	IV	I	II	III	First 9 Months
GDP	9.2	8.5	12.1	9.1	8.4	5.0	3.4	3.0	1.6	2.6
Agriculture	2.4	5.6	7.6	6.4	4.8	5.6	4.8	3.4	2.9	3.3
Industry	12.8	9.4	14.8	8.8	9.0	5.8	3.5	3.9	1.7	3.1
Manufacturing	13.6	9.6	15.1	9.3	9.5	5.3	3.2	3.8	1.3	2.8
Services	8.6	8.9	10.9	9.7	9.7	5.7	3.5	2.9	1.3	2.6
Construction	18.3	11.3	15.5	13.1	10.3	7.0	2.7	0.3	0.4	1.0
Total Consumption	6.0	7.3	11.5	8.4	8.1	2.2	0.6	-0.3	0.1	0.1
Public	2.0	4.5	7.0	9.0	10.3	-4.3	5.5	4.4	4.4	4.7
Private	6.7	7.8	12.1	8.3	7.8	3.4	-0.1	-1.0	-0.5	-0.5
Gross Fixed Capital Form.	30.5	18.5	35.7	29.0	15.0	1.3	1.4	-7.2	-7.6	-4.6
Public	17.7	-3.3	-0.9	-0.2	0.3	-9.5	2.5	-4.0	11.2	3.5
Private	33.6	23.1	41.9	35.1	18.2	3.9	1.3	-7.7	-11.1	-5.9
Total Final Dom. Demand	10.8	9.9	16.6	13.2	9.6	2.0	0.8	-2.1	-1.7	-1.1
Total Domestic Demand	13.5	9.6	17.0	13.8	7.6	1.8	-1.2	-2.7	-1.8	-1.9
Exports of Goods and Serv.	3.4	6.4	8.7	0.5	10.2	6.6	12.3	20.9	11.9	15.0
Imports of Goods and Serv.	20.7	10.9	28.0	18.9	6.8	-5.1	-6.1	-3.7	-2.4	-4.0

Source: TURKSTAT

Note: Services sector is derived by subtracting agriculture and industry sectors from total sectors.

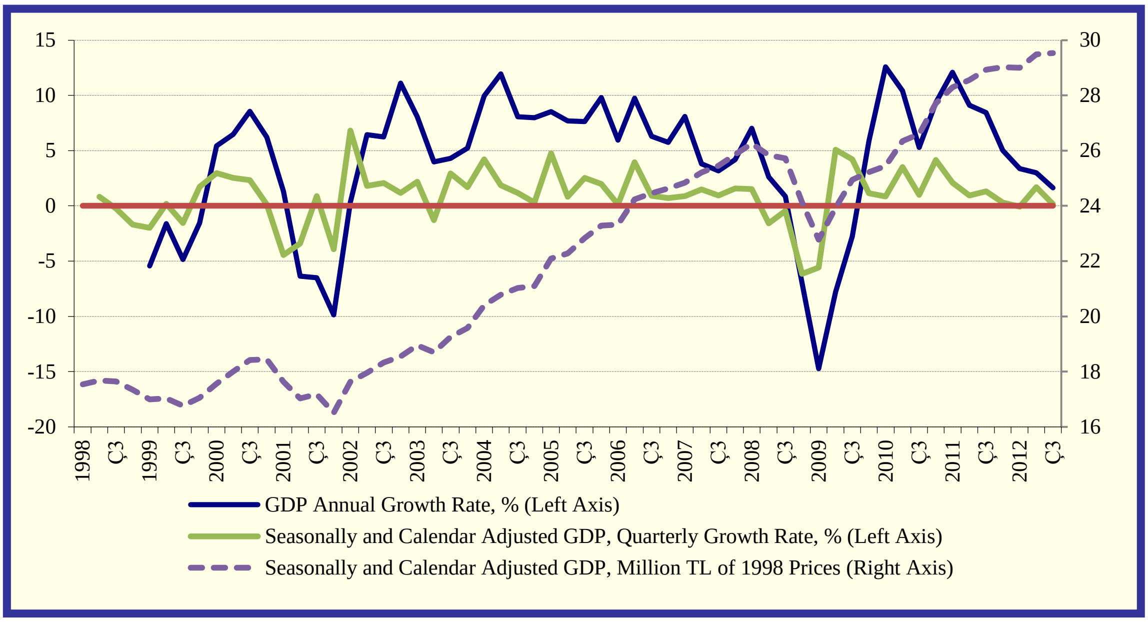
Scrutinizing the gross domestic product by expenditure items for 2011, it is observed that the contribution of total consumption to growth increased by 0.9 percentage points compared to previous year and realized as 5.8 percentage points. During this period, the growth rate of private consumption increased by 1.1 percentage points compared to 2010 and realized as 7.8 percent, while the growth rate of public consumption increased by 2.5 percentage points and reached 4.5 percent. The contribution of total fixed investment to growth in 2011 declined to 4.4 percentage points. While private sector fixed capital investments grew by 23.1 percent in the same period, public sector fixed capital investment declined by 3.3 percent. Machinery & equipment investment, which increased by 26.1 percent, was the main driver of high private sector investment growth. As a result of high growth rates in consumption and investment expenditures, the contribution of total final domestic demand to growth was 10.2 percentage points and had an important role on strong growth in 2011. During this period, the contribution of change in stocks to growth was realized as -0.3 percentage points.

With the depreciation of the Turkish Lira in August 2011 and the increase in the export share of alternative markets, particularly Africa and the Middle East, goods and services exports followed a favorable path in the second half of the year and increased by 6.4 percent in 2011. On the other hand, with the slowdown in domestic demand due to the measures taken to rebalance the composition of demand and the depreciation of the Turkish Lira, the growth rate of goods and services imports stood at 10.9 percent. Thereby, thanks to these positive developments in the foreign trade in the second half of the year, the contribution of net exports to growth was recorded as -1.5 percentage points.

Due to the acceleration of the slowdown in domestic demand, which has started in the second half of 2011, GDP growth rate was recorded as 2.6 percent in the first nine months of 2012.

Investigating the gross domestic product by expenditure items for the first nine months of 2012, it is observed that despite the increase of 4.7 percent in public consumption compared to the same period of the previous year, the growth rate of total consumption expenditures remained at the level of 0.1 percent as a result of 0.5 percent contraction in private consumption expenditures. On the other hand, due to the decline in private sector fixed capital investment, gross fixed capital formation declined by 4.6 percent during this period and the contribution of final domestic demand to growth stood at -1.1 percentage points. The contribution of change in stocks to growth was realized as -0.9 percentage points in the first nine months of 2012.

Figure 2.1: GDP Developments



Source: TURKSTAT

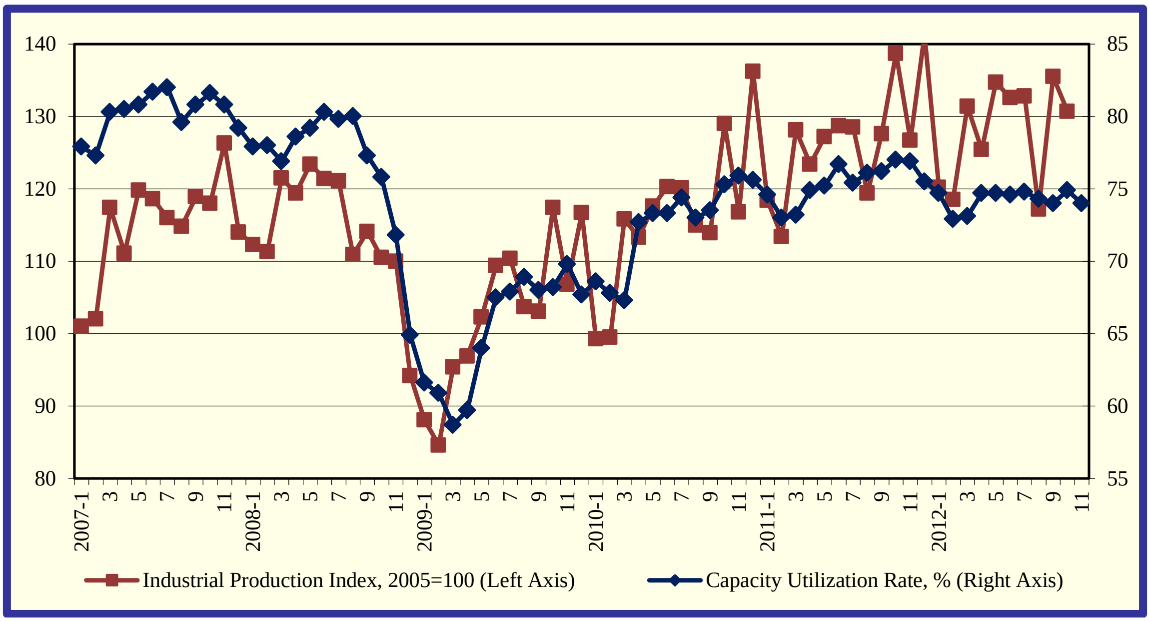
In addition to export market diversification efforts, with the current low level of Turkish Lira against foreign exchange basket and policies put into practice to slow down the economy in the second half of 2011, the trade balance continued to improve in the first nine months of 2012. During this period, while goods and services imports decreased by 4 percent, goods and services exports increased by 15 percent in real terms. Hence, the contribution of net exports to growth increased significantly and realized as 4.6 percentage points. Considering the negative contribution of domestic demand to growth during this period, which was recorded as -2 percentage points, the positive contribution of net exports to growth performance in the first nine months was remarkable. Thereby, the targeted rebalancing between domestic and external demand has been achieved to a significant extent.

As a result of these developments, in the first nine months of 2012, contributions to GDP growth of private consumption was -0.4 percentage point, public consumption was 0.5 percentage point, private fixed investment was -1.3 percentage points, and public fixed investment was 0.1 percentage point.

Considering the sectoral developments in 2011, value added of the industry sector increased by 9.4 percent, above the PEP (2012-2014) forecast of 7.2 percent. Thereby, the sector share in total production increased to 22.5 percent. Value added in manufacturing industry, a sub-sector of the industrial sector, increased by 9.6 percent in 2011, while its contribution to growth was 2.3 percentage points. Value added in services sector increased by 8.9 percent during the same period and its contribution to growth was 5.6 percentage points. Analyzing the sub-sectors of the services sector, it is observed that particularly the construction, wholesale and retail trade, transport, storage and communication, financial intermediation sub-sectors were quite effective on the strong growth performance in 2011.The share of the agricultural sector was 9 percent of GDP in 2011 and its value added increased by 5.6 percent.

In the first nine months of 2012, value added in agriculture sector increased by 3.3 percent. On the other hand, the industrial sector value added growth was limited to 3.1 percent due to the slowdown in domestic demand. Considering the sub-sectors, the increase in value added was realized as 2.8 percent in the mining & quarrying sector and in the manufacturing industry and 6.2 percent in the electricity, gas, steam and hot water production and distribution sector.

Figure 2.2: Industrial Production Index and Capacity Utilization Rate



Source: TURKSTAT and CBRT

Industrial production index increased by 2 percent in the January-October period of 2012 (Figure 2.2). In the same period, the growth in intermediate goods production was almost equal to the growth in industrial production. The growth in energy sector production was higher than the growth in industrial production while growth in durable goods production was lower than the growth in industrial production in the same period. There have been significant production increases in main sectors such as manufacturing of other transport equipment (74.1 percent), manufacturing of wood and cork products excluding furniture (24.3 percent), manufacturing of computer, electronic and optical products (10.4 percent), manufacturing of tobacco products (16 percent) and manufacturing of basic metals (7.1 percent).

In line with the slowdown in economic activity, the capacity utilization rate in manufacturing industry declined by 1.1 percentage points on average in January-November period of 2012, compared to the same period of the previous year and was realized as 74.2 percent.

The value added in the services sector increased by 2.6 percent in the first nine months of 2012. Scrutinizing the sub-sectors, it is observed that the production in all sub-sectors showed an increase in this period, however growth rates have lost momentum compared to last year. Low value added growth rates, particularly 0.9 percent in wholesale and retail trade sector and 1.5 percent in construction sector, have limited the services sector growth rate. Considering services sub-sectors in the first nine months of 2012 growth rates have been 4 percent in transportation, 2.9 percent in financial intermediation services, 1.7 percent in ownership and dwelling, 6.7 percent in real estate and business activities sectors. Value added growth in education and health & social work services sectors have been realized as 4.2 percent and 4.7 percent respectively in the same period.

2.1.1.2. Labor Market

In 2011, employment growth was realized above the PEP (2012-2014) forecast. With the effect of both the measures taken in the scope of coping with unemployment and high growth; unemployment rate, which was 9.8 percent in 2011, declined to 9.2 percent (seasonally adjusted) in August 2012.

In 2011, industrial sector value added increased by 9.4 percent while employment growth was 4.6 percent implying a slowdown compared to the previous year. In the industrial sector 208 thousand new jobs were created, of which 151 thousand was in manufacturing sector. As a result, the share of industrial sector in aggregate employment was 19.5 percent.

Table 2.2: Labor Market Developments

(15+Age, Thousands)

	Annual		2011				2012		
	2010	2011	I	II	III	IV	I	II	III
Working Age Population	52,541	53,593	53,152	53,439	53,734	54,027	54,365	54,599	54,841
Labor Force Part. Rate, %	48.8	49.9	48.5	50.5	51.0	49.4	47.9	50.5	50.7
Female Force Part. Rate, %	27.6	28.8	27.2	29.8	30.0	28.3	27.4	30.2	30.1
Male Force Part. Rate, %	70.8	71.7	70.6	72.0	72.8	71.3	69.1	71.4	71.9
Labor Force	25,641	26,725	25,766	26,995	27,406	26,696	26,058	27,554	27,812
Employment	22,594	24,110	22,802	24,445	24,884	24,267	23,338	25,282	25,367
Unemployed	3,046	2,615	2,964	2,550	2,521	2,429	2,721	2,272	2,445
Employment Rate, %	43.0	45.0	42.9	45.7	46.3	44.9	42.9	46.3	46.3
Unemployment Rate, %	11.9	9.8	11.5	9.4	9.2	9.1	10.4	8.2	8.8
Non-Agriculture, %	14.8	12.4	14.2	12.0	11.9	11.4	12.7	10.4	11.3
Among Young People, %	21.7	18.4	20.6	17.5	18.6	17.0	18.3	15.9	17.2
Female, %	13.0	11.3	12.5	10.8	11.5	10.4	11.1	9.3	11.1
Employment by Sectors									
Agriculture	5,683	6,143	5,573	6,273	6,704	5,990	5,427	6,363	6,564
Non-Agriculture	16,911	17,967	17,229	18,172	18,180	18,277	17,911	18,919	18,803
Industry	4,496	4,704	4,652	4,777	4,682	4,700	4,684	4,760	4,745
Services	12,415	13,263	12,577	13,395	13,498	13,577	13,227	14,159	14,058

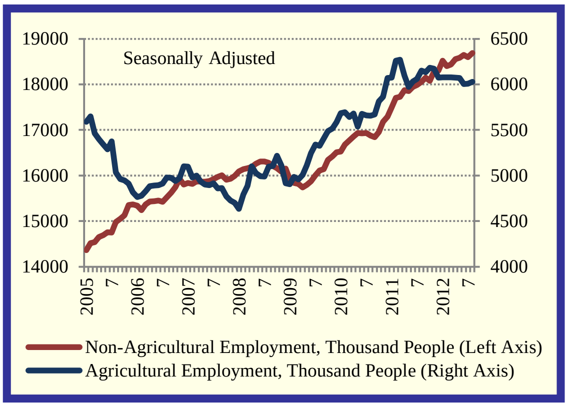
Source: TURKSTAT

While value added in the services sector increased by 8.9 percent, employment in this sector increased by 6.8 percent in 2011. Main driver of this performance was the construction sector employment with a 17.1 percent increase. Employment in construction sector and wholesale and retail trade sector increased by 245 thousand and 150 thousand respectively and so 848 thousand new jobs were created in the services sector. Thus in the non-agricultural sector, employment increased by 6.2 percent and 1,056 thousand new jobs were created throughout 2011.

Figure 2.3: Industry and Services Employment

Source: Ministry of Development calculations

Figure 2.4: Agricultural and Non-Agricultural Employment

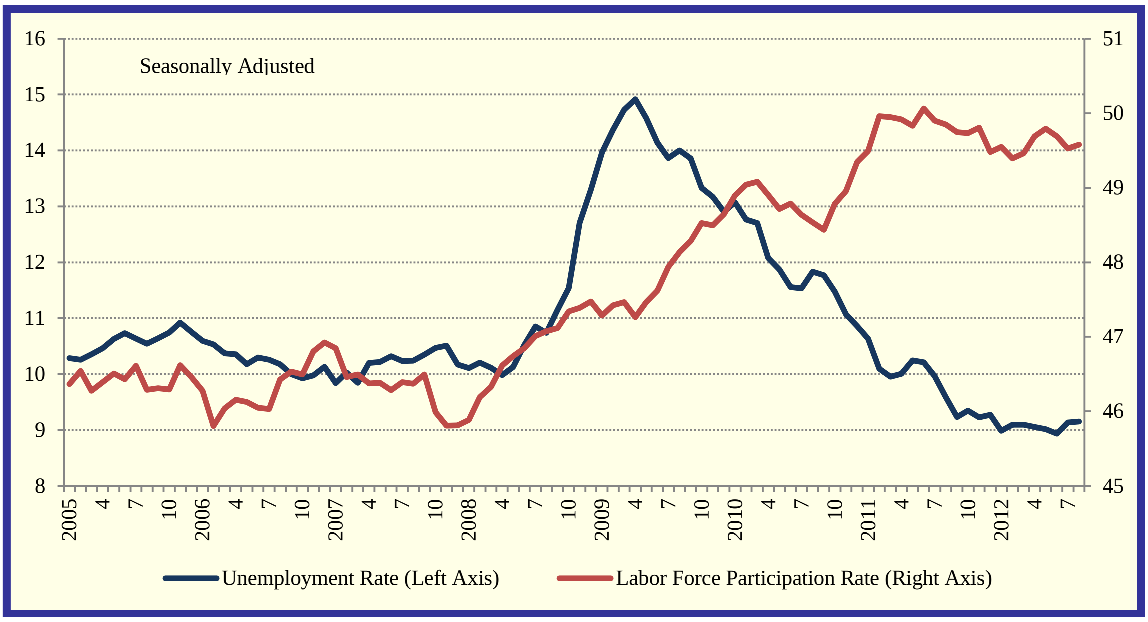


Source: Ministry of Development calculations

A noteworthy issue for the labor market developments in 2011, was the high rate of increase in agricultural employment. In this year, 460 thousand new jobs were created and thus employment increased by 8.1 percent in agricultural sector. As a result, the share of sector in total employment was 25.5 percent.

As a result of these developments in agricultural and non-agricultural sectors, 1,516 thousand new jobs were created and the employment increased by 6.7 percent in 2011. The unemployment rate, which was 11.9 percent in 2010, declined to the level of 9.8 percent in 2011 in spite of the 1.1 percentage point increase in participation rate. Therefore, Turkey has been one of the countries which has decreased unemployment rate most rapidly since 2009. This decline in unemployment rate has been observed in all sub-groups such as female and young people. This fact is important in terms of showing the widespread effectiveness and thus the success of the policies.

Figure 2.5: Unemployment Rate and Labor Force Participation Rate (Percent)



Source: TURKSTAT

Seasonally adjusted industrial sector employment, which recorded remarkable increases in spite of increasing uncertainties in the world economy until April 2012, started to decline in the following four months (Figure 2.3). Seasonally adjusted employment in the services sector has continued to grow at a lower rate in recent months. Therefore, seasonally adjusted employment in non-agricultural sector has followed a horizontal path in recent months. However, the employment in agricultural sector, which increased in the first two quarters of 2012, has slightly decreased in the third quarter of the year (Figure 2.4).

In August 2012, seasonally adjusted total employment increased by 58 thousand people compared to the previous month while increased by 404 thousand people compared to the end of previous year. In this context, seasonally adjusted employment rate reached to 45 percent with the 0.1 percentage point rise compared to end of year. In parallel to these developments, unemployment rate has continued to decrease and seasonally adjusted unemployment rate was recorded as 9.2 percent in August 2012. Scrutinizing the seasonally adjusted series, it is seen that unemployment rate follows a stable path around 9 percent (Figure 2.5).

2.1.2. Inflation, Monetary and Exchange Rate Policies

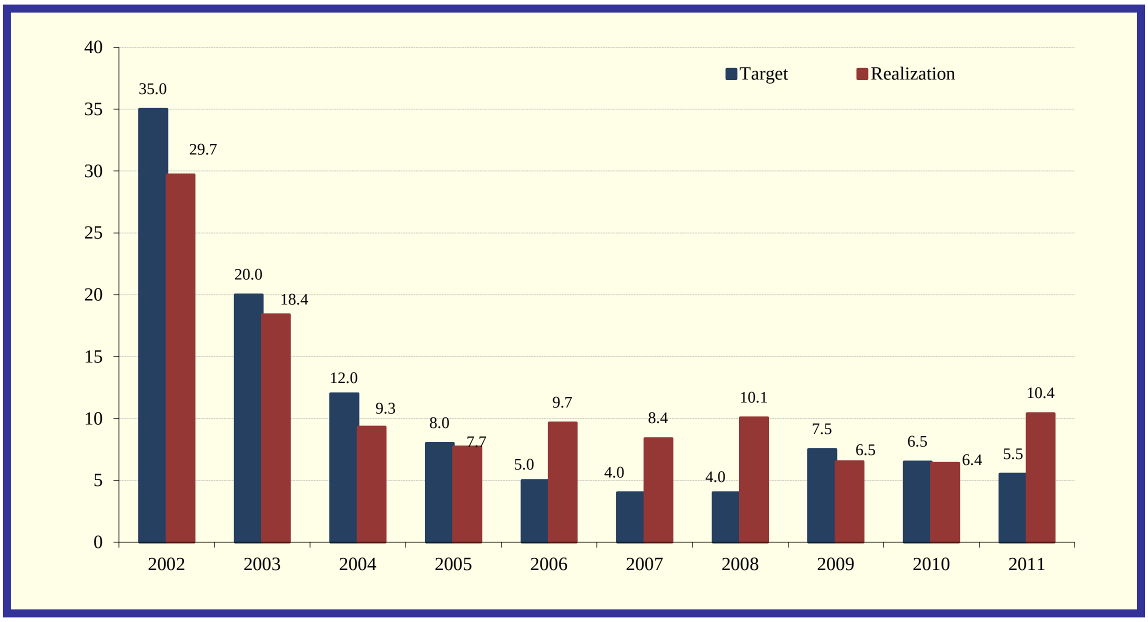
2.1.2.1. Inflation

Having hit a historically-low level with 3.99 percent at the end of the first quarter of 2011, annual CPI inflation trended upwards in the rest of the year due to the developments in food prices, administered prices, tax adjustments and the depreciation of the Turkish Lira and climbed to 10.45 percent at the year-end (Figure 2.6). Annual inflation soared particularly due to the low base in unprocessed food products and high-rated monthly increases in May; but declined upon the correction in the said group’s prices in June. Special Consumption Tax (SCT) rates were raised in some motor vehicles, mobile telephones, alcoholic beverages and tobacco products, and electricity and natural gas tariffs were increased in October. These arrangements added 1.6 percentage points to inflation. Across subcategories, annual energy inflation trended upwards in 2011. Annual inflation in processed food group also displayed increases during the year. However, due to unprocessed food prices, inflation in food group followed a fluctuating course throughout 2011. As for the services group, annual inflation remained on a mild track; while the core goods group showed increases due to import prices in the first half and exchange rate developments in the second half of the year. Therefore, annual inflation in core inflation indicators SCA-H and SCA-I[3] has increased. Consequently, being fuelled mostly by the depreciation in the Turkish Lira, annual CPI inflation realized far above the year-end target of 5.5 percent.

Data released up to November suggest that annual inflation exhibited a downward trend in 2012. In this period, adjustments in the SCT and administered prices added around 1.5-1.6 percentage points to inflation in total. In particular, electricity and natural gas tariffs that were raised in April added 0.5 percentage points to annual inflation. Meanwhile, the adjustments in SCT rates introduced in September coupled with the new electricity and natural gas tariffs, which became effective as of October 1, added around 1.1 percentage points to annual inflation in total. Across subcategories, annual energy inflation, the upward trend of which reversed in May, increased owing to the developments in international oil prices in September, and upon the adjustments in administered prices in October. In 2012, the upward trend in the annual inflation in processed food group reversed in July. Seasonally adjusted unprocessed food prices posted a decline in the first half of the year, yet increased in the second half, except October. Thus, having increased since July due to the unprocessed food prices, annual food inflation went down in October. Annual inflation in services edged up compared to end-2011 figures; whereas that in core goods recorded a continuous decline. Therefore, in tandem with the outlook in the core goods group, core inflation indicators also followed a declining trend throughout the year. As a result, annual CPI inflation stood at 6.37 percent in November.

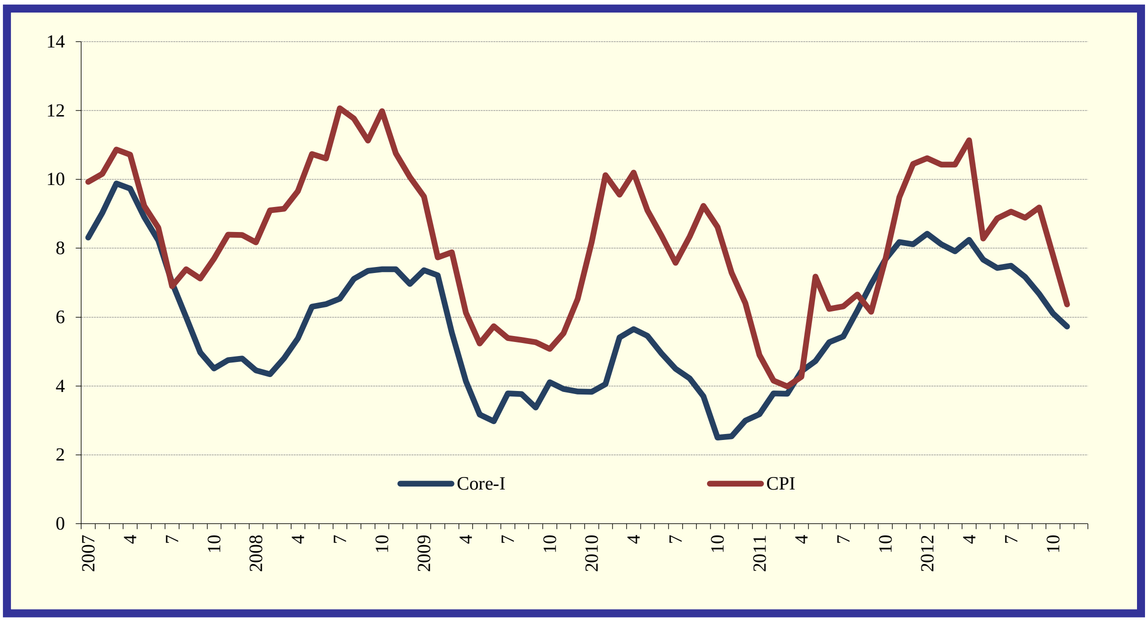
[3] Core CPI-H: Indicators for the CPI Having Specified Coverages-H (Unprocessed food products, energy and alcoholic beverages, tobacco products and gold excluded CPI).
Core CPI-I: Indicators for the CPI Having Specified Coverages-I (Energy, food and non-alcoholic beverages, alcoholic beverages, tobacco products and gold excluded CPI).

Figure 2.6: Annual Inflation Targets and Realizations (CPI, %)



Source: CBRT, TURKSTAT

Figure 2.7: CPI and Core CPI (Annual Percentage Change)



Source: TURKSTAT

2.1.2.2. Monetary and Exchange Rate Policy

Following the global financial crisis, monetary policy in many countries started to address financial stability, in addition to price stability. In the last two years, the Central Bank of the Republic of Turkey enhanced the inflation targeting regime and designed a new monetary policy strategy in order to contain macro-financial risks driven by global imbalances. In line with the new strategy put into force as of the last quarter of 2010, the Central Bank developed policies towards reducing macro-financial risks, thanks also to the favorable inflation outlook in the mentioned period. Accordingly, in addition to the traditional policy tool of the one-week repo auctions, required reserves, reserve option mechanism (ROM), interest rate corridor and other liquidity policies were actively used.

In the period from the adoption of the new policy framework in November 2010 to intensifying uncertainties in the European economy in August 2011, the Central Bank aimed at limiting short term capital flows and preventing excessive appreciation of the Turkish Lira on one hand, and ensuring the rebalancing between external and domestic demand on the other. In this period, the Central Bank widened the interest rate corridor by reducing the overnight borrowing rate and increased the downward volatility of overnight market rates by letting interest rates in overnight markets to be lower than policy rates. Meanwhile, required reserve ratios were raised significantly in the same period to avert excessive credit growth and contain domestic demand. Since August 2011, as concerns over global growth and sovereign debt problems in some European countries intensified, the Central Bank narrowed the interest rate corridor through raising the overnight borrowing rate and rearranged the Turkish Lira required reserves to reduce the liquidity needs of the banking system. Also, the policy rate was reduced moderately. In addition to these policy instruments, for the provision of TL liquidity permanently and at a lower cost to the Turkish banking system, while at the same time bolstering the build-up of the Central Bank's FX reserves Central Bank provided an allowance enabling banks to hold 10 percent of their TL-denominated required reserves in dollar and/or euro in September. This upper limit was raised to 20 percent in October.

Due to the excessive depreciation of the Turkish Lira since August, which was a consequence of the deterioration of the global risk appetite, and the adjustments in administered prices in the last quarter of the year, it became obvious that in the short-term the rise in inflation would be higher than envisaged. In order to prevent this from influencing medium-term inflation expectations and outlook, the Central Bank implemented a sizable tightening in October 2011. In this regard, the interest rate corridor was widened upwards by an O/N lending rate hike of 350 basis points and average funding rate was raised by lowering 1-week repo funding. On the other hand, required reserve ratios were slightly decreased so as to avoid an unfavorable tightening in liquidity conditions due to the increase in overnight interest rates. Furthermore for meeting the TL liquidity requirement of the Turkish banking system permanently and at a lower cost, the upper limit for FX reserves that may be held to meet Turkish Lira reserve requirements was raised from 20 percent to 40 percent of Turkish Lira liabilities. Additionally, in order to strengthen the gold reserves and to provide more flexibility in the banking system's liquidity management, up to 10 percent of the reserve requirements maintained for Turkish Lira liabilities has been allowed to be maintained as "standard gold".

Having achieved the desired outcomes with respect to alleviating macro financial risks, monetary policy has focused on maintaining price stability as of October 2011. In this context, on December 29, 2011 the Central Bank has delivered additional tightening for one week. As a complementary instrument, unsterilized (effective) foreign exchange sales and interventions were used in order to prevent inflation expectations to be adversely affected from exchange rate movements detached from fundamentals. In this context, direct foreign exchange sales interventions have been conducted in October 18 and December 30, 2011 and January 2-4, 2012.

In the first quarter of 2012, despite the favorable course of global risk perceptions, the Central Bank maintained its cautious stance owing to the upside risks on cost factors. By taking into account the improvement in global risk perceptions on easing concerns over the Euro Area, the upper limit of the interest rate corridor was lowered by 100 basis points in February. But still the tight stance was maintained and an additional monetary tightening was delivered during March 23 and March 29, 2012. On the other hand, in order to provide a permanent and flexible funding for banks, besides enhancing gold reserves, 20 percent of the required reserves for TL liabilities were facilitated to be held as standard gold, as opposed to the previously 10 percent.

In April and May 2012, additional monetary tightening was implemented more frequently (May 4-11, May 21-25) with an aim to contain the adverse effects of temporary factors on inflation outlook and limit the risks regarding the pricing behavior. Implementation of more frequent additional tightening not only helped contain credit growth but also reduced inflation uncertainty by curbing exchange rate volatility. These policies, in turn, have prevented a possible deterioration in inflation expectations, amid a period of intensified supply side pressures and double digit inflation. Moreover in May 2012, flexibility regarding the allowance to hold Turkish Lira reserve requirements in foreign currency was increased and the upper limit was raised from 40 percent to 45 percent in order to support financial stability. On the other hand, so as to diminish the cost gap to arise from holding Turkish Lira required reserves in Turkish Lira or foreign exchange, a higher fraction of foreign exchange per each unit of Turkish Lira was decided upon for additional increases in allowance ratios. Thus, the sum corresponding to the 40 percent of Turkish Lira required reserve liabilities was to be multiplied by “1” as in the past, while the second tranche corresponding to 5 percent was to be multiplied by “1.4”. Then, it was facilitated to hold these liabilities upon the resulting amount in dollar and/or euro. This facility was raised by 5 points to 55 percent in June and July and for the sum that corresponds to third and fourth tranches of 5 percent, coefficients were determined as “1.7” and “1.9”. Additionally, the upper limit for the facility to hold Turkish Lira required reserves in gold was raised to 25 percent in June. Meanwhile, the amount corresponding to 20 percent of the facility was to be used by being multiplied by “1” as in the previous case; whereas the second tranche corresponding to 5 percent was to be multiplied by “1.5”.

In August, the upper limit for FX reserves that might be held to maintain Turkish Lira reserve requirements has been raised to 60 percent and the reserve requirement to be maintained in FX for the additional 5 percent tranche has been decided to be multiplied by a factor of “2”. Furthermore, to support financial stability, the reserve option coefficient (ROC) for the first tranche corresponding to 40 percent of Turkish Lira reserve requirements has been raised to “1.1”. Meanwhile, the upper limit for gold reserves that might be held to maintain Turkish Lira reserve requirements has been raised from 25 percent to 30 percent, where this 5 percent additional tranche will be multiplied by a ROC of “2”.

In September, additional monetary easing by the central banks of developed economies has led to an improvement in the risk appetite in global financial markets. As this development has the potential to lead to an acceleration of capital inflows, with an aim to support financial stability, the Central Bank increased the reserve option coefficients and narrowed the interest rate corridor by decreasing O/N lending rate by 150 basis points. In this context, the ROCs for all tranches of FX reserves that might be held for Turkish Lira reserve requirements have been increased by “0.2” points. In October, with an aim to boost the financial stability, the ROCs for all tranches of FX reserves that might be held for Turkish Lira reserve requirements have been increased by “0.1” points and O/N lending rate was cut by 50 basis points.

2.1.3. Financial Sector

Turkish banking sector has successfully maintained its strong structure and stability in 2012 despite the negative developments experienced and delaying signs of recovery in global markets in recent years. Even though the number of banks operating in the sector was 48 in September 2012, same as at the end of previous year, the banking sector sustained its expansion through alternative distribution channels, the number of customers and other operational indicators.

Analyzing Turkish banking sector balance sheet, it is observed that asset size which amounted to 648.1 billion dollars as of end-2011 increased to 735.5 billion dollars in September 2012. The credit growth was the main determinant behind asset escalation. In this context, the credit volume of the sector has reached to 424.8 billion dollars by a 16.8 percent increase as of September 2012 compared to end of 2011.

During the same period, the share of securities in total assets has been decreasing relatively while the share of loans has continued increasing. Accordingly, the share of loans in total assets which was 56.1 percent in 2011 increased to 57.8 percent in September 2012. The main reason behind this strong increase in loans was the decline in public borrowing needs which was also gradually paving way to lower market interest rates. Besides real sector loans, consumer loans have showed a significant growth trend in recent years. Low market interest rates, by improving consumer confidence, played an accelerating role in rising consumer loans.

When strength indicators of banking system are analyzed, it is seen that capital adequacy ratio of the sector, which has been 16.5 percent in September 2012, is quite above 8 percent legal threshold and 12 percent target limit. The scope of current own funds of Turkish banking sector is mostly comprised of Tier-I capital which represents cash capital elements and has a buffer role against troubles. Current sound capital structure increases resilience of the sector against sudden shocks and this sound structure supports maintaining stability in economy.

As credit risk indicator of the sector, ratio of non-performing loans to gross loans increased to 5.3 percent in 2009 following the emergence of global crisis and pursued a declining trend, decreasing to 2.95 percent as of September 2012. The ratio of the sector's foreign exchange net general position to own funds was 1.6 percent as of September 2012, which are far from risky levels. The ratio of off-balance sheet transactions to assets, which has grown in recent years, has the purpose of hedging of financial risks.

Table 2.3: Banking Sector Overview

	2005	2006	2007	2008	2009	2010	2011	Sep-12
Main Aggregates								
Assets (Billion Dollars)	295.9	356.0	502.0	481.0	560.0	656.5	648.1	735.5
Loans (Billion Dollars)	113.7	111.0	246.0	241.0	267.0	343.1	363.5	424.8
Deposits (Billion Dollars)	187.1	179.0	308.0	299.0	345.6	402.4	370.3	414.7
Number of Banks	47	50	50	49	49	49	48	48
Number of Employees (Thousands)	138.7	151.0	167.8	182.7	184.2	191.2	195.3	199.2
Performance Indicators								
Net Profit (Billion Dollars)	3.7	2.6	0.0	8.8	13.6	14.4	10.6	9.6
Return on Assets (%)	1.7	2.5	2.8	2.0	2.6	3.0	1.7	1.4
Rate of Return for Equity Capital (%)	12.1	20.1	21.7	16.8	20.3	20.1	15.5	11.5
Loans / Total Assets (%)	38.0	44.0	49.2	50.2	47.1	52.3	56.1	57.8
Risk Indicators								
Capital Adequacy Ratio (%)	23.7	22.1	19.0	18.0	20.6	18.7	16.6	16.5
FX Position in Balance Sheet (Billion Dollars)	-1.9	-5.5	-8.3	-3.3	-11.6	-14.0	-17.8	-19.3
Net General FX Position (Billion Dollars)	-0.1	0.1	0.2	-0.1	0.4	0.1	0.3	1.6
Non-Performing Loans / Gross Loans (%)	4.8	3.8	3.5	3.7	5.3	3.7	2.7	3.0
Securities Portfolio / Assets (%)	36.0	31.8	21.3	26.5	31.5	27.9	22.6	20.1
Off-Balance Sheet Transactions / T. Assets (%)	50.6	55.5	66.3	65.0	69.5	103.1	134.9	152.3

Source: BRSA

Turkish banking sector continued to make profit during the global crisis period, even though not as high as previous periods. Banking sector net profit which was 10.6 billion dollars in 2011 realized as 9.6 billion dollars in the first nine months of 2012. Considerably high return on assets and return on own funds ratios are realized as 1.4 percent and 11.5 percent respectively within the first nine months of 2012 which were 1.7 percent and 15.5 percent respectively in 2011.

Stock market had a decreasing trend in 2011 and the ISE 100 Index declined to 51,267 with a 22.3 percent fall. In 2012 stock prices picked up and the Index has shown an increase of 41.5 percent in the first ten months of 2012, closing at 72,529. ISE 100 Euro Index, which had been at 1,432 with a 34.7 percent decline from the end of the previous year, increased by 48.9 percent in the first ten months of 2012, closing at 2,133. The share of foreign investors in the stock market was on average at 62.9 percent in the first 10 months of 2012. The share of foreign investors in the stock market, which was 65 percent in December 2010, declined to 62 percent in December 2011 and increased to 63 percent in October 2012.

The increasing trend in debt instrument markets that started in 2010 has been continuing. The value of private sector debt instruments, which was 13.7 billion TL at the end of 2011, has increased to 26 billion TL at the end of September 2012.

There were 59 companies operating in insurance and private pension sector, as of 31 September 2012. 35 of these companies were operating in the area of non- life insurance, 17 in life insurance and pension area, 6 in life insurance area and 1 in reinsurance area. As of the same date, the premium production in insurance sector in eight months realized as 14.3 billion TL with a 13 percent increase compared to same period of previous year. Total assets of the sector has been 46.9 billion TL as of August 2012.

Private pension system has sustained its stable growth in 2012, similar to preceding years. Compared to September 2011, the number of participants reached 2.9 million increasing by 15 percent and total fund amount was 18.5 billion TL by increasing 32 percent as of September 2012. The Law No. 6327, enacted in June 29 of 2012, introduced crucial amendments regarding the private pension system to increase the effectiveness of the system. According to the amendment, state incentive of tax deduction from income tax base of participants will be replaced by a new state incentive as of January 2013. Under the new incentives, the state will pay a matching contribution of 25 percent for every contribution paid by the participant. Moreover, the amendments contains provisions for promoting group pension plans with institutional participation, increasing the value added to the participants by reducing operational costs & fees and increasing effectiveness of operations in the system.

In the compulsory earthquake insurance system, which was formed to meet the earthquake loss in housing through insurance, total numbers of compulsory earthquake policies reached 4,518 thousands by 24 percent increase, as of 15 November 2012. On the other hand, legal infrastructure of the compulsory earthquake was reinforced by the Disaster Insurance Law No. 6305 and this Law became effective as of 18 May 2012. Additional measures have been taken in the law to ensure an increase in insurance.

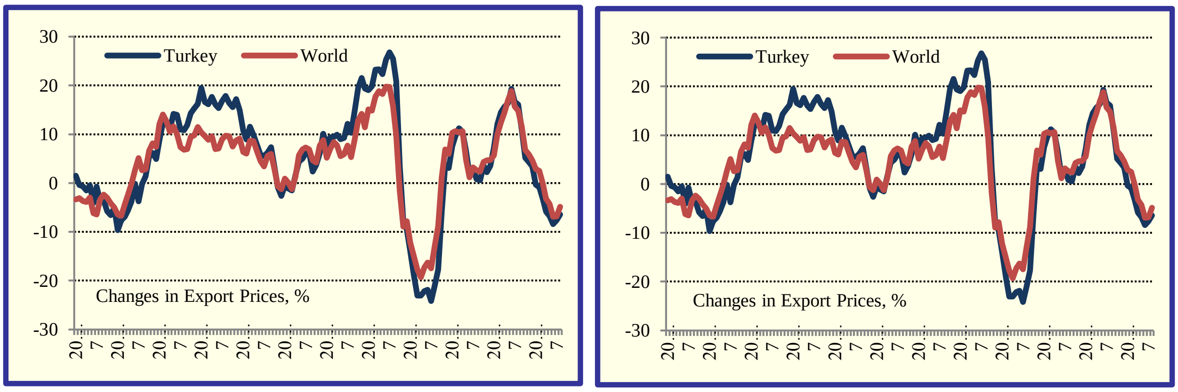
2.1.4. Balance of Payments

2.1.4.1. Current Account

Domestic demand which increased rapidly in 2010, sustained its pace in the first half of 2011, while external demand continued to be weak. Rapid increase in imports compared to exports led to a rise in foreign trade deficit and current account deficit. In the same period, current account deficit increased by 65.1 percent compared to previous year and reached to 77 billion dollars in 2011; while foreign trade volume increased to 375.7 billion dollars (Table 2.4). Thus, foreign trade volume to GDP ratio, which was 40.9 percent in 2010, reached 48.5 percent in 2011.

With slowdown in domestic demand due to measures taken in the second half of the 2011 and export market diversification efforts, exports growth has accelerated while significant decrease was recorded in imports. Gold exports, which has significantly increased recently, has contributed to the successful export performance. As a result of these developments, foreign trade deficit and current account deficit decreased rapidly. In January-October 2012 period, trade deficit declined to 55.4 billion dollars from 76.1 billion dollars and current account deficit declined to 41.1 billion dollars from 65 billion dollars compared to same period of previous year.

Figure 2.8: Developments in Exports and Export Prices



Source: IMF-IFS, TURKSTAT

In 2011, Turkish exports recorded an increase of 18.5 percent, of which 6.2 percent was real increase and 11.7 percent was price increase, while world exports increased by 19.4 percent (Figure 2.8). In 2012, despite ongoing risks and problems in developed economies, successful market diversification efforts have prevented weak export performance. In the first nine months of 2012, world export contracted by 0.5 percent. In the same period, nominal exports of Turkey increased by 13.4 percent and reached 126.3 billion dollars, despite slow growth performance of trading partners and 4.8 percent decline in export prices (Figure 2.8).

In line with the economic recovery in the post crisis period, imports have accelerated and reached 240.8 billion dollars with an increase of 29.8 percent, in 2011. However imports, which began declining in the last quarter of 2011, decreased by 1.8 percent in annualized terms in October 2012 due to contraction in domestic demand as a result of macro-prudential measures. In the same period, the highest contraction belongs to imports of consumer goods with 12 percent. Imports of capital goods decreased by 10.4 percent, while imports of intermediate goods increased by 1.9 percent.

Table 2.4: Balance of Payments

(Billion Dollars)

	Annual		**January-October**	
	2010	**2011**	**2011**	**2012**
Current Account	**-46.6**	**-77.0**	**-65.0**	**-41.1**
Trade Balance	-56.4	-89.1	-76.1	-55.4
Total Exports	120.9	143.4	118.5	134.3
Exports (fob)	113.9	134.9	111.4	126.3
Total Imports	-177.3	-232.5	-194.6	-189.7
Imports (cif)	-185.5	-240.8	-201.6	-195.8
Balance on Services	15.5	18.0	16.6	19.1
Credit	34.7	38.6	33.6	35.8
Tourism Revenues	20.8	23.0	20.5	20.1
Debit	-19.3	-20.6	-17.0	-16.7
Balance on Income	-7.1	-7.6	-6.7	-5.9
Credit	4.5	4.0	3.5	3.9
Debit	-11.6	-11.6	-10.1	-9.8
Current transfers	1.4	1.7	1.2	1.1
Capital and Financial Account	**43.9**	**65.6**	**53.6**	**34.5**
Capital Account	-0.1	0.0	0.0	0.0
Financial Account (Excluding Reserves)	56.8	63.8	55.4	55.5
Direct Investment	7.6	13.6	10.3	7.2
Direct Investment in Turkey	9.0	16.1	12.1	10.6
Direct Investment Abroad	-1.5	-2.5	-1.8	-3.4
Portfolio Investment	16.1	22.0	16.5	30.7
Other Investment	33.1	28.2	28.6	17.6
Assets	7.0	11.1	10.6	3.4
Liabilities	26.1	17.1	18.0	14.3
Trade Credits	2.1	2.0	3.2	0.4
Loans	9.7	18.9	17.6	4.7
Monetary Authority	0.0	0.0	0.0	0.0
General Government	1.4	-0.8	-0.4	-1.6
Banks	12.9	12.5	11.9	1.6
Other Sectors	-4.6	7.2	6.1	4.7
Currency and Deposits	13.8	-4.3	-3.3	8.7
Monetary Authority	-0.6	-1.9	-1.7	-2.0
Banks	14.3	-2.4	-1.7	10.6
Other Liabilities	0.5	0.5	0.5	0.5
Reserve Assets	-12.8	1.8	-1.7	-21.0
Net Errors and Omissions	**2.7**	**11.4**	**11.3**	**6.6**

Source: CBRT

Table 2.5: Foreign Trade by Broad Economic Categories Classification

(Billion Dollars)

	Annual					January-October				
	2010	Share %	2011	Share %	Change %	2011	Share %	2012	Share %	Change %
Total Exports	**113.9**	**100**	**134.9**	**100**	**18.5**	**111.4**	**100**	**126.3**	**100**	**13.4**
Capital Goods	11.8	10.3	14.2	10.5	20.6	11.7	10.5	11.2	8.9	-3.7
Intermediate Goods	56.4	49.5	67.9	50.4	20.5	56.3	50.5	69.4	54.9	23.2
Consumption Goods	45.3	39.8	52.2	38.7	15.2	43.0	38.6	45.3	35.9	5.4
Other	0.4	0.4	0.6	0.4	35.0	0.4	0.4	0.4	0.3	-5.8
Total Imports	**185.5**	**100**	**240.8**	**100**	**29.8**	**201.6**	**100**	**195.8**	**100**	**-2.9**
Capital Goods	28.8	15.5	37.3	15.5	29.3	30.8	15.3	27.4	14.0	-11.0
Intermediate Goods	131.4	70.8	173.1	71.9	31.7	145.2	72.0	145.7	74.5	0.4
Consumption Goods	24.7	13.3	29.7	12.3	20.0	24.9	12.4	21.8	11.1	-12.7
Other	0.5	0.3	0.7	0.3	35.3	0.7	0.3	0.8	0.4	26.3

Source: TURKSTAT

Foreign trade by country groups does not show a significant change in 2011, compared to previous year. Share of EU countries in exports decreased by 0.1 percentage point and realized as 46.2 percent in 2011 and the share of other countries in exports realized as 51.9 percent, same as previous year. Share of imports from EU countries in total imports declined to 37.8 percent in the same period, indicating 1.1 percentage points decline. Exports have displayed high performance with the effect of successful implementation of policies to diversify export markets, despite increasing problems in EU economies since the last quarter of 2011. Thus, share of other countries in exports reached to 60 percent in January-October 2012 period (Table 2.6).

Table 2.6: Foreign Trade by Country Groups

(Billion Dollars)

	Annual					January-October				
	2010	Share %	2011	Share %	Change	2011	Share %	2012	Share %	Change
Merchandise Exports	**113.9**	**100**	**134.9**	**100**	**18.5**	**111.4**	**100**	**126.3**	**100**	**13.4**
European Countries (EU-27)	52.7	46.3	62.3	46.2	18.3	52.2	46.9	48.6	38.5	-7.0
Other Countries	59.1	51.9	70.0	51.9	18.4	57.1	51.3	75.8	60.0	32.7
Other European	11.4	10.0	13.0	9.6	14.1	10.5	9.4	11.7	9.3	11.8
North Africa	7.0	6.2	6.7	5.0	-4.6	5.5	4.9	7.8	6.2	41.3
Other Africa	2.3	2.0	3.6	2.7	60.9	2.9	2.6	3.2	2.6	12.2
North America	4.2	3.7	5.5	4.0	28.7	4.4	4.0	5.6	4.4	26.0
Central America &Caraips	0.6	0.5	0.6	0.5	4.7	0.5	0.5	0.7	0.5	28.1
South America	1.2	1.1	1.8	1.4	48.7	1.6	1.4	1.8	1.4	14.3
Near And Middle East	23.3	20.5	27.9	20.7	19.9	22.8	20.4	36.0	28.5	58.0
Other Asia	8.6	7.5	10.2	7.6	18.9	8.4	7.6	8.6	6.8	1.9
Australia & N. Zealand	0.4	0.4	0.5	0.4	19.4	0.4	0.4	0.4	0.3	2.2
Other Countries	0.1	0.1	0.2	0.1	61.1	0.2	0.1	0.1	0.1	-41.7
Turkish Free Zones	2.1	1.8	2.5	1.9	22.1	2.0	1.8	1.9	1.5	-5.5
Merchandise Imports	**185.5**	**100**	**240.8**	**100**	**29.8**	**201.6**	**100**	**195.8**	**100**	**-2.9**
European Countries (EU-27)	72.2	38.9	91.1	37.8	26.3	76.4	37.9	71.7	36.6	-6.2
Other Countries	112.5	60.6	148.7	61.7	32.2	124.3	61.7	123.2	63.0	-0.9
Turkish Free Zones	0.9	0.5	1.0	0.4	18.2	0.9	0.4	0.9	0.4	-0.7

Source: TURKSTAT

Services balance of 15.5 billion dollars in 2010, increased to 18 billion dollars in 2011 with the effect of the rise in tourism revenues. In January-October 2012 period, services balance grew by 2.5 billion dollars compared to the same period of previous year and realized at 19.1 billion dollars.

In 2011, income account deficit reached to 7.6 billion dollars with an increase of 0.5 billion dollars. In January-October 2012 period, an improvement of 0.8 billion dollars was recorded in the income balance compared to same period of previous year and the deficit receded to 5.9 billion dollars.

Surplus of current transfers, which was 1.4 billion dollars in 2010, increased to 1.7 billion dollars in 2011. In January-October 2012 period, current transfers decreased by 0.2 billion dollars compared to same period of previous year and recorded a surplus of 1.1 billion dollars.

2.1.4.2. Capital and Financial Account

The effects that caused slowdown in growth rate of world economy led capital inflows to emerging market and developing economies to be realized as 503 billion dollars, below the level of 2010[4]. Despite the deceleration of capital inflows, capital inflows excluding reserves to Turkey recorded its historical maximum level of about 64 billion dollars. This development indicates that Turkish economy, with its high growth performance and low risk profile, decouples from other emerging market economies in this period.

Net direct investment to emerging market and developing economies increased to 462.4 billion dollars in 2011, almost its historical maximum level. As a result of ongoing global economic uncertainties, aforementioned figure is expected to decline to its 2010 levels and realized as 393.8 billion dollars in 2012. Worldwide expansion of direct investment flows in 2011 also affected Turkey and net foreign direct investment, which was 7.6 billion dollars in 2010, increased to 13.6 billion dollars. In 2011, foreign direct investment was recorded as 16 billion dollars of which 11 billion dollars was in the form of mergers and acquisitions[5]. As of October 2012, net foreign direct investment declined to 7.2 billion dollars compared to the same period of previous year.

With the help of relatively low risk profile of Turkey, purchases in debt securities were influential in portfolio investment inflows reaching 22 billion dollars in 2011. In this year, while net inflows of 14.8 billion dollars in government domestic borrowing instruments (GDBI) was recorded, borrowing of 4.3 billion dollars was recorded through debt securities issued abroad by Treasury. Moreover, banks provided capital inflows of 2.8 billion dollars through issuing debt securities abroad in 2011. As of October 2012, net portfolio investment to Turkey reached to 30.7 billion dollars and in its sub-items, net inflows of 13.6 billion dollars in GDBI, net inflows of 3.8 billion dollars in debt securities issued by Treasury abroad, net inflows of 5.9 billion dollars in banks' debt security issues abroad and net inflows of 3.0 billion dollars of equity securities were recorded.

In 2011, other investments item decreased compared to last year. Decline in TL denominated deposits of foreign banks was influential in this development. In January-October period of 2012, net inflows of 17.6 billion dollars were recorded in other investments item. Net credit usage of banks and other sectors amounted to 1.6 billion dollars and 4.7 billion dollars respectively and the rise in deposits of banks amounting 10.6 billion dollars were influential in this development.

Consequently, in January-October 2012 period, capital inflows realized as 55.5 billion dollars, of which 21 billion dollars were recorded as reserve assets. In this context, net capital and financial account was realized as 34.5 billion dollars. Therefore, net omission and error item recorded a positive 6.6 billion dollars balance.

[4] IMF World Economic Outlook Report, October 2012.
[5] Minister of Economy, International Foreign Direct Investment Report 2012.

2.2. Medium Term Macroeconomic Scenario

After the global crisis that started in 2008, stability in the world economy has not been achieved fully yet. Although decreased in the second half of 2012, the risks to the world economy still continue since the uncertainties in developed economies could not be completely eliminated.

In an environment of global uncertainty, Turkish economy has performed successfully with the macroeconomic measures put into practice, strong public finance and banking sector. Turkish economy recorded high growth rates following the crisis and necessary steps are taken to bring the economy to a balanced growth path within the framework of the soft landing scenario.

The main objectives of Pre-Accession Economic Programme (2013-2015) in accordance with the Medium Term Programme (2013-2015) are; to increase the growth to its potential level, to sustain the decreasing trend in the current account deficit, to ameliorate the public balances, to enhance the employment, to continue fighting against inflation and consequently, to strengthen the macro-economic and financial stability.

To enhance employment, as well as the policies ensuring stable growth, policies to improve quality of labor force, flexibility of labor market, participation in the labor force will be given priority.

The competitiveness of the economy, the efficiency of the public expenditures, good governance, education system, juridical system, tax system, informality, the continuation of structural transformation in the fields of local administration, regional development and sustainable development, the realization of urban transformation are among the main priorities of the Programme.

2.2.1. Real Sector

2.2.1.1. Demand Components of Growth

The economy has started to slow down with the effects of macro prudential policies implemented in the last quarter of 2011 and this trend has continued in the first nine months of 2012. It is foreseen that gradual recovery will begin in the last quarter of the year with the contribution of base effect and relative easing in monetary policy. Thus, Turkish economy is going to slow down gradually in 2012, as targeted.

Table 2.7: Demand Components of Growth

(Percentage Change, at 1998 Prices)

		Forecast			
	2011	**2012**	**2013**	**2014**	**2015**
Total Consumption Expenditure	7.3	1.0	3.1	4.3	4.3
Private	7.8	0.6	3.1	4.4	4.4
Public	4.5	3.9	3.6	3.4	3.3
Total Investment Expenditure	17.2	-3.6	6.5	7.3	7.5
Gross Fixed Capital Formation	18.5	-0.7	6.8	6.7	6.4
Private Fixed Investment	23.1	-1.7	7.1	7.0	7.0
Public Fixed Investment	-3.3	5.4	5.4	5.1	2.4
Change in Stocks [1]	-0.3	-0.8	-0.1	0.1	0.2
Exports of Goods and Services	6.4	14.1	4.2	5.9	6.1
Imports of Goods and Services	10.9	0.0	4.0	6.0	6.3
Gross Domestic Product	8.5	3.2	4.0	5.0	5.0
Domestic Demand	9.6	-0.1	3.9	5.0	5.1
Domestic Final Demand	9.9	0.6	4.0	4.9	4.8

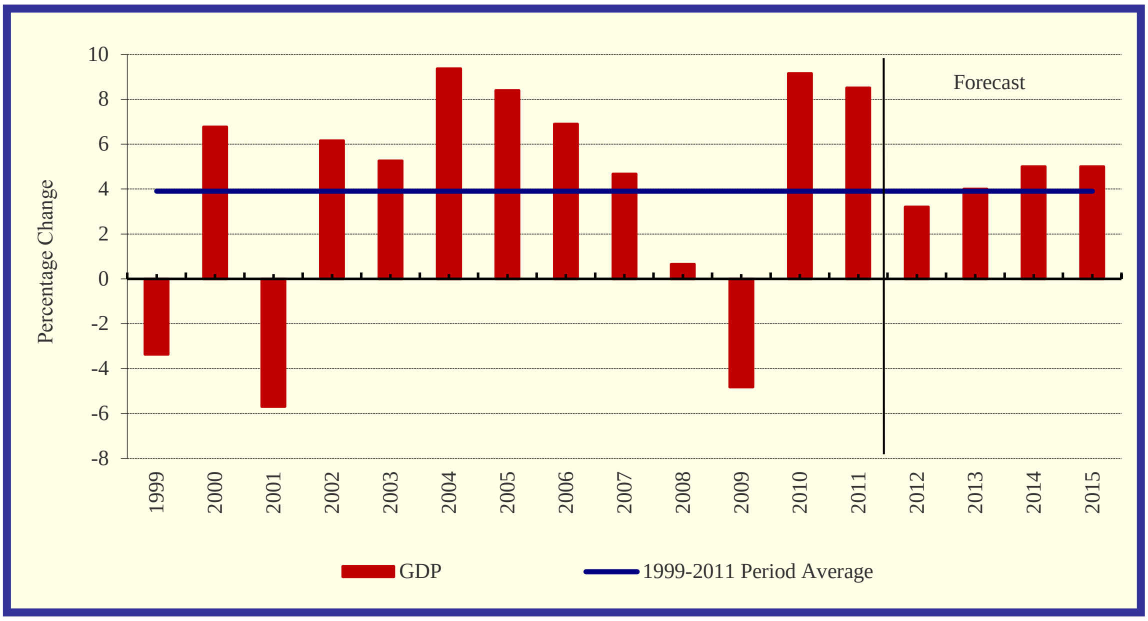
Source: Realization TURKSTAT, forecast Ministry of Development.
(1) Contribution to GDP growth.

A slowdown both in private consumption and private investment growth was observed in first half of 2012. In this period, private consumption expenditures contracted by 0.5 percent while contraction in private investment expenditures was realized as 3.4 percent. Along with the recovery in rest of the year, it is predicted that private consumption expenditures will increase by 0.6 percent and private investment expenditures will contract by 1.7 percent (Table 2.7). Contribution of net exports to growth is expected to be 3.3 percentage points for the whole year. Thereby, GDP growth is expected to be 3.2 percent in 2012. Considering the developments in third quarter of the year, forecasted growth rate is assessed to carry downward risk and the contraction in domestic demand is expected to be higher than the MTP (2013-2015) projections, whereas the contribution of net exports to growth is expected to substitute this effect.

Public consumption expenditures, which increased by 4.7 percent in the first nine months of 2012 compared to the same period of previous year, is envisaged to increase by 3.9 percent in the whole year. Public sector fixed capital investments, which increased by 3.5 percent in the same period, is expected to increase in the last three months as well and grow by 5.4 percent in 2012.

Turkish economy achieved the targeted soft landing following the high growth rates recorded in 2010 and 2011. Thereby, considering aforementioned developments and forecasts, the economy is expected to grow by 3.2 percent in 2012, yet with some downward risks. With the decrease in global uncertainties, in the medium term, Turkish economy is predicted to grow close to its potential and GDP growth is expected to be 4 percent in 2013, 5 percent in 2014 and 2015 (Figure 2.9).

Figure 2.9: GDP Growth



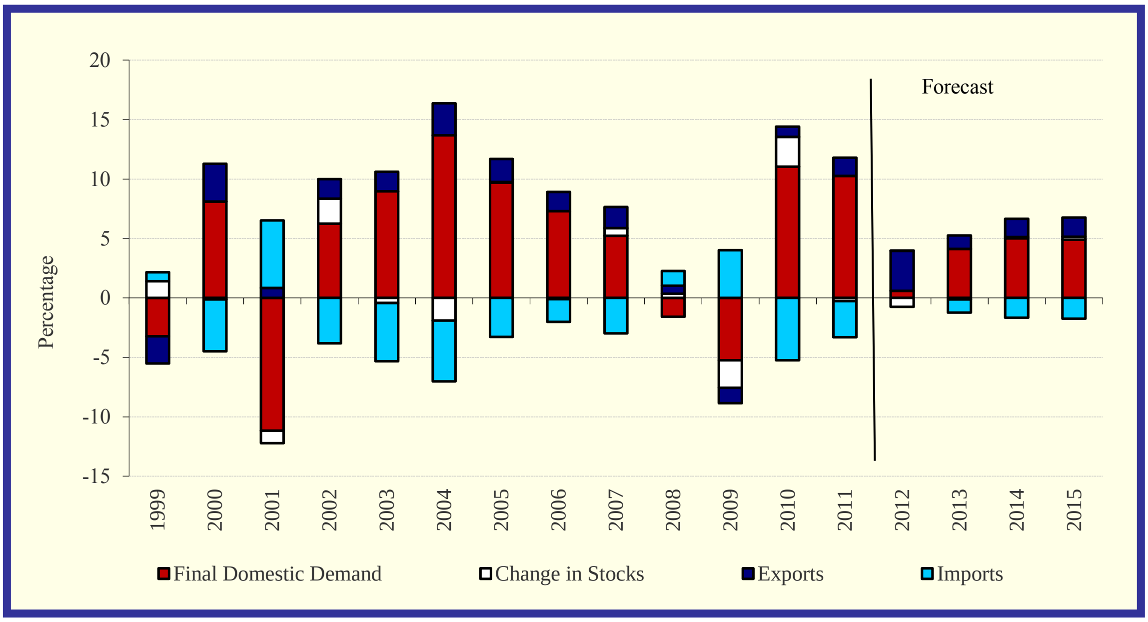
Source: Realization TURKSTAT, forecast Ministry of Development.

From 2013 onwards, private consumption expenditures are expected to accelerate in parallel with GDP growth as a result of domestic and external demand rebalancing policies. Private sector investments are also foreseen to rise along with the global recovery and stability in the Programme period.

Along with the policies for strengthening fiscal discipline in the medium term, the contribution of both public consumption and investment expenditures to growth is expected to decrease. In this period, it is forecasted that public consumption will increase by 3.4 percent and public investments will increase by 4.3 percent on average annually.

In consistent with Turkey's growth strategy, economic growth in PEP (2013-2015) period is expected to be private sector driven. Net exports, which have contributed to growth positively in 2012 due to the decline in domestic demand, are predicted to have a zero contribution to growth in the forthcoming period along with domestic demand rebalancing. In this context, it is forecasted that both exports and imports of goods and services will increase by 5.4 percent annually on average in the Programme period.

Figure 2.10: Contributions to GDP Growth



Source: Ministry of Development calculations.

2.2.1.2. Investment-Saving Balance

With the decisively and timely implemented fiscal and monetary policies during the global crisis period, Turkish economy recorded high growth performance in 2010 and 2011. In parallel with improvements in financial conditions and expectations, the ratio of private sector investments to GDP reached 18 percent in 2011 by 3 percentage points increase compared to previous period. On the other hand, share of public fixed capital investments in GDP was realized as 3.7 percent with 0.3 percentage point decline in this period. Change in stocks to GDP ratio was realized as 2 percent and thus, share of total investment expenditures reached to 23.8 percent with 4.3 percentage points rise compared to previous year (Table 2.8).

In addition to measures to decrease current account deficit, economy has started to slow down since the last quarter of the year as a result of ongoing global uncertainty in 2011. This situation has continued along with the deterioration of global growth expectations in 2012 and the effects of domestic and external demand rebalancing policies' becoming apparent. In this period, while share of private fixed capital investments in GDP was 17.1 percent with a 1.3 percentage points decline compared to previous year, share of public fixed capital investments in GDP stood at around 3.5 percent level. It is predicted that share of private fixed capital investments in GDP will be 18 percent and share of public fixed capital investments in GDP will increase to 3.9 percent in 2012. Therefore, the ratio of total investment expenditures to GDP is expected to reach 21.9 percent at the end of 2012.

In PEP (2013-2015) period, growth is expected to follow a slower path compared to post-crisis recovery period. With the impact of policies supporting private sector investments aiming to reduce the current account deficit in medium and long-term, private fixed capital investments are expected to increase by 12.9 percent on average in 2013-2015 period. In this context, it is forecasted that the ratio of private sector investments to GDP will reach to 19.2 percent at the end of the Programme period. On the other hand, public fixed capital formation is expected to be 3.9 percent of GDP at the end of the period. Thus, it is predicted that share of total fixed capital investments in GDP will reach to 23.1 percent in 2015.

With the slowdown started in the last quarter of 2011, imports decreased to a significant extent and this has contributed to the decline in the current account deficit considerably. As a result of rapid decline in current account deficit and inability to increase domestic savings, it is foreseen that the ratio of total savings to GDP will recede to 21.1 percent by a decline of 2.7 percentage points in 2012. In addition to measures taken in 2011 and 2012, with measures to be implemented in PEP (2013-2015) period, it is predicted that by following an increasing path domestic saving rates will reach 16.1 percent of GDP at the end of the period. During the Programme period, foreign savings need is expected to decrease with the increase in domestic savings.

Table 2.8: Investment-Savings Balance

(Percent of GDP)

				Forecast			
	2009	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
Total Investment	14.9	19.5	23.8	21.1	21.5	22.0	22.6
Fixed Capital Formation	16.9	18.9	21.8	21.9	22.5	22.8	23.1
Public	3.7	4.0	3.7	3.9	4.0	4.0	3.9
Private	13.2	15.0	18.0	18.0	18.5	18.9	19.2
Change in Stocks	-1.9	0.6	2.0	-0.9	-1.0	-0.8	-0.5
Total Savings	14.9	19.5	23.8	21.1	21.5	22.0	22.6
Domestic Savings	12.6	13.2	13.9	13.7	14.4	15.1	16.1
Foreign Savings	2.2	6.3	10.0	7.3	7.1	6.9	6.5

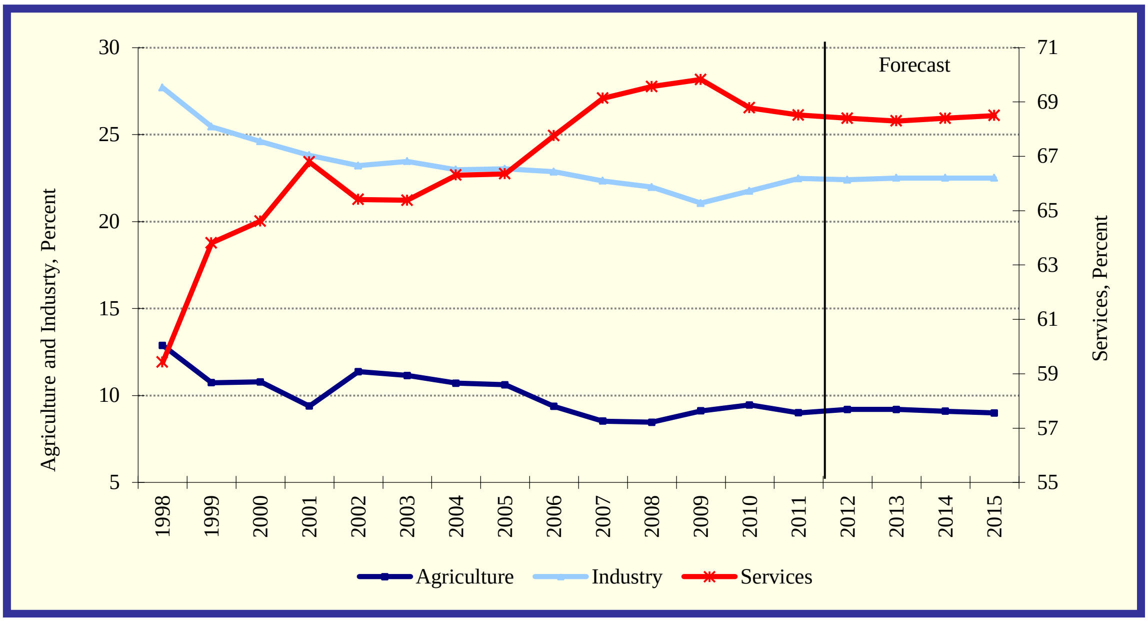
Note: Ministry of Development calculations (National accounts data of TURKSTAT are used).

2.2.1.3. Growth by Sectors

In 2011, agriculture sector recorded relatively lower growth rate compared to industry and services sectors and its share was realized as 9 percent by a decline 0.5 percentage point compared to the previous year. Value added in agriculture sector, which has increased by 3.3 percent in the first nine months of 2012, is expected to increase by 3.7 percent in 2012, and share of the sector in total production is projected to reach to 9.2 percent. In 2013-2015 period, the increase of value added in agriculture sector is expected to slow down and reach to its trend. In this context, it is foreseen that agricultural value added will increase by 3 percent on average during the Programme period and the share of the sector in GDP will remain constant around 9 percent by the end of the period.

Value added of industry sector increased by 3.1 percent in the first nine months of 2012 compared to previous year. While growth of manufacturing sector was recorded as 11.2 percent in the first nine months of 2011, it was 2.8 percent in the same period of 2012. While growth of energy sector decreased to 6.2 percent from 8 percent in the same period, mining sector growth decreased to 2.8 percent from 3.3 percent. It is foreseen that value added of industry sector will increase by 3.1 percent in 2012. In Programme period, industry sector value added is expected to increase by 4.7 percent annually on average implying that its share in GDP will remain constant.

Figure 2.11: Production by Sectors



Source: Realization TURKSTAT, forecast Ministry of Development.

Services sector, which is driven by transport, storage and communication sector, financial intermediation sector and real estate, renting and business activities sector, has recorded 2.6 percent growth in the first nine months of 2012 compared to same period of previous year. In parallel with some of the leading indicators in industry sector, value added in services sector is expected to increase by 3.2 percent in 2012, below the previous PEP forecast. Growth of the sector is expected to accelerate in 2013-2015 period and to be 5 percent annually on average. Thereby, the share of the services sector in GDP is foreseen to remain constant around its 2011 level during the Programme period.

Table 2.9: Value-Added by Sectors

(Percent)

	Realization			Forecast			
	2009	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
	Growth Rates[1] (1998 Prices)						
Agriculture	3.6	2.4	5.6	3.7	3.0	3.0	3.0
Industry	-6.9	12.8	9.4	3.1	4.0	5.1	5.0
Services	-3.2	8.6	8.9	3.2	4.2	5.5	5.4
GDP	-4.8	9.2	8.5	3.2	4.0	5.0	5.0
	Percent of GDP[2] (Current Prices)						
Agriculture	9.1	9.5	9.0	9.2	9.2	9.1	9.0
Industry	21.1	21.8	22.5	22.4	22.5	22.5	22.5
Services	69.8	68.8	68.5	68.4	68.3	68.4	68.5
GDP	100.0	100.0	100.0	100.0	100.0	100.0	100.0

[1] Agriculture, industry and services sectors growth rate was calculated by constant prices, GDP growth rate was calculated by purchaser's prices.
[2] Financial intermediation services indirectly measured and taxes-subsidies were allocated with respect to sectoral weights.

2.2.1.4. Sources of Growth

Analyzing the sources of growth, it is observed that periodical developments have affected the long-term composition of sources of growth. With the impact of crises and instabilities, annual average growth rate was realized as 4.3 percent in the 1985-2000 period. It is seen that the contribution of Total Factor Productivity (TFP) to growth was recorded at a low rate of 0.2 percent and investments were the main driving factor in this growth structure (Table 2.10 and Table 2.11). On the other hand, the structure has changed since 2002. The impact of the 2001 crisis and the sharp decoupling of post crisis period from the previous periods have become more evident when 2001-2011 and 2002-2011periods are compared. The 2001 crisis brought down the average growth rate by 1 percentage point and also caused serious TFP losses. While the TFP increased by 0.9 percent in the period including the crisis year, it displayed a high growth rate of 1.4 percent in the period excluding the crisis year. It is observed that the TFP increased by a higher rate in 2002-2011 period when the unfavorable impact of the global crisis in 2009 on the Turkish economy was excluded. Within the sources of growth framework, it is seen that developments after 2000 have been in favor of capital stock but against the TFP. Evaluating employment by periods, it is observed that employment has displayed a more stable pattern in terms of contribution to growth. In 2002-2011 period, employment increased by 2.1 percent and its contribution to the growth was realized as 23.7 percent.

Table 2.10: Increases in Production Factors

(Percent)

Dönem	GDP Growth	Capital Stock Growth	Capital Stock Growth *	Employment Growth	TFP Growth
1985-2000	4.3	7.6	7.5	1.7	0.2
2001-2011	4.3	5.3	5.5	1.9	0.9
2002-2011	5.3	5.6	6.5	2.1	1.4
1985-2011	4.3	6.7	6.7	1.8	0.5
2013-2015	4.7	6.0	6.2	2.0	0.9

Source: Calculations of Ministry of Development
* Capital stock increase corrected by capacity utilization rate.

Table 2.11: Contribution to Growth by Factors of Production

(Percent)

Period	Capital Stock	Employment	TFP
1985-2000	71.3	23.0	5.7
2001-2011	53.4	26.4	20.2
2002-2011	50.4	23.7	25.9
1985-2011	64.0	24.4	11.6
2013-2015	54.8	25.3	19.9

Source: Calculations of Ministry of Development

Following the crisis in 2009, Turkish economy has recorded high growth rates of 9.2 per cent and 8.5 per cent in 2010 and 2011, respectively. In 2011, TFP has recorded a low growth rate of 0.2 percent and employment has displayed a high growth rate of 6.7 percent. Due to the high increase in employment, the contribution of employment to growth was realized as 46.4 percent in 2011. In the same year, capital stock and TFP contributed to growth by 51.7 percent and 1.9 percent, respectively.

With the contribution of macro-prudential measures to mitigate domestic demand and vulnerability and the developments in global economy, the slowdown started in second half of 2011 has continued in 2012, as well. Depending on the slowdown in the economy and other developments, the growth forecast of 2012 was revised downward to 3.2 percent. It is foreseen that in 2012 TFP will contribute negatively to the growth and the main contributors to growth will be capital stock and employment. In this regard, capital stock corrected by capacity utilization rate is expected to increase by 4.9 percent and employment, by displaying a better performance compared to the growth, is foreseen to increase by 2.6 percent with the positive developments in labor markets.

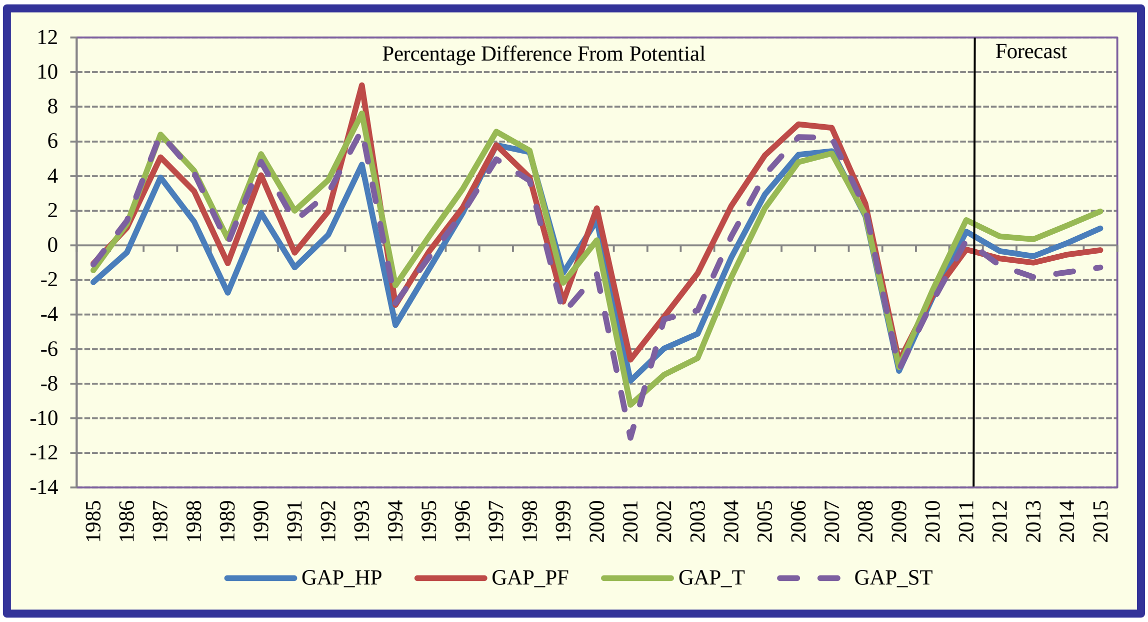
In PEP (2013-2015) period, Turkish economy is expected to grow by 4.7 percent annually on average despite the ongoing problems in the global economy. In this period, it is foreseen that the capital stock will increase by 6 percent annually on average and the employment will increase by 2 percent with the ongoing active labor market policies. In the Programme period, TFP is forecasted to increase by 0.9 percent which is the average growth rate of 2001-2011 period. With this growth rate of TFP, a more balanced pattern is expected to realize in PEP period in terms of contribution to growth. Considering the aforementioned growth rates of production factors, the capital stock, employment and TFP are expected to contribute to the growth by 54.8 percent, 25.3 percent and 19.9 percent, respectively.

2.2.1.5. Potential Output

The output gap estimations based on alternative methods point out that starting from 2004 the output level was above its potential level and there were overheating signals in the economy. This situation continued until 2009 and with the negative impact of the global crisis on Turkish economy, GDP contracted by 4.8 percent. All output gap estimations indicate that negative output gap as a percentage difference from the potential output was around 7 percent in 2009.

The rapid recovery in 2010 and 2011 has led to the narrowing of negative output gap. All alternative methods indicate that the output level has been below its potential in 2010 and around the potential level in 2011. With the policies to rebalance domestic and external demand, Turkish economy has slowed down in 2012. Along with this slowdown, output level has retreated below its potential again.

Figure 2.12: Output Gap



GAP_HP : Output gap calculated by Hodrick-Prescott method.
GAP_PF : Output gap calculated by production function method.
GAP_T : Output gap calculated by linear method.
GAP_ST : Output gap calculated by split-time linear method.

In PEP (2013-2015) period, in context of macroeconomic forecasts, it is envisaged that output level will move around its potential and in 2015 there will be moderate overheating. In this regard, no inflationary pressure from the demand side is expected in the Programme period.

2.2.1.6. Labor Market

In the first three quarters of 2012, non-agricultural employment increased by 3.8 percent, while agricultural employment decreased by 1.1 percent compared to same period of previous year. Therefore, employment continued to increase but a slower pace compared to the same period of previous year and increased by 2.6 percent. In parallel to the rise in employment, unemployment rate decreased to 8.8 percent in the third quarter of 2012 by a decline of 0.4 percentage point. In this period, labor force participation rate decreased by 0.3 percentage point and was realized as 50.7 percent and contributed to decline in unemployment rate, as well.

With the effect of ongoing uncertainties and risks in global economy, Turkish economy is expected to slow down in 2012 and this expectation is taken into account in labor market projections. In this context, while non-agricultural employment is expected to increase by 3.7 percent in 2012, employment in agricultural sector is expected to decrease by 0.9 percent. Thus, total employment is forecasted to increase by 2.6 percent (Table 2.12). In 2013-2015 period, non-agricultural employment is expected to increase by 1.6 million people in line with the economic growth and the share of non-agricultural employment in total employment is expected to reach 77 percent at the end of the period. In this period, agricultural employment is foreseen to decrease 0.2 percent annually on average. Considering these forecasts regarding agricultural and non-agricultural employment, total employment is estimated to increase by approximately 1.5 million people during the Programme period.

Seasonally adjusted labor force participation rate, has followed a flat path in the first eight months of 2012. In this context, labor force participation rate is expected to remain at its current levels and realize as 49.6 percent in 2012. It is forecasted that in 2013 labor force participation rate will remain constant around its 2012 level and with moderate increases will reach 49.7 percent and 49.8 percent in 2014 and 2015 respectively.

Table 2.12: Developments in the Labor Market

(15+ Age)

	Realization		Forecast			
	2010	2011	2012	2013	2014	2015
Working Age Population (Thousand Person)	52,541	53,593	54,724	55,737	56,739	57,724
Labor Force Participation Rate (Percent)	48.8	49.9	49.6	49.6	49.7	49.8
Labor Force (Thousand Person)	25,641	26,725	27,161	27,673	28,199	28,735
Employment	22,594	24,110	24,728	25,223	25,728	26,243
Agriculture	5,683	6,143	6,090	6,075	6,060	6,045
Non-Agriculture	16,911	17,967	18,639	19,149	19,669	20,199
Unemployed	3,046	2,615	2,433	2,450	2,471	2,491
Employment Increase (Percent)	6.2	6.7	2.6	2.0	2.0	2.0
Agriculture	8.5	8.1	-0.9	-0.2	-0.2	-0.2
Non-Agriculture	5.4	6.2	3.7	2.7	2.7	2.7
Employment Rate (Percent)	43.0	45.0	45.2	45.3	45.3	45.5
Unemployment Rate (Percent)	11.9	9.8	9.0	8.9	8.8	8.7

Source: Realization TURKSTAT, forecast Ministry of Development

Within the context of these expectations, unemployment rate is forecasted to decline to 9 percent in 2012. It is predicted that during the Programme period labor force participation rate will increase to a limited extent whereas unemployment rate will decrease slightly. Hence, unemployment rate is expected to be 8.9 percent in 2013 and to decrease to 8.7 percent by the end of the period.

2.2.2. Inflation, Monetary and Exchange Rate Policies

The Central Bank will continue to implement inflation targeting regime in 2013, consistent with its primary objective of price stability. The ultimate objective is to decrease the inflation rate to levels consistent with the Maastricht criteria. The Central Bank envisions a target path for inflation that entails a gradual progress to price stability, considering the structural transformation in the Turkish economy, the convergence process to the developed economies, and the rigidities in price setting behavior remaining from high inflation environment. In this context, the end-year inflation targets for 2013 and 2014 are set to 5 percent. The end-year inflation target for 2015 will be announced at the policy document “Monetary and Exchange Rate Policy for 2013” which will be published in December 2012.

During the inflation targeting practice, reserve requirements and overnight interest rate corridor in addition to the key policy instrument, i.e. one week repo rate, have been used as effective monetary policy tools since the last quarter of 2010. The Central Bank, when deemed necessary, would allow the market interest rate to divert from the policy rate and to be determined within the interest rate corridor at a level that the Central Bank accepts to be in line with the economic conditions. In addition, the reserve option mechanism has been used effectively since September 2011 as a complementary tool to interest rate corridor in terms of smoothing the volatility in domestic markets caused by the capital flows.

The floating exchange rate regime will be sustained in 2013. Under the current exchange rate regime, the foreign exchange rate is not used as a policy tool and the Central Bank does not have a nominal or real exchange rate target. In 2011, the Central Bank bought 6.5 billion dollars from the market via foreign exchange buying auctions and provided the market with 11.2 billion dollars liquidity via foreign exchange selling auctions. Upon the assessment that it would be appropriate to suspend the foreign exchange buying auctions in the days in which the implementation and reflections of the decisions taken European Union Leaders' Summit that was held in July 2011 would be closely monitored, foreign exchange buying auctions were halted on 25 July 2011. In this context, the Central Bank did not hold foreign exchange buying auctions in 2012 but provided the market with 1.45 billion dollars liquidity via foreign exchange selling auctions[6]. When unhealthy price formations are observed due to the possible loss of depth in foreign exchange market, the Central Bank may intervene directly compatible with the spirit of floating exchange rate regime. In this context, the Central Bank provided liquidity to the market by an amount of 2.4 billion dollars in 2011 and 1 billion dollars in 2012 via direct foreign exchange intervention. On the other hand, in order to enhance the mobility of foreign exchange liquidity in the Interbank Foreign Exchange Market, the Central Bank resumed its activities as an intermediary in the foreign exchange deposit markets in Foreign Exchange and Banknotes Markets as of 10 November 2011, until the elevated uncertainties in the international markets disappear.

The financial-stability-oriented decisions of the Central Bank since November 2010 were mainly driven by targets of slowing down the excessively rapid growth of the private sector's foreign liabilities and improving the quality of these liabilities. The Central Bank places utmost importance on the surveillance of the expected decline in the current account deficit and the observed improvement in the quality of its financing. In this framework, it is crucial that credit growth rates remain at reasonable and sustainable levels. In this regard reserve requirements, reserve option mechanism and effective liquidity management through interest rate corridor will be the key policy instruments to contribute to financial stability in the forthcoming period.

2.2.3. Balance of Payments

2.2.3.1. Current Account

Following the high growth performance of Turkish economy in the post-crisis period, domestic demand and imports increased rapidly, while external demand growth remained relatively sluggish. Thereby, foreign trade deficit and current account deficit reached 89.1 billion dollars and 77 billion dollars in 2011 respectively. In MTP (2013-2015), as a result of macro-prudential measures taken especially to slow down credit growth and slow down domestic demand, foreign trade deficit and current account deficit, which tend to decrease after 2011, are expected to fall to 73.4 billion dollars and 58.7 billion dollars in 2012 respectively. The latest figures indicate that current account balance will improve more than expected.

Economic growth in Turkey's trading partners is expected to be relatively higher compared to 2011 and 2012. With the impact of the policies to increase exports as well, exports in nominal terms are projected to reach 187.1 billion dollars in 2015 with an annual average growth rate of 8 percent in PEP (2013-2015) period. Real exports of goods are expected to show a modest growth of 2.8 percent in 2013 after a high increase of 15 percent in 2012. This growth is forecasted to accelerate to 6.9 percent and 7.3 percent in 2014 and 2015, respectively. Non-monetary gold exports and imports, which had high growth rates in 2012, are expected to turn back to its previous years.

[6] As of November 14, 2012.

Imports, which grew rapidly in 2011 parallel to the strong economic performance, are expected to contract by 0.4 percent in 2012 in nominal terms with the impact of measures taken. The high rates of increases realized in imports during the strong economic growth periods will be replaced by mild increases in the Programme period thanks to the policy measures considering the balance between domestic and external demand. In this regard, imports are envisaged to reach 291.2 billion dollars in 2015 with an annual average increase of 6.7 percent. Thus, real import growth is forecasted as 5.4 percent annually on average in the same period.

Energy cost will continue to constitute a significant part of the current account deficit of Turkey in the medium term. Energy and oil prices are expected to exhibit a flat path in the forthcoming period due to the slow increase in global economic activity. Thus, import increases resulting from energy prices are projected to remain low compared to previous periods. In this context, energy imports (chapter 27th), which is expected to be 59.1 billion dollars in 2012, will reach 65.4 billion dollars at the end of PEP period.

Increase in the number of tourists visiting Turkey accelerated in 2011 but slowed down in 2012. This tendency is expected to turn back to its previous period average and thus, the tourism revenues are forecasted to reach 28.4 billion dollars in 2015 with a steady increase throughout the period. Services balance is expected to rise to 19.9 billion dollars at the end of the 2012 and 25.5 billion dollars in 2015 due to increase in tourism revenues which is the largest item of the services balance.

In 2013-2015 period, with the contributions of strengthening fiscal discipline and policies aiming to increase domestic savings and to decrease the high import dependency of production, the current account deficit to GDP ratio is projected to recede gradually towards sustainable levels. In this context, current account deficit to GDP ratio is expected to be 7.1 percent, 6.9 percent and 6.5 percent in 2013, 2014 and 2015, respectively.

2.2.3.2. Capital and Financial Account

As a result of macro-prudential measures, economic activity has started to slow down since last quarter of 2011. This situation has mitigated dependence on foreign finance which has increased significantly in recent years. Besides, capital inflows which have decreased in the first half of 2012 due to financial turmoil in Euro Area, have accelerated again in the second quarter as a consequence of new measures taken by developed country central banks to alleviate macro financial risks. Assuming the recent improvement in risk perceptions are sustained and underpinned by deeper institutional reforms in the Euro Area, inflows of private capital to emerging market economies are expected to stay firm during the rest of this year[7]. In this framework, financial account balance excluding reserves is expected to reach 73.1 billion dollars in 2012. Reserve assets are projected to increase by 17.5 billion dollars throughout the year with the help of reserve option mechanism implemented by the central bank to support financial stability.

In the forthcoming period, two opposing factors are foreseen to affect capital flows to emerging market economies. More monetary stimulus by developed country central banks against a weaker global economic outlook due to uncertainties, reflect balance of two opposing factors on capital flows[8]. Capital inflows are expected to continue in the following years with macroeconomic framework of the Turkish economy strengthened by macro prudential measures as well as measures taken towards improving business environment. In the context of Medium Term Programme (2013-2015) projecting a decline in dependence on foreign savings, capital inflows to Turkish economy are expected to realize at 60.8 billion dollars, 63.6 billion dollars and 64.8 billion dollars in 2013, 2014 and 2015, respectively. Furthermore, credit note of Turkey which was raised to investment grade level by a rating agency in November of 2012 indicates that conditions will be more supportive in terms of quality and availability of finance in the forthcoming period.

Economic slowdown and lower profitability of firms in the Euro Area caused direct investments to emerging market economies to decelerate in first three quarters of 2012 compared to

[7] IIF, Capital Flows to Emerging Market Economies, October 2012
[8] IIF, Emerging Europe: Weathering The Storm, November 2012

the same period of the previous year[8]. However, direct investments to emerging market economies are expected to rise in following years in parallel to the recovery in global economic growth. Along with macroeconomic stability, implementation of the strategy for fighting against informality brought by the Turkish Commercial Code and new stimulus package are expected to support direct investment inflows. In this framework, direct investments which are expected to realize as 9.3 billion dollars in 2012 and reach 15.6 billion dollars in 2015 implying an acceleration through the Programme period.

Table 2.13: Balance of Payments Forecasts

(Billion Dollars)

	Realization			**Forecast**			
	2009	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
Current Account	**-13.4**	**-46.6**	**-77.0**	**-58.7**	**-60.7**	**-63.6**	**-64.7**
Balance on Goods	-24.9	-56.4	-89.1	-73.4	-77.4	-81.0	-83.8
Total Exports	109.6	120.9	143.4	158.5	167.5	182.4	197.8
Exports (fob)	102.1	113.9	134.9	149.5	158.0	172.3	187.1
Total Imports	-134.5	-177.3	-232.5	-231.9	-244.9	-263.4	-281.6
Imports (cif)	-140.9	-185.5	-240.8	-239.5	-253.0	-272.2	-291.2
Balance on Services	17.3	15.5	18.0	19.9	22.6	23.7	25.5
Credit	33.9	34.7	38.6	40.3	44.0	46.7	49.7
Tourism Revenues	21.3	20.8	23.0	23.5	25.4	27.0	28.4
Debit	-16.6	-19.3	-20.6	-20.5	-21.5	-23.0	-24.3
Balance on Income	-8.2	-7.1	-7.6	-6.8	-7.7	-8.1	-8.4
Current Transfers	2.4	1.4	1.7	1.6	1.8	1.9	2.0
Workers' Remittances	1.0	0.9	1.0	1.0	1.0	1.1	1.1
Capital and Financial Account	**9.2**	**43.9**	**65.6**	**55.5**	**60.7**	**63.6**	**64.7**
Capital Account	-0.1	-0.1	0.0	-0.1	-0.1	-0.1	-0.1
Financial Account (Excluding Reserves)	9.4	56.8	63.8	73.1	60.8	63.6	64.8
Direct Investment	6.9	7.6	13.6	9.3	13.3	14.4	15.6
Direct Investment in Turkey	8.4	9.0	16.1	12.6	15.0	16.1	17.3
Direct Investment Abroad	-1.6	-1.5	-2.5	-3.3	-1.7	-1.7	-1.7
Portfolio Investment	0.2	16.1	22.0	25.2	12.4	11.5	12.2
Assets	-2.7	-3.5	2.7	2.9	-1.0	-0.7	-0.6
Liabilities	2.9	19.6	19.3	22.3	13.4	12.2	12.7
Other Investment	2.3	33.1	28.2	38.6	35.1	37.8	37.1
Assets	11.0	7.0	11.1	8.2	-2.8	-0.3	-4.0
Liabilities	-8.7	26.1	17.1	30.4	37.9	38.0	41.1
Reserve Assets	-0.1	-12.8	1.8	-17.5	0.0	0.0	0.0
Net Errors and Omissions	**4.1**	**2.7**	**11.4**	**3.2**	**0.0**	**0.0**	**0.0**

Source: Realization CBRT, forecast Ministry of Development.

Foreign direct investments, which have been mostly in the form of mergers and acquisitions and generally focused on financial intermediation services and retail sectors, are expected to be directed to new investments with the new stimulus package. In this regard, the share of manufacturing sector in direct investments is foreseen to increase. Therefore, foreign direct investments are expected to contribute more to employment and technology transfer.

In January-October period of 2012, major part of portfolio investments was observed to focus on government domestic borrowing instruments issued by Treasury. This situation reflects the improvement in country risk. In the same period, purchases of equity securities by international investors were fairly limited. In this framework, portfolio investments are expected to realize at 25.2 billion dollars throughout this year. In the following period, capital flows to emerging market economies are expected to concentrate on direct investments and other investments by acceleration of global economic recovery. In light of this information, portfolio investments are projected to realize at about 12 billion dollars annually in the Programme period.

In the first three quarter of 2012, increase in deposits of non-resident banks and persons were influential in capital inflow recorded in other investment item. Besides, as opposed to 2011, banks were net re-payers of long term loans, thus their debt roll-over ratio decreased. This situation is not attributed to difficulties in finding foreign finance but to the slowdown in the domestic credit growth. As opposed to these developments, other investment is again expected to be the main item in current account financing in 2012 and the Programme period, as well. In this framework, other investment is expected to be 36.6 billion dollars annually on average in the Programme period.

2.2.4. Main Risks in Projections

Uncertainties in the global economic outlook increased in the first half of 2012, year-end expectations have deteriorated in the second half. Considering that Turkish economy has rapidly increased integration with the world economy in recent years, slower than expected global economic recovery is seen as the most significant risk factor for the PEP (2013-2015) period. In this context, European Union’s economic outlook, which is also effective on the global economic outlook, has the power to influence overall economic performance in Turkey significantly due to the high volume of trade and capital flows in between. Although this effect has been weakened by the successfully implemented foreign trade market diversification efforts in recent years, taking into account the fact that exports to the European Union still constituted 46.2 percent of total exports in 2011, it is clear that the problems in European economies would still adversely affect Turkish economy. Possible adverse developments in world economy or in European economy would adversely affect export performance and thereby lead to an increase in foreign trade deficit and current account deficit, would adversely affect growth performance, and also adversely affect public finances through decreases in tax revenues.

Being dependent on foreign sources of energy, macroeconomic performance of Turkey would be directly and significantly effected from developments in the global energy markets in the Programme period, as it was in the past. Therefore significant rises in energy and commodity prices, which are generally expected to remain flat in general in PEP (2013-2015) period, would make inflationary cost effects, and would also increase current account deficit.

As Turkey has large amount of construction activities in and high trade volume with Middle East and North Africa countries, it has been affected from the recent political turmoil in these areas. Although stability has been quickly established in most of these countries, problems still persist in some like Syria and also risk of new turmoil in some other countries still exists. Turkish economy, that has once again started to increase trade volume with these countries with attainment of stability, would be adversely affected by new turmoil in these regions.

Besides the risks that may adversely affect Turkish economy, there are some positive risks which may result in higher than expected performance in the Programme period. Faster than expected recovery in the European economies during the Programme period, would lead to higher than forecasted export and growth performance.

With its sound public finances and high growth performance after the global crisis, Turkish economy has constituted a global success story. In this process, confidence in Turkish economy increased, risk perception decreased and the country's steadily rising credit rating has been increased to investment level by a rating agency for the first time after a long period. Country credit grade is expected to increase further in the forthcoming period with the continuance of the policy framework built with MTP (2013-2015) and PEP (2013-2015). Rise in the country credit grade, an indicator of the overall strength of the economy, would have a positive effect on growth through lower cost of borrowing in the economy and higher capital inflow to the economy, as it would decrease the country credit note. All these said, policy attention would be required to avoid financial destabilizing effects of increasing capital inflows.

3. PUBLIC FINANCE

Fiscal policy will be carried out, considering revenue, expenditure and debt amounts prescribed in the Medium Term Programme, with an approach that will strengthen macroeconomic stability, promote private sector-led growth process and help fight against current account deficit and inflation. Public expenditure policy will be based on effective and efficient use of allowances by public institutions in line with the policies and priorities and in accordance with the multi-year budgeting, allocated amounts shall not exceed. Public revenue policy will be implemented through formation of an effective, simple and fair tax system to support sustainable development, to increase domestic savings, to promote employment and investments and to contribute mitigation of informality and regional development disparities. Public financial statistics, being an important element of transparency in public financial management, will be published in compliance with international standards. Works will be conducted to establish public financial management information system.

General government and central government budget aggregates provided in Pre-accession Economic Programme (2013-2015) are based on Medium Term Programme (2013-2015) and 2013 Annual Program.

3.1. General Government Balance and Public Debt

The general government balance, generated by the Ministry of Development, consists of institutions within the scope of central government, local authorities, social security institutions and general health insurance funds, revolving funds and Unemployment Insurance Fund. When obtaining total general government expenditure and revenue, in line with the international standards SEEs are excluded gross values of transactions is considered and no off-setting between revenue and expenditure items was made.

Within the calculation process of general government expenditures and revenues of the sub-sectors; a public revenue items is accounted as income only in the accounts of unit that obtain the revenue, similarly it is accounted as expenditure in only the final spending units' account. Thus, double counting problem in transfer transactions between sub-sectors is avoided. As a result of this process, the balance figures of sub-units are changing, but it does not change the total general government balance. Total general government expenditure and revenue figures are obtained through consolidation of sub-units' expenditure and revenue amounts which are calculated by using above methodology.

Box 3.1: The Differences Between General Government Balances Prepared in the Context of PEP and Fiscal Notification

Through various adjustments made in the scope of the debt stock and accounting records, general government deficit is being harmonized with the budget deficit and debt definitions of the European Union, and every year these are sent to the relevant units of the European Union in the form of fiscal notification tables.
While preparing fiscal notification 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 budget deficit are added to the budget; and accounts which do not comply with the definition of revenue (privatization, revaluation differences, revenue of issuing coins, etc.) or expenditure (risk account, etc.) but which are included in the budget are eliminated from the budget.
- Revenues and expenditures, which are reported in the budget on a cash basis, are changed to the required values on an accrual basis. The differences between the accrued and the collected amounts are corrected.
- Interest expenditures on the public debt stock are calculated on an accrual basis and allocated to the year to which they belong.

As a result of these adjustments, general government published by Ministry of Development within the context of Pre-Accession Economic Programme and general government prepared for fiscal notification differs from each other.

While preparing general government figures, within the framework of the consolidation approach adopted;

- The shares transferred to local governments and funds from the general budget tax revenues and other transfers are cleared from the central government budget base and displayed in the balances of local governments or funds to which they are related,
- The current transfers to the social security and general health insurance system from the central government budget are cleared from the budget expenditure base and social security and general health insurance system revenue base,
- The amounts transferred to the central government budget from revolving funds, extra budgetary funds and Unemployment Insurance Fund are cleared from the central government budget revenue base and expenditure base of relevant units,
- Fiscal relations among the institutional units included in the scope of general government except for the central government budget are structured in a way to prevent double counting.

3.1.1. Fiscal Policy Strategy and Medium Term Objectives

In medium term, without compromising fiscal discipline, the fiscal policy will be implemented in parallel with the aims of maintaining macroeconomic stability and decreasing current account deficit. Besides, works on strengthening the structural side of the public financial management system will be continued by means of continuing the regulations which will increase transparency, accountability and effectiveness in the medium term.

Within this scope, main policies to be implemented in the period of 2013-2015 are as follows:

3.1.1.1. Revenue Policy

- Stability and predictability in implementation and regulation of tax policies will be essential.
- Implementations of tax policies, aimed at supporting R&D activities and creating a production structure which increases international competitiveness of the economy, will be continued.
- Works regarding the reviewing of the basic tax laws in accordance with necessities will be continued.
- Tax policy will be used effectively in case of need in fighting with problems, specifically with insufficient domestic savings and current account deficit, which threaten the sustainability of growth.
- Calculation of the tax expenditures emerged due to the exceptions, exemptions and deductions will be widened and maintained to be shared by the public opinion.
- Works on increasing tax compliance and broadening the tax-base will be continued.
- In the designation and implementation of tax policies, priorities concerning climate change and energy use economizing will also be taken into account.
- In order to use public sector owned immovables effectively, efficiently and economically, all the alternatives including sale will be taken into consideration.

3.1.1.2. Expenditure Policy

- Policies aimed at improving the quality of human capital and life quality of society will continue to be pursued by giving priority to education, health and social expenditures.
- Strategic planning and performance-based budgeting, introduced in order to increase fiscal transparency and accountability and strengthen decision-making processes of

public administrations, will be extended and resource allocation process will be based on strategic plans and performance programs.

- Spending programs will be revised in order to increase productivity. For this purpose, an administrative mechanism will be established.
- In order to ensure efficiency in social aids, efforts to reach the real needy people will continue and works launched in 2010 to establish connection between social aids and employment will be accelerated.
- Transfers to social programs and agricultural sector will be examined to assess whether the intended benefits are obtained.
- Impact analysis capacity of public administrations will be strengthened.
- Effectiveness of the public procurement system will be increased.
- Medication and treatment expenditures will be rationalized to avoid unnecessary use of drugs and health service without compromising the quality.
- Auditing models taking into account previous behaviors of health service providers will be developed; software, hardware and education infrastructure will be strengthened in risk analysis and data mining fields.
- The deduction from the general budget tax revenues of the local administrations on account of the liabilities to the public sector will be made regularly and the ratio of deductions will be determined in a way that it will avoid new debt creation and help reducing the debt stock.

3.1.1.3. Public Borrowing Policy

- Debt management policy implementation based on strategic benchmarking will be continued.
- Borrowing will be mainly made in TL denominated and fixed rate instruments to the extent that market conditions allow. Liquidity risk will be reduced by extending the average maturity of debts and sufficient level of reserve assets.
- In order to ensure balanced distribution of debt service between terms and to increase the price efficiency in the secondary market, buy-back and switching auctions will be conducted.
- In order to obtain a healthy yield curve and providing liquidity in the secondary market, re-issuing instruments in decreasing maturity policy will be sustained.
- In order to expand the investor base of domestic government bonds, works on new borrowing instruments will be maintained.
- Primary dealership system will be continued.
- Information about borrowing such as financing programs, domestic borrowing strategies and tender announcements will continue to be announced on a regular basis.

3.1.1.4. Public Financial Management and Audit

- In order to ensure an effective external audit in the public, the implementation capacity of Court of Accounts will be strengthened.
- It will be ensured that internal control systems in public administrations are established in a healthy way and internal and external audit are conducted in coordination and effectively.
- Compliance of public administrations with the internal control and internal audit standards will be enhanced.

- Quantity and competency of human resources of public financial management will be enhanced to strengthen management responsibility in public administrations.
- The organizational capacity of internal audit units will be enhanced and their position in the organizational structure of public administrations will be strengthened.
- The Internal Audit Coordination Board, which functions as central harmonization unit in the area of internal audit, will be restructured.

3.1.2. Current Situation and Medium Term Perspective

3.1.2.1. Current Situation

3.1.2.1.1. Developments in the Central Government Budget Revenues and Expenditures

Following a strong performance in 2010, high economic growth continued in 2011 as well and this affected budgetary revenues positively. In 2011, central government total budget revenues was above the budget predictions by 17.8 billion TL and reached 22.9 percent of GDP. In addition, tax revenues and non-tax other revenues to GDP ratios were realized as 19.6 percent and 3.3 percent, respectively.

With the Law No. 6111 dated 13 February 2011 regarding restructuring of some overdue receivables of the state, important facilities were granted for the collection of accumulated receivables of the state. Within the context of this practice, the amount of collection was 13.3 billion TL in 2011. It is evaluated that the net contribution of the central government budget revenues of aforementioned development is around 5 billion TL.

In 2011, income tax and corporate tax collections were above the budget projections by an amount of 1.5 billion TL and 3.8 billion TL respectively, thus taxes on income, profits and capital gains was realized as 5.8 percent of GDP. Revenue collection due to the Law No. 6111 contributed to the increase in corporate income tax collection.

Due to the ongoing recovery in domestic economic activity and high increase in imports, indirect taxes collection was higher than the budget projections by 16.2 billion TL. Accordingly, Special Consumption Tax (SCT), domestic Value Added Tax (VAT) and VAT on imports collections was above the projections by 3 billion TL, 3.1 billion TL and 7.6 billion TL, respectively.

At the end of 2011, the total expenditures of central government budget was 24.2 percent of GDP, while primary expenditures and interest payments were 21 percent and 3.3 percent of GDP, respectively.

Total personnel expenditures, composed of personnel expenses, state premiums to social security institutions and reserve appropriations for personnel expenditures, realized above the budget appropriation by 140 million TL.

In 2011, expenditures on purchase of goods and services were above the initial appropriation by an amount of 2.7 billion TL. Besides the increase in bitumen bill of General Directorate of Highways, increase in green card expenditure and additional appropriation needs required for projects carried out by line ministries were effective on the mentioned development.

In 2011, current transfers were below the initial appropriation 5.3 billion TL. As a result of the increase in social security premiums collected within the context of payment facilities provided for some of the public receivables by Law No. 6111, health, pension and social assistance expenditures were below the initial appropriation by 9.6 billion TL and this was the most effective factor on the mentioned development. Besides, realization of some transfers such as shares allocated to local governments and funds from the tax revenues, scholarships, agricultural subsidies, KOSGEB’s SMEs supports and, transfers of Social Services and Child Protection Agency (SHÇEK) were above the related budget appropriations.

In 2011, sum of capital expenditures and capital transfers were above the budget appropriations by 11.6 billion TL. In particular, expenditures made in the scope of projects and activities in the field of transportation sector, local and rural development, was effective in this development.

Due to the decline in capital transfers to SOEs, nonuse of risk account and the fall in interest payments, interest and lending expenses resulted 6 billion TL lower than the initial appropriations of 2011 budget.

As a consequence of above mentioned developments, central government budget deficit was realized as 17.8 billion TL in 2011 corresponding to 1.4 percent of GDP, while the program defined primary balance had a surplus of 1.2 percent of GDP.

It is considered that high economic growth observed in 2010 and 2011 will decelerate to a moderate level in 2012. In 2012, the central government budget revenues to GDP ratio is expected to remain at 2011's level of 22.9 per cent. However, due to the spending pressures particularly from the personnel expenditures and the current transfers, budget expenditure is expected to be above the previous year's level and reach 25.3 percent of GDP.

In 2012, central government budget revenues to GDP ratio is expected to be 22.9 percent. In this respect, as a ratio to GDP, tax revenues and non-tax revenues are expected to be 19.5 percent and 3.5 percent, respectively. In spite of transfer of 5.7 billion TL dividend income of the CBTR to the Treasury, no tax revenues as a ratio to GDP is expected to be 0.2 percentage point lower than budget target due to the decrease in privatization revenues.

The slowdown in economic growth due to the measures to reduce the current account deficit and failure of the some State Economic Enterprises to fulfill their tax obligations, SCT and VAT revenues increased to a limited extent in 2012.

Table 3.1: Central Government Budget Balance

(Share in GDP, Percent)

	2010	2011	2012*	2013**
Expenditures	**26.8**	**24.2**	**25.3**	**25.7**
Primary Expenditures	22.4	21.0	21.9	22.3
Personnel Expenditures	5.7	5.6	6.1	6.2
Social Sec. Ins. Government Premium Expenditures	1.0	1.0	1.0	1.1
Goods and Services Purchase Expenditures	2.7	2.5	2.3	2.1
Current Transfers	9.3	8.5	9.0	9.6
Capital Expenditures	2.4	2.4	2.4	2.1
Capital Transfers	0.6	0.5	0.4	0.3
Lending	0.8	0.4	0.7	0.7
Reserve Appropriation	0.0	0.0	0.0	0.2
Interest Payments	4.4	3.3	3.4	3.4
Revenues	**23.1**	**22.9**	**22.9**	**23.6**
Tax Revenues	19.2	19.6	19.5	20.3
Non-Tax Revenues	3.1	2.9	3.1	2.5
Capital Revenues	0.3	0.2	0.1	0.6
Grants, Aids and Special Revenues	0.5	0.2	0.2	0.2
Primary Surplus	0.7	1.9	1.1	1.2
Programme Defined Primary Surplus	-0.5	1.2	0.2	0.5
Borrowing Requirement	**3.6**	**1.4**	**2.3**	**2.2**

Source: Ministry of Development, Ministry of Finance
* Realization Forecast
** Programme

In 2012, income tax and corporate tax collections are expected to be higher than the budget targets by 2.9 billion TL and 1.4 billion TL, respectively. The high rate of increase at the registered employment and wages was effective in the increase of income tax collection.

With the Decision of the Council of Ministers No. 2012/3735 and dated 22 September 2012, lump-sum amounts and rates of excise tax included Law No. 4760 and duties levied on title transactions were increased. In this context, lump-sum amounts of excise tax on alcoholic beverages were increased by 17 percent and lump-sum SCT amount for petroleum products was increased by 0.3 TL. SCT rates were increased by 3 percentage points from 37 percent to 40 percent for passenger cars that have an engine size not exceeding 1600 cm^3. Besides, duties levied on title transactions, which was 16.5 per thousand, were raised to 20 per thousand. In 2012, the positive impact of these arrangements on budget revenues is expected to be around 2.3 billion TL.

In 2012, it is estimated that collection from SCT, which constitutes an important share of the central government tax revenues, will be higher than the budget target by 0.7 billion TL, as a consequence of abovementioned tax increases in September. In addition, SCT collections on alcoholic beverages and motor vehicles are expected to be above the budget targets by 0.3 billion TL and 1.6 billion TL , respectively.

In 2012, due to the slowdown in domestic economic activities below the expectations, domestic VAT collection is expected to be lower than the budget targets by 1.5 billion TL and with the impact of decline in the volume of imports and failure of the some State Economic Enterprises to fulfill their tax obligations, collection of VAT on imports is envisaged to be lower than the budget target by 3.9 billion TL.

Uncertainties in the international markets have affected the privatization process negatively. In this context, privatization revenues which was targeted 10.5 billion TL, are expected to be 1.4 billion TL at the end of the year. Non-tax revenues excluding privatization revenues are envisaged to be higher than budget target by 7.3 billion TL with the contribution of the high amount of the dividend which is obtained from public banks.

Besides, the net effect of the restructuring on the central government budget revenues is estimated to be around 2 billion TL within the context of Law No. 6111.

In 2012, central government primary expenditures is expected to be above the initial budget appropriation by 13 billion TL and to realize at the level of 21.9 percent of GDP with an increase of 0.9 percentage point compared to the previous year. Interest payments to GDP ratio, which was 3.3 percent in 2011, is estimated to decrease by 0.1 percentage point with respect to initial appropriation and expected to be 3.4 percent. Thus, total expenditure of central government budget is estimated to be above the initial appropriation by 11.7 billion TL and to realize 25.3 percent of GDP.

In 2012 budget, 99.1 billion TL of appropriation has been allocated to personnel expenditures as total of personnel expenses, contributions to the state social security institutions and reserve appropriations of personnel expenditure. Due to the wage rises of 4 percent in January and 4 percent in July, additional increase of 2.68 percent given as inflation difference compensation, additional recruitments and other improvements on fiscal and social rights, personnel expenditures is estimated to be 102.1 billion TL and 7.1 percent of GDP at the end of 2012.

Expenditures on purchase of goods and services are expected to be above the initial appropriation by 4.5 billion TL and 2.3 percent of GDP at the end of 2012. In addition, the increase in bitumen bill of General Directorate of Highways, increase in defense and security spending and additional resource needs of public institutions have been effective on this development.

In 2012, current transfers, estimated to be below the initial appropriation by 1 billion TL and its ratio to GDP is estimated to be 9 percent. The collection of social security contributions have been positively affected by the increase in the minimum wage and the number of active insured over the predictions and health care, pensions and social assistance expenditures is expected to be below the initial appropriation in 2012. Shares allocated to local governments and funds are estimated to be higher than the initial appropriation due to the performance of the taxes such as income and corporation tax which are subject to the allocation. Agricultural subsidies as well as other current transfers are expected to be higher than the budget estimate.

Capital expenditures are projected to be 27.9 billion TL in 2012 central government budget. Capital expenditures are expected to increase by 5.8 billion TL and to be 33.7 billion TL at the end of the year and its GDP ratio is expected to remain at the previous year's level of 2.4 per cent. This development stemmed from additional investments in the field of education and transportation.

Capital transfers are estimated to be 1.3 billion TL higher than the initial appropriation in 2012 and estimated to be 0.4 percent of GDP as a result of the housing construction due to the earthquake in Van and additional needs of special province administrations and other administrations.

Lending expenditures are expected to be higher than the initial appropriation by 1 billion TL and to be 0.7 percent of GDP, due to the increase of aids to other countries.

In the light of the above mentioned developments, central government budget deficit which was programmed to be 21.1 billion TL and 1.5 percent of GDP for 2012 is expected to be 33.5 billion TL and 2.3 percent of GDP. In this context, the central government budget balance deterioration from the previous year is estimated to be 1 percentage point.

3.1.2.1.2. Developments Regarding General Government Revenues and Expenditures

General government balance, which improved substantially thanks to the tight fiscal policy implemented since the 2000s, recorded surplus in 2006 with the contribution of privatization revenues and one-off revenues. However, due to the decline in mentioned revenues and the increase in primary expenditures, general government balance ran deficit in 2007 and 2008. General government deficit to GDP ratio reached 5.5 percent in 2009 with the impact of stimulus packages introduced to mitigate the impact of the global crisis on economy.

Table 3.2: General Government Revenues and Expenditures - 1

(Share in GDP, Percent)

	2008	**2009**	**2010**	**2011**
Taxes	18.1	18.5	19.7	20.1
Direct	5.9	6.0	5.6	5.9
Indirect	11.7	11.8	13.4	13.5
Wealth	0.6	0.6	0.7	0.7
Non-Tax Revenues	1.9	2.0	1.8	1.8
Factor Incomes	5.6	6.2	5.5	5.0
Social Funds	6.5	7.4	8.1	9.2
Total	32.1	34.2	35.1	36.1
Privatization Revenues	0.9	0.5	0.4	0.3
Total Revenues	**32.9**	**34.6**	**35.5**	**36.4**
Current Expenditures	15.7	17.7	17.1	16.6
Investment Expenditures	3.4	3.3	3.4	3.3
Fixed Investment	3.4	3.3	3.4	3.3
Change in Stocks	0.0	0.0	0.0	0.0
Transfer Expenditures	15.5	19.1	18.0	16.8
Current Transfers	14.8	18.1	16.8	15.9
Capital Transfers	0.7	1.0	1.2	0.9
Stock Revaluation Fund	0.0	0.0	0.0	0.0
Total Expenditures	**34.6**	**40.1**	**38.5**	**36.8**
Borrowing Requirement	**1.6**	**5.5**	**3.0**	**0.4**
Borrowing Req. Exc. Privatization Revenues	**2.5**	**5.9**	**3.4**	**0.7**
Primary Expenditures	29.2	34.4	33.9	33.4
Primary Surplus	3.8	0.3	1.5	3.0
Program Defined Primary Surplus	1.5	-1.7	0.0	1.8

Source: Ministry of Development

High growth recorded in 2010 and 2011 affected public sector balances in a positive manner. Strong recovery and the increase in domestic demand and foreign trade contributed to tax and social security premium collection and the restructuring of some public receivables within the scope of regulation provided additional revenues. As a result the ratio of general government deficit to GDP decreased to 3 percent in 2010 and 0.4 percent in 2011.

3.1.2.1.3. Medium Term Perspective

In the calculation of the general government figures, main assumptions about revenues and expenditures for the period of 2013-2015 are as follows:

- Lump-sum taxes and fees will be updated by taking the general economic environment into account.
- Arrangements, which would lead to a significant amount of revenue loss, will be avoided.
- Tax policies will be implemented in a way to enhance financial quality.
- SEE prices will be determined in line with the programme targets.
- Pensions of the transferred SII and Bağ-Kur pensioners will be increased in January and July 2013 by 5.32 percent and 2.34 percent respectively in accordance with the inflation forecasts of the second half of the 2012. Also, a fair adjustment system in pensions will be implemented gradually in 2013.
- Salary and wage increases of public servants have been determined by collective bargaining as 3 percent and 3 percent for the first half and second half of 2013.
- Measures will be taken in order to rationalize medicine and treatment expenditures without compromising the quality of health services.
- Arrangements will be made to increase the effectiveness of social assistance.

In 2012, general government tax revenues to GDP ratio is expected to decrease by 0.1 percentage point compared to previous year. While there is an increase in direct taxes, indirect taxes decreased due to the slowdown in economic growth with the impact of measures taken to decrease current account deficit and the failure of some State Economic Enterprises to fulfill their tax obligations.

Additionally, ongoing uncertainties in international markets affected the privatization process adversely. In this respect, general government privatization revenues are expected to decrease by 0.2 percentage point compared to the previous year. On the other hand, general government revenues other than privatization and taxes are expected to be 17 percent as a ratio to GDP with an increase of 0.9 percentage point compared to the previous year due to the increase in social security premiums collected from public and private sector and the dividend transferred from the Central Bank.

General government expenditures excluding interest payments are expected to be 35.1 percent as a ratio to GDP with an increase of 1.7 percentage points in 2012 compared to the previous year as a result of the increase in current expenditures and current transfers. Moreover, the ratio of interest payments to GDP is expected to increase by 0.2 percentage point and to be 3.5 percent.

The ratio of borrowing requirement of local governments to GDP is expected to increase by 0.1 percentage point compared to the previous year. Additionally, borrowing requirement of social security and general health insurance to GDP ratio is expected to be 1.4 percent with an increase of 0.2 percentage point. The reasons behind this are the receipts stemming from the restructuring of some public receivables being lower than expected, the increase of transfers for the premiums of those who do not have the ability to pay and higher costs of treatment.

As a result of the above mentioned developments, general government deficit to GDP ratio is expected to increase by 1.2 percentage points and to be 1.6 percent in 2012. General government surplus excluding interest payments and privatization revenues to GDP ratio is expected to decrease by 0.9 percentage point compared to the previous year and to be 1.8 percent.

In 2013, general government tax revenues to GDP ratio is estimated to be 20.7 percent with an increase of 0.8 percentage point as a result of the increase in indirect taxes. As a ratio to GDP, direct taxes, indirect taxes and wealth taxes are estimated to be 5.9 percent, 14.2 percent and 0.7 percent respectively.

The sum of general government non-tax revenues and factor revenues as a ratio to GDP, which is expected to be 7.5 percent in 2012, is estimated to decrease to 6.9 percent in 2013. The lower amount of dividend transfer from Central Bank and the abolishment of university tuition fees are the reasons behind this decrease. In 2013, due to increase in the number of social insurant and premium payments for those who do not have the ability to pay, social funds to GDP ratio is expected to be 9.7 percent with an increase of 0.3 percentage point compared to the previous year.

Table 3.3: General Government Revenues and Expenditures - 2

(Share in GDP, Percent)

	2012	2013	2014	2015
Taxes	19.9	20.7	20.5	20.2
Direct	6.0	5.9	5.8	5.8
Indirect	13.3	14.2	14.0	13.7
Wealth	0.7	0.7	0.7	0.7
Non-Tax Revenues	1.9	1.6	1.6	1.7
Factor Incomes	5.6	5.3	4.9	4.7
Social Funds	9.4	9.7	9.6	9.5
Total	36.9	37.3	36.6	36.1
Privatization Revenues	0.1	0.3	0.5	0.4
Sale of Degraded Forest Land	0.0	0.3	0.1	0.1
Total Revenues	**37.0**	**37.9**	**37.2**	**36.6**
Current Expenditures	17.5	17.7	17.3	16.8
Investment Expenditures	3.5	3.4	3.5	3.5
Fixed Investment	3.5	3.4	3.5	3.4
Change in Stocks	0.0	0.0	0.0	0.0
Transfer Expenditures	17.6	18.3	17.6	17.2
Current Transfers	16.8	17.5	17.0	16.6
Capital Transfers	0.8	0.8	0.6	0.6
Stock Revaluation Fund	0.0	0.0	0.0	0.0
Total Expenditures	**38.6**	**39.4**	**38.4**	**37.5**
Borrowing Requirement	**1.6**	**1.5**	**1.2**	**0.9**
Borrowing Req. Exc. Privatization Revenues	**1.7**	**2.1**	**1.8**	**1.4**
Primary Expenditures	35.1	35.9	35.1	34.4
Primary Surplus	1.9	2.0	2.0	2.1
Program Defined Primary Surplus	0.7	0.8	0.9	1.1

Source: Ministry of Development

Considered together with the revenues expected from the sale of degraded forest land, general government privatization revenues are expected to increase by 0.5 percentage point compared to previous year and to be 0.6 percent as a ratio to GDP in 2013. In this regard, general government revenues excluding privatization revenues and the revenues expected from the sale of degraded forest land is estimated to increase by 0.4 percentage point and to be 37.3 percent of GDP while general government total revenues are expected to reach 37.9 percent of GDP by increasing 0.9 percentage point in 2013.

The ratio of general government current expenditures to GDP is expected to increase by 0.2 percentage point compared to the previous year and to be 17.7 percent in 2013 with the impact of the increase in local government expenditures. Due to the increase in social security expenditures, general government transfers to GDP ratio are estimated to be 18.3 percent with an increase of 0.7 percentage point. In this period, capital expenditures to GDP ratio is projected to be 3.4 percent.

General government primary expenditures to GDP ratio, which is estimated to be 35.1 percent in 2012, is projected to be 35.9 percent in 2013. Additionally, the ratio of general government interest payments to GDP is expected to maintain the same level as 2012 and to be 3.5 percent. As a result, general government total expenditures to GDP ratio is projected to increase 39.4 percent.

As a result of the developments expressed above, general government deficit to GDP ratio is expected to be 1.5 percent and general government primary surplus to GDP ratio is estimated to be 2 percent in 2013. Moreover, general government balance excluding interest payments and privatization revenues is expected to run a surplus of 1.7 percent as a ratio to GDP at the end of 2015.

3.1.3. Structural and Cyclical General Government Balance

Structural general government balance was obtained with consolidation of the balances of central government budget, local administrations, social security institutions, general health-care insurance, extra-budgetary funds, revolving funds and unemployment insurance fund.

Unlike PEP 2011, while determining structural revenues, the sensitivity of social funds (social contributions) to cyclical developments is calculated by taking the employment and wage increases into consideration instead of the relationship between GDP and potential GDP (Y^P/Y). Furthermore, some items of unemployment insurance and social security institutions balance, which are considered as sensitive to conjuncture, are accepted as insensitive to economic developments (Box 3.2).

Unlike general government balance analyzed in public finance chapter, actual general government balance does not cover the privatization revenues and one-off revenues. Revenues and expenditures of the actual general government balance also cover temporary effects resulted from economic fluctuations. Structural general government balance reflects the revenue and expenditure levels that would be under the assumption that economy was operating at potential level.

Tablo 3.4: General Government Balance Analysis [1]

	Output Gap (Y/Yp) [2]	General Government Balance / GDP		Primary General Government Balance / GDP		Cyclical Balance / GDP
		Actual Balance	Structural Balance [3]	Actual Balance	Structural Balance [3]	
1999	-1.59	-9.99	-9.74	1.25	1.31	-0.09
2000	1.43	-9.87	-10.28	3.17	2.95	0.26
2001	-7.84	-12.63	-9.82	4.91	6.34	-1.97
2002	-5.97	-11.78	-9.36	3.49	4.99	-1.82
2003	-5.12	-8.37	-6.78	4.93	5.84	-1.22
2004	-0.70	-4.44	-4.41	5.89	5.86	0.00
2005	2.93	-0.77	-1.58	6.40	5.80	0.77
2006	5.24	-0.90	-2.09	5.24	4.37	1.08
2007	5.44	-1.90	-3.24	3.97	2.94	1.18
2008	1.69	-3.21	-3.52	2.21	1.99	0.25
2009	-7.26	-6.15	-4.00	-0.42	1.31	-1.83
2010	-3.02	-3.37	-2.61	1.15	1.78	-0.68
2011	0.80	-1.47	-2.07	1.89	1.32	0.58
2012	-0.33	-2.43	-2.46	1.09	1.05	0.04
2013	-0.63	-2.27	-2.12	1.21	1.33	-0.13
2014	0.12	-1.81	-1.84	1.43	1.41	0.02
2015	0.98	-1.40	-1.61	1.65	1.48	0.19

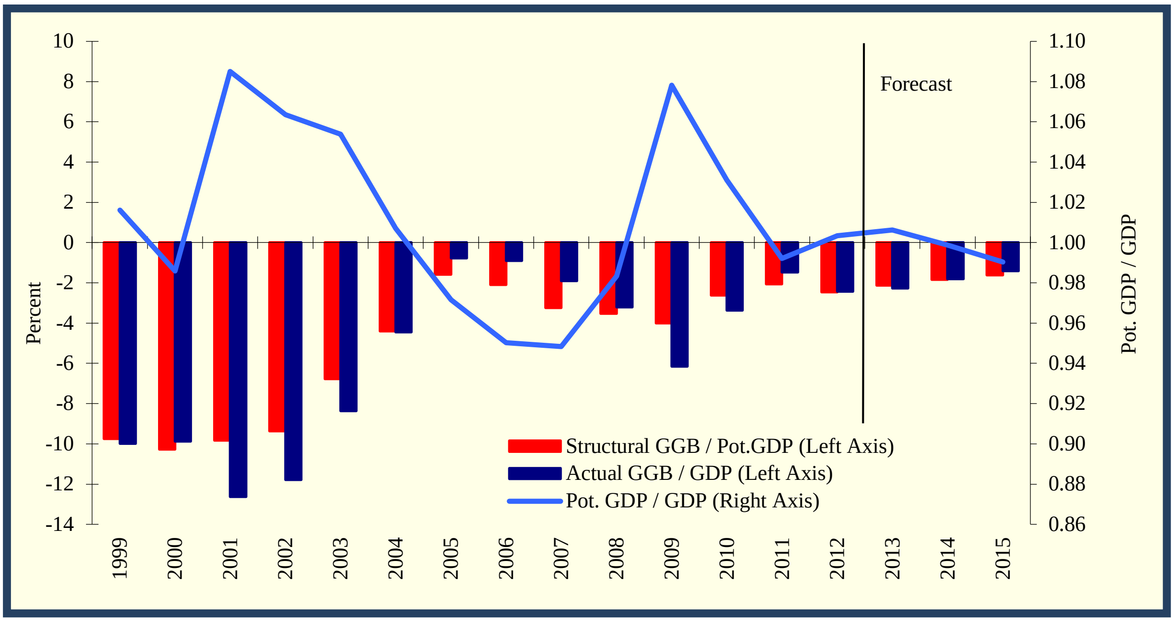
(1) It refers to balance excluded public claims restructuring, 2B Revenues, privatization and other one-off revenues.
(2) Percentage difference from potential.
(3) Structural balance is ratio of potential GDP.

In 2011, in addition to the high growth rates achieved, the decline in budget interest expenditures, restructuring of public claims and so forth led to a decrease in deficit of the actual budget and social security institutions and thus actual general government deficit. As a result of these developments, in 2011, the ratio of actual general government deficit to GDP decreased by 1.9 percentage points compared to 2010. On the other hand, decrease in the ratio of structural general government deficit to potential GDP was limited by 0.6 percentage point. The decrease in actual general government deficit was resulted from increases in social security revenues and decreases in budget expenditures, mainly decreases in domestic capital transfers, domestic lending and interest payments. Similar to the situation of actual deficit, increases in social security revenues and decreases in central government budget expenditures were also effective on the decline of the structural general government deficit.

In 2012, despite revenue measures taken in the last period, the actual general government deficit increased with the slowdown in economic growth. The ratio of general government deficit to GDP is estimated to realize as 2.4 percent with 1 percentage point deterioration compared to the previous year due to the increase in budget expenditures, mainly increases in personnel expenditures, current transfers and interest payments. Correspondingly, the ratio of structural general government deficit to potential GDP is expected to deteriorate by 0.4 percentage points.

The actual and structural general government deficits, which have started to display upward trend in 2012, are expected to decrease in 2013-2015 period, with the additional measures taken. This expected improvement in structural balance will result from the amelioration of revenues in 2013, and it will be stemmed from the decline in expenditures for the years 2014 and 2015. Thus, in accordance with the main objective of strengthening macroeconomic stability, the ratio of actual and structural general government deficit to GDP and potential GDP consecutively, are expected to realize as 1.8 percent and 1.9 percent on average in the period of 2013-2015 (Figure 3.1).

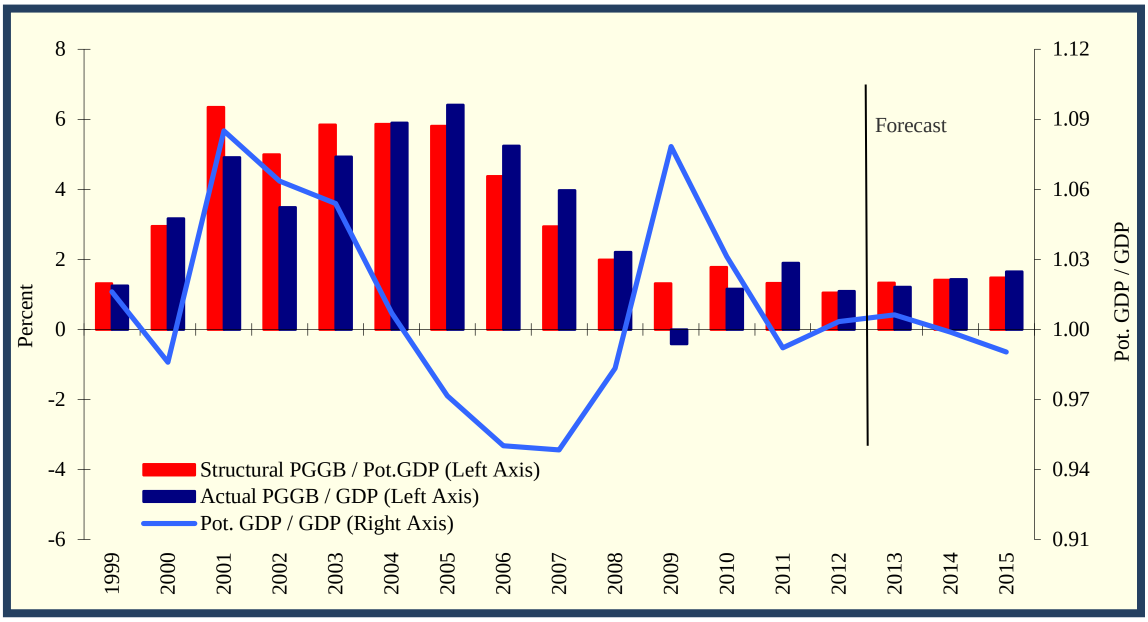
Figure 3.1: General Government Balance



GGB: General Government Balance Excluding Public Claims Restructuring, Privatization, 2B Revenues and Other One-Off Revenues
Pot. GDP: Potential GDP.

In the context of a similar analysis excluding interest expenditures, it is observed that the actual and structural general government balance have deteriorated to some extent in 2012 (Figure 3.2). As from 2013, with the contribution of measures taken, it is anticipated that both actual and structural primary general government surpluses will begin to increase and the ratio of actual and structural general government primary surpluses to GDP and potential GDP, are expected to realize as 1.4 percent annually on average in 2013-2015 period.

Figure 3.2: Primary General Government Balance

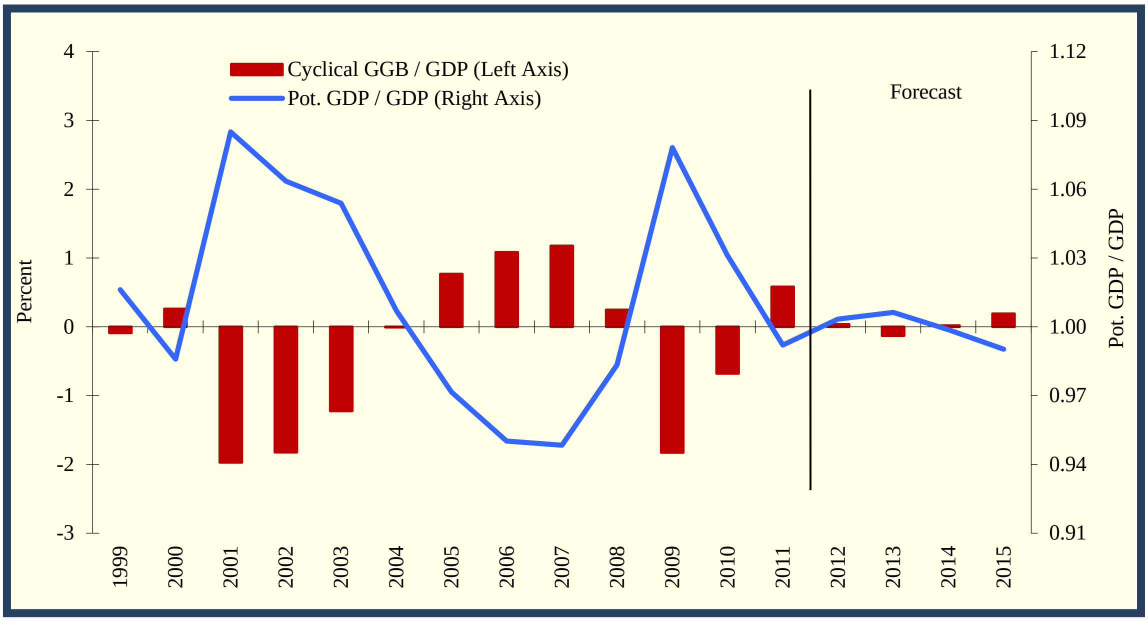


PGGB: Primary General Government Balance
Pot. GDP: Potential GDP

Cyclical general government balance is calculated by subtracting the structural general government balance from the actual general government balance. Since the privatization revenues and one-off revenues are excluded in the calculations of structural and actual general government balances, cyclical balance only reflects the impacts of conjunctural developments.

The cyclical effect is estimated to decline as from 2009 where it was substantially high as a consequence of the divergence of GDP from its potential. Especially during the PEP period, the cyclical effect on general government is forecasted to decline remarkably together with the expected economic recovery (Figure 3.3).

Figure 3.3: Cyclical General Government Balance



GGB: General Government Balance
Pot. GDP: Potential GDP

Box 3.2: Structural and Cyclical General Government Balance Calculation Methodology

The concept of actual general government balance means the balance reflecting impacts of temporary and permanent factors, thus including cyclical movements which effect revenue and expenditure items. On the other hand, the structural general government balance expresses fiscal policy stance free from the effects of economic fluctuations by means of eliminating the effects of cyclical movements on general government balance. The structural general government balance is defined as follows:

$$b^* = \frac{\sum_i T_i^* - G_j^* + X}{Y^P}$$

b^*	: structural general government balance (as a ratio to potential GDP),
T_i^*	: structural value of revenues in category i,
G_j^*	: structural value of expenditures category j,
X	: other general government items that are assumed to be not affected from cyclical movements,
Y^P	: potential output.

The relationship between structural revenues and expenditures and their actual values is shown as follows;

$$\frac{T_i^*}{T_i} = \left[\frac{Y^P}{Y}\right]^{\alpha i}; \quad \frac{Td_i^*}{Td_i} = \left[\frac{C^P}{C}\right]^{\delta i}; \quad \frac{SF_i^*}{SF_i} = \left[\frac{E^P}{E}\right]^{\varepsilon_i}; \frac{G_i^*}{G_i} = \left[\frac{Y^P}{Y}\right]^{\beta j}$$

T_i	: actual revenues in category i,
Td_i	: actual indirect tax revenues in category i,
SF_i	: actual social funds in category i,
G_j	: actual expenditures in category j,
Y	: actual national output,
C	: actual private sector consumption expenditures,
C^P	: potential private sector consumption expenditures,
E	: actual wage and employment,
E^p	: potential wage and employment,
α_i	: output elasticity of category i revenue,
δ_i	: private consumption elasticity of category i revenue,
ε_i	: wage and employment elasticity of category i revenue,
β_i	: output elasticity of category j expenditure.

<u>Revenues:</u>

Tax revenues displaying cyclical movements are categorized into three groups. These categories are income taxes, corporate taxes and indirect taxes.

Sensitivity of income taxes to cyclical developments is influenced by the characteristics of the revenue components that are subject to taxation. Therefore, the items that are less sensitive to conjunctural movements in income taxes, such as wages, are separated.

While calculating the sensitivity of indirect taxes to cyclical developments, the relationship between consumption and potential private consumption (C^P/C) is taken into consideration instead of the relationship between GDP and potential GDP (Y^P/Y).

While calculating structural revenues; non-tax revenues, which are sensitive to conjectural movements, such as revenues from SEE's, tax penalties, valuable paper sales revenues, Treasury shares from GSM operators, are accepted sensitive to economic developments.

The wealth taxes, which are less sensitive to economic developments, are considered insensitive to conjuncture.

Whole of the tax revenues of funds are considered sensitive to conjuncture. While making income tax, corporate tax and indirect tax allocation, the transfers made from the general budget are considered.

While determining sensitivity of tax revenues of local administrations to economic developments, the items which are less affected by conjunctural developments, especially the property tax item, are sorted out. A major part of tax revenues are considered as sensitive to conjuncture although they vary according to years. A large part of indirect taxes are considered as insensitive to economic developments and the taxes included in the structural balance account and affected by conjuncture are shown as indirect taxes.

Whole of the revolving funds tax revenues are considered as sensitive to conjuncture.

A small part of non-tax revenues of local administrations which mostly include performing of duties given by the law are considered as sensitive to conjunctural developments.

Only 5 percent of revolving funds factor revenues; and as changing by years, 10 to 20 percent of local administrations are considered as sensitive to conjunctural developments. Since a major part of property incomes in local administrations covers natural monopoly service, it is considered as less sensitive to conjunctural developments.

In social security balance, the major part of social funds and the whole of premium revenues (social funds) of unemployment insurance are considered as sensitive to conjuncture. The sensitivity of social funds to cyclical developments is calculated by taking the employment and wage increases into consideration.

In unemployment insurance balance, the interest revenues are considered as sensitive, and other factor revenues are considered as insensitive to conjuncture.

One-off revenues, such as privatization, are not included in actual and structural balance calculations.

In revenue elasticity calculations, the elasticity of indirect taxes is assumed to be unity. On the other hand, elasticities of other revenue items are estimated by ordinary least squares method.

<u>Expenditures:</u>

Budget expenditures are classified into two categories in terms of their sensitivity to cyclical movements; sensitive and insensitive. The expenditures sensitive to cyclical movements include the items such as green card payments, duty losses, some parts of agricultural subsidies and risk account. On the other hand, the insensitive expenditures include items such as investment, personnel, capital transfers and interest expenditures items.

The items such as transfers to household which are included in the transfer expenditures of local administrations and capital increases of companies are considered as sensitive to conjunctural developments.

The fact that the urban infrastructure need is continuous and extensive shows that the increases in investment expenditures of local administrations depend on financing opportunities rather than being sensitive to economic developments. Therefore, only one fourth of investment expenditures are considered as sensitive to conjunctural developments in parallel with the increase in income.

Although it changes by years, a small part of the non-personnel current expenditures of local administrations are considered as sensitive to conjunctural developments.

In unemployment insurance balance, 40 percent of the expenditures made within the scope of active labor programmes are considered sensitive and the current expenditures other than these expenditures are considered as insensitive to conjuncture.

Whole of the transfer expenditures of unemployment insurance, especially the insurance payments, is considered as sensitive to conjuncture.

In fund balance, the 50 percent of the transfers made by the Social Aid and Solidarity Promotion Fund is considered as sensitive and remaining current transfers are considered as insensitive.

Calculations are made by considering the expenditures of social security institutions and revolving funds insensitive to conjunctural developments.

Income elasticity of expenditures, which are sensitive to cyclical movements are calculated using ordinary least squares method.

<u>Cyclical General Government Balance:</u>

The difference between actual general government balance and structural general government balance is defined as cyclical general government balance:

$$b^{**} = b - b^{*}$$

b^{**}: cyclical general government balance (as a ratio to GDP),
b : actual general government balance (as a ratio to GDP),
b^{*} : structural general government balance (as a ratio to potential GDP).

3.1.4. Public Debt Management

3.1.4.1. Institutional Responsibilities for Debt Management and Borrowing Limits

The Undersecretariat of Treasury executes debt management in line with the borrowing limit determined pursuant to the Article 5 of the Law No.4749 on Regulating Public Finance and Debt Management, enacted in April 2002.

This Law establishes the principles of public debt and risk management as follows:

- To follow a sustainable, transparent and accountable debt management policy in line with monetary and fiscal policies, considering macroeconomic balances,
- To meet financing need at the lowest possible cost in medium and long term, in accordance with the reasonable risk level determined considering cost factors, domestic and foreign market conditions.

Net borrowing limit is described as the amount of difference between the initial budget appropriations and estimated revenues specified in the budget law of the relevant fiscal year. In line with the same article of the Law, this limit could be increased up to 5 percent within the year by considering the needs and developments in debt management. In the cases where such amount is not sufficient, an additional increase of five percent may be made only by Cabinet Decree upon the view of the Undersecretariat of Treasury and offer of the Ministry to which the Undersecretariat of Treasury is affiliated.

3.1.4.2. Debt Management Strategy

Within the scope of accountable, transparent and sustainable borrowing policies which are compatible with the monetary and fiscal policies, ensuring the optimal cost target in the medium and long term at a reasonable risk level, strategic benchmarking policy has been continued since 2003. Depending on the cost and risk calculations, to manage the public debt efficiently against the main risks of liquidity, exchange rate and interest rate, following measures were taken as the main pillars of the borrowing policy in 2012:

- To borrow mainly in TL,
- Using fixed rate TL instruments as the major source of domestic borrowing and thereby decreasing the share of debt which has interest rate re-fixing in the following 12 months,
- To increase the average maturity of domestic borrowing taking market conditions into consideration and decrease the share of debt maturing within 12 months,
- To keep a certain level of cash reserve in order to reduce the liquidity risk associated with cash and debt management.

In line with the risk and cost targets, borrowing strategies complying with strategic benchmarks will be continued in the forthcoming period.

3.1.4.3. Public Debt Stock

3.1.4.3.1. Current Situation

As a result of the ongoing economic program, fiscal discipline and efficient borrowing strategies, considerable improvements were observed in the EU defined general government debt stock as from 2001; the ratio of EU defined general government debt stock to GDP, which was 77.9 percent in 2001, declined to 39.2 percent at the end of 2011.

Central government total debt stock increased by 44.8 billion TL compared to its 2010 level and reached 518.4 billion TL by the end of 2011. As of November 2012, debt stock reached 530.9 billion TL. In line with the policies to decrease interest rate sensitivity of the debt stock, the ratio of fixed rate debt in the total stock increased by 3.2 points compared to its 2010 level and reached 59.2 percent at the end of 2011 and this ratio has been 59.3 percent as of November 2012.

Table 3.5: EU Defined General Government Debt Stock

(Percent of GDP)

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
EU Defined General Government Debt	74.0	67.7	59.6	52.7	46.5	39.9	40.0	46.1	42.4	39.2

Source: Undersecretariat of Treasury

Compared to its 2010 level, central government domestic debt stock increased by 15.9 billion TL and reached 368.8 billion TL by the end of 2011. As of November 2012, it reached 387.8 billion TL. When the ratio of the respective stock to GDP is considered, it is seen that it descended to 28.4 percent in 2011, from 32.1 percent in 2010.

Table 3.6: Central Government Gross Debt Stock

(Percent of GDP)

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Domestic Debt Stock	42.8	42.7	40.2	37.7	33.2	30.3	28.9	34.6	32.1	28.4
Foreign Debt Stock	26.5	19.4	16.5	13.4	12.3	9.3	11.1	11.7	11.0	11.5
Total	69.2	62.2	56.6	51.1	45.5	39.6	40.0	46.3	43.1	39.9

Source: Undersecretariat of Treasury

The central government foreign debt stock has been 143.2 billion TL as of November 2012. Considering the interest composition of foreign debt stock, the share of fixed rate debt has been 79.6 percent of foreign debt stock as of November 2012.

Table 3.7: Central Government Debt Stock Composition by Interest Rate Type

	DOMESTIC DEBT STOCK			EXTERNAL DEBT STOCK	
	Fixed	Floating	Indexed to CPI	Fixed	Floating
2007	128,148	104,681	22,481	57,869	20,306
2008	140,614	112,528	21,686	76,121	29,373
2009	155,076	137,270	37,658	80,872	30,632
2010	175,740	124,070	53,031	89,511	31,208
2011	192,358	112,118	64,302	114,620	34,951
2012 November	200,770	110,672	76,309	114,005	29,169

	TOTAL DEBT STOCK							
	Fixed	Floating	Indexed to CPI	TOTAL	Fixed	Floating	Indexed to CPI	TOTAL
	Million TL				Share in the Total Debt Stock, Percent			
2007	186,018	124,987	22,481	333,485	55.8	37.5	6.7	100.0
2008	216,736	141,900	21,686	380,321	57.0	37.3	5.7	100.0
2009	235,948	167,902	37,658	441,508	53.4	38.0	8.5	100.0
2010	265,251	155,279	53,031	473,561	56.0	32.8	11.2	100.0
2011	306,979	147,069	64,302	518,350	59.2	28.4	12.4	100.0
2012 November	314,775	139,841	76,309	530,925	59.3	26.3	14.4	100.0

Source: Undersecretariat of Treasury

Thanks to the decrease of share of short term securities in debt stock through their redemptions and issuance of long term securities in line with the strategic benchmarks, average time to maturity of central government debt stock increased from 2.9 year at the end of 2005, to 4.6 as of November 2012.

Analyzing the borrowing realizations in 2012, the average cost of fixed rate TL denominated borrowing which was 8.7 percent in 2011 has been 8.8 percent as of December 2012. The average maturity of the domestic cash borrowing which was 44.7 months in 2011 has been 60.8 months by December 2012.

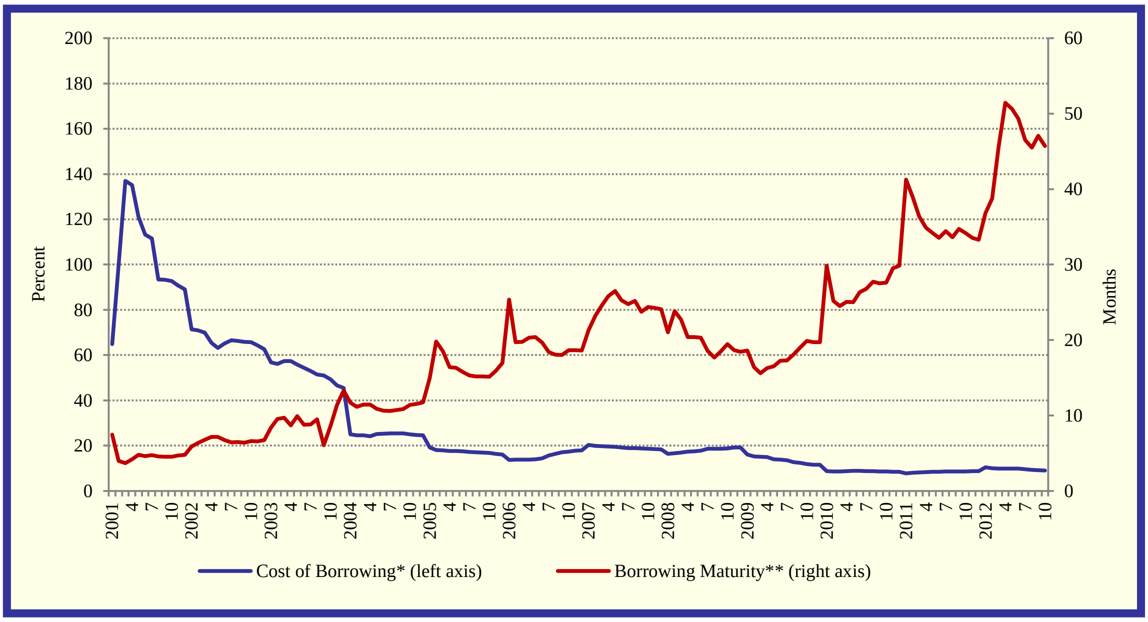
Table 3.8: Average Time to Maturity of the Central Government Debt Stock

	2005	2006	2007	2008	2009	2010	2011	2012 November
Domestic Debt Stock	2.0	2.0	2.1	2.0	2.0	2.6	2.6	2.9
Foreign Debt Stock	5.7	7.0	7.7	7.9	7.9	8.8	9.0	9.2
Total	2.9	3.4	3.4	3.6	3.5	4.1	4.4	4.6

Source: Undersecretariat of Treasury

In order to increase the domestic savings, broaden the investor base and diversify the financing instruments, Lease Certificates have been issued for the first time in 2012 both in the domestic and international markets. The nominal value of TL denominated Lease Certificate is approximately 1.6 billion TL with maturity of 2 years.

Figure 3.4: Average Time to Maturity of the Central Government Debt Stock



(*) Annual cumulative cost of fixed rate TL denominated borrowing is displayed.
(**) Annual cumulative maturity of cash domestic borrowing is illustrated.
Source: Undersecretariat of Treasury

3.1.4.3.2. Contingent Liabilities

The Undersecretariat of Treasury provides repayment guarantees for foreign borrowing of public administrations (defined in Law No. 4749, Article 3) in order to minimize the investment financing costs, ensure sustainable growth and meet funding requirements of multi-year investment projects of the mentioned institutions. Furthermore, based on and limited with the provisions of the relevant law, Undersecretariat of Treasury provides investment guarantees within the scope of Built-Operate-Transfer, Built-Operate, Transfer of Operating Rights and similar financing models.

Endogenous Credit Rating Model which considers the debt-receivable relationship between the institutions and the Treasury and financial statements of these institutions, was put into practice in January 1, 2007, in order to improve the management of contingent liabilities confronting the Undersecretariat of Treasury. In this context, the limit for Treasury guarantees and on-lent foreign loans, guarantee and on-lent fees and partial guarantee ratios are calculated using this model based on the expected losses from organizations in order to alleviate risks arising from contingent liabilities.

In this context, the limit covering repayment guarantees, investment guarantees and on-lent foreign loans to be provided under the Law No. 4749 is set by budget law every year. The limit to be applied for the Treasury guarantees to be provided under the Law No. 4749 was set as 2 billion dollars in 2008. In addition to this guarantee opportunity, as from 2009, the foreign financing to be used on-lent was taken into the scope of this limit and it was determined as 4 billion dollars in 2009, as 3 billion dollars in 2010, 2011, 2012 and 2013.

If a Treasury guarantee is provided under the Law No. 4749, a fee up to 1 percent of the guaranteed amount is charged to the related institution. On the other hand, upon amendment made in the Law No. 4749 in 2008, if on-lent foreign loan is provided, a fee up to 1 percent of the on-lent amount is charged to the related institution as well. In the partial guarantee practice, credits except export credits obtained from the international and regional organizations and foreign Official Export Insurance Agencies, are guaranteed up to 95 percent of the total liabilities.

Risk Account has been set up in 2003 in order to eliminate the disruptions in the cash and debt management caused by the amounts paid by the Treasury due to Treasury guarantees and budget appropriation was started to be allocated every year as of this date. As the repayments to the Risk Account is sufficient for the undertakings realized from the account no budgetary allocations, which is one of the items of the revenues of the account, has been used since 2009.

3.1.4.3.3. Repayment Guarantee

The repayment guaranteed debt stock has increased from its level of 8.3 million dollars in 2011 to 8.5 million dollars by end of second quarter of 2012. The increase in the level of stock is due to the guarantees provided to public banks and private investment and development banks.

Although there is an increase in the repayment guaranteed debt stock, the undertaking ratio which was 9 percent by of the end of 2011 dropped to the level of 5.6 percent by the end of November 2012.

Regarding the payment projection of the Treasury repayment guaranteed foreign debt stock, an increase parallel to the disbursements is observed in the medium term.

Table 3.9: Projection of Treasury-Guaranteed Foreign Debt Service*

(Million Euro)

	Principal	Interest	Total
2013	496	123	618
2014	567	110	677
2015	649	97	746
2016+	4.775	530	5.305

(*) As of June 2012, based on usage, provisional.
Source: Undersecretariat of Treasury

3.1.4.3.4. Investment Guarantees

Undersecretariat of Treasury has provided investment guarantees to energy and infrastructure sectors as well as repayment guarantees. Within the context of investment guarantees provided 1.9 billion dollars has been undertaken in total as of November 2012.

3.1.4.3.5. Treasury Receivables

As of November 2012, the local administrations have 66.8 percent, SEEs has 15.1 percent and other receivables have 18.1 percent shares in the Treasury’s receivables stock.

In January- November 2012 period, cash payments of the institutions (66.7 percent) has the highest share within the collections. In the same period, the deductions made from tax income shares of the Municipalities by the Ministry of Finance constitutes 29.6 percent of the collections whereas the deductions made from tax income shares of the Municipalities by the İller Bank constitutes 1.4 percent of the collections. The collections made pursuant to the Law No. 6183 and transfers from other institutions are 2.3 percent of collections in the mentioned period.

3.1.4.3.6. General Government Debt Stock Projections for 2012-2015 Period

As a result of the prudent fiscal policies implemented and the high growth rates achieved in an environment of enhanced confidence and economic stability in the last decade, the ratio of the general government debt stock to GDP has decreased significantly. However, due to the economic contraction due to the global crisis and increase in the budget deficit, general government debt stock increased slightly and was realized as 46.1 percent of GDP in 2009. Thanks to the measures taken and economic program implemented, it reverted back to decreasing trend and was realized as 39.2 percent at the end of 2011. On the other hand, it is anticipated that the stock ratio will tend to decrease in the period of 2012-2015 and fall down to the level of 31 percent at the end of 2015.

Table 3.10: Projections of EU Defined General Government Debt Stock

(Share in GDP, Percent)

	2011	2012	2013	2014	2015
	Realization	Projection			
EU Defined General Government Debt Stock	39.2	36.5	35.0	33.0	31.0

Source: Medium Term Programme (2013-2015)

3.1.5. Budgetary Implications of Major Structural Reforms

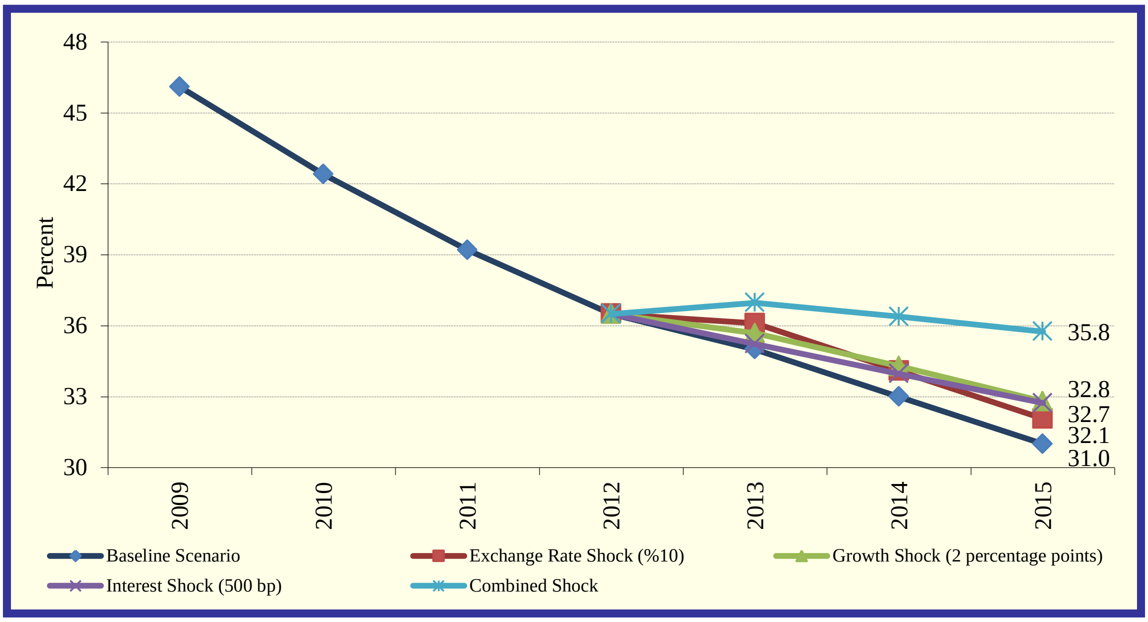
The burden of Treasury undertaking of five-points of employer share of disability, old age and death premiums due to the Law No. 5763 has been 0.37 percent, 0.35 percent and 0.36 percent (as a ratio to GDP) on the social security balances in 2009, 2010 and 2011 respectively. It is expected to create an additional burden of 0.39 percent, 0.42 percent, 0.42 percent and 0.43 percent (as a ratio to GDP) in 2012, 2013, 2014 and 2015 respectively.

3.2. Sensitivity Analysis

Thanks to fiscal policies and debt management practices based on strategic benchmarks implemented since 2002, the resilience of the public debt stock against shocks improved significantly. In an environment where uncertainties regarding global growth performance have increased, sustainability analysis regarding the course of public debt stock against various macroeconomic shocks in the period of 2013-2015 are presented below.

In various scenarios, reaction of EU defined general government debt stock to GDP ratio in response to the exogenous shocks; such as the exchange rate, real growth rate and the real interest rate shock, are analyzed (Figure 3.6). Within the context of the growth shock scenario, 2 percentage points decrease in the real growth rate is kept as in the previous year's PEP. As the growth rates in the base scenario are lower than the previous year's PEP, 2 percentage points decrease in the real growth rate refers to a relatively higher level of shock compared to last year's sustainability analysis. Therefore, in the analyses below, impacts of 10 percent increase in the exchange rates, 2 percentage points decrease in the real growth rate and 500 base points increase in the real interest rates compared to the base scenario in each year have been assessed separately and jointly. Examining the scenarios stated above, compared to the base scenario, it is evaluated that the debt stock will record an increase of 1.1 percentage points under the exchange rate shock; 1.7 percentage points under the real interest rate shock and 1.8 percentage points under the growth rate shock in 2015. In the combined shock scenario in which all shocks are taken into consideration together, it is expected that the debt stock might increase by 4.8 percentage points compared to the baseline scenario. Even though the growth shock is assumed higher than the previous year's sustainability scenarios, the deviation of debt stock to GDP ratio in 2015 between the baseline scenario and the combined shock scenario is lower than that of last year's analysis. These results also indicate that the sensitivity of the debt stock against external shocks has been reduced compared to 2011. Even in the combined shock scenario, debt stock to GDP ratio is expected to decline in the medium term.

Figure 3.5: Sustainability Scenarios



3.3. Public Finance Risks

In the 2013-2015 period, risks that might constitute obstacles to reach the determined objectives in the public finance are summarized below:

- In the case that growth rate is realized lower than expected, the central government revenue performance and the employment increase parameter will be adversely affected; therefore, there is a possibility of increase in the financing needs. This situation, under the circumstance of social security insurance premium collections being lower than projections and health-care expenditures are not taken under control, will increase the transfers to the social security institutions from the central government budget.
- Failing to update the fixed taxes and fees will adversely affect the revenue performance.
- With the Decision of the Council of Ministers No. 2012/3305 and dated 15 June 2012, tax cuts and tax exemptions came into force with the new incentive regime. This development may adversely affect the revenue performance.
- Privatization revenues will be lower than the expectations in case of ongoing uncertainties in the international markets.
- The Law No.6292, regarding the sale of degraded forest land, was published in the Official Gazette dated 26 April 2012. Collections stemming from this Law will be below the expectations if participants fail to fulfill the obligations.

3.4. Quality of Public Finance

The high growth performance in 2010 and 2011 positively affected the public sector indicators. The strong recovery of domestic demand and foreign trade in this period boosted tax revenues and social security contributions, as a result the general government deficit in 2011 stood at 0.4 percent of GDP. In order to sustain this performance, it is important to use public sources in a way that they promote potential growth, and to design fiscal policy consistently with private sector-led growth perspective.

As part of the efforts to establish an effective and efficient tax system which supports investment, employment and fight against informal economy, works on new Income Tax Law will be finalized. In addition, Tax Procedure Law will be revised in order to enhance compatibility with modern tax system in terms of taxpayer rights, conflict resolution and valuation and to strengthen deterrence of tax penalties.

Public investments will be focused on the economic and social infrastructure projects, aiming reduction of regional development disparities and improvement of regional development potential, in particular on the investments within the scope of the Southeast Anatolia Project, East Anatolia Project, Konya Plain Project and the East Black Sea Project. The investments required for the realization of the policies and priorities introduced for membership to the EU will be accelerated.

Central government initial investment budget of 2012 was amounted to 27.8 billion TL, 23.9 percent of which was allocated to transportation and communication sector, 21.1 percent to the education sector and 18.8 percent to the agriculture sector. Besides, an additional 5.8 billion TL of capital allowance was provided to projects in the areas of education and transportation during the year. In 2013-2015 period, the primary objective of public investments policy will be increasing efficiency of public investment, giving priority to infrastructure that support productive activities and social needs and promoting activities towards institutional, sectorial, regional and EU integration targets. Within this context, capital expenditure in 2013 budget was increased by 20 percent relative to previous year initial appropriations. Public-Private Partnership (PPP) model introduced in order to benefit from capital and management skills of private sector and alternative financing facilities will continue to be implemented.

With the Decision of the Council of Ministers No. 2012/3305 dated 15 June 2012, a new incentive scheme, which aims to increase employment, reduce current account deficit via supporting domestic production of import-dependent products, was put into force. In this new incentive system, in addition to the advantages previously granted to investors, income tax withholding support and VAT refund are also granted. By income tax withholding incentive, investors will have the advantage of discounting income tax equal to minimum wage income tax for a period of ten years in 6th region. Within the VAT refund incentive, for investments amounted to 500 million TL and above, the VAT paid for construction works will be refunded in proceeding year up to end of 2023. In addition, the corporate income tax incentive was extended to earnings of all activities during the investment periods benefit from discounted rates. For investment projects executed in the scope of incentive scheme, social security premiums of workers will also be paid by Ministry of Economy.

As of the incentives offered by Small and Medium Industry Promotion and Development Agency (KOSGEB), 790 million TL of spending is envisaged for the period 2013-2015. The current transfer expenditures in the central government budget within the scope of the incentive payments is expected to be 2.2 billion TL in 2013.

The Decree No. 2009/15197 on the Principles and Procedures regarding the Treasury Support to be Provided to Credit Guarantee Institutions, which was prepared in order to provide easier access of SMEs to financing opportunities, was published on the Official Gazette on 15 July 2009. Pursuant to the aforementioned decree, it is determined to provide an amount of 1 billion TL to credit guarantee institutions. After that regulation, the first credit guarantee institution which will be provided with support by the Undersecretariat of Treasury was determined as KGF. On the other hand, so as to facilitate application conditions for SMEs, resolve financing problems of the companies engaging in activities in the area of ship construction and ship management and reduce costs of beneficiaries, regulations were made regarding more active operation of the system by means of some amendments made in the aforementioned Decree in 2010 and 2011. After the regulations ratified in 2011, utilization period was extended to 15 July 2013. Credit amounting to a total of 1,491 million TL was issued for 2,624 SMEs during the period between July 2009, in which the said support became operative, and November 2012.

For the R&D incentives managed by TÜBİTAK, 800 million TL for 2012 and a total of 2.7 billion TL for 2013-2015 period were envisaged to be spent. In order to create a productive and competitive economic environment through the support of R&D activities, the Law No. 5746 was enacted to be implemented until 2023. In accordance with this Law, it is now possible to deduct 100 percent of the R&D expenditures from the tax liabilities while this has been applied as 40 percent under the Corporate Tax Law and Income Tax Laws since 2004. Within the context of this law, withholding tax support for the income tax as well as the insurance premium for the R&D staff and offers techno-enterprise capital support for innovative ideas are also envisaged.

The Social Support Programme (SODES) which was put into implementation in GAP provinces in 2008 in order to effectively meet the need of improving human capital and providing social integration under the component titled Providing Social Development of GAP Action Plan was extended in a way to cover DAP provinces in 2010. In 2011, the number of provinces in the scope of the program has increased to 30 by incorporating 5 provinces in pilot scheme. Within the scope of the mentioned programme, it is estimated that a total resource of TL 916 million will be used in the period of 2012-2015.

The Project for the Support of the Infrastructure of Villages (KÖY-DES), which has been implemented since 2005 and developed to meet the common needs of the local administrations such as drinking water, sewage and roads, will continue in 2013-2015. Accordingly, it is programmed that 1.8 billion TL will be allocated to this project in the period of 2013-2015. For the program initiated to help financing of drinking water and sewage projects of municipalities, Water and Sewerage Infrastructure Project (SUKAP), 1.7 billion TL is allocated for the 2013-2015 period.

The share of social expenditures of the budget has also significantly increased in recent years. The total of expenditure items such as training of disables, social security premiums for green card owners, social transfers, shares allocated to Social Assistance and Solidarity Fund (SYDTF) from tax revenues will expected to be around 16.5 billion TL in 2013.

3.5. Institutional Features of Public Finance

Significant structural changes are being made to improve the institutional capacity in the public financial management. Some of the recent regulations designed for this purpose are presented below.

3.5.1. Public Financial Management and Control Law

As a result of the competition exam conducted to increase the public administrations' capacity of competent personnel in the field of financial management and control, 82 assistant experts became entitled to be appointed to the cadre of "Financial Services Specialists".

In line with the Public Financial Management and Control Law No. 5018 and the secondary legislation promulgated according to this Law, vocational trainings necessary for introduction to the profession and for subsequent periods were conducted for the Financial Services Specialists and Assistant Financial Services Specialists.

The draft version of The Public Internal Control Manual, prepared to provide guidance to the public administrations in their endeavors aimed at the effective implementation of the new financial management and control system brought with the Public Financial Management and Control Law No. 5018, was published in the web site. In addition, the works related to the improvement of the Financial Management and Control Central Harmonization Unit Handbook are still in progress.

All of the activities envisaged in the Contract of the Twinning Project on Strengthening the Public Financial Management and Control System in Turkey were successfully completed. The organization of the trainings required in the accomplishment of the obligations related to the establishment of financial management and control system is continuing.

Works for the amendments planned on the Public Financial Management and Control Law No. 5018 are still in progress. As of October 2012, excluding regulatory and supervisory agencies there are 759 internal auditors working in the 207 public administrations within the scope of general government that are subject to the internal audit provisions of the Law No. 5018. As a result of Internal Audit Candidate Selection Exams which were held in 2010, 2011 and 2012, the number internal auditor candidates who had public internal auditor certificate reached to 288. Those candidates that were deemed to be successful in Internal Audit Candidate Selection Exam held on 20 October 2012 will be subjected to a 3 months internal audit training as of December 2012.

Principles and Procedures for Grading of Public Internal Auditor Certificates was published in the Official Gazette dated 17 February 2012 and No. 28207. Training on communication skills was organized in March and April 2012 with the participation of internal auditors working in the public administrations and in June, the opening ceremony of a new project, which will be jointly conducted with the World Bank, was held and the activities within the scope of this project still continue. Public Internal Audit Report 2011 was published with the Council Decision dated 6 August 2012 and No. 8.

Moreover, within the scope of Internal Audit Quality Assurance and Improvement Programme, in 6 pilot institutions (Ministry of National Education, Ministry of Customs and Trade, Social Security Institution, General Directorate of Highways, Gazi University and Ankara Metropolitan Municipality) external assessment has been conducted. The contract concerning the Public Internal Audit Automation Software Development Project was signed with the contracting company on 5 October 2012.

4. STRUCTURAL REFORMS

4.1. Enterprise Sector

4.1.1. Privatization

The total amount of privatization of which sales/transfer operations were completed was 1.4 billion dollars in 2011. This amount reached to 3 billion dollars as of the end of November 2012. The main privatizations are sales of 23.9 percent public shares of Türkiye Halk Bankası A.Ş. (state bank), 76.8 percent public shares of Acıpayam Selüloz Sanayii ve Ticaret A.Ş., 10.3 percent public shares of PETKİM Petrokimya Holding A.Ş., 20 percent public shares of Kayseri ve Civarı Elektrik T.A.Ş., and various immovable properties belonging to other institutions in this term.

The total amount of privatization which are at the stage of approval/contract is 1.1 billion dollars and such implementations include Aras and Akdeniz electricity distribution companies, some river power plants, public shares in Doğusan Boru Sanayii ve Ticaret A.Ş., and immovables belonging to various state entities.

The privatization implementations for which transfer operations were completed as of the end of November in 2012 are shown in Table 4.1.

Table 4.1: Privatization Transactions Completed in 2011

Company	Privatization Transaction	Sales Price (Dollars)
Türkiye Halk Bankası A.Ş. (% 23.9)	Public Offering	2,509,480,259
Acıpayam Selüloz Sanayii ve Ticaret A.Ş. (% 76.8)	Block sale	1,970,000
PETKİM Petrokimya Holding A.Ş. (% 10.3)	Block sale	168,500,000
Kayseri ve Civarı Elektrik T.A.Ş. (% 20)	Block sale	16,050,000
Others	Sales and transfers of various real estates and facilities	311,905,014
Total		**3,007,905,273**

Approval and sales/transfer operations of Akdeniz Electricity Distribution Company, 56.1 per cent public shares in Doğusan Boru Sanayii ve Ticaret A.Ş., and some river plants belonging to EÜAŞ, for which tender processes were completed, are expected to be completed. The tender announcement has been made one more time for Boğaziçi and Gediz Electricity Distribution Companies of which tenders were cancelled.

The tender announcements have been published in order to privatize Hamitabat Elektrik Üretim ve Ticaret A.Ş. (electiricity generation company), and Kangal and Seyitömer thermal power plants belonging to EÜAŞ. In addition, the tender announcement was made in order to privatize 9.9 per cent public shares in Kayseri Şeker Fabrikası A.Ş. (sugar factory).

Privatization tenders of sugar factories consisting of B portfolio group (Malatya, Erzincan, Elazığ, and Elbistan Sugar Factories) and C portfolio group (Kastamonu, Kırşehir, Turhal, Yozgat, Çorum, and Çarşamba Sugar Factories) belonging to TŞFAŞ were cancelled by Privatization High Council.

In order to privatize some motorways, by the method of “transfer of operation rights”, the tender announcement was made. In addition, in order to privatize 100 per cent shares of Başkent Doğalgaz Dağıtım A.Ş. (natural gas distribution company), tender announcement has been published.

The privatization of Izmir Port belonging to Turkish State Railways and of which tender had been cancelled was decided as cruise and cargo ports separately. The privatization tender of İzmir Cruise Port by transfer of operation rights was cancelled due to being just one offer.

The completion of privatization procedure of Boğaziçi, Gediz, İstanbul Anadolu Yakası, Toroslar, Akdeniz, Aras, Vangölü, and Dicle Electricity Distribution Companies and start of privatization works for some electiricity generation plants belonging to EÜAŞ are foreseen in 2013.

4.1.2. Competition Law and Policies

A draft law, regarding the antitrust legislation in Turkey, was sent to TGNA, and is in the agenda of general assembly. Preparations as to a guide on competitive impact assessment which is part of regulatory impact analysis and which allows regulations to be designed in a way to be as less anticompetitive as possible have been completed and submitted for approval.

A Cooperation and Information Exchange Protocol was signed between the Turkish Competition Authority and the Banking Regulation and Supervision Agency (BRSA). According to the text of the protocol, Competition Authority and BRSA will be able to exchange information concerning those subjects and developments which are important for the establishment and protection of a competitive environment in financial sector, they will be able to hold assessment meetings, and they will be able to share final decisions in supervision, examination, inquiry or investigation processes for those subjects which fall under the jurisdiction of the other party.

With the Law No.6015 which aims; regulation of state aids according to agreements between Turkey and EU, determination of methods and principals of monitoring and auditing by setting essentials and principals of reporting of them to concerned authorities; State Aid Monitoring and Supervision Board, and General Directorate of State Aids to run secretariat of the aforementioned Board, have been established, and thereby authority on state aids has become operational. Draft regulations about the law are being prepared and are planned to be issued and become effective until 30 June 2013. After this date, duties set in the Law will be fulfilled by this authority.

4.1.3. Improvement of the Investment Environment

In the context of studies made for the improvement of the Investment Environment since 2001, a significant progress has been recorded in improving the business climate and increasing investments. In 2011, studies were conducted with the participation of the private sector and public institutions in order to improve the efficiency of Coordination Council for the Improvement of the Investment Environment (YOİKK). As a result of studies; YOİKK structure, working procedures and principles were renewed with the decision of the Council of Ministers No. 2012/2 dated 16 January 2012.

The new Turkish Commercial Code; which was prepared by considering the new developments in international substantive law and law regimes, multilateral trade and electronic commerce and liability laws as well as the need to harmonize the Commercial Code with other laws and EU legislation, was published in the Official Gazette on 14 February 2011. The Law which sets out the enforcement and application of Turkish Commercial Code was also published at the same time. New regulations in the areas of the definition of commercial undertakings and tradesmen, trading companies, companies according to their scale, intellectual property rights, electronic transactions, transportation of goods, securities and stocks and shares, maritime law, insurance law and building consumer awareness was brought by this Law. The renewed Turkish Commercial Code which entered into force on 1 July 2012 to a large extent will come into force on 1 January 2013, completely.

Final date for conducting regulations about notification, monitoring and supervision of state supports postponed to 30 June 2013 by Decree Law 661.

New investment incentive system regarding Decision on State Aid to Investments No. 2012/3305 came into force by being published in the Official Gazette dated 19 June 2012. The number of regional groups increased from 4 to 6 based on their development level and the regions were formed on a provincial basis in the new investment incentive system. Regional incentive system, in addition to general incentive system and the incentives for the areas of large scale investments added a new application to the system in order to support domestic production in intermediate goods and products that are highly dependent on imports.

4.1.4. Utilities and Network Industries

4.1.4.1. Energy

The works for the liberalization of the energy market have been carried on also in 2012. The expected benefits of the electricity privatization are the reduction of costs by productive enterprises and reflecting them to consumers, decreasing high energy losses, empowerment of the financial structure of the sector by increasing accrual and collection rates, increasing the contribution of the private sector for supply security and realization of the renovation & expansion investments by the private sector.

Share of private sector in electricity generation has reached to 60 percent at the end of 2011. The increase in share of private sector in electricity generation is expected to continue in the forthcoming years. In 2012, privatization tender of Hamitabat Power Plant, which is operated by Electricity Generation Company (EUAS) and has an installed power of 1.156 MW, has been launched. Privatization works for 3 of 8 distribution companies (Boğaziçi, Gediz and Akdeniz electricity distribution companies) which are still owned by public sector have been continued. Works for tendering process are still ongoing.

As a consequence of the transfer of natural gas import agreements to private sector, which was carried out for the liberalization of natural gas market, the share of public natural gas company BOTAS, which is the main importer in wholesale market, has decreased to 87.5 percent in 2011. With 10.8 percent share of private companies in wholesale market and 1.7 percent share of production companies, the total share of alternative suppliers has increased to 12.5 percent. The agreement for 6 billion cubic meter amount of gas, which was imported from the Russia-Turkey West Pipeline by BOTAS in the past, has come to an end in 2011. Renewal of this agreement by private sector companies will contribute significantly to development of competition in supply market.

4.1.4.2. Telecommunication

Law No. 4502, which was put into force in 2000 and amended the Telegraph and Telephone Law no. 406, paved the way to liberalization process in the telecommunications sector in Turkey and Telecommunications Authority was established as the independent regulatory body. On the other hand, in accordance with the same Law, monopoly rights of the incumbent operator Turk Telekom in the field of fixed telecommunication services expired by the beginning of 2004 and introduction of competition in the sector was aimed.

According to Electronic Communications Law, numbered 2813, and Law on the Establishment of Information and Communications Technologies Authority (ICTA), numbered 5809, one of the main tasks of ICTA is to achieve full liberalization in the sector. Effective implementation of regulatory and supervisory activities by the Authority is crucial to establish a sustainable competitive environment in the sector. On the other hand, ICTA and Competition Authority are consulting each other with regard to decisions on the telecommunications sector. Accordingly, with regard to the establishment, development and protection of competition in the electronic communications sector in order to increase the effectiveness of co-operation and co-ordination, Protocol of Cooperation between the Information and Communication Technologies Authority and the Competition Authority was signed on 2 November 2011 and entered into force.

ICTA has completed sectoral secondary legislation and authorized numerous operators since 2000. In order to be able to deliver services, it is indispensable for these operators to interconnect with the incumbent operator under reasonable terms and access to infrastructures it controls. To this end, relevant markets and operators with significant market power (SMP) in these markets have been identified. SMP operators send their reference access and interconnection offers to ICTA and these are published after the approval by the Authority. Reference interconnection charges of the fixed incumbent and mobile network operators are provided in the following table with their effective dates.

Table 4.2: Interconnection Tariffs (Taxes Excluded)

Enforcement Date	Call Origination and Call Termination Charges on Turk Telekom Network (Kr/min.)			Call Termination Charges on Mobile Networks (Kr/min.)		
	Local	In-zone	Out-zone	Turkcell	Vodafone	Avea
1 January 2007	-	2.00	3.7	14.0	15.2	17.5
1 March 2007	-	1.89	3.0	13.6	14.5	16.7
1 April 2008	-	1.71	2.7	9.1	9.5	11.2
1 May 2009	1.39	1.71	2.7	6.55	6.75	7.75
1 April 2010	1.39	1.71	2.24	3.13	3.23	3.7

Source: Information and Communication Technologies Authority

As indicated in the table, interconnection charges of SMP operators, particularly those of mobile operators have been reduced considerably in the previous period. Furthermore, pursuant to the decision of ICTA board taken in July 2011, Turk Telekom added wholesale line rental services into its reference interconnection offer, which was updated in August 2011. Wholesale line rental charges are shown in the table below. Wholesale line rental implementation is effective since the beginning of February 2012.

Table 4.3: Wholesale Line Rental Tariffs (Taxes Excluded)

Enforcement Date	Turk Telekom Wholesale Line Rental Tariffs					
	Activation Charge (TL)			Line Rental Charge (TL/Month)		
	PSTN	ISDN BA	ISDN PA	PSTN	ISDN BA	ISDN PA
2011	5.64	11.28	1,629.32	9.48	18.96	284.40

Source: Information Technologies and Communications Authority

Wholesale tariffs of bit stream access model have been updated many times, the price level has been decreased and new high speed tariff packages have been added to xDSL portfolio by Turk Telekom. In the scope of wholesale level for the purpose of resale and bit stream access, there has been a decrease in February 2012 by amount of 15 percent in price level of limited packages and 5 percent in price level of unlimited packages, and also decrease in July 2012 by approximately amount of 13 percent in the price level of high speed DSL tariffs. In addition, in order to take into consideration people in need of social protection, there has been discount on price for tariffs. Within this framework, it has been provided disabled people in 2011 and 1st degree relatives of ghazis and martyrs in 2012 to benefit from 25 percent discount on some DSL tariff packages.

Table 4.4: Local Loop Access Charge Tariffs

Enforcement Date	Turk Telekom Local Loop Unbundled Shared Access Charge Tariffs	
	Subscriber Loop Establishment Charge (TL)	Subscriber Loop Usage Charge (TL/Month)
2008	110	5.75
2009	74	5.75
2010	38.6	5.50
2011	38.55	5.49
2012	38.55	5.49

Source: Information and Communication Technologies Authority

In addition to this, there has been update for resolving the problems in the implementation of reference unbundling access to the local loop offer. The price for access to the local loop has last updated in August 2010. Prices for access to the local loop for the last five years are shown in the preceding table.

As of September 2012, in terms of fixed telephony revenues share of alternative operators is 12.6 percent in fixed telephone services market and 22.8 percent in fixed broadband services market in terms of fixed broadband subscriber figures.

Fierce competition exists among three mobile services operators and mobile number portability, which was introduced in November 2008, drove competition further in this field. As a consequence of considerable reduction in call termination charges in mobile networks and introduction of mobile number portability, it is observed that mobile network operators are introducing innovative mobile tariffs to the benefit of users.

Besides, Türk Telekom Reference ATM/FR/ME Internet Resale Offer was firstly approved by ICTA in 2011, and there have been significant amount of discounts on tariffs in the scope of reference offer. For instance, there has been average discount of 18 percent on tariffs of IP Transit Service.

Similarly, "Reference Leased Line Offer" (RLLO) which is related to Leased Circuit Services offered by Turk Telekom at the wholesale level is approved by our Authority in 2011 for the first time. With the approval of RLLO, tariff reductions were made on average 15 percent of domestic leased circuit service, 18 percent of Point to Point Metro Ethernet service, 17 percent of Point to Point G.SHDSL service. Studies regarding the approval of the code of practice and tariffs for Partial Leased Line service are in progress.

Within the scope of the churn regulation which came into force after the approval of the Authority in 2010, a total of approximately 733 thousand subscribers changed the service provider as of the end of October'2012 and with the contribution of this regulation, alternative DSL internet service providers has reached 13 percent market share. In addition, the number of subscribers of Naked DSL service which allows DSL subscription without subscription to the PSTN has reached 633 thousand after a two-year implementation period.

4.2. Financial Sector

4.2.1. Banking Sector

As the main sub-regulations in banking sector have been completed substantially, regulations in 2012 are supplementary of those made in previous years. With the regulations in 2012, amendments were made generally in the light of new needs on the current regulations concerning corporate management, internal systems, provision practices, accounting rules and measurement of interest rate risk of banks.

Activities on application of Basel II by banks operating in Turkey are carried out by the Banking Regulation and Supervision Agency (BRSA) within the scope of the National Programme and Programme for the Adaptation to Acquis. Basel-II regulations published in the Official Gazette dated 28 June 2012 No. 28337 have been in effect since 1 July 2012. In addition to Basel II provisions, these regulations include Basel 2.5 provisions which are known as CRD-III (Capital Requirement Directive) regulations in the regulatory framework of European Union. Moreover, it is planned to finalize the workings on Turkish banking legislation's compliance with the Basel III standards in 2013 which was prepared by Basel Committee on Banking Supervision in order to strengthen banking systems after global crisis.

There has been progress in supervision and regulation to strengthen financial stability. In order to close some of the gaps in the regulatory framework the rules on asset classification and provisioning requirements has been tightened.

Moreover, with the amendments made relative to some items that are considered calculating total and foreign currency liquidity adequacy, it was aimed to increase resiliency against financial shocks.

In order to increase the stress test implementation capacity of BRSA, model based scenario analyses were developed. Works on improvement of the model are continuing towards including economic growth, real sector and current account data.

While routine relations with equivalent authorities in other countries and international institutions maintained in foreign relations field, the memorandum of understandings were signed with National Bank of Belgium, Korea Financial Supervisory Service, Central Bank of Iraq in 2012, relating to information exchange and cooperation in banking supervision field and thus, the number of countries signed MoU reached to 31.

4.2.2. Capital Market

At the end of 2011 and in 2012, the following steps were taken in order to protect investors in the capital markets and create a stable and efficient market considering the EU directives:

- Drafting for a new Capital Markets Law that was carried out with the purpose of achieving harmonization with EU legislation, updating regulations to match current market circumstances, increasing the use of capital markets in financing the real sector, and improving investor protection. The Draft Capital Markets Law was finalized and passed by Turkish Grand National Assembly as of December 2012 and sent to president for approval.
- The custody and registration with regard to Government Domestic Borrowing Instruments (GDBI) at the Central Registry Agency (CRA) in the name of investors has been initiated.
- After secondary regulations came into force concerning leveraged transactions and the institutions that can carry out such transactions, processes regarding the licensing procedure of related intermediaries have been continued.
- With regulations in relation to Corporate Governance, three distinct categories have been determined according to the systemic importance of firms, which have then been subjected to different degrees of regulation according to their categories. In addition, many changes have been made in relation to directors and board of directors of listed companies in line with EU legislation and recommendations.
- Regulations allowing unlisted publicly held companies to be traded on the Free Trading Platform of the Istanbul Stock Exchange were made by a new communiqué. Regulations were also made with regard to de-mergers of publicly held companies.
- With respect to real estate investment companies, in order to keep regulation in line with the developing needs of the market, to reflect changes regarding corporate governance in regulations and to diversify the instruments which can be included in real estate investment company portfolios, several amendments were made to the communiqué on real estate investment companies.
- With amendments to the communiqué on investment funds, certain restrictions especially with respect to capital protected funds and capital guaranteed funds were abolished, foreign investment funds were allowed to enter into repo and reverse repo transactions in foreign OTC markets and fund service units were regulated.
- Regulations were made concerning collateral deposited by portfolio management firms due to capital market activities with a communiqué.
- New regulations were made to enable repo and reverse repo transactions on certain shares in the organized market and to ensure the final purchase and sale and delivery of shares that were purchased through such transactions.
- In order to ensure development of capital markets, works were maintained within the framework of "Capital Market Institutions Investor Campaign Cooperation Protocol" signed by other institutions together regarding enhancing investor base and financial education. Also, "Capital Market Information And Awareness Investigation" were realized.
- In the context of cooperation with regulatory authorities in other jurisdictions memorandum of understanding have been concluded with the regulatory authorities of

Korea, Maldives and Tunisia. Furthermore, upon requests received training programs have been conducted for certain foreign regulatory authorities.

The list of actions to be carried out in the period of 2013-2015 in order to increase supply and demand in capital markets, ensure confidence and stability in the markets, create legislation in compliance with the EU and international standards, and establish necessary infrastructure for implementation of this legislation are as follows:

- After the new Capital Markets Board has been passed by the Parliament, secondary regulations that will ensure harmonization with the EU acquis and catering to the needs of the market will be completed.
- Regulations will be made in relation to classifying financial services in line with the EU acquis and enabling financial intermediaries to restructure themselves in a flexible manner that will cater to the needs of their clients.
- Studies on establishing Takasbank as a central counterparty will be continued.
- Regulations on ratings in relation to capital markets and institutions that provide ratings will be revised in line with the EU acquis, international developments and market needs.
- A comprehensive monitoring system in relation to derivatives, including warrants and single stock options, which are expected to begin trading before the end of 2012 is planned to be implemented.
- In order to achieve efficiency in the detection and prevention of market abuse, the Communiqué on Market Abuse will be published, after the new Capital Markets Law comes into force. In line with the provisions of this communiqué and using additional regulations that will be made by the ISE, the CMB intends to take more effective measures in relation to market abuse.
- To develop the legal infrastructure and raise awareness on national level studies regarding interest-free financing instruments, works will be conducted in cooperation with the Islamic Development Bank.
- Further memorandum of understanding will be concluded and bilateral cooperation opportunities will be explored with foreign regulatory authorities. Studies will be conducted to enable the systematic provision of training and experience sharing programs for foreign regulatory authorities.

4.2.3. Insurance Sector

Solvency II Committee was established on February 2009 in order to inform the insurance sector about Solvency II by Undersecratariat of Treasury. The committee members consist of representatives from the Undersecretariat of Treasury, Turkish insurance sector, Turkish Actuarial Society and independent auditing firms.

On the other hand, QIS 5 studies were initiated in the Turkish insurance sector with a conference held in 10th of December 2010 and finalized in June 2011 by participation of 43 insurance companies. In the coming period, Solvency II issues will be on the agenda and necessary preparations will be made in order to comply with Solvency II.

National Insurance Symposium “Past, Present and 2023 Targets and Expectations of Insurance Sector” was organized in 28th of May 2012, which corresponds to our “National Insurance Week”. In this Symposium, activities that will be carried out within the scope of action plans that are envisaged in Insurance Awareness and Promotion Strategy and steps that will be taken regarding these activities are shared with institutions and organizations in the sector. In national insurance week, in order to improve public awareness on insurance, awareness programs to various parties (traders, craftsmen, industrialists and university students) are organized throughout Turkey. Similar programs will be organized by Undersecretariat of Treasury in the coming period.

4.3. Labor Market

Within the framework of a sustainable growth focused on employment, developing employment opportunities in line with the requirements of a competitive economy and information society, reducing unemployment, attaining a more flexible labor market structure while maintaining security, establishing an effective relationship between education and employment and extending active labor program are the main priorities.

As of 31 December 2011, 55.8 million people out of a total population of 74.7 million are at working age in Turkey. While the share of 0-14 age group in the total population is decreasing, the share of working age population and elderly population is increasing.

With the help of the recent efforts aiming to increase employment and decrease unemployment and rapid GDP growth, rapid recovery observed in the labor market in 2010 has been continued in 2011 as well. According to Household Labor Force Survey in 2011, labor force participation rate increased from 48.8 to 49.9 compared to previous year and reached the highest level since 2002. Labor force increased by 4.2 percent and employment rate went up by 6.7 percent in 2011. Considering the 8.5 percent of growth rate and significant rises in labor force participation rate in 2011, the importance of the increase in employment becomes clear.

Due to the impacts of the global crisis which became evident in the last months of 2008 unemployment rate that ascended 14 percent decreased to 9.8 percent in 2011 and 8.8 percent as of August 2012. Turkey was one of the four countries which could reduce the unemployment rate in 2012 compared to 2008. The others were Germany, Luxembourg and Israel. Furthermore, most rapid decline in unemployment rate was seen in Turkey among OECD countries in 2011, compared to 2009 that global crises reached a peak. In the same period, unemployment rate in EU-27 was around 11 percent. These positive improvements reflected to the non-agricultural and young unemployment rates as well. Non-agricultural unemployment rate declined from 14.8 percent in 2010 to 12.4 percent in 2011 and in the same period young unemployment rate decreased from 21.7 percent to 18.4 percent. As of August 2011, these rates were realized as 11.3 percent and 17.2 percent, respectively.

Table 4.5: Basic Employment and Labor Indicators

(15 + Age, Percent)

	Turkey			EU-27		
	2009	2010	2011	2009	2010	2011
Labor Force Participation Rate (LFPR)	47.9	48.8	49.9	69.0	68.8	69.0
Female	26.0	27.6	28.8	62.0	62.4	63.3
Male	70.5	70.8	71.7	76.3	75.4	75.1
Employment Rate	41.2	43.0	45.0	61.1	60.7	60.9
Female	22.3	24.0	25.6	54.7	54.7	55.4
Male	60.7	62.7	65.1	67.7	66.9	66.8
Unemployment Rate	14.0	11.9	9.8	11.5	11.9	11.7
Female	14.3	13.0	11.3	11.7	12.5	12.5
Male	13.9	11.4	9.2	11.3	11.4	11.1
Rural	8.9	7.3	5.8	-	-	-
Urban	16.6	14.2	11.9	-	-	-
Youth Unemployment Rate (15-24)	25.3	21.7	18.4	20.6	20,6	22.3
Non-Agricultural Unemployment Rate	17.4	14.8	12.4	-	-	-

Source: TURKSTAT, EUROSTAT

The population out of labor force and the number of people who are ready to work but not looking for job have been continued to decrease in 2011.

Analyzing the total labor force participation and employment rates by gender, which are lower than the EU averages but displaying increasing trends, it is observed that these are almost same for male but low for female compared to the EU averages. In 2011, female participation rate increased from 62.4 to 63.3 in EU and 27.6 to 28.8 in Turkey compared to the previous year. At the same period, female employment rate increased by 0.7 percentage points in EU and 1.6 percentage points in Turkey. Despite the recent remarkable improvements in the labor market, female participation and employment rates are still lower than the EU level. With migration to the urban areas from rural areas, women, who were previously employed in agricultural activities in rural areas, can not participate in the labor force due to the insufficiency of their qualifications for urban jobs. Besides, even when they are employed, they generally work with low wages and in the unregistered sectors. This situation crates an impediment in front of the entry of women into the labor market.

Scrutinizing the employment by sectors, it is observed that the highest amounts of jobs were created in construction sector among the non-agricultural sectors. In 2011, while growth rate was 9.4 percent in industry, 11.3 percent in construction, 8.9 percent in services sector and 5.6 percent in agriculture, employment increased by 4.6 percent in industry, 17.1 percent in construction, 5.5 percent in services and 8.1 percent in agriculture sector. The increasing trend in the share of agricultural employment since 2007 continued in 2011 as well.

Table 4.6: Employment Share by Sector

(Percent)

	2010	**2011**
Agriculture	25.2	25.5
Industry	19.9	19.5
Services	48.6	48.0
Construction	6.3	7.0

Source: TURKSTAT

In line with the improvements in the labor market, informal employment rate decreased by 1.1 percentage point and dropped to 42.1 percent, while this rate in non-agricultural sectors decreased by 1.3 percentage points and declined to 27.7 percent in 2011.

The main factors behind this favorable development in the labor market have been rapid economic recovery in the post-crisis period, the implemented employment packages and the employment measures in the Law No.6111.

Although labor productivity increased in the recent periods in our country, it is still much lower than the level of EU countries due to reasons such as the low quality of vocational education, inadequacy of on-the-job training and lifelong education activities, deficiencies in capital accumulation and technological renovation processes. According to ILO data, labor productivity, which is calculated as the purchasing power parity adjusted GDP per hour worked, increased to 23.9 dollars from 10 dollars between the years 2002 and 2011. However, this figure stands at 55 in France, 47.2 in Italy, 48.9 in Spain, 43.5 in England and 45 in Germany in 2011.

Labor Health and Safety Law No. 6331 was enacted on 30 June 2012.

In line with the EU and ILO norms and standards and amendments on the Constitution of Republic of Turkey which were made with regard to collective labor law by the Law No.5982 Unions and Collectıve Labor Contract Law entered into force on September, 2012.

Considering the fact that labor force participation rates increase along with education level, increasing schooling rates has utmost importance. In the recent periods, the schooling rates have increased significantly. Demand for vocational and technical education, which has an importance for the labor market, increased in the recent years with the reforms especially at the level of secondary education.

Table 4.7: Trends in Gross Schooling Rates

(Percent)

	1998-1999 (1)	2010-2011	2011-
Pre-School (2)	10.2	45.3	46.4
Primary Education (3)	94.3	107.6	108.4
Secondary Education (3,4)	57.1	93.3	92.6
- Standard High Schools	32.2	52.6	51.9
- Vocational-Technical High Schools	24.9	40.7	40.7
Higher Education Total (5)	16.3	72.5	81.6
- Formal	9.0	38.2	42.9

Source: Ministry of National Education. Higher Education Council (YÖK)
(1) Compulsory basic education was extended to 8 years.
(2) Calculated for 4-5 age group.
(3) Air-correspondence primary and high school students are included.
(4) Starting from 2008-2009, 14-17 age group is used for the calculation of schooling rates.
(5) These figures include students in universities and other education institutions but exclude graduate students; for 17-20 age group.

In Turkey in 2011, 63.2 percent of the labor force, 68.3 percent of the employed people, and 57.8 percent of the unemployed people have less than high school education including the illiterate. The mismatch between labor supply and demand due to the low qualification and productivity of the existing labor force is an important factor reducing the efficiency of labor market.

Table 4.8: Education Level of the Labor Force in 2011

(Percent)

	Labor Force	Employed	Unemployed	Labor Force Participation Rate	Employment Rate	Unemployment Rate
Illiterate	4.5	4.8	2.1	20.5	19.6	4.6
Pre-High School	58.7	59.0	55.7	47.8	43.3	9.3
High Schools	10.4	10.0	13.4	52,1	45.5	12.6
Vocational and Technical High Schools	9.7	10.0	10.9	65.5	58.3	11.0
Higher Education	16.7	16.2	17.9	79.3	71.0	10.4
Total	**100.0**	**100.0**	**100.0**	**49.9**	**45.0**	**9.8**

Source: TURKSTAT

Active labor policies aimed at improving skills of the individuals who have low qualifications and difficulties in entry to the labor market, creating jobs and training the labor force maintain their importance. Hence, the resources allocated for active labor program are increased in Turkey. The expenditures made by İŞKUR within the scope of active labor program reached almost 409 million TL in 2011 and 608 million TL as of August 2012.

Table 4.9: Active Labor Force Programs Provided by İŞKUR

	Expenditure (Thousand TL)	Number of Beneficiaries
2006	27,974	17,106
2007	29,672	22,834
2008	35,511	31,927
2009	30,366	213,852
2010	392,644	211,627
2011	408,597	250,016
2012*	607,903	284,098

Source: İŞKUR
* As of August 30, 2012.

2,799 job and occupation consultants were employed by İŞKUR's local offices in 2011 and 2012 additional 1,201 job and occupation consultants will be employed.

In 2011, 87,680 unemployed people received training in 3,864 training courses organized by İŞKUR. 60,695 unemployed people received training in 2,652 courses with employment guarantee. Within the scope of the Public Works Programmes, 59,906 people received training in 2,293 courses. Entrepreneurship training was provided to 23,314 people for starting up their own business in 872 courses. Besides, 4,240 disabled and 4,438 convict and ex-convict unemployed persons were provided vocational training by İŞKUR.

Some progress was achieved in employment of women having problems regarding entrance into labor market in 2011. As a matter of fact, while 49,697 unemployed women registered in İŞKUR was placed in jobs in 2010, this figure increased to 101,708 in 2011. There was a significant increase in employment of disabled persons, who constitute another group having problems in entering to the labor market, in 2011 compared to 2010. While 32,257 disabled people were placed in jobs in 2010, 38,349 disabled people were placed in jobs in 2011.

Labor market research conducted by İŞKUR since 2007 need to be reviewed to contribute to the design and implementation of active labor program in accordance with the needs of market at national and local level.

The Operation of Improving Quality of Public Employment Services aims to improve the quality and effectiveness of public employment services by means of increasing institutional and administrative capacities of İŞKUR, Provincial Employment and Vocational Education Boards.

Preparation works of National Employment Strategy aiming improvement of labor market, decreasing unemployment and increasing skilled employment is planned to be completed by the end of 2012 with the coordination of Ministry of Labor and Social Security and with the contribution of social partners. This strategy is especially targeting to improve flexicurity perspective in working life.

National and international markets increasingly demand labor that is creative, has high analytical thinking abilities, can quickly adapt to new skills and can use information and communication technologies effectively. In this context, compulsory education is extended to 12 years and new curricula in order to increase the quality of education are being implemented. New elective course programs are developed in primary and secondary education. On the other hand although the quality and quantity of in-service training for teachers are inadequate work is on progress to make it effective.

In Turkey, there is a need to support formal and mass education with technologies, increase informatics literacy qualities of teachers and students and develop information and communication technology infrastructure in schools in order to equip students with technological competences. In this context Education and Technology Improvement Action to Increase Opportunities (FATİH) project is initiated and students and teachers access to technology is increased. Efforts are continuing to provide effective use of Information Technology (IT) classes in education and disseminate broadband internet access services to all schools and educational institutions.

It is of utmost importance to effectively direct vocational and technical education to provide the qualified intermediate labor force required by the labor market. The share of students in vocational and technical education increased to 47.95 percent by the 2011-2012 academic year. Vocational and technical secondary education school programs are prepared and implemented in a modular structure which is responsive to the needs of the labor market, flexible and competency-based. In order to maximize the usage of the vocational and technical education institutions, full-time full-year education principle is introduced. In addition, combination of secondary-level vocational and technical educational institutions under the Ministry of National Education with the new organizational law of the General Directorate of Vocational and Technical Education has been an important development in terms of increasing the efficiency of these institutions. Following this development, expectations has increased about a formation of structure in the real sense, in terms of programs rather than different types of school. Facilitating transitions between the different educational levels in order to reduce drop outs of students from system Students and compensating failures, understandable and encouraging system approach should be adopted. To address this approach in an integrated manner and carry out practices within the vocational and technical education Vocational Education and Training Strategy are being prepared. Also in the context of Vocational High Schools to be more efficient work is in progress.

Efforts continue to develop the capacities of Professional Qualifications Agency to manage the national professional qualifications system. The Professional Qualifications Agency, which is an important part of the national competences system, began its works for improving the professional standards by considering the needs of labor market and for making certification after evaluating the students. Also preparation of National Qualification Framework is in progress. In parallel with the increase in the published occupational standards there is a need in accelerating exam, accreditation and certification activities.

The Lifelong Learning Strategy Document was accepted by the High Planning Council decision dated 5 June 2009 and put into implementation. In this context, legislation and awareness activities for the promotion of lifelong learning in provinces are continuing.

Furthermore, the “Action Plan for Enhancing the Relation between Employment and Vocational Education”, which was prepared with participation of all relevant partners in coordination with the Ministry of Labor and Social Security in order to provide the vocational and technical education in line with the needs of labor market, implement active labor market policies effectively, increase employability of the labor force by means of overcoming the problem of vocational competence, entered into force. Within the framework of the action plan an effective monitoring and evaluation committee is created, legislative regulations have been made and integration of the databases that are monitoring the graduates are in progress.

On the other hand, with the cooperation of the Ministry of Education, Ministry of Labor and Social Security, TOBB and İŞKUR “Specialized Vocational Training Centers” project which is implemented since 2010, 111 vocational and technical high schools in 81 provinces are equipped in terms of machinery and infrastructure. It is aimed to increase, the quality of formal education and vocational training courses through providing in-service training for the teachers in accordance with the renewed equipment and labor market demands.

In addition, with the amendment to the Law No.5580, it is decided that support will be provided for each student training in vocational and technical education schools that are opened in organized industry zones. In this context, the Ministry of Education and the Ministry of Science, Industry and Technology signed a protocol in order to strengthen vocational education and training in organized industry zones.

Flexible working conditions prevalent in EU countries can not be practiced effectively in our country. Dissemination of flexible working conditions is of particular importance to increase employment, reduce unemployment and informal employment, and increase employment of women and disadvantaged groups within the context of social inclusion. Within this framework, the need to encourage flexible working forms and to strengthen their relation with social security maintains its importance. In this context, some of the priorities that is planned to be implemented in the next years are following:

- Regulations that will enable to flexible working forms such as tele-working, telecommuting, job-sharing and flexible working hours model will be enacted as well as other forms in the Labor Law and these working types will be more spread and implemented.
- Severance Payment Fund will be established thereby preserving the acquired rights of workers and competiveness of enterprises within the sustainable actuarial balance.
- The Economic and Social Council will be restructured in order to increase the efficiency of existing social dialogue mechanisms in our country.
- In line with the increase of resources allocated to İŞKUR under the active labor market programs, the physical environment and qualified staff needs of İŞKUR Provincial Directorates will be met in order to ensure that these programs are implemented more

efficiently and the quality of services provided by İŞKUR is improved. Furthermore, the career counseling services offered by İŞKUR will be scaled up and streamlined.

- The activities of private employment agencies will be diversified. In this context, ongoing works about required regulations that enable these agencies to contract temporary work will be finalized.

Table 4.10: Matrix of Policy Commitments: Labor Market

(1000 Euros)

	2011	2012	2013	2014	2015
1. Encouraging Employment of Young People Operation					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-140	-863	-100	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-140	863	100	---	---
2. Improving Quality of Public Employment Services Operation					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-894	-631	-375	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	894	631	375	---	---
3. The Women Employment Support Operation					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-915	-50	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	915	-50	---	---	---
Total Net Budgetary Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-1.949	-1.544	-475	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	1.949	-1.544	-475	---	---

4.4. Agriculture Sector

4.4.1. Agriculture

The basic objectives of agricultural policies are; to ensure food security and safety and to form a sustainable agricultural structure that is harmonized with the EU.

In this context, while the policy instruments are implemented to direct production according to demand, priority will be given to the necessary transformation of the agricultural structure in order to cope with the competition in the Union after Turkey's accession. Within this scope, significant supports contributing to the structural transformation in the agriculture sector are given in Table 4.11. In addition, projects for increasing the contribution of these supports to achieve sustainable agricultural structure and technical support provided under the EU Financial Cooperation are given in Table 4.12.

The legislation related to the establishment and duties of Ministry of Food, Agriculture and Livestock replacing the Ministry of Agriculture and Rural Affairs was enacted by the Decree Law No. 639, dated June 8, 2011. Raising the institutional and human capacity of the Ministry has been an ongoing process in 2012.

Agricultural supports have been implemented pursuant to the Agricultural Law No. 5488 of 2006. Conditional area-based payments, like payments for organic farming, soil analyses, Environmentally Based Agricultural Land Protection (ÇATAK), use of certificated seed and seedling and unconditional area-based payments like diesel and fertilizer support have been phased in so as to guide agricultural production after 2004.

The share of area-based payments in total support budget was 49.3 percent in 2007 and realized 31.7 percent in 2012. In 2013, this share is estimated to be 28.9 percent.

Further, in order to provide structural transformation that is necessary for competitiveness of livestock sector within the Union after full membership, the share of livestock supports in total support budget has been increased from 14 percent in 2007 to 28.5 percent in 2012 and is foreseen to be 27.5 percent in 2013. In this context, area-based fodder crops support payments, milk incentive premium, payments per head of pure bred cows and additional payment implementations in case of registration and of being disease-free were foreseen.

Moreover, deficiency payments and payments for rural development have been carried forward in 2012.

In addition to implementation of the cattle identification system, Tagging and Vaccination of Sheep and Goats Project with the EU grant was started in 2009 for identification of sheep and goats, second phases of Rabies Control Project and Foot and Mouth Disease Control Project were launched in 2011. Works related to these projects are still in progress. However, "Control of Foot and Mouth Disease - 2nd Phase" project that was envisaged to be implemented all over the Turkey was limited to only the Thrace Region by an arrangement made in 2012. Re-allocation studies are ongoing. Besides, Restructuring of Border Inspection Posts Project, which commenced in 2007 within the scope of EU Financial Cooperation in order to improve related administrative capacity, has been completed, but the efforts for the elimination of the deficiencies related to the organizational capacity are carried on.

Moreover, works on the establishment of land parcel identification system which is main instrument of Integrated Management and Control System are followed within the framework of Investment Programme.

The share of Supports Programme for Rural Development Investments, which is implemented in order to establish institutional capacity for implementation of EU Rural Development Policies, had a share of 1.4 percent in total support budget in 2007 and it is foreseen to be 4.4 percent in 2013 including national co-finance contribution for rural development programme in the EU Pre-Accession Financial Instrument. While there is a need to differentiate this practice considering regional characteristics, it is also essential to consider the complementarity of this programme with similar one expected to be realized in the coming period within the scope of the EU Financial Cooperation.

In the framework of above mentioned issues, taking into consideration the requirements of EU accession process, a support strategy will be prepared together with a schedule that would enhance predictability with respect to the development of an infrastructure. The ultimate goal will be subsidies based on registered agricultural holdings with the capability of area-based administration and control, and ensuring efficiency and quality improvement through registration that will enable structural transformation in animal husbandry and transforming animal stock to pure culture breed.

In the fisheries sector, priority will be given to improving the institutional structure, increasing the effectiveness of resource management in capture fisheries and ensuring environmentally friendly production in aquaculture. In this context, Fisheries Law will be amended in order to ensure sustainable fisheries and the compliance with EU Common Fisheries Policy. In addition to that, the works on construction of offices at the landing points, improvement of fisheries information system and spreading the usage of remote sensing method for ensuring the effectiveness of control services have been continued.

The harmonization works related to the food safety, veterinary services and phytosanitary legislation with the EU acquis and international standards are proceeding within the framework of the strategy determined within the scope of the opening criteria of Chapter 12. The food control system is reinforced via public investments through modernization of laboratories and application of new analysis methods as well as accreditation works. The compliance of animal originated food processing enterprises with the EU food legislation is primarily considered within the framework of

Law No. 5996 and secondary legislation. After the procedures and support mechanism of upgrading of food enterprises having deficiencies are put into effect, modernization programmes will be realized by these enterprises.

The privatization process of public sugar factories is still in progress and finalization of amendments on sugar sector legislation are expected in order to activate quota management and supervision.

Table 4.11: Matrix of Policy Commitments: Agriculture-I (Main Developments in Agriculture Support)

(1000 Euros)

	2011	2012	2013	2014	2015
1. Area Based Supports					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-967,407	-1,056,522	-1,151,556	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	967,407	1,056,522	1,151,556	---	---
2. Supports for Livestock Sector Pursuant to the Decree 2005/8503					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-721,881	-1,043,478	-1,095,111	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	721,881	1,043,478	1,095,111	---	---
3. Support for Rural Development Investments					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-130,544	-134,348	-177,333	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	130,544	134,348	177,333	---	---
4. Agricultural Insurance					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-103,743	-126,087	-140,444	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	103,743	126,087	140,444	---	---
Total Net Effect on Budget					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-1,923,575	-2,360,435	-2,564,444	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	1,923,575	2,360,435	2,564,444	---	---

Source: 2013 Annual Programme.
Note: The values of agricultural support budget in 2013 Annual Programme are converted to euro by using average exchange rates with respect to related years.

Table 4.12: Matrix of Policy Commitments: Agriculture - II (Important Projects in Agriculture [1])

(1000 Euros)

	2011	2012	2013	2014	2015
1. Restructuring the Border Inspection Points Project					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	---	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	---	---	---	---
2. Controlling of Rabies Project (2)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	1,276	360	28	0	0
B.1. Direct Effect on Budgetary Revenues	1,549	443	50	0	0
B.2. Direct Effect on Budgetary Expenditures	273	83	22	0	0
3. Tagging and Vaccination of sheep and goats					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	4,821	6,243	0	0	0
B.1. Direct Effect on Budgetary Revenues	4,871	6,625	0	0	0
B.2. Direct Effect on Budgetary Expenditures	50	382	0	0	0
4. Avian Influenza and Human Pandemic Preparedness and Response					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-5,872	---	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---

B.2. Direct Effect on Budgetary Expenditures	5,872	---	---	---	---
5. Land Parcel Identification System Project					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	11,292	11,162	11,735	-1,936	-1,951
B.1. Direct Effect on Budgetary Revenues	13,299	13,010	13,954	0	0
B.2. Direct Effect on Budgetary Expenditures	2,007	1,848	2,219	1,936	1,951
6. Combatting Against FMD Project (2)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	8,558	8,917	1,080	2,006	0
B.1. Direct Effect on Budgetary Revenues	10,392	10,874	1,124	2,222	0
B.2. Direct Effect on Budgetary Expenditures	1,834	1,957	44	215	0
Total Net Effect on Budget					
A. Implementation Profile		---		---	
B. Net Effect on Budget	20,075	26,682	12,843	3,943	-1,951
B.1. Direct Effect on Budgetary Revenues	30,111	30,952	15,128	2,222	0
B.2. Direct Effect on Budgetary Expenditures	10,036	4,270	2,285	2,152	1,951

(1) In EU-funded projects, impact on budgetary revenues results from EU contributions with grant and investment component in the related projects.
(2) Second phase implementation of projects were commenced in 2011.

4.4.2. Rural Development

In the Ninth Development Plan period (2007-2013), the main objective of the rural development policy is to enable rural communities to achieve sustainable working and living conditions in its region. The efforts to finalize the monitoring and evaluation structure of the Rural Development Plan, prepared in accordance with stated aims continue.

The process of accreditation and conferral of management of the Agriculture and Rural Development Support Institution for the center and 20 provincial offices, which implement the 1st phase of the IPA Rural Development Programme (IPARD Programme) covering the period of 2007-2013, has been completed. In the 22 provinces where implementation will start in the 2nd phase of the programme, physical infrastructure and personnel are ready and accreditation process has been completed, and application for delegation of authority has been submitted to the European Commission. As of the last quarter of 2012, a total of 7 call for projects has started and 5 of them have been finalized. 646 project applications have been received in the first 5 calls and grant contracts have been awarded for 251 winning projects, which cover support for about 186 million TL. Project selection for the 6th, 7th and 8th calls currently proceed.

The implementation of the projects contributing to acceleration of rural development in Turkey; Sivas-Erzincan Development, Anatolian Water Basins Rehabilitation, Diyarbakır-Batman-Siirt Development, Ardahan-Kars-Artvin Development, Improving Life Conditions of Small Scaled Farmers in East Black Sea Region, Çoruh River Basin Rehabilitation, GAP Integrated Rural Development and Identification and Expanding of Local Structure and Architecture in Rural Areas, continue.

Grant schemes in the areas of agriculture and rural development, which became ubiquitous, partially thanks to EU accession process, continue. Currently the most important ones are Rural Development Investment Support Programme (KKYDP) managed by the Ministry of Food, Agriculture and Livestock, IPARD assistance implemented by the Agriculture and Rural Development Support Institution and grant schemes of development agencies.

A resource of 550 million TL was allocated in 2012 for the Village Infrastructure Support Project (KÖYDES), which have been implemented in 79 provinces in order to eradicate the road and drinking water infrastructure problems of villages and sub-villages, other than Istanbul and Kocaeli provinces, since 2005. The allocation in 8 years has been 7.94 billion TL. Projects on small-scale irrigation and sewerage systems were included in KÖYDES in 2010 and 2011.

4.5. Administrative Reform

4.5.1. Strategic Planning and Performance Based Budgeting

All the public institutions, except five, have prepared their first strategic plans in parallel to the transition program which is laid down in the Regulation on Principles and Procedures regarding Strategic Planning in Public Administrations. Preparations of strategic plans in new public institutions have been continuing.

Preparation of strategic plans by the State Owned Economic Enterprises (SEEs) is decreed by the General Investment and Financial Programmes of 2008 and 2009 upon the Decision of the Council of Ministers. Within this scope, 15 out of 19 SEEs completed their strategic plans as of December 2012 and works are in progress in the remaining four.

Stakeholder Engagement in Strategic Planning and Policy Making Project made by the Ministry of Development is finished. Within the scope of the project, the current status of engagement is assessed, a framework aimed at determining how engagement can be more beneficial in strategic plan assessments made by the Ministry of Development is developed and training programmes and panel discussions aimed at increasing awareness about engagement are organized.

By-law on the Procedures and Principles of Strategic Planning in Public Administrations which was enacted in 2006 and the Strategic Planning Guide for Public Administrations will be reviewed in the light of the previous studies and experiences, and necessary amendments will be made in 2013 in order to overcome the problems encountered and to enable the system function more effectively.

Preparation works for the IPA project titled as Improved Strategic Management Capacity for Central Administrations were completed and the project is currently at the bidding phase. Implementation of the project is expected to start by the end of year 2012. By this project, capacity improvement activities, for the Ministry of Development, other administrations having central guidance role and administrations under the obligation of preparing strategic plans, will be carried out in the area of strategic planning. Besides, a monitoring and evaluation system will be set up for strategic plans.

The performance programmes prepared by the administrations which completed their strategic plan works based on the By-law on the Performance Programmes to be Prepared by Public Administrations and the Performance Programme Preparation Guide regulated by the Ministry of Finance pursuant to the Law No.5018, shall be submitted to the Plan and Budget Commission in order to be evaluated together with the budgets of the related administrations during the meeting on the Draft Law regarding Central Management Budget.

In this context, the General Directorate of Budget and Financial Control of the Ministry of Finance developed a Performance Budget Module within the e-budget system in order to create cost tables with parameters of the performance programme, provide infrastructure in establishment of budget connection and to collect and report the data centrally. Besides, the Performance Monitoring and Evaluation section has been added to the mentioned module and put into service for the use of public administrations in order to monitor, evaluate and report the performance programmes. In this regard, the process of monitoring, evaluating and reporting the performance programmes has started. The performance programmes of 76 public administrations, among 2012 final performance programmes sent to the Ministry of Finance, have been examined and evaluated. These evaluations have been shared with public administrations for providing guidance in preparation of their performance programmes.

In addition to technical assessments, Ministry of Finance monitors implementation and realization level of performance programmes.

4.5.2. Economic and Social Council

Efforts are continuing to make changes in Economic and Social Council Law to make the ESC more functional, with more participation in the context of European Union standarts.

4.6. Other Reform Areas

4.6.1. Regional Development

One of the five development axes defined in the Ninth Development Plan of Turkey covering the period of 2007-2013 is Ensuring Regional Development. In the framework of development approach based on local dynamics and internal potential, the main objectives of regional development policies are as follows:

- making central-level policies more compatible and effective,
- increasing institutional capacity at local level,
- disseminating economic development and social welfare across the country in a balanced way,
- directing inter-regional migration propensity towards intra-region,
- ensuring balanced distribution of the population in space,
- establishing a healthy urbanization structure,
- reducing socio-economic development disparities between urban and rural areas by enhancing welfare in rural areas.

Preparation studies for National Regional Development Strategy aiming to ensure national level coordination of regional development and competitiveness, to strengthen the compliance between spatial and socio-economic development policies and to create a general framework and guidance for the regional and local scale plans and strategies, is ongoing.

The Research on Socio-Economic Development Ranking of Provinces and Regions (SEDI-2011), previously released in 2003, was completed. This research was the base for the regional supports under the new Support Scheme announced on April 6th, 2012.

Eastern Anatolia Project Regional Development Administration, Konya Plain Project Regional Development Administration and Eastern Black Sea Project Regional Development Administration, which were established in 2011, have primarily concentrated on institutionalization activities. On the other hand they also conducted planning, programming, and coordination activities.

Particularly in the less developed regions, Growth Centers that have high growth potential and that can serve to their periphery are determined. Works for the better accessibility of these centers and fortification of their physical and social infrastructures have continued. Studies for the special support programme that started in 2008 have been continued also in 2012. Pilot application of the programme has been commenced in Diyarbakır in 2008. The total fund allocated for Diyarbakır is 68,45 million TL until 2011. Furthermore, as part of the programme implementation which is extended to Erzurum, Şanlıurfa and Van provinces, 36,45 million TL were allocated to Erzurum, 45,95 million TL to Şanlıurfa and 38,65 million TL to Van in 2010 and 2011. Budget of the programme for 2012 is 80 million TL.

In the GAP region, the amount of investment allocated at the beginning of 2008 increased to 2 billion TL from 1 billion TL in the mid-year as a result of the entry of GAP Action Plan into force. In 2009, 2010, 2011 and 2012, 3 billion TL, nearly 4 billion TL, 4.3 billion TL and 4.7 billion TL were allocated for total investments in the region respectively. As a result, share of investments in the region in the total public investments rose to approximately 14 percent from the level of 7 percent along with the start of implementation of GAP Action Plan.

For GAP AP, there is a need for financial resource amounting to 27.2 billion TL in terms of 2011 prices in the period of 2008-2012 for the projects and activities more than 300. It is envisaged that 23.6 billion TL of this resource will be allocated from the central budget. Allowance for the investments within the scope of GAP AP in 2008 was 1.9 billion TL. The total allowance allocated to the activities within the scope of GAP AP was 2.66 billion TL, 3.8 billion TL, 3.9 billion TL and 3.6 billion TL for the years 2009, 2010, 2011 and 2012 respectively.

Establishment of development agencies which are considered an important tool in regional development policies was completed in all NUTS II regions. On the first stage, the agencies have focused on institutional capacity building, publicity and rising awareness activities. The agencies began rapidly to work for determining priority areas of the region and providing financial and technical support for the projects in these areas.

- Project supports which have been provided since 2008 by development agencies are increasing in terms of the number of supporting agencies, number of supported priority areas and projects and amount of support.
- As of November 2012, four agencies made 11 calls for proposals, which were amounting to 146.3 million TL. 79 out of 354 project applications were selected among 2 of these calls for proposals. Project application and selection process for the rest of calls are continuing.
- In addition, the agencies provide direct activity support and technical support in the regions. Consolidated table for the financial support is given below.

Table 4.13: Information on Regional Development Agencies

Grant Programme/Direct Financial Support Provided by Development Agencies (Million TL)				
Year	**Priority Area**	**Grant Amount***	**Project Application**	**Supported Projects**
2008	6	42.2	1,129	240
2009	9	83.3	2,576	398
2010	55	342.9	9,471	1,653
2011	64	288.9	6,048	1,716
2012**	11	146.3	354	79
Total	145	903.6	19,941	4,100
Direct Activity Support Programme (Million TL)				
Year	**Number of Programs**	**Grant Amount***	**Project Application**	**Supported Projects**
2009	1	0.3	11	6
2010	8	4.5	560	109
2011	26	18	1,302	392
2012**	18	14.6	371	118
Total	53	37.4	2,244	625
Technical Assistance Programme (Million TL)				
Year	**Number of Programs**	**Grant Amount***	**Project Application**	**Supported Projects**
2010	8	3.3	783	513
2011	17	6.4	1,500	883
2012**	18	6.3	529	224
Total	43	16	2,812	1,620
Number of Staff in Development Agencies				
Year	**General Secretary**	**Internal Audit**	**Specialist**	**Officer**
2012***	23	12	762	156
Total	953			

* Contractual for 2008-2011 period, declared for 2012.
** Process is continuing.
*** As of November 2012.

Project and Activity Support module in Development Agencies Management System (DAMS) was brought into the use of development agencies. Software development works are continued for other modules. Electronic Documentation and Archive Management System under DAMS was set up in all 26 agencies during March-November 2012. Studies to develop a system infrastructure for making electronic correspondence between the Ministry, agencies and the Regional Development Administrations are continuing.

In order to ensure effective, efficient, transparent and accountable functioning of the IPA system in Turkey and to contribute to the preparations of Turkey for the EU Cohesion Policy, technical assistance project entitled as Capacity Improvement in Economic and Social Cohesion Policy (ESC-II) have been implemented. Within the context of the project, capacity building activities for the institutional actors took part in the implementation of components III and IV of IPA and preparations for Structural Funds are undertaken. Furthermore, activities to increase the effectiveness of development agencies in using the funds under EU financial cooperation are implemented.

Studies on the design and infrastructure of Province Coordination and Monitoring System (PCMS), developed for handling investments and socio-economic developments in a local and regional development perspective, has been finalized within the framework of TUBİTAK Programme for Supporting Research and Development Projects of Public Institutions. The project was commenced on 1 March 2009. The first prototype was put into operation as of 4 February 2010 and the second one in 21 October 2010. Currently, there are nearly 7,000 users of the system in 81 provinces. Additional system development, maintenance and support activities will be continued.

Table 4.14: Matrix of Policy Commitments: Regional Development

(1000 Euros)

	2011	2012	2013	2014	2015
1. GAP Action Plan					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-1,481,071	-1,603,591	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	1,481,071	1,603,591	---	---	---
2. Development Agencies					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-43,059	-195,832	-209,841	-214,663	-220,292
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	43,059	195,832	209,841	214,663	220,292
3. KÖY-DES					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-236,824	-239,350	-256,450	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	236,824	239,350	256,450	---	---
Total Net Effect on Budget					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-1,760,954	-2,038,773	-466,291	-214,663	-220,292
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	1,760,954	2,038,773	466,291	214,663	220,292

4.6.2. Health and Social Security Reform

4.6.2.1. Health Transformation Program

The first part of Health Transformation Project which has implemented since 2004, was completed in 2009 and carried out with World Bank in order to support the Health Transition Programme. Health Transformation and Social Security Reform Project, which is continuation of the Health Transition Project, was started on the second half of 2009 and will be ended in 2013.

Within the framework of the Health Transformation Programme, institutions responsible for implementing provision of health services have been restructured. In this context, central and local organization of the Ministry of Health re-arranged with the Law No. 663 on the Organization and Duties of Ministry of Health and Its Affiliates dated on 11 February 2011. Aiming to carry on works related to primary health care services, prevention and control programs for communicable diseases and non-communicable diseases and consumer & employee safety, Turkey Public Health Agency has been established instead of Refik Saydam Hygiene Centre by this law. Turkey Public Hospitals Authority was established in order to carry out tasks such as implementing the processes of establishing, operating, merging and separation of hospitals, oral and dental health services and similar organizations; ensuring the establishment and operation of public hospital unions which will be established within the Authority; planning human resources, investment and fiscal issues of its affiliated organizations. Turkey Pharmaceuticals and Medical Devices Agency is established in order to do licensing of Pharmaceutical, biological products, medical devices and cosmetic products, make regulation and supervision, and develop strategies and projects.

Avoiding deterioration of health and premature deaths due to chronic disease, Ministry of Health has put into implementation programs such as Turkey and Cardiovascular Diseases Prevention and Control Program, Turkey Diabetes Prevention and Control Program, Turkey Chronic Respiratory Diseases (Asthma-COPD) Prevention and Control Program. Obesity Prevention Program and The National Action Plan, Fight Against Tobacco, National Cancer Control Program, and the National Mental Health Action Plan. In addition, in the context of Healthy Eating and Active Life Programme in Turkey for the period 2010-2014, in order to prevent an unbalanced diet and obesity for children, foods and beverages having high energy density but low-nutrient have been prohibited in school canteens and cafeterias. With this regard, milk, ayran, yogurt, fruit juice, freshly squeezed fruit juice and fruit have been mandated.

124,085 patients have been reached so far within the scope of Home Health Care Services and 80,388 active patient have been following. Moreover, it is expected that 150,000 patients will be reached in 81 provinces.

Family Medicine Information System has been started to be used in all 81 provinces and the integration of data collected from the hospitals has been largely completed. Central Hospital Appointment System (MHAS) has been extended to all around the country.

While the rate of public health expenditures to GDP was 3.7 percent in 2002, this rate was 4.5 percent in 2011, and it is expected to be 4.4 percent in 2012. In order to follow medicine and medicine expenditures, Medicine Following System, which is the first common implementation in the world for tracing all phases of the medicine with data matrix system, was developed in 2010. The first phase of MFS including compulsory production notice from producers and consumption notice from consumers was as of 1 January 2010. The second phase in which all stakeholders have to do the production, import, sale, disbursement, repayment, deactivation, buying endorsement, export and sale cancellation notices has started.

4.6.2.2. Social Security Reform

The efforts to make social security system having a structure that has fiscal sustainability, effective audit mechanism and enabling it to provide quality services continue within the Social Security Institution. In this regard, the works started by SSI in order to make all insurance processes in automation are under way.

Health services of public personnel were taken over by SSI as of 15 January 2010. Thereby, the public personnel have been taken in the scope of General Health Insurance. People who are under the coverage of Green Card system which allows the citizens not having power to pay to benefit from health services, are started to be taken to the scope of General Health Insurance as of 2012.

Table 4.15: Matrix of Policy Commitments: Health Care-Social Security

(1000 Euros)

	2011	**2012**	**2013**	**2014**	**2015**
1. Health Transformation and Social Security Reform Project					
A. Implementation Profile	---	---	---	---	---
B. Net Effect On Budget	92,111	95,890	---	---	---
B.1. Direct Effect on Budgetary Revenues	100,000	100,000	---	---	---
B.2. Direct Effect on Budgetary Expenditures	7,889	4,100	---	---	---
Total Net Budgetary Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Effect On Budget	92,111	95,890	---	---	---
B.1. Direct Effect on Budgetary Revenues	100,000	100,000	---	---	---
B.2. Direct Effect on Budgetary Expenditures	7,889	4,100	---	---	---

4.6.3. R&D and Innovation

The main objectives of the science and technology policy are to improve the innovation capability of the private sector, to increase competence in science and technology, and to transform this competence to economic and social benefits. In Turkey, the share of the R&D expenditure in GDP was 0.86 percent in 2011 however, the EU-27 average was 1.84 percent in 2008. It is aimed to increase this ratio to 2 percent in Turkey in 2013. In this context, the public R&D investment, which was 319 million TL in 2003, was increased to 1,830 million TL in 2012 with an increase of 473 percent.

The share of the R&D activities performed by the private sector in overall R&D activities, which was 33.8 percent in 2005, rose to 45.5 percent in 2010. However, considering that this rate is below the EU-27 average of 63.9 percent in 2008, the need for increasing effectiveness of the private sector in R&D activities arises. Within this framework, supports and incentives for R&D projects were increased on the one hand; and the number of the Technology Development Zones (TDZ) and research centers, which were established to bring together the stakeholders that generate knowledge and convert it to new products and processes, and to enable the companies within their structure to benefit from various incentives, were increased on the other hand. As of September 2012, 45 TDZ’s have been established, and 32 of them are operational. Investments are carried on for the establishment and operation of the inactive TDZ’s. The number of the companies operating in the Technology Development Zones rose to 1,936 as of the end of September 2012.

Besides, after Law No.5746 on Supporting Research and Development Activities, which was codified to regulate tax incentives provided for R&D activities entered into effect in 2008 131 R&D Center application were made and 129 R&D Centre Certificates had been issued as of September 2011. The firms received R&D Centre Certificate are expected to make R&D expenditure amounting to 2.5 billion TL and to employ 15,000 R&D personnels in 2012.

It is aimed to increase the R&D capacity and R&D demand of the private sector, particularly SMEs’, in 2013. Improvement of R&D activities which are carried out by private sector will be supported and R&D supports provided for SMEs will be generalized. Pre-competitive R&D collaborations and the programs for enhancing the cooperation among private sector, universities and research institutions will also be supported.

Another matter as important as enhancement of the sources allocated to R&D activities is making up the researcher shortage. In Turkey, while 30.4 percent of the total R&D employees were employed by the private sector in terms of Full-time Equivalent (FTE) in 2005, this ratio rose to 45.9 percent in 2010. At the same time, this ratio was 52 percent for EU-27 countries as of 20008. Share of women researchers in the total researchers in terms of FTE, which is an important criterion for gender equality in working life, was calculated as 34 percent for Turkey in 2007 while this ratio was above the EU-27 average of 31 percent.

The number of academicians will be increased and balanced distribution of them will be ensured across the country within the scope of enhancing researcher human resources. Besides, in order to cover the academician shortage of developing universities, especially the newly established universities, academician development programs will be expanded.

In line with enhancing scientific and technologic cooperation with the EU countries and being a part of European Research Area, Turkey has participated to Seventh Framework Programme on Science and Technology of EU. Turkey continues the preparation efforts for Horizon 2020 Program which is the main science and technology of EU in post-2013 term.

4.6.4. Information and Communication Technologies

Most of the efforts on Information Society Strategy covering the years 2006-2010 and its annex Action Plan have been completed, aiming at transforming Turkey into an information society, one of the main objectives of Ninth Development Plan. In this context, efforts for determining policy and strategy steps to be taken after 2010 are underway.

Within the objective of educating human resources required by information society, the Ministry of National Education has provided broadband Internet access to 96 percent of elementary school students and to all of the secondary school students as of November 2010. The FATİH Project, includes distribution of tablet PCs to primary and secondary school students, provision of interactive boards, laptops, other IT equipment and internet access infrastructure to approximately 620 thousand classrooms. In addition to effective use of ICT in education, the project provides opportunities for improvement of ICT literacy, deployment of broadband access infrastructure and development of software and ICT services sector.

According to the Use of Information and Communication Technology (ICT) in Households Survey announced by TURKSTAT in August 2012, the ratio of individuals using the internet is 47.4 percent, and 45.1 percent of those use the internet to interact with public agencies. According to the ICT Usage in Enterprises Survey published by TURKSTAT in November 2012, ratio of the enterprises that have internet access was 92.5 percent while ratio using the internet to interact with the public agencies was 81.5 percent among these enterprises.

Within the objective of creating more qualified labor force which produces higher value added, the Qualified Informatics Employees Project carried out by İŞKUR aims to train more qualified informatics employees in the areas needed by the information and communication technologies sector by means of the education programmes developed by international ICT firms. As of November 2012, 489 people have been trained in Ankara, Adana, Denizli and Konya. In the provinces of Adana and Denizli 159 people received certificates and 49 people were employed.

Secure electronic signature has been gained the same conclusive force as a handwritten signature, with Electronic Signature Law, No 5070, and related legislation. After that, electronic applications started to be developed in order to support the electronic signature infrastructure. Currently, five electronic certification service providers are active, however the number of the electronic signature users has been increasing steadily due to the increase in the number of applications. As of October 2012, the total number of produced qualified electronic certificates is 677,011. 234,888 of these certificates are being used mobile signatures, which was put into practice in 2007. At present many public and private organizations are using e-signature in their institutional procedures. As of October 2012, the number of active electronic certificates used in these applications is 400,332; 328,235 of these are traditional electronic certificates and 71,097 are mobile electronic certificates.

Regulation on Registered Electronic Mail (REM) System which has been prepared on the basis of the Turkish Commercial Law, No: 6102, is completed. The process of authorization regarding REM service providers is underway. The records which are kept by the Registered Electronic Mail System with secure electronic signature and time stamp for all transactions that occur during transmission from sender to receiver are considered evidence and have legal validity. REM System users have to open an account at any of REM service providers to benefit from the system. The number of electronic signature users is expected to increase when KEP is used actively in Turkey

Thanks to Constitutional Amendment on 2010, the right of demand the protection of personal data has been granted to persons. This right also covers right to obtain, delete, and receive information about proper usage and to request for correction regarding their personal data. According to the Constitutional Amendment, personal data can only be processed, in the cases provided by law or the person's express consent. This amendment also provisioned that principles and procedures regarding personal data, shall be set forth by Law. The Draft Law on Protection of Personal Data became null and void due to expiring of the legislative term. It is expected that the draft law will be updated and presented again to TGNA.

Within the scope of the works carried out in the area of cyber crimes, Turkey signed the Cyber Crime Convention of European Council No. 185 on November 10, 2010. Besides the Cyber Crime Convention, the works regarding approval of the Conventions No. 108 and 181 of the Council will be started.

A Council of Ministers Decision regarding Execution, Management and Coordination of National Cyber Security Activities was issued and published on 20th October 2012, Official Gazette no: 28447. The Decision covers the terms and conditions to which all real and legal persons participating in the operation of critical infrastructure related with information and communication technologies are obliged to abide by. It aims to set the measures to establish the security and protect the confidentiality of both services and operations offered or received via information technologies by public institutions and also relevant systems in the provision of these. The Decision also established a Cyber Security Board chaired by the Minister of Transport, Maritime Affairs and Communications. The Board is responsible for deciding the measures to be taken related to cyber security, ratification of plans, programs, reports, terms, conditions and standards prepared and assuring the application and coordination of these efforts.

Electronic Communications Law numbered 5809 (art. 35) authorizes Ministry of Transport, Maritime Affairs and Communications as the regulator for internet domain names. The Ministry designated ICTA to deploy an IT system for ".tr" and to make necessary regulations for this issue. Studies are in progress to activate this new system, named TRABİS.

As of September 2012, fixed telephone, mobile telephone and broadband subscriber penetration rates are 18.7 percent, 89.9 percent and 26.1 percent in Turkey, respectively. At the same date, the number of subscribers using broadband service over fibre optic connections was 549 thousand. As of the end of September 2012, the number of 3G subscribers reached 40.3 million and the number of subscribers using mobile broadband access services reached more than 11.5 million. As of December 2012, 648 authorizations were granted for 412 operators.

The effectiveness of alternative infrastructure operators in the market and coverage of their fibre optic networks have been increasing lately. The length of fibre optic cables these operators own reached 41,645 km in September 2012, while this figure was 9,216 km at the end of 2008. Within the scope of mobile number portability, 50 million subscribers ported their numbers as of December 2012. This number is 310 thousand for fixed telephone numbers.

In 2012, Turkey has continued its works within the framework of EU Information and Communication Technologies Policy Support Programme, which is one of the components of the Competitiveness and Innovation Framework Programme of EU and to which Turkey has been a party since January 1, 2009.

In line with the policy of transition to terrestrial digital broadcasting, the Law No. 3984 on Broadcasts of Radio and Television Organizations was repealed. In order to comply with the developments in the broadcasting sector and the EU Acquis, the Law No. 6112 Broadcast Services and Organizations of Radio and Televisions was entered into force after being published on the Official Gazette on 3 March 2011.

Draft decree law aiming gradual liberalization of the postal services market; establishment of an effective competitive environment; separation of policy making, regulation and operation functions in the postal sector; and restructuring the sector in line with relevant EU directives, was submitted to the Prime Ministry.

4.6.5. Transportation

The draft of Liberalization of Turkish Rail Transport Law has been prepared and the enactment process of the draft is continuing.

To make weight and size controls of the commercial vehicles possible in line with the EU standards, a comprehensive investment plan has been prepared for increasing the number of control stations up to 300 until the year 2020.

Concerning the project on withdrawal of the vehicles which have completed their life economically and technically, 76.390 old vehicles in total have been withdrawn from the market as of 31 December 2011 in line with the communiqué issued by our Ministry. The communiqué on withdrawal of the vehicles produced in 1990 or before that year is in force.

EU technical support project "weight and dimension controls of the commercial vehicles" consist of supply and service components. Service component of the project started in April 2012. Supply component of the project is in tender process, and tender assessment procedure has started in November 2012. Supply component of the project is planned to start in April 2013.

The Directive on the Transport of Dangerous Goods by Road that covers provisions about the implementation of the European Agreement concerning the International Carriage of Dangerous Goods by Road (ADR) will be in force gradually from 2011 to 2014. By the decree law number 655 which was published on 1 November 2011, on the Official Gazette number 28102, Directorate General for the Regulation of Transport of Dangerous Goods and Combined Transport was established and it was included in the new institutional structure of the Ministry of Transport, Maritime Affairs and Communications. The transport of all dangerous goods by all modes is under the responsibility of aforementioned Directorate General.

Regulations on Civil Aviation Management inspection applications, necessary air navigation performance approaching operations, implementation of security management system, quality management systems and standardization in airports, language proficiency revision 01, aeronaut licensing (SHT-1E Rev.2), helicopter pilot licensing, certificated suppliers, theoretical knowledge, safety assessment inspections on foreign aircrafts, aircraft maintenance education institutions, ambulance, search, rescue and humanitarian aid flights were published in 2012.

Regulations on passenger rights were completed and published.

Another project accepted in 2010 was the Preparation of a Feasibility Report regarding the Education Centre Planned to be established from the EU IPA Fund within the scope of Enhancing Administrative Capacity in the Field of Education on Security and Safety Requirement of Turkish Civil Aviation Project, with a budget of 200 thousand, and it has been completed on 24 May 2011. The next stage of the Project, pre-tender and control documents preparation tender was completed by September 3rd, 2012.

ISG International Airport Investment Development and Operation Inc., Fraport IC İçtaş Antalya Airport Terminal Investment and Operations in Antalya, Corendon Airlines, Turkish Ground Services, Sky Airlines, TAV Istanbul Airport Operations , Erzincan Airport and Kocaeli Cengiz Topel Airport are qualified as Accessible Airport Enterprise.

To eliminate damages to human health and environment, 21 enterprises are qualified as Green Enterprise.

Table 4.16: Matrix of Policy Commitments: Transportation

(1000 Euros)

	2011	2012	2013	2014	2015
1. Transport Operational Programme (1)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-8,345	-3,500	-23,880	-8,750	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	8,345	3,500	23,880	8,750	---
Total Net Budget Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-8,345	-3,500	-23,880	-8,750	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	8,345	3,500	23,880	8,750	---

(1) Indicative amounts for Köseköy-Gebze and Irmak-Karabük-Zonguldak Railway Rehabilitation, Signalization and Technical Assistance Projects.

4.6.6. Energy

The primary objective of the energy sector is to provide energy, which is required as a consequence of the economic development and social progress, in a continuous, high quality and reliable manner with the minimum cost in a competitive free market. For this purpose, Turkey attaches utmost importance and gives priority to realizing energy market reforms and adapting the national energy legislation fully with the EU energy legislation. In this context, fundamental sectoral laws were completed at great extent and efforts for establishing a fully competitive energy market are continuing.

Turkey determined as a national target to work synchronized with-parallel to European Network of Transmission System Operators for Electricity (ENTSO-E) and to operate the electricity system in a more economic, qualified and reliable manner by sharing backup. Beginning from 02 June 2011, a limited capacity allocation for electricity trade between Turkey, Greece and Bulgaria in accordance with the European Union rules and ENTSO-E practices was authorized. Along with this permission, a certain amount of electricity trade from Europe to Turkey and from Turkey to Europe became possible. It has recently been determined to complete the third and last phase of trial operation period in 2013.

For ensuring continuity in the petroleum market, keeping adequate amount of petroleum stock to prevent risks in case of crises or extraordinary circumstances and to perform our country obligations as required by international agreements, and aligning the stock system with the EU legislation and establishing a more robust stock management, a draft bill was prepared by the Ministry of Energy and Natural Resources and is expected to be enacted in the next period.

The natural gas infrastructure program performed from the second half of the 1980s enabled Turkey to construct main pipelines for gas importation from the various exporter countries in the region. Within this period, a significant portion of domestic transmission lines was also been completed and access to natural gas was realized for the fundamental consumption areas. As a result of realized investments of 12,215 km transmission and related city connection lines in 72 of 81 provinces, access to natural gas was reached and residential use was commenced in 62 provinces. The new medium-term target is determined to provide gas supply for residential use in all 81 provinces.

Turkey acknowledges the enhancing of energy efficiency as an important topic. In this regard, Energy Efficiency Strategy Paper (2012-2023) has been enacted and entered into force after being published on the Official Gazette dated 25 February 2012 and numbered 28215. This Strategy Paper, which aims to improve the cooperation between public sector, private sector and non-governmental organizations, can be considered as a roadmap for all parties.

By means of the Regulation on Increasing Efficiency in Energy Resources and Energy Usage, the efficiency increasing project (VAP) and "voluntary agreement" (GA) models were put into force in order to support the works for energy efficiency to be made in the industry. As of

2012, 25 of 32 projects previously determined to support under VAP scheme have been completed. In 22 facilities which voluntary agreements were signed, annual energy saving has been calculated as 44,500 TOE (ton oil-equivalent). The total provided support for the enterprises under GA scheme is 2.2 Million TL whereas this support will result in 32 Million TL annual savings in terms of energy expenditures.

In order to alleviate the supply security risk, works for developing renewable energy sources are also ongoing in Turkey. With the Amendment to Law on Utilization of Renewable Energy Resources for the Purpose of Generating Electrical Energy, a new support mechanism for renewable energy was developed. As a result of this regulation, utilization of renewable resources for electricity generation has been continuously rising. In the first 10 months of 2012, the total installed power of wind turbines has increased approximately 22 percent and 380 MW of new capacity has been connected to the electricity grid. In the same period, total installed power of hydroelectric power plants has reached to 18,750 MW with the addition of new 1,610 MW, which implies 9 percent increase in hydraulic capacity with respect to previous year. This increasing trend is likely to continue since incentives for renewable energy attracts private capital and the credit opportunities provided by international financial organizations extends.

Even though there are renewable power plants generating electricity by using hydraulic, geothermal, wind and biomass resources, solar energy has not yet been utilized for electricity generation in Turkey. With the Amendment mentioned above, the maximum total solar capacity that would be connected to electricity grid until 31 December 2013 was determined as 600 MW.

Some legal and technical regulations have been realized for solar electricity generation in 2012. In this regard, Notification of Measurement Standards for License Applications Based on Wind and Solar Energy has been published on the Official Gazette dated 31 March 2012 and numbered 28250. By this Notification, measurement data has become one of the prerequisites for the applications of solar licenses. This Notification has crucial importance as it will support to develop solar power market successfully and provide a roadmap for entrepreneurs who are eager to invest in this field. Another important progress for solar power regulation is the issuance of By-law on Competition of License Applications for Electricity Generating Facilities Based on Solar Power on the Official Gazette dated 29 May 2012 and numbered 28307.

The works for allowing usage of nuclear energy for the purpose of electricity generation have been continued in 2012. The project company which is established for constructing a nuclear power plant (NPP) in Mersin-Akkuyu with a total installed power of 4,800 MW continued its works. In this context, the project company has applied for Environmental Impact Assessment report of Akkuyu NPP and related works have been ongoing.

Table 4.17: Legal Regulations Realized in Energy Market in 2012

Date	Number	Name	Description
31 March 2012	Official Gazette numbered 28250	Notification of Measurement Standards for License Applications Based on Wind and Solar Energy	The objective of the Notification is to define the principals and procedures regarding the standardized measurements in the license applications realized for establishing wind and solar power plants.
29 May 2012	Official Gazette numbered 28307	By-law on Competition of License Applications for Electricity Generating Facilities Based on Solar Power	The objective of the By-law is to define the principals and procedures regarding the competition that will be realized for solar power plants.

One project has been completed in 2012 with the EU and 2 projects to be carried out in the next period within the framework of the reforms in energy sector:

- The service contract of Project for Rehabilitation of the Frequency Control Performance of Turkish Electricity System for Synchronous Parallel Operation with UCTE, which was proposed by TEIAS within the scope of the Pre-Accession Financial Assistance

Programming-2007 in order to ensure integration of Turkish electricity system with European electricity system and which was approved by the European Commission was signed in December 2010. The project was completed in February 2012. There is no national co-financial contribution margin for the project.

- The Project of Improving the Structure and Capacity of TEIAS was offered within the scope of Pre-Accession Financial Cooperation Programming-2009 and was accepted by the European Commission. The Financing Agreement-2009 required for implementation of the project and the Operational Agreement was signed in December 2010 and March 2011 respectively. Tendering stage of the project has been started after the finalization of the works for the technical requirements which are essential for the project tender. The project is expected to commence actually in 2013. Total budget of the project is approximately 2,005,500 euros and its part to be covered by national co-financing amounts 200,550 euros, corresponding to 10 percent of this budget.
- The Project of Adaptation of Grid Regulation with ENTSO-E Legislation proposed by TEIAS within the scope of Pre-Accession Financial Assistance Programming-2010 was approved by the European Commission. The Financing Agreement-2010 between European Union and Turkey was signed in April 2011. The Operational Agreement of the project was signed in November 2011 and the tendering stage of the project has been initiated after the finalization of the works for the technical requirements which are essential for the project tender. The project is expected to commence actually in 2013. Total budget of the project is 1.5 million euros and its part to be covered by national co-financing amounts 150,000 euro, corresponding to 10 percent of this budget.

Table 4.18: Matrix of Policy Commitments: Energy

(1000 Euros)

	2011	2012	2013	2014	2015
1. Project of Improving the Structure and Capacity of TEIAS					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	---	-201	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	---	201	---	---
2. Project of Adaptation of Grid Regulation with ENTSO-E Legislation					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	---	-201	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	---	201	---	---
Total Net Budget Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	---	-351	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	---	351	---	---

ANNEX TABLES

Table 1.a: Macroeconomic Prospects

	ESA Code	2011	2011	2012	2013	2014	2015
		Level (Mil. TL)	Rate of Change				
1. Real GDP, at 1998 prices	B 1 * g	114,889	8.5	3.2	4.0	5.0	5.0
2. GDP, at current prices	B 1 * g	1,298,062	18.1	10.5	9.5	10.8	11.1
Components of Real GDP (1998 Prices, Percentage Change)							
3. Private Consumption Expenditure	P3	78,851	7.8	0.6	3.1	4.4	4.4
4. Public Consumption Expenditure	P3	11,834	4.5	3.9	3.6	3.4	3.3
5. Gross Fixed Capital Formation	P51	29,935	18.5	-0.7	6.8	6.7	6.4
6. Changes in Inventories and Net Acquisition of Valuables*	P52+P53	14	-0.3	-0.8	-0.1	0.1	0.2
7. Exports of Goods and Services	P6	27,145	6.4	14.1	4.2	5.9	6.1
8. Imports of Goods and Services	P7	32,890	10.9	0.0	4.0	6.0	6.3
Contribution to Real GDP Growth							
9. Final Domestic Demand	---	---	10.2	0.6	4.1	5.0	4.9
10. Changes in Inventories and Net Acquisition of Valuables	P52+P53	---	-0.3	-0.8	-0.1	0.1	0.2
11. External Balance on Goods and Services	B11	---	-1.5	3.3	0.0	-0.1	-0.2

* Contribution to growth

Table 1.b: Price Developments

Percentage Changes, Annual Averages	ESA Code	2011	2012	2013	2014	2015
1. GDP Deflator	---	8.9	7.1	5.3	5.5	5.8
2. CPI	---	6.5	9.2	7.0	4.9	5.0

Table 1.c: Labor Market Developments

	ESA Code	2011	2011	2012	2013	2014	2015
		Level	Rate of Change, Percent				
1. Employment, persons (Thousands)*	---	24,110	6.7	2.6	2.0	2.0	2.0
2. Unemployment Rate (ILO Definition)	---	2,615	9.8	9.0	8.9	8.8	8.7
3. Labor Productivity Growth	---	---	1.7	0.6	2.0	2.9	2.9
4. Compensation of Employees	---	---	---	---	---	---	---

*****+15 years-old

Table 1.d: Balance of Payments

Percentages of GDP	ESA Code	2011	2012	2013	2014	2015
1. Current Account	---	-10,0	-7,3	-7,1	-6,9	-6,5
- Balance of Goods	---	-11,5	-9,2	-9,0	-8,8	-8,4
- Balance of Services	---	2,3	2,5	2,6	2,6	2,6
- Balance of Incomes	---	-1,0	-0,9	-0,9	-0,9	-0,8
- Balance of Current Transfer	---	0,2	0,2	0,2	0,2	0,2
2. Capital and Financial Account (Including Reserves)	---	8,5	6,9	7,1	6,9	6,5
Statistical Discrepancy	---	1,5	0,4	0,0	0,0	0,0

Source: Realization CBRT, forecast Ministry of Development

Table 2: General Government Budgetary Prospects

Percentages of GDP	ESA Code	2011	2012	2013	2014	2015
Net Lending by sub-sectors*						
1. General Government	S13	0.4	1.6	1.5	1.2	0.9
2. Central Government	S1311	0.1	0.9	0.6	0.7	0.5
3. Funds	S1311	-0.2	-0.1	-0.2	-0.3	-0.2
4. Local Administration	S1313	0.0	0.1	0.3	0.0	0.0
5. Social Security Fund	S1314	1.3	1.4	1.6	1.5	1.4
6. Revolving Funds	S1311	-0.2	-0.1	-0.1	-0.1	-0.1
7. Unemployment Fund	---	-0.7	-0.7	-0.7	-0.7	-0.7
General Government (S13)						
8. Total Receipts	TR	36.4	37.0	37.9	37.2	36.6
9. Total Expenditures	TE	36.8	38.6	39.4	38.4	37.5
10. Net Lending	EDP.B9	0.4	1.6	1.5	1.2	0.9
11. Interest Payments	EDP. D41+FISIM	3.4	3.5	3.5	3.2	3.1
12. Primary Balance	---	3.0	1.9	2.0	2.0	2.1
Components of Revenues						
13. Taxes	---	20.1	19.9	20.7	20.5	20.2
14. Social Funds	D61	9.2	9.4	9.7	9.6	9.5
15. Factor Incomes	D4	5.0	5.6	5.3	4.9	4.7
16. Other	---	2.2	2.0	2.2	2.2	2.1
17. Total Receipts	TR	36.4	37.0	37.9	37.2	36.6
Components of Expenditures						
18. Total Consumption	P32	16.6	17.5	17.7	17.3	16.8
19. Total Social Transfers	D62+D63	4.5	5.1	5.4	5.4	5.2
20. Interest Payments	EDP. D41+FISIM	3.4	3.5	3.5	3.2	3.1
21. Subsidies(1)	D3	0.8	0.8	0.7	0.7	0.6
22. Gross Fixed Capital Formation	P51	3.3	3.5	3.4	3.5	3.5
23. Other	---	8.1	8.2	8.7	8.3	8.3
24. Total Expenditures	TE	36.8	38.6	39.4	38.4	37.5

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

Table 3: General Government Debt Developments

	ESA Code	2011	2012	2013	2014	2015
Percentage of GDP						
1. Gross Debt	---	39.2	36.5	35.0	33.0	31.0
2. Change in Gross Debt	---	---	-2.7	-1.5	-2.0	-2.0
Contributions to Change in Gross Debt						
3. Primary Balance	---	---	-1.9	-2.0	-2.0	-2.1
4. Interest Expenditure	EDP D.41	---	3.5	3.5	3.2	3.1
5. Current GDP Growth	---	---	-3.8	-3.3	-3.6	-3.4
6. Other	---	---	-0.5	0.3	0.4	0.5

Table 4: Cyclical Developments*

	2011	2012	2013	2014	2015
1. Real GDP Growth (1998 Prices,%)	8.5	3.2	4.0	5.0	5.0
2. Net Lending of General Government / GDP (%)	0.4	1.6	1.5	1.2	0.9
3. Net Interest Expenditure / GDP (%)	3.1	3.3	3.3	3.0	3.0
4. Potential GDP Growth (%)	4.4	4.4	4.3	4.2	4.1
5. Output Gap (Percentage Difference from the Potential)	0.8	-0.3	-0.6	0.1	1.0
6. Cyclical Component / GDP (%) **	-0.6	-0.0	0.1	-0.0	-0.2
7. Cyclically Adjusted Balance / Potential GDP (%) **	2.1	2.5	2.1	1.8	1.6
8. Cyclically Adjusted Primary Balance / Potential GDP (%) **	-1.3	-1.1	-1.3	-1.4	-1.5

*General Government
** (+) refers to deficit. (-) refers to surplus.

Table 5: Divergence from Previous Update

	2011	2012	2013	2014	2015
GDP Growth (Percent)					
Previous Update	7.5	4.0	5.0	5.0	---
Latest Update	8.5	3.2	4.0	5.0	5.0
Difference	1.0	-0.8	-1.0	0.0	---
General Government Net Lending (Percentage of GDP)					
Previous Update	1.0	0.8	0.8	0.4	---
Latest Update	0.4	1.6	1.5	1.2	0.9
Difference	-0.6	0.8	0.7	0.8	---
General Government Gross Debt (Percentage of GDP)					
Previous Update	39.8	37.0	35.0	32.0	---
Latest Update	39.2	36.5	35.0	33.0	31.0
Difference	-0.6	-0.5	0.0	1.0	---

Table 6: Basic Assumptions on the External Economic Environment Underlying the Pre-Accession Economic Programme (2012-2014) Framework*

	2011	2012	2013	2014	2015
Exchange Rates					
Parity (USD/ €)	1.39	1.28	1.23	1.23	1.23
Real Exchange Rate (Percentage Change)**	-10.8	-0.5	1.7	0.2	0.3
GDP Growth					
Euro Area (Real. Percentage Change)	1.4	-0.4	-0.2	1.2	1.5
World Trade (In Real Terms)					
World Import Volume Increase (Percent)	5.8	3.2	4.5	5.8	6.1
International Prices					
EU CPI (Percentage Change)	3.1	2.5	1.8	1.6	1.8
US CPI (Percentage Change)	3.1	2.0	1.8	1.8	1.8
Oil Prices ($ / barrel)	113.4	112.1	110.0	110.0	110.0

*IMF, World Economic Outlook, October 2012.
** (+) shows appreciation, (-) shows depreciation.

Table 7: Structural Reform Agenda and Developments

Measures in Previous PEP	Realization Status (Y/N)	Date[9]	Comments
Privatization			
The privatization of electricity distribution companies	N	2012	Privatization tenders of Electricity Distribution Companies (Vangölü, Boğaziçi, Dicle, İstanbul Anadolu Yakası, Toroslar and Akdeniz) were cancelled.
Privatization of public share in Acıpayam Selüloz Co.	Y	2012	Transfer contract of public shares in Acıpayam Selüloz Sanayii ve Ticaret A.Ş. was signed.
Privatization of TCDD İskenderun Port	Y	2011	Transfer contract of TCDD İskenderun Port was signed at the end of December.
The privatization of river power plants	Y	2012	Privatization procedures of some river plants belonging to EÜAŞ were completed.
The privatization of TŞFAŞ (Sugar Factories Co.)	N	2012	Privatization tenders of sugar factories consisting of B portfolio group (Malatya, Erzincan, Elazığ, and Elbistan Sugar Factories) and C portfolio group (Kastamonu, Kırşehir, Turhal, Yozgat, Çorum, and Çarşamba Sugar Factories) belonging to TŞFAŞ were cancelled. The works are carried on to privatize all sugar factories until the end of 2015.
Financial Sector			
Preparation of a new Capital Market Law which is in harmony with EU regulations	Y	2012	Following the completion of drafting and the collection of comments on the new Capital Markets Law, the draft law was finalized and passed by TGNA as of December 2012 and sent to the President for approval.
Publication of secondary legislation following the enactment of law, to ensure compliance with EU regulations and market requirements.	N	2013	Drafting work in relation to secondary regulations that will be published after the new Capital Markets Law comes into force is being carried out.
Regulation and classification of financial services within the framework of the EU acquis and on the structuring of these services in a way to provide flexibility to financial intermediaries in order to satisfy the needs of customers.	N	2013	Related provisions have been included in the draft Capital Markets Law. Drafting work is being carried out in relation to secondary regulation, which will be published after the new Law comes into force to regulate the containing details concerning implementation.
Regulations for activating housing finance and introducing new products such as real estate investment fund and venture capital investment fund shall be made.	N	2012-2013	Studies on related regulation will be continued after the new Capital Markets Law enters into force.
Works are carried out in order to improve technical infrastructure of CMB-ISE Cooperative Surveillance Programme.	Y	2012	The technical infrastructure of the Programme has been improved and it is now in the testing phase.
Works will continue for the development of private sector debt securities, securitization products, derivative products and interest-free financing instruments markets.	Y	2012-2013	The regulation concerning interest-free financing instruments has entered into force in 2012 and applications in this field are being continued. At the same time, regulations on interest-free financing are currently being revised based on demands from market participants and the related studies are about to be completed.

[9] The date or foreseen date of realization.

Enhancing the structure in relation to Central Settlement and Central Custody Transactions	N	2012-2013	In relation to central settlement and custody institutions, after the new Capital Markets Law comes into force, principles on the organization and activities of such institutions will be regulated in line with IOSCO and FSB principles. Furthermore studies are currently being carried out in relation to the establishment of Takasbank as a central counterparty.
Capital markets compliance with the EU acquis about the capital adequacy of the intermediary institutions	N	2012-2013	Since financial activities will be redefined in the new Capital Markets Law and especially since OTC derivatives that are subject to complex valuation provisions will be regulated by the CMB, the need has arisen to revise provisions on capital adequacy. It is planned to publish related regulations after the new Law comes into force.
	Agriculture		
Amendment of Fisheries Law	N	2013	In order to ensure the sustainable fisheries and the compliance with EU acquis, Fisheries Law will be amended, including arrangements on resource management and securing high quality product.
	Information and Communication Technologies		
The Draft Law on Protection of Personal Data	N	2013	The Draft Law will be presented again to the TGNA in new legislative period.
Cyber Crime Convention of European Council No.185	N	2013	Turkey signed the Cyber Crime Convention of the European Council, No.185 on 10 November 2010. Ratification procedure by the TGNA is still in progress.
By-law on Processing of Personal Data and Protection of Privacy in the Telecommunications Sector	Y	2012	By-Law on Processing of Personal Data and Protection of Privacy in the Electronic Communications Sector, which was published in the Official Gazzette dated 24/07/2012 and will come into force after 6 months from the publishing date, is completed in order to comply with the "Directive 2002/58/EC concerning processing of personal data and protection of privacy in the electronic communications sector" and the "Directive 2006/24/EC on retention of data generated or processed in connection with the provision of publicly available electronic communications services or of public communications networks".
	Energy		
Continuation of the privatization works for the electricity distribution companies	Y	2012	The privatization works of electricity distribution assets have been continued in 2012. It is expected that the privatization of electricity distribution regions will be completed in 2013.
Continuation of the privatization works in electricity generation assets	Y	2004-2014	The privatization tender for Hamitabat Power Plant has been announced. It is expected that the privatization of electricity generation companies will be continued in 2013.
Project of Improving the Structure and Capacity of TEIAS	N	2009-...	Within the scope of fortification of the institutional structure and expansion of the technical capacity of the Turkish Electricity Transmission Company (TEIAS), live maintenance for the electricity transmission system, development of occupational safety and training activities, revision of human resources policies, improvement of the IT structure and restructuring of the organization are planned. The Project was submitted in scope of Pre-Accession

			Financial Cooperation Programming-2009 and was accepted by the European Commission. The Financing Agreement 2009 required for implementation of the project and the Operational Agreement were signed in December 2010 and March 2011 respectively. Tendering stage of the project has been started after the finalization of the works for the technical requirements which are essential for the project tender. The project is expected to commence actually in 2013.
Project of Adaptation of Grid Regulation with ENTSO-E Legislation	N	2010-…	The project was proposed within the necessity of legislation change emerged as a result of studies for the operating of Turkish electricity system synchronized parallel with to continental Europe's electricity system within the scope of Pre-Accession Financial Cooperation Programming-2010 and was approved by the European Commission. The Financing Agreement-2010 was signed in April 2011. The Operational Agreement of the project was signed in November 2011 and the tendering stage of the project has been initiated after the finalization of the works for the technical requirements which are essential for the project tender. The project is expected to commence actually in 2013.
Activities to provide electricity supply security	Y	2007-2013	Necessary measures will be taken to activate the licenses for investment and to complete the investments within the envisaged periods. Investments for efficiency improving and rehabilitation in public power plants will be continued.
Activities to provide oil supply security	N	2013	A law will be enacted for keeping adequate amount of petroleum stock, aligning the stock system with the EU legislation and establishing a more robust stock management.
Institutional division of coordination and supervision activities in nuclear energy field	N	2007-2013	The regulation and surveillance activities in the field of nuclear energy will be carried out by a new established institution. Research, technology development and implementation activities will remain under the responsibility of TAEA.