REPUBLIC OF TURKEY

PRE-ACCESSION ECONOMIC PROGRAMME 2014 - 2016

ANKARA
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The Pre-Accession Economic Programme (2014-2016) has been adopted by High Planning Council Decision No. 2014/1.

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ABBREVIATIONS

BIST	Borsa İstanbul
BOTAŞ	Petroleum Pipeline Corporation
BRSA	Banking Regulation and Supervision Agency
CBRT	Central Bank of the Republic of Turkey
CML	Capital Markets Law
CMB	Capital Markets Board
CPI	Consumer Price Index
DAMS	Development Agencies Management System
DAP	Eastern Anatolia Project
DOKAP	Eastern Black Sea Project
DSL	Digital Subscriber Line
ECOFIN	Economic and Financial Affairs Council
ENTSO-E	European Network of Transmission System Operators for Electricity
EU	European Union
EUROSTAT	Statistical Office of the European Communities
EÜAŞ	Turkish Electricity Production Company Inc.
ESMA	European Securities and Markets Authority
FATİH	Education and Technology Improvement Action to Increase Opportunities
FED	Federal Reserve System
FX	Fixed Exchange Rate
GAP	South Eastern Anatolian Project
GDBI	Government Domestic Borrowing Instrument
GDP	Gross Domestic Product
GGP	General Government Balance
HPC	High Planning Council
HPP	Hydroelectric Power Plant
ICT	Information and Communication Technology
IFS	International Financial Statistics
ILO	International Labor Organization
IMEIGAP	Action Plan for Enhancing the Relation between Employment and Vocational Education
IMF	International Monetary Fund
IPA	Instrument for Pre-Accession Assistance
IPARD	IPA Rural Development Funds
İŞKUR	Turkish Employment Organization
IT	Information Technology
ITCA	Information Technologies and Communications Authority
KOP	Konya Plain Project
LLL	Lifelong Learning
MTP	Medium Term Programme
NPP	Nuclear Power Plant
OECD	Organization for Economic Co-operation and Development
OMO	Open Market Operations
PEP	Pre-Accession Economic Programme
PSTN	Public Switched Telephone Network
REM	Registered Electronic Mail
ROC	Reserve Option Coefficient
ROM	Reserve Option Mechanism

SCA-H	Special CPI Aggregates H Index
SCA-I	Special CPI Aggregates I Index
SEEs	State Economic Enterprises
SMEs	Small and Medium Sized Enterprises
SMP	Significant Market Power
SODES	Social Support Program
SUKAP	Water and Sewerage Infrastructure Project
TAEA	Turkish Atomic Energy Authority
TCDD	Turkish State Railways
TDİ	Turkish Maritime Organization Inc.
TDZ	Technology Development Zones
TEDAŞ	Turkish Electricity Distribution Company
TFP	Total Factor Productivity
GNAT	Grand National Assembly of Turkey
TL	Turkish Lira
TOBB	Union of Chambers and Commodity Exchanges of Turkey
TURKSTAT	Turkish Statistical Institute
TÜBİTAK	Scientific and Technological Research Council of Turkey
USA	The United States of America
VAT	Value Added Tax
VET	Vocational Education and Training
WLR	Wholesale Line Rental
WTI	West Texas Intermediate

1. POLICY FRAMEWORK AND OBJECTIVES

Turkey, as an acceding country for European Union (EU) membership, has been preparing the Pre-Accession Economic Programme (PEP) and has been submitting 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 (2014-2016) 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. 2014/1.

Official policy documents setting medium and long term policy framework in Turkey are Development Plans, Medium Term Programs and Annual Programs. Implementation period of Ninth Development Plan was completed as of 2013 and Tenth Development Plan was enacted by approval of the GNAT. Tenth Development Plan, which has been prepared in a global economic environment with protracted risks, uncertainties, changes and transformations, with emerging and reshaping power balances among developed and developing economies, will serve for the 2023 Vision targets reaching 100th anniversary of Republic of Turkey. In this respect, the Tenth Development Plan, covering the 2014-2018 period, will be an important milestone in advancing our society to high prosperity levels, in line with the 2023 targets.

The Tenth Development Plan is designed to include not only high, stable and inclusive economic growth, but also issues such as the rule of law, information society, international competitiveness, human development, environmental protection and sustainable use of resources. In this regard, Turkey's economic and social development processes are discussed with a holistic and multi-dimensional view, and a participatory approach has been adopted within a human-oriented development framework.

The main objective of the Tenth Development Plan, covering the 2014-2018 period is to become a country that would reach better position in international value chain, become a high income country and overcome absolute poverty problem (Box 1.1).

Pre-Accession Economic Programme is based on Medium Term Programme (2014-2016), which was enacted in October 2013 to provide a basis for economic and social policies for the following three years within the scope of the Tenth Development Plan (2014-2018). The developments realized in the short period after publication of Medium Term Programme (MTP) till the preparation of PEP do not necessarily change the medium term framework set in the MTP. Therefore, the framework of MTP for medium-term outlook and projections has been kept in PEP.

The macroeconomic framework of PEP has been prepared by taking into consideration the uncertainty environment caused by fluctuations in international financial markets since May 2013 and global liquidity prospects. Under the conjuncture of uncertainties about economic policies in developed countries and tighter external financing conditions, keeping prudent macroeconomic policy mix applied in recent years has critical importance in terms of preserving Turkish economy's resilience and mitigating its fragility against global risks. In this framework, the main objective of the Pre-Accession Economic Programme is on the one hand to reduce the current account deficit gradually and on the other to increase growth, through minimizing the effects of global uncertainty on the economy.

Simultaneous decline of total investments and savings in recent years has increased the need for structural policies in this area. To this end, increasing domestic savings, directing existing resources to productive areas, increasing the economy's productivity level through accelerating capital accumulation and industrialization process are primary policy areas of PEP. Moreover, transformation of the existing production is targeted via reducing import dependency and increasing innovation capacity of the economy. The structural policies towards these areas will contribute to the increase in potential growth rate and the decrease in saving-investment gap through enhancing competitiveness of the economy in the medium term. Structural reforms that are designated to realize the objectives and priorities of Development Plan and Medium Term Program are essential

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

in this respect. The developments in these areas will serve for supporting private fixed capital investments and foreign direct investments on the one hand and for attaining a sound financing structure of current account deficit on the other.

The Central Bank of Republic of Turkey (CBRT) will continue inflation targeting regime 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. A target path for inflation is envisioned 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 inflation targeting regime, financial stability will also continue to be taken into consideration. This policy framework is mainly driven by a view to slow down the rapid growth of the private sector's foreign liabilities and to improve the quality of these liabilities.

Maintaining strong stance in public finance is important in terms of confidence in economy. In PEP period, fiscal policies will be supportive for the goals of strengthening economic and financial stability, keeping current account deficit under control through increasing domestic savings and raising growth potential of the economy.

Sustainability of public finances will be pursued by keeping public sector borrowing requirement at reasonable levels, and achievements in public finances in the past will be continued in future periods as well. Primary expenditures will be kept under control by prioritization of expenditure programs and increasing efficiency of expenditures. Fiscal space, which will be created by public current expenditure rationalization, will be used in public infrastructure investments, incentives and R&D supports that would stimulate economic growth.

Fiscal policies will be implemented to increase the quality of public revenues in order to construct a stronger public finance considering the sensitivity of public finances to cyclical movements. Policies will not be implemented that result in rise in expenditures permanently in the medium and long run by using one-off revenues.

In the second chapter of the Pre-Accession Economic Programme, 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 2014-2016 period are presented. In the third chapter, fiscal policies for the PEP 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.

Box 1.1: Tenth Development Plan (2014-2018)

Development Plans are the principle policy documents, binding for public sector and guiding for private sector that set the long-term development vision together with economic and social policies and priorities that are consistent with this vision. The Tenth Development Plan covering the period of 2014-2018 was enacted after its approval by the GNAT on 1 July 2013. Tenth Development Plan has four main pillars. The first pillar of "Qualified Human, Strong Society" aims to achieve a more strong and prosperous society and improve human capital. Under this subject, the policies that will ensure growth to be inclusive by spreading prosperity across all segments of society are covered. The second pillar of "Innovative Production, High and Stable Growth" targets improving the growth performance of Turkish economy and strengthening it with an innovative production structure. It is targeted to have a more stable economy with a sound macroeconomic structure that produces in global standards, places higher position in value chain, has higher technology-based product range and managed to reduce import dependency and external financing need. The third pillar of "Livable Places, Sustainable Environment" includes objectives and policies that aim to increase economic and social benefits via environmentally friendly approaches and reduce development disparities across regions. The last pillar of "International Cooperation for Development" includes coherent and complementary policies at national, regional and global scale that efficiently utilize international cooperation during development process.

"Innovative Production, High and Stable Growth" pillar of the Tenth Development Plan, targets to achieve high and stable growth by transforming the economy towards an export-oriented, private-led, competitive production structure via increasing productivity and accelerating industrialization. In order to attain this goal, the growth strategy of the Plan focuses on five principle policy areas: macroeconomic stability, human capital and labor market, technology and innovation, physical infrastructure and institutional quality. For progress in these policy areas; increasing domestic savings, strengthening achieved gains in price stability, financial structure and fiscal policy, improving science, technology and innovation capacity, accomplishing desired transformation in the manufacturing sector, improving entrepreneurship and supporting SMEs, enhancing intellectual rights, utilizing information and communication technologies efficiently and improving logistics and transport infrastructure are set as priority areas.

Figure: Growth Strategy of the Tenth Development Plan

The Tenth Development Plan includes special implementation programs named as "Priority Transformation Programs". These programs aim to increase the efficiency of development efforts and the applicability of the Plan. Programs are designed for critical reform areas which; are important for achieving 2023 targets and the objectives of Tenth Development Plan; could provide solutions for the main structural problems; is usually in more than one ministerial area of responsibility and require effective coordination and responsibility among institutions. Having designed with both sectoral and cross-sectoral perspectives and expected to finalize within five years, these programs will significantly contribute to the achievement of Plan targets.

As a result of the polices in the Plan, it is targeted that GDP will grow by 5.5 percent annually on average during the Plan period, while nominal GDP and GDP per capita will reach 1.3 trillion dollars and 16 thousand dollars at the end of the Plan period. The unemployment rate is expected to recede to 7.2 percent at the end of Plan period with the labor force participation rate converging to levels in developed countries. Additionally, together with the policies for increasing exports and for reducing the import dependency, the current account deficit will no longer be a problem and current account deficit to GDP ratio will decrease to 5.2 percent at the end of the period.

2. MACROECONOMIC OUTLOOK

Despite a long time has passed since the beginning of the global economic crisis that began in 2008, a steady and sustainable recovery in the world economy has not been established yet. Overcoming the crisis continues in different phases. Although a moderate recovery in global economy continues, new risks and uncertainties have emerged.

During the global crisis, with the simultaneous monetary expansion and economic stimulus packages implemented especially in the US and Euro Area and with the effects of international coordination, further deepening of the crisis was prevented. However, the recovery tendency in global economy could not be sustained in 2012. The downside risks originating from developed countries such as recession in Euro Area, fiscal sustainability, discussions of separation of troubled countries from monetary union and debates of fiscal cliff and debt ceiling in the US, were dominant in 2012. On the other hand, many of the developing economies, which are the driving force of global growth, have tended to slow down due to weak domestic demand, several structural factors and deteriorating external conditions.

As a result of these developments, the world growth rate which was 3.9 percent in 2011 declined to 3.2 percent in 2012, according to IMF data. The decrease in the growth rate of emerging markets and developing economies from 6.2 percent to 4.9 percent was the determining factor in this decline.

Growth in the US economy continues at a moderate pace, economic outlook is improving. Indeed, growth rate of the US economy, which was 1.8 percent in 2011, realized as 2.8 percent in 2012. Positive developments in economic indicators recorded since the first half of 2013 indicates that recovery tendency in the economy is gaining strength. The US economy is expected to grow by 1.6 percent in 2013 and 2.6 percent in 2014. On the other hand, it is early to pronounce that growth performance of the US has reached a healthy and sustainable structure. Expansionary policies implemented during the crisis have led to excessive growth of FED's balance sheet and with the beginning of economic recovery in the US, exiting from expansionary monetary policies has come into agenda.

On 22 May 2013, FED announced to taper bond purchases if a steady growth in the economy were observed. These releases were perceived as a signal of exiting from expansionary monetary policy by markets. In this period, capital outflows from emerging economies surged, bond interest rates have increased, stock markets and national currencies have depreciated.

Recently, as a result of improvement in the US economic growth rates, low unemployment and inflation rates, as well as budget reconciliation which prevented possible crisis in the fiscal field, new decisions were taken to reduce monetary expansion at the FED meeting held on 17-18 December 2013. Starting to be implemented from January 2014, bond purchase program which was 85 billion dollars per month has been reduced to 75 billion dollars, a decrease of 10 billion dollars.

The policies implemented in the aftermath of the crisis reduced the systemic risk in Euro Area and provided stability in financial markets to a certain extent. However, the recovery achieved in financial sector did not reflect on real sector as expected. Euro Area, which contracted at the rate of 0.6 percent in 2012, had positive growth rate in the second quarter of 2013, following the end of recession continued since the last six quarter. However, the economic outlook is still weak. Euro Area is expected to contract by 0.4 percent in 2013 as a result of weak economic outlook in the periphery countries and grow by 1 percent in 2014.

To summarize, besides the ongoing recovery tendency in the global economy, growth performance of countries is decoupling. While growth in developed economies is accelerating, it is decelerating in developing economies. The growth rate of China, which was 7.7 percent in 2012, has been the lowest growth rate recorded since 1999.

After these developments in global economy and financial turbulence observed in developing countries stemming from FED's statements, international organizations have revised their growth forecasts downwards. The world growth forecasts for 2013 and 2014 were reduced to 2.9 percent and 3.6 percent respectively in October 2013, which were 3.6 percent and 4.1 percent in October 2012 by IMF.

Growth forecasts for advanced economies, emerging markets and developing economies were also revised downward by IMF. Advanced economies are expected to grow by 1.2 percent and 2 percent in 2013 and 2014, respectively. Emerging markets and developing economies are expected to grow by 4.5 percent in 2013, which is reduced by approximately 1 percentage point compared to forecasts in September 2012 whilst the growth rate in 2014 is projected to be 5.1 percent.

Decreasing trend in world trade volume has also continued. Growth rate of world trade volume receded to 2.7 percent in 2012 from 6.1 percent in 2011, due to slowdown in global economic activity. Depending upon recovery in global economic activity, world trade volume is expected to grow by 2.9 percent in 2013 and 4.9 percent in 2014.

Notwithstanding expansionary monetary policies implemented in developed countries, there was no significant inflationary pressure at global scale. Global inflation rate, which was 3.9 percent in 2012, is projected to be 3.8 percent both in 2013 and 2014. Inflationary pressures are expected to be weak at global scale due to decline in oil and commodity prices in the forthcoming period, whereas inflation might increase in developing countries due to recovery in their domestic demands.

Weak global growth outlook emerges as a determining factor on commodity prices, especially on energy and industrial metals. Following a volatile path, WTI crude oil price per barrel averaged 105 dollars in 2012. Crude oil price is expected to remain at the same level in 2013. Although downward trend in oil prices is expected to continue in medium term, geopolitical uncertainties could lead to temporary price increases.

Insufficient employment creation, high level of young unemployment and skill losses have been major problems for many advanced economies due to weak economic growth. In 2012, unemployment rate realized as 8 percent in OECD, 8.1 percent in the US and 11.4 percent in Euro Area. Any prominent recovery in unemployment rates is not anticipated on global scale due to weak economic activity in 2013.

In advanced countries, public debts are still at high levels despite the fiscal measures taken. Even though fiscal consolidation plans were implemented in Euro Area, general government gross debt stock to GDP ratio, which was 88.2 percent in 2011, raised up to 93 percent in 2012. During the same period, this rate increased from 99.4 percent to 102.7 percent in the US. In Japan, the announcement of stimulus package to reinvigorate the economy indicates that general government gross debt stock to GDP ratio, which was up to 238 percent in 2012, might further increase in the forthcoming period. No reduction in debt ratios of advanced economies is envisaged in the forthcoming period even though budget deficits are expected to decrease with the contractionary fiscal policies.

Capital flows to developing economies have been following a volatile course. Net financial capital flows, which were approximately 237 billion dollars in 2012, are projected to be 398 billion dollars in 2013 and 366 billion dollars in 2014.

Weak global economic growth outlook has increased the significance of international policy coordination and G-20 has gained importance as the main platform of global economic cooperation and coordination. In G-20 summits in 2013; sustainable, strong and balanced growth, employment increase and enhancing the international cooperation to ensure stability in financial markets were emphasized.

Pre-Accession Economic Programme, has been prepared by closely monitoring the recent global economic developments, especially in the European Union which is the Turkey’s main 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. Reel Sector

2.1.1.1. Growth

A significant deterioration in current account balance was recorded in 2011 due to strong domestic demand together with sluggish foreign demand and increase in energy prices. In addition, inflation tended to rise and uncertainties increased in the global economy. Some macro-prudential measures had been taken as of the second half of the year in order to impede these developments to threaten the economy and to rebalance the domestic-foreign demand composition of the economy (Box 2.2). As a result of these measures, economic growth decelerated beginning from the third quarter of 2011. This effect continued in 2012, the slowdown in the economy became more evident and GDP growth rate receded to 2.2 percent in 2012. The declines in private consumption and investment expenditures above the expectations caused GDP growth rate to be realized below the PEP (2013-2015) forecast.

Scrutinizing the national income by expenditure items for 2012, it is observed that private consumption decreased by 0.6 percent as a result of macro-prudential measures taken in order to curb down the current account deficit. As a result of decrease in machinery and equipment investments by 7 percent, private fixed capital investments declined by 4.8 percent. Consequently, private sector, which is primary driving force of growth, contributed negatively to growth for the first time except crises by -1.4 percentage points. In the same period, the increases in public consumption and investment were realized as 6.1 percent and 9.3 percent, thereby the total contribution of public sector to growth was realized as 1 percentage point. The contribution of change in stocks to growth was realized as -1.4 percentage points as result of the significant fall in stocks. Thus, the contribution of the final domestic demand to growth was realized as -0.5 percentage point, whereas the contribution of domestic demand was -1.9 percentage points.

Table 2.1: Growth Rates and Demand Components

(Annual Percentage Change, at 1998 Prices)

	Annual		2012				2013			
	2011	2012	I	II	III	IV	I	II	III	First 9 Months
GDP	8.8	2.2	3.1	2.8	1.5	1.4	3.0	4.5	4.4	4.0
Agriculture	6.1	3.1	5.6	3.7	2.1	3.4	4.5	5.7	2.9	3.9
Industry	9.7	1.9	3.2	3.4	1.5	-0.4	1.4	3.4	4.3	3.1
Manufacturing	10.0	1.8	2.9	3.2	1.1	-0.1	1.9	3.7	4.9	3.5
Services	9.0	2.4	3.2	2.8	1.4	2.3	4.2	5.4	6.1	5.2
Construction	11.5	0.6	2.4	-0.8	-0.8	1.5	5.9	7.6	8.7	7.4
Total Consumption	7.3	0.3	0.3	-0.4	0.4	1.0	3.9	5.9	4.5	4.8
Public	4.7	6.1	5.5	4.4	5.5	8.5	7.6	7.8	0.6	5.2
Private	7.7	-0.6	-0.4	-1.2	-0.3	-0.4	3.4	5.6	5.1	4.7
Gross Fixed Capital Form.	18.0	-2.7	-1.5	-4.3	-3.3	-1.7	2.5	4.0	6.0	4.1
Public	-2.2	9.3	-1.7	4.0	6.8	21.8	83.9	37.7	9.1	37.2
Private	22.3	-4.8	-1.5	-5.6	-5.3	-6.8	-7.0	-1.9	5.3	-1.4
Change in Stocks[1]	-0.2	-1.4	-2.3	-1.6	-0.6	-1.3	0.0	2.5	1.9	1.5
Total Final Dom. Demand	9.8	-0.4	-0.1	-1.5	-0.5	0.3	3.6	5.4	4.8	4.6
Total Domestic Demand	9.5	-1.8	-2.3	-3.0	-1.1	-1.0	3.7	7.9	6.6	6.1
Exports of Goods and Serv.	7.9	16.7	12.6	23.2	14.4	16.7	5.2	0.1	-2.2	0.8
Imports of Goods and Serv.	10.7	-0.3	-8.4	-1.7	3.0	6.6	7.4	12.1	6.0	8.5

Source: TURKSTAT

(1) Contribution to GDP growth.

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

While domestic demand contracted more than expected in 2012, contribution of net exports to growth was realized above the expectations. With the contribution of significant increase in gold exports, exports of goods and services increased by 16.7 percent. On the other hand, domestic demand contracted and imports of goods and services decreased by 0.3 percent due to measures taken for rebalancing demand composition of the economy. Hence, the contribution of net exports of goods and services to growth was realized as 4.1 percentage points.

The recovery in domestic demand has started as of the first quarter of 2013 and GDP growth rate was realized as 4 percent in the first nine months of the year.

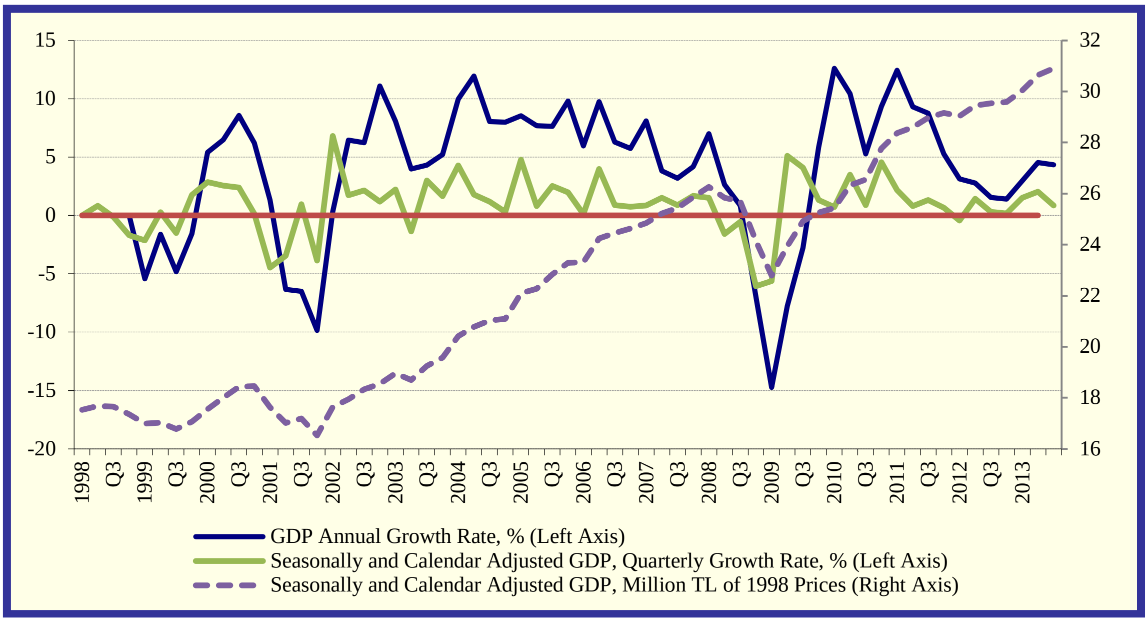
Analyzing the expenditure items for the first nine months of 2013, it is observed that private consumption expenditures rose by 4.7 percent compared with the same period of the previous year as a result of the increased consumer confidence and decreased uncertainties. With an increase of 5.2 percent in public consumption expenditures, the total increase in consumption expenditures was realized as 4.8 percent. The differentiation in the third quarter of 2013 from the other quarters was observed in public consumption. Public consumption increased just by 0.6 percent compared with the same period of the previous year. Hence, public consumption decelerated considerably compared with the significant acceleration during the last period. Although private fixed capital investment expenditures declined by 1.4 percent in the first nine months of 2013, with the relatively high increase of 37.2 percent in public fixed capital investments, total fixed capital investments rose by 4.1 percent for the same period. Second differentiation in expenditure items was recorded in private sector fixed capital investments in the third quarter of 2013 compared to the other quarters. Private fixed capital investments recorded a positive increase for the first time in this quarter after 18 months and rose by 5.3 percent. As a result of these developments, the increase in final domestic demand was realized by 4.6 percent in the first nine months of 2013.

In the first nine months of 2013, exports of goods and services increased only by 0.8 percent due to sluggish foreign demand and contraction in gold exports. On the other hand, imports of goods and services increased by 8.5 percent as a result of recovery in domestic demand. A noteworthy development in the third quarter of 2013 is the 2.2 percent contraction first time in exports of goods and services after a long period of time. This is mainly due to the base effect recorded in gold exports.

Scrutinizing the sub-items of domestic demand in the light of these developments, it is observed that private sector contributed to growth by 2.8 percentage points in the first nine months of 2013 with 3.1 percentage points and -0.3 percentage point of the contribution coming from consumption and fixed capital investment, respectively. The contribution of government consumption to growth was realized as 0.5 percentage point, whereas the contribution public fixed capital investment was realized as 1.3 percentage points in the same period. Thus, government sector contributed to growth by a total of 1.8 percentage points. The contribution of net exports to growth was realized as -2.2 percentage points and declined significantly compared to the same period of previous year due to the relatively low increase in exports of goods and services compared with the high increase in imports of goods and services. In this period, where the contribution of change in stocks to growth was realized as 1.5 percentage points, the contribution of domestic demand was realized as 6.1 percentage points. Thus, a domestic demand-led growth was recorded in the first nine months of 2013.

Considering the sectoral developments in 2012, it is observed that the value added of agriculture sector increased by 3.1 percent and its share in GDP did not show a significant change. In this period, the value added of the industry sector increased by 1.9 percent, below the PEP (2013-2015) forecast of 3.1 percent. Thereby, the sector share in total production decreased to 21.8 percent in nominal terms and its contribution to growth was realized as 0.5 percentage point. Value added in manufacturing industry, main sub-sector of the industrial sector, increased by 1.8 percent in the same period, while its contribution to growth was realized as 0.4 percentage point. Value added in services sector increased by 2.4 percent in the same period and its contribution to growth was realized as 1.5 percentage points. Considering the sub-sectors of the services sector, it is observed that particularly transport, storage and communication; financial intermediation and real estate, renting and business activities were the driving sectors of the services sector.

Figure 2.1: GDP Developments



Source: TURKSTAT

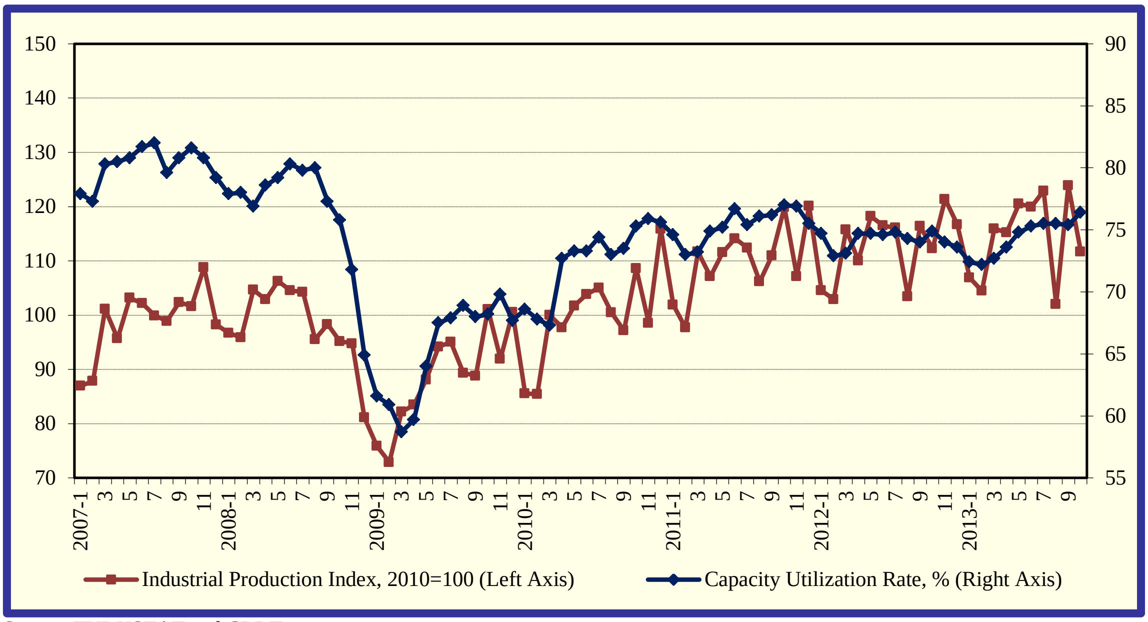
Scrutinizing the sectoral developments in the first nine months of 2013, it is observed that value added in agriculture sector increased by 3.9 percent and the increase in industrial sector value added was recorded as 3.1 percent. As a matter of fact, considering sub-sectors the value added of mining and quarrying sector decreased by 3.3 percent and the value added of manufacturing industry increased by 3.5 percent. Electricity, gas, and water supply sector recorded 0.4 percent increase.

Industrial production index increased by 2.4 percent in January-October period of 2013 (Figure 2.2). Considering the seasonally adjusted series, it is observed that the industrial production index, which has been fluctuating recently, increased by 5.8 percent in September 2013, whereas it decreased by 3.1 percent in October 2013 compared to the previous months. Scrutinizing the sub-sectors in the same period, the increases in the production of intermediate goods, capital goods and non-durable consumer goods were higher than the growth in industrial production, while the increases in production of energy sector and durable consumer goods were lower than the increase in industrial production. Significant production increases were recorded in sectors such as manufacturing of food products (4.8 percent), manufacturing of electrical equipment (8.8 percent), manufacturing of motor vehicles, trailers and semi-trailers (8.5 percent) and manufacturing of furniture (9.7 percent).

Capacity utilization rate of manufacturing industry, which is another leading indicator for economic activity, increased by 0.2 percentage point on average in January-November period of 2013, compared to the same period of the previous year and was realized as 74.5 percent. Seasonally adjusted capacity utilization rate also increased modestly and realized as 75.7 percent in November.

The value added in the services sector increased by 5.2 percent in the first nine months of 2013. Scrutinizing the sub-sectors, it is observed that the production in all sub-sectors increased; in fact growth rates accelerated in the same period compared to last year. Considering the main sub-sectors, it is observed that growth rates were recorded as 7.4 percent in construction, 4.5 percent in wholesale and retail trade, 8.7 percent in financial intermediation and 6.5 percent in real estate, renting and business activities sectors. In the same period, growth rates in education and health and social work sectors were realized as 4.6 percent and 5 percent, respectively.

Figure 2.2: Industrial Production Index and Capacity Utilization Rate



Source: TURKSTAT and CBRT

2.1.1.2. Labor Market

In 2012, employment growth was realized above the PEP (2013-2015) forecast. Despite low growth, with the effects of measures taken to cope with unemployment, unemployment rate realized as 9.2 percent in 2012. Employment in services sector was especially effective in this development.

In 2012, industrial sector value added increased by 1.9 percent while employment growth was 1 percent, implying a slowdown compared to the previous year. In the industrial sector 47 thousand new jobs were created due to job losses in some subsectors, whereas 53 thousand additional jobs were provided in manufacturing sector. As a result, the share of industrial sector in total employment was realized as 19.1 percent.

Table 2.2: Labor Market Developments

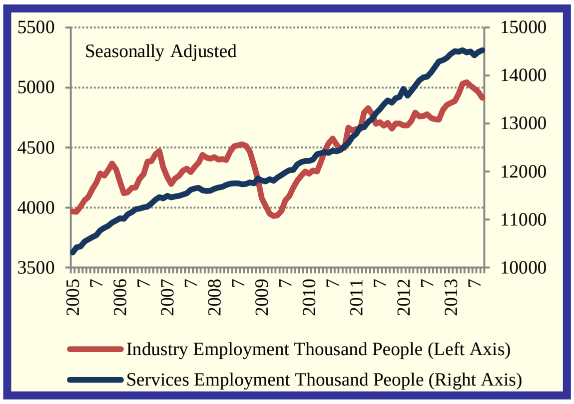
(15+Age, Thousand)

	Annual		2012				2013		
	2011	2012	I	II	III	IV	I	II	III
Working Age Population	53,593	54,724	54,365	54,599	54,841	55,083	55,250	55,485	55,715
Labor Force Part. Rate, %	49.9	50.0	47.9	50.5	50.7	50.7	49.6	51.6	51.6
Female	28.8	29.5	27.4	30.2	30.1	30.2	29.6	31.8	31.3
Male	71.7	71.0	69.1	71.4	71.9	71.8	70.3	72.0	72.6
Labor Force	26,725	27,339	26,058	27,554	27,812	27,921	27,430	28,657	28,766
Employment	24,110	24,821	23,338	25,282	25,367	25,291	24,546	26,130	25,960
Unemployed	2,615	2,518	2,721	2,272	2,445	2,630	2,884	2,526	2,806
Employment Rate, %	45.0	45.4	42.9	46.3	46.3	45.9	44.4	47.1	46.6
Unemployment Rate, %	9.8	9.2	10.4	8.2	8.8	9.4	10.5	8.8	9.8
Non-Agriculture, %	12.4	11.5	12.7	10.4	11.3	11.7	12.9	11.0	12.3
Among Young People, %	18.4	17.5	18.3	15.9	17.2	18.8	20.4	16.6	18.7
Female, %	11.3	10.8	11.1	9.3	11.1	11.6	12.1	10.7	12.4
Employment by Sectors									
Agriculture	6,143	6,097	5,427	6,363	6,564	6,027	5,531	6,283	6,511
Non-Agriculture	17,967	18,724	17,911	18,919	18,803	19,264	19,015	19,847	19,449
Industry	4,704	4,751	4,684	4,760	4,745	4,814	4,886	5,044	4,964
Services	13,262	13,975	13,227	14,158	14,058	14,452	14,127	14,802	14,487

Source: TURKSTAT

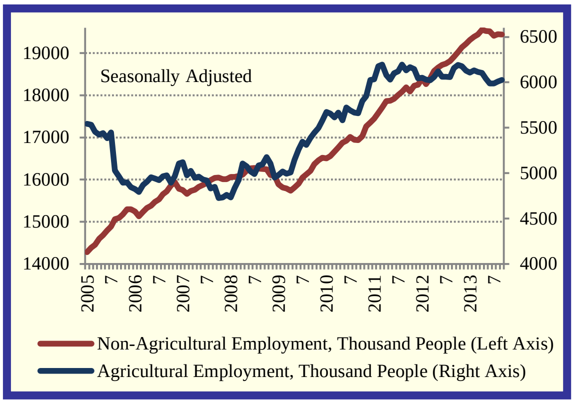
In the services sector, while value added increased by 2.4 percent, employment increased by 5.4 percent in 2012. Contribution of construction sector to the employment performance in services sector was negligible. Employment in construction sector and wholesale and retail trade sector increased by 33 thousand and 22 thousand respectively, while 713 thousand new jobs were created in the services sector. Thus, in the non-agricultural sector, employment increased by 4.2 percent and 760 thousand new jobs were created in 2012.

Figure 2.3: Industry and Services Employment



Source: TURKSTAT

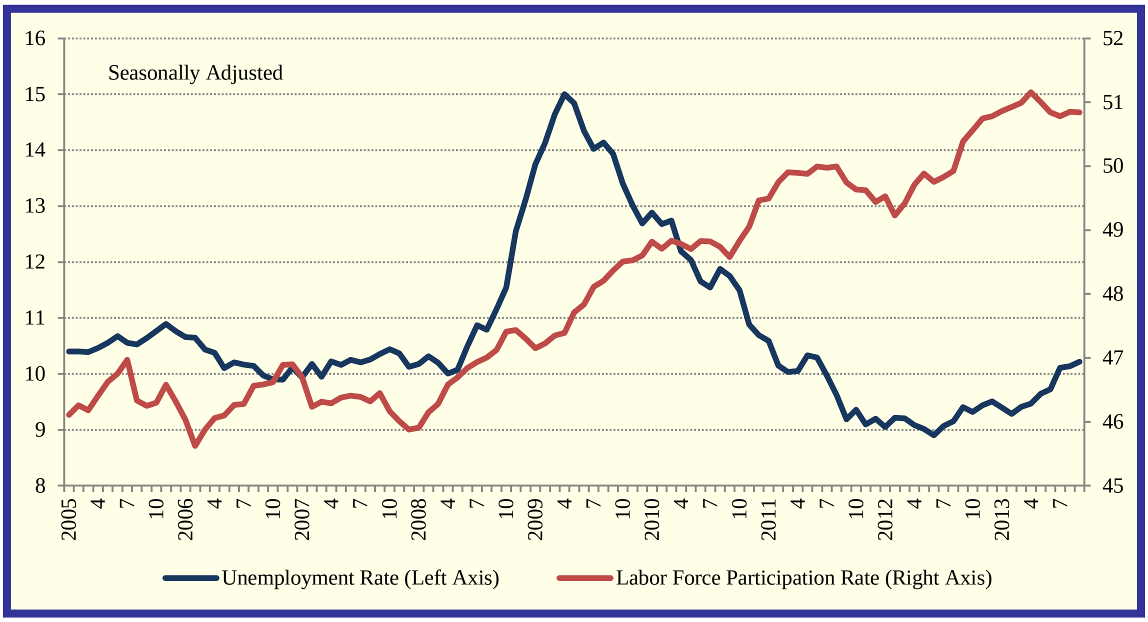
Figure 2.4: Agricultural and Non-Agricultural Employment



Source: TURKSTAT

A noteworthy issue regarding labor market developments in 2012 was the shrinking agricultural employment. In this year, 46 thousand jobs were lost and thus employment decreased by 0.7 percent in agricultural sector. As a result, the share of agricultural sector in total employment, which was 25.5 percent in 2011, declined to 24.6 percent in 2012.

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



Source: TURKSTAT

As a result of these developments in agricultural and non-agricultural sectors, 711 thousand new jobs were created and employment increased by 2.9 percent in 2012. The unemployment rate, which was 9.8 percent in 2011, declined to 9.2 percent in 2012 in spite of 0.1 percentage point increase in labor force participation rate. Thereby, 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, which indicates overall effectiveness and thus the success of the policies.

After following a flat course in 2012, seasonally adjusted industrial sector employment recorded significant increases starting from last quarter of 2012 until May 2013 and then started to decline (Figure 2.3). Seasonally adjusted employment in the services sector remained unchanged in the third quarter. Therefore, seasonally adjusted employment in non-agricultural sector has slightly decreased in the third quarter of 2013. However, employment in agricultural sector decreased in the first two quarters of 2013 and recovered in the third quarter (Figure 2.4).

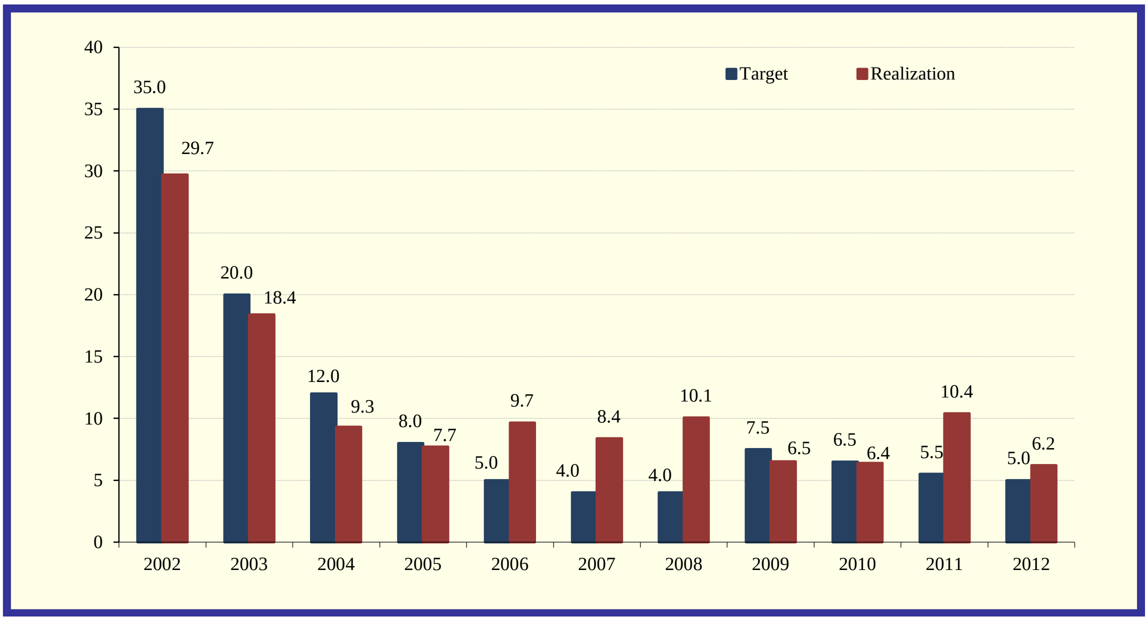
In September 2013, seasonally adjusted total employment increased by 117 thousand people compared to the end of the previous year while the labor force participation rate did not change compared to the end of the previous year. However, due to insufficient employment compared to the increase in labor force, seasonally adjusted unemployment rate rose to 10.2 percent in September 2013 (Figure 2.5).

2.1.2. Inflation, Monetary and Exchange Rate Policies

2.1.2.1. Inflation

Having hit 11.14 percent in the April 2012, annual CPI inflation trended downwards in the rest of the year and decreased to 6.16 percent at the year-end (Figure 2.6). Annual inflation declined particularly due to diminishing lagged effects of the depreciation of the TL and favorable course in unprocessed food prices compared to historical levels. In addition, slowing domestic demand and stable exchange rate made positive contribution to inflation outlook. Across subcategories, annual energy inflation preserved high levels due to public arrangements in April and October of 2012. Annual inflation in food group ended 2012 with a low level owing to unprocessed food prices. As for the services group, annual inflation remained on a mild track; while the core goods group inflation decreased due to removal of the effects of TL depreciation. Therefore, annual core inflation indicators SCA-H and SCA-I recorded decreases. Consequently, due to the removal of the effects of depreciation in the TL and favorable course in unprocessed food prices, annual CPI inflation decreased by 4.3 percentage points compared to previous year and stayed within uncertainty band.

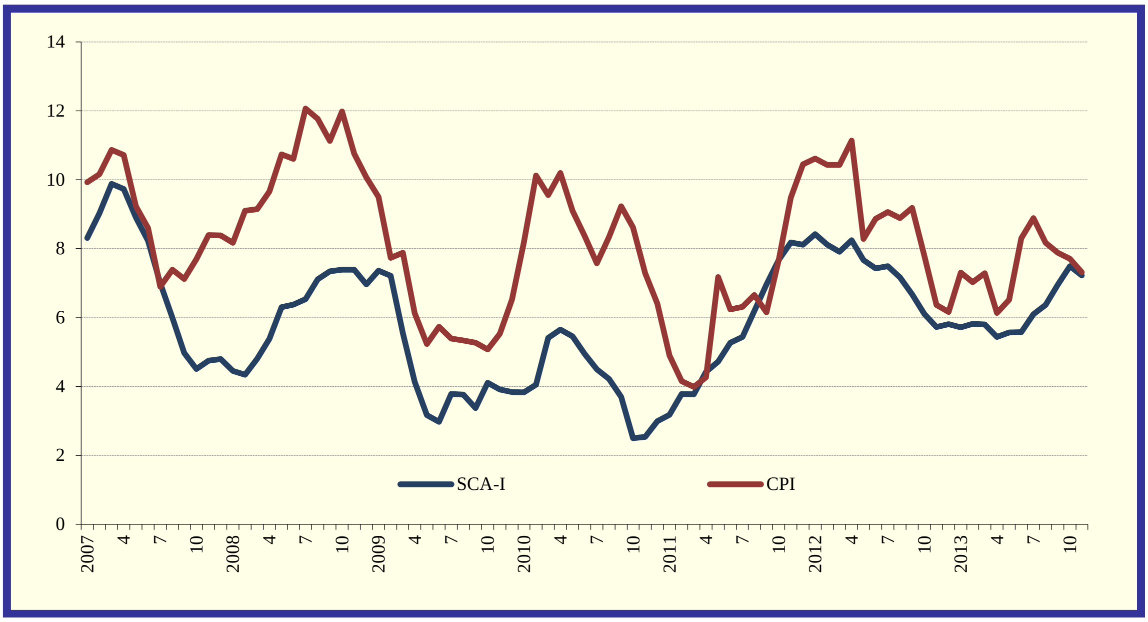
Figure 2.6: Annual Inflation Targets and Realizations (CPI, %)



Source: CBRT, TURKSTAT

Data released up to November suggest that annual inflation exhibited an upward trend in 2013. In this period, annual inflation increased mostly due to tax adjustments in the tobacco products, the rise in unprocessed food inflation and the effects of TL depreciation. Across subcategories, annual energy inflation hit a historical low level with 2.68 percent in November owing to the absence of public price adjustments within the year despite the TL depreciation. While the annual inflation in processed food group slowed down compared to year-end of 2012, annual unprocessed food inflation preserved a high level especially after June. Thus, annual food inflation increased to 9.77 percent as of November. In this period, annual inflation in services recorded gradual increases and that in core goods increased in the second half of the year due to the effects of TL depreciation. Therefore, core inflation indicators, which remained on a mild track in the first half of the year, showed an upward trend starting from July. As a result, annual CPI inflation stood at 7.3 percent and annual change in core inflation indicator of I stood at 7.2 percent as of November.

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



Source: TURKSTAT

2.1.2.2. Monetary and Exchange Rate Policies

Following the global financial crisis, monetary policy in many countries started to address financial stability, in addition to price stability. In the last three years the Central Bank of the Republic of Turkey (CBRT) 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, CBRT 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 last quarter of 2012, uncertainties regarding the global economy persisted, causing CBRT to maintain a flexible monetary policy framework, while considering macro financial risks as well. Under these circumstances of accelerated capital inflows, so as to balance risks to financial stability, interest rates were kept low on the one hand, and macro prudential measures were continued, on the other. Improvement in risk perceptions for Turkey, vigorous use of the reserve options mechanism and the mild course of commercial loans enabled a reasonable reduction in the upper band of the interest rate corridor. Consequently, the interest rate corridor was narrowed by a 50-basis points O/N lending rate cut in November. Moreover, in order to support financial stability, FX reserve options coefficients (ROC) were raised by 0.1 percentage point in November for all tranches bigger than 40 percent. Meanwhile, gold reserve options coefficients in all tranches were raised by 0.2 percentage point in November; and by 0.1 percentage point in December. In December, the policy rate was reduced by 25 basis points. In order to support financial stability and extend the maturity of FX-denominated liabilities of the banking sector, FX reserve requirement ratio for deposits with 1 year or longer maturities besides other FX liabilities with maturities longer than 3 years was raised by 0.5 percentage point in December.

In the first quarter of 2013, in the environment of faster-than-expected credit growth amid robust capital flows, short-term interest rates were kept low to contain risks to financial stability on one hand, and macro prudential measures were continued in order to increase FX reserves, on the other. Accordingly, in January and February, the O/N lending and borrowing rates were reduced by 25 basis points. Furthermore, due to reduced need for a widened interest rate corridor given the automatic stabilization property of the reserve options mechanism, the O/N lending rate was lowered by 100 basis points in March. Continued policy rate reductions in other emerging economies, expectations for an increase in global liquidity due to the decisions taken by the Bank of Japan and re-acceleration of the capital inflows to Turkey led to lowering of O/N lending and borrowing interest rates by 50 basis points in April to rebalance the risks regarding the financial stability.

In order to support financial stability and extend the maturity of FX-denominated liabilities of the banking sector, TL and FX required reserve ratios for short term deposits and other liabilities were increased modestly. Moreover, in order to complete the establishment process and thereby enhance the efficiency of the reserve options mechanism, the tranches of 35-40 percent and 15-20 percent were added to the FX reserve option ratios and the gold reserve option ratios, respectively. In addition, except for the first tranche, FX reserve option coefficients were increased by 0.1 and 0.2 percentage points in March and April whereas gold reserve option coefficients were increased by 0.1, 0.1 and 0.2 percentage points in January, March and April respectively.

In the beginning of the second quarter, due to maintenance of strong capital flows and credit growth above the reference value, short-term interest rates were kept low to rebalance risks regarding financial stability and macro prudential measures were sustained in order to increase FX reserves. Accordingly, in May, policy rate and O/N lending and borrowing rates were reduced by 50 basis points. In May, FX reserve requirement ratios were raised in order to balance risks to financial stability; accordingly, the effective reserve requirement ratio was increased to 11.9 percent. Moreover, to enhance the efficiency of the ROM, the tranche of 30-35 percent was added to the FX reserve options coefficients, and the ROC in all tranches excluding the first one was raised by 0.1 percentage point. In the meantime, due to aggravated uncertainties regarding global monetary policies as of end-May, emerging economies experienced capital outflows and excessive volatility in the exchange rates. Because of the excessively volatile exchange rates and the growth of credit above the reference value, CBRT delivered temporary additional monetary tightening and launched FX selling auctions in the succeeding period to underpin the effect of monetary tightening.

In the third quarter of the year, in order to prevent the distortion of the general pricing behavior due to global uncertainties as well as the depreciation of the TL and soaring inflation, the upper band of the interest rate corridor was increased by 75 and 50 basis points in July and August, respectively. Moreover, CBRT decided neither to conduct FX selling auctions nor to provide the banks with TL liquidity via primary dealers facility on the days of additional monetary tightening. In this period, CBRT adopted a monetary policy stance that focuses on inflation indicators while at the same time aims to contain the negative effects of elevated uncertainties regarding global monetary policies. Accordingly, it continued to provide the market with foreign exchange liquidity via FX selling auctions.

The fact that FED adopted a data-dependent monetary policy regarding stimulus tapering and that announced data demonstrates a fluctuating course gave rise to elevated levels of volatility in global financial markets. In this period, CBRT decided to increase the predictability of the TL liquidity policy in order to limit the impacts of global monetary policy uncertainties on domestic economy. To this end, it decided to pursue a strategy of reducing interest rate uncertainty in order to prevent the economy to go astray toward a cycle not compatible with macroeconomic fundamentals. Accordingly, CBRT has been announcing total and remaining days of additional monetary tightening. Moreover, CBRT began to conduct FX selling auctions at each day of additional monetary tightening and started to announce the minimum amount that will be sold at each of the FX selling auction that will be conducted for any day of additional tightening. The minimum amount of FX selling through auctions, which can be adjusted by CBRT depending on the conjuncture, is now 50 million dollars but the amount of daily foreign exchange selling auctions might be raised up to 10 times of the announced minimum amount.

In November, CBRT decided to strengthen the cautious stance and reduce the volatility of short term money market rates. To this end, one month repo auctions were terminated, as a result of which interbank money market rates materialized around 7.75 percent. In addition, the maximum outstanding amount of the funding provided via one-week repo auctions was reduced from 10 billion TL to 6 billion TL in December. The total amount of funding facility offered to primary dealer banks within the framework of open market operations was reduced from 7 percent to 2 percent of the outstanding TL denominated Treasury securities purchased from Treasury auctions. Thus, the total amount of funds available to primary dealer banks through this facility was reduced approximately from 23 billion TL to 6.5 billion TL.

In 2014, the CBRT will continue to consider financial stability by balancing macroeconomic risks and will enhance the effectiveness of the monetary policy and liquidity management. In accordance with this policy, foreign selling auctions will be conducted in 2014. The minimum foreign exchange selling auction amount is planned to be 100 million dollars per day in January 2014. In addition to the FX selling auctions, the foreign exchange reserve option coefficients after the tranche over 40 percent is raised by 0.4 point. With this measure a decline in ROM utilization rate is expected. All these precautions will increase TL liquidity need of the banking system.

In addition to these precautions, one-week repo auctions will continue to be held at the interest rate for one-week repo auctions via the quantity auction method at Stable Funding Rate-1. In this context, to be effective from 6 January 2014, the upper limit for total amount of bids to be offered by each institution that are parties to OMO shall be twice the share of TL required reserves to be maintained by the institution within the amount of the total TL required reserves to be maintained by banks. Moreover, in order to simplify the structure of reserve requirements that are used as a monetary and macro-prudential policy tool, a new approach has been adopted. Accordingly, instead of deducting specified items from the total domestic liabilities, only the items subject to reserve requirements will directly be taken into account while calculating liabilities subject to reserve requirements. Thus, immaterial items, which do not have a direct impact on the monetary policy but reduce the efficiency of the operational processes, have been excluded from coverage of reserve requirements.

2.1.3. Financial Sector

Turkish banking sector has continued to grow and maintained its stable structure in 2013 with the effect of favorable macroeconomic stance and upgrade in credit ratings. As of October 2013, number of banks increased to 50 compared to the previous year-end due to a new foreign-capital bank given establishment and operating permission. Moreover, the sector maintained its development as regards alternative distribution channels, number of customers and other operational sizes.

When the balance sheet of Turkish banking sector is analyzed, it is seen that asset size which was about 773.4 billion dollars at the end of 2012 increased to 825.5 billion dollars in October 2013. Loan growth was main determinant of asset development. Subsequent to the continuation of the recovery in global markets and rising of the country rating to investment level, an increasing trend started in corporate loans as of the last quarter of 2012. Due to the upgrade of the country rating by a second rating agency in May 2013, loan growth in the sector accelerated. Within this scope, as of October 2013 loan volume of the sector has increased to 499.7 billion dollars with an 11.4 percent rise compared to the end of 2012, especially by the impact of the increase in corporate/commercial loans.

Table 2.3: General View of Turkish Banking Sector

	2006	2007	2008	2009	2010	2011	2012	October 2013
Fundamental Sizes								
Asset Size (Billion Dollars)	356.2	500.8	482.2	560.1	656.5	648.1	773.4	825.5
Loans (Billion Dollars)	156.1	246.0	242.2	263.7	343.1	363.5	448.4	499.7
Deposit (Billion Dollars)	219.2	307.2	299.2	345.6	402.4	370.3	435.7	454.0
Number of Banks (Nr)	50	50	49	49	49	48	49	49
Number of Personnel (Thousand)	151.0	167.8	182.7	184.2	191.2	195.3	201.5	212.9
Performance Indicators								
Net Term profit (Billion Dollars)	8.1	12.8	8.8	13.6	14.4	10.6	13.3	11.0
Return on Assets (%)	2.5	2.8	2.0	2.6	2.5	1.7	1.8	1.4
Return on Equity (%)	20.1	21.7	16.8	20.3	20.1	15.5	15.7	12.4
Loan/ Total Assets (%)	44.0	49.2	50.2	47.1	52.2	56.1	58.0	60.5
Loan /Deposit (%)	62.1	79.9	80.6	77.3	85.3	98.2	102.9	110.1
Risk Indicators								
Capital Adequacy Ratio (%)	22.1	19.0	18.0	20.6	18.7	16.6	17.9	15.8
On-Balance Sheet FX Position (Billion Dollars)	-5.5	-8.3	-3.3	-11.6	-14.0	-17.8	-15.5	-25.9
FX Net General Pos./Equity Standard Ratio (%)	0.1	0.2	-0.1	0.4	0.1	0.3	2.2	1.0
NPL /Gross Loans (%)	3.8	3.5	3.7	5.3	3.7	2.7	2.9	2.8
Securities Portfolio /Assets (%)	31.8	21.3	26.5	31.5	28.6	23.4	19.7	17.4
Off-balance Sheet Transactions /T. Assets (%)	55.5	66.3	65.0	69.5	103.1	134.9	143.1	115.7

Source: BRSA

As of October 2013, while the share of securities in total assets is decreasing, the share of loans keeps increasing. In the mentioned period, the share of securities in total assets decreased from 19.7 percent to 17.4 percent, while the share of loans increased from 58 percent to 60.5 percent. The deposit to loan conversion ratio, which kept increasing in parallel with the increase in loans and reached to 110.1 percent in October 2013 from 102.9 percent as of end-2012, also indicates that the sector gradually fulfills its intermediation function stronger.

Beginning from end-May of 2013, depending especially on the volatility in capital flows created by global uncertainties, a decrease in the value of TL was seen as well as fluctuations in financial markets. However, soundness and performance indicators of the banking system maintain its positive outlook. As of October 2013, the sector's capital adequacy ratio is 15.8 percent, which is highly above the legal ratio of 8 percent and the target ratio of 12 percent. The existing equity capital of the Turkish banking sector is mostly composed of Tier-I representing cash capital elements which serve as a buffer against troubles. Due to its strong capital structure, the sector's resilience against sudden shocks is increasing and this strong basis supports the stability in economy.

The ratio of non-performing loans to gross loans, which indicates the sector's credit risk, keeps its decreasing trend and declined from 2.9 percent by the end of 2012 to 2.8 percent as of October 2013. The ratio of FX net general position to equity standard is 1 percent as of October 2013, which does not constitute a significant risk. Off-balance sheet transactions whose ratio to assets is increasing in recent years are for risk-protection.

Turkish banking sector continued making profit during the global crisis. The banking sector net profit which was 13.3 billion dollars in 2012 realized as 11 billion dollars in the first ten months of 2013. Return on assets and return on equities which were respectively 1.8 percent and 15.7 percent in 2012 realized as 1.4 percent and 12.4 percent in first ten months of 2013.

In accordance with the Capital Markets Law No. 6362 enacted on 30 December 2012, existing securities, gold and derivatives exchanges were merged under Borsa İstanbul Inc. in April 2013.

Stock market displayed an upward trend in 2012 and BIST 100 index increased by 52.3 percent at the end of 2012 in comparison to the end of previous year, reaching 77,676 points. The index maintained its upward trend at the beginning of 2013 but started to decline towards the middle of the year. These developments caused the index to move back to its levels at the end of 2012, realized as 77,178 as of the end of October. BIST 100 Euro index, which reached 2,276 points at the end of 2012 with an increase of 58.9 percent compared to the end of the previous year, declined by 16.8 percent in the first ten months of 2013 and closed at 1,948 points. The share of foreign investors in the stock market maintained its average level and realized at 65.8 percent at the end of 2012 and 63.3 percent at the end of the first ten months of 2013.

Growth trend in debt instrument markets that started in 2010 has continued. The value of private sector debt instruments, which was 27.4 billion TL at the end of 2012, has increased to 34.8 billion TL at the end of October 2013.

There were 59 insurance companies and 1 reinsurance company operating in insurance and private pension sector, as of 30 June 2013. 35 of these insurance companies were operating in the area of non-life insurance, 17 in life insurance and pension area and 7 in life insurance area. In the same period, six-month premium production in insurance sector realized as 12.5 billion TL with a 24.8 percent increase compared to same period of previous year. Total assets of the sector have been 57.5 billion TL as of June 2013.

The private pension system accelerated its growth in 2013, mainly due to the new state incentive of matching contribution that started at the beginning of January 2013. As of 30 November 2013, the number of participants reached to 4 million 19 thousand. Within the first eleven months of 2012, the increase in the number of participants was 416 thousand, whereas within the same period of 2013 this figure has been 891 thousand. Total fund amount of the system, excluding state incentive, has risen by 24.1 percent compared to end of 2012, reaching to 25.3 billion TL as of 30 November 2013.

In the compulsory earthquake insurance system, which was formed to meet the earthquake damages in housing through insurance, total number of compulsory earthquake insurance policies reached to 5 million 943 thousand as of 25 October 2013, with a 34 percent increase compared to same period of previous year.

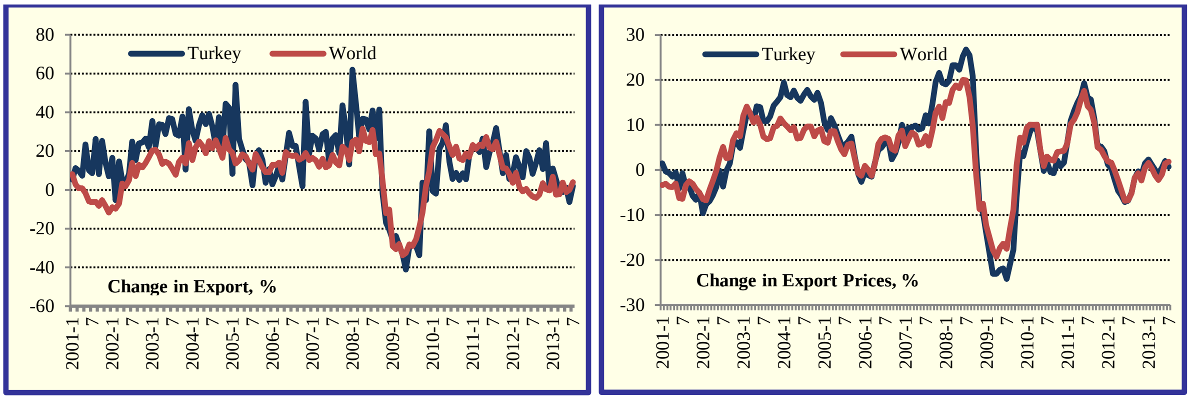
2.1.4. Balance of Payments

2.1.4.1. Current Account

Total exports increased remarkably as a result of market and product diversification and contribution of gold exports in 2012. On the other hand, imports recorded a contraction due to sluggish domestic demand and policies limiting credit growth rate. Thus, trade deficit and current account deficit declined in this year. In fact, the current account deficit declined to 48.5 billion dollars, which was 75.1 billion dollars in 2011, and trade deficit declined to 65.3 billion dollars from 89.1 billion dollars, at the end of 2012. In the same period, trade volume reached 389 billion dollars from 375.7 billion, thus trade volume to GDP ratio, which was 48.5 percent in 2011, reached 49.5 percent in 2012.

Exports, which increased as a result of alternative policies despite the ongoing global problems in 2012, have followed a flat course in 2013. Gold exports, which was at high levels in 2012, declined significantly in the first ten months of 2013 compared to same period of previous year and thus its positive contribution to export performance declined. Acceleration in gold imports and positive developments in domestic demand were effective in increase of imports in 2013. As a result of these developments, in January-October 2012 period, trade deficit increased to 66.2 billion dollars from 54.7 billion dollars and current account deficit increased to 51.9 billion dollars from 39.6 billion dollars compared to same period of previous year.

Figure 2.8: Developments in Exports and Export Prices



Source: IMF-IFS, TURKSTAT

Table 2.4: Balance of Payments

(Billion Dollars)

	Annual		January-October	
	2011	**2012**	**2012**	**2013**
Current Account	**-75.1**	**-48.5**	**-39.6**	**-51.9**
Trade Balance	-89.1	-65.3	-54.7	-66.2
Total Exports	143.4	163.2	134.6	134.1
Exports (fob)	134.9	152.5	126.1	124.5
Total Imports	-232.5	-228.6	-189.2	-200.3
Imports (cif)	-240.8	-236.5	-195.8	-207.1
Balance on Services	20.1	22.6	20.5	21.6
Credit	40.7	43.2	37.2	40.9
Tourism Revenues	25.1	25.3	22.2	25.0
Debit	-20.5	-20.5	-16.8	-19.2
Balance on Income	-7.8	-7.2	-6.3	-8.2
Credit	4.0	5.0	3.9	3.7
Debit	-11.8	-12.2	-10.2	-11.8
Current transfers	1.8	1.4	1.0	0.9
Capital and Financial Account	**65.7**	**47.3**	**35.8**	**48.1**
Capital Account	0.0	0.0	0.0	-0.1
Financial Account (Excluding Reserves)	63.9	68.1	56.8	59.7
Direct Investment	13.7	8.9	7.8	7.2
Direct Investment in Turkey	16.0	13.0	11.2	9.2
Direct Investment Abroad	-2.3	-4.1	-3.4	-2.0
Portfolio Investment	22.0	40.8	30.3	22.8
Other Investment	28.2	18.4	18.7	29.7
Assets	11.1	-0.6	3.1	2.5
Liabilities	17.1	19.0	15.6	27.2
Trade Credits	2.0	1.0	0.4	3.6
Loans	18.9	9.7	6.0	14.6
Monetary Authority	0.0	0.0	0.0	0.0
General Government	-0.8	-2.1	-1.6	-0.7
Banks	12.5	5.2	2.4	14.6
Other Sectors	7.1	6.6	5.3	0.6
Currency and Deposits	-4.3	7.8	8.7	8.6
Monetary Authority	-1.9	-2.2	-2.0	-1.7
Banks	-2.4	10.0	10.7	10.2
Other Liabilities	0.5	0.5	0.5	0.6
Reserve Assets	1.8	-20.8	-21.0	-11.5
Net Errors and Omissions	**9.4**	**1.2**	**3.7**	**3.8**

Source: CBRT

In 2012, Turkish exports recorded an increase of 13 percent, while world exports increased by around 0.1 percent. Export prices decreased by 3.1 percent, real export increased by 16.7 percent. World exports, which increased by around 1.5 percent in the first three quarters of 2013, displayed a better performance compared to the same period of previous year. With the impact of recovery in EU economies, exports to those countries have resurged. Despite all these developments, due to base effect in gold exports, total exports reached 138.7 billion dollars with a decrease of 0.8 percent in January-November period. In the same period, exports excluding gold increased by 6.5 percent. Recent figures point out that slowdown in exports of gold and recovery in non-gold exports continue in November.

Imports realized as 236.5 billion dollars with a 1.8 percent decline due to measures in the context of rebalancing policies in 2012. However, the slight upward trend in imports, which started in last quarter of 2012, has accelerated in the first eleven months of 2013. Thus, in January-November 2013 period, imports reached 228.5 billion dollars with a 5.4 percent increase compared to the same period of previous year. In the same period, 87.1 percent increase in the gold imports is noteworthy. This rapid increase in gold imports in this period might be attributed to purchases for compensating the decline in gold stocks resulting from exports in 2012 and to demand effect due to rapid decline in international gold prices. This increase is considered to be effective for the decrease in gold stocks to compensate in 2012 and the rapid decline in international prices. In this period, imports excluding gold increased by 2.6 percent level, and realized as 214.8 billion dollars. As a result of recovery of domestic demand, imports of consumer goods increased by 13.5 percent in the first eleven months of 2013, imports of capital goods and intermediate goods imports increased by 7.8 percent and 4 percent, respectively.

Table 2.5: Foreign Trade by Broad Economic Categories Classification

(Billion Dollars)

	Annual					January-November				
	2011	Share %	2012	Share %	Change %	2012	Share %	2013	Share %	Change %
Total Exports	**134.9**	**100.0**	**152.5**	**100.0**	**13.0**	**139.9**	**100.0**	**138.7**	**100.0**	**-0.8**
Capital Goods	14.2	10.5	13.7	9.0	-3.2	12.4	8.9	14.1	10.2	13.6
Intermediate Goods	67.9	50.4	82.7	54.2	21.7	76.4	54.6	68.7	49.5	-10.2
Consumption Goods	52.2	38.7	55.6	36.4	6.4	50.6	36.2	55.3	39.9	9.4
Other	0.6	0.4	0.5	0.3	-7.0	0.4	0.3	0.6	0.4	35.3
Total Imports	**240.8**	**100.0**	**236.5**	**100.0**	**-1.8**	**216.7**	**100.0**	**228.5**	**100.0**	**5.4**
Capital Goods	37.3	15.5	33.9	14.3	-9.0	30.6	14.1	33.0	14.4	7.8
Intermediate Goods	173.1	70.8	174.9	74.0	1.0	160.9	74.3	167.3	73.2	4.0
Consumption Goods	29.7	13.3	26.7	11.3	-10.1	24.3	11.2	27.6	12.1	13.5
Other	0.7	0.3	1.0	0.4	34.1	0.9	0.4	0.6	0.3	-32.2

Source: TURKSTAT

The share of EU countries in exports decreased by 7.4 percentage points compared to the previous year and realized as 39 percent in 2012. The share of other countries in exports rose by 7.8 percentage points and realized as 59.5 percent as a result of weak recovery in EU countries and market diversification efforts. Share of imports from EU countries in total imports declined to 37.1 percent in the same period, indicating a 0.9 percentage point decline. Share of exports from EU economy realized as 41.7 percent in the first eleven months of 2013, representing a 2.8 percentage points rise, as a result of more favorable expectations towards solution of problems in EU. In the same period, share of other countries in exports declined slightly and realized as 56.7 percent as a result of an increase in exports to EU.

Table 2.6: Foreign Trade by Country Groups

(Billion Dollars)

	Annual					**January-November**				
	2011	**Share %**	**2012**	**Share %**	**Change %**	**2012**	**Share %**	**2013**	**Share %**	**Change %**
Merchandise Exports	**134.9**	**100.0**	**152.5**	**100.0**	**13.01**	**139.9**	**100.0**	**138.7**	**100.0**	**-0.8**
European Countries (EU-28)	62.6	46.4	59.4	39.0	-5.1	54.4	38.9	57.8	41.7	6.2
Other Countries	69.8	51.7	90.8	59.5	30.1	83.3	59.6	78.7	56.7	-5.5
Other European	12.7	9.4	14.2	9.3	11.2	13.0	9.3	13.1	9.4	0.6
North Africa	6.7	5.0	9.4	6.2	40.9	8.6	6.1	9.1	6.6	6.3
Other Africa	3.6	2.7	3.9	2.6	7.7	3.5	2.5	3.7	2.7	4.6
North America	5.5	4.0	6.7	4.4	22.0	6.1	4.3	6.0	4.3	-1.2
Cent. America&Caribbean	0.6	0.5	0.8	0.5	22.9	0.7	0.5	0.9	0.7	33.6
South America	1.8	1.4	2.2	1.4	19.1	2.0	1.4	1.9	1.4	-2.9
Near And Middle East	27.9	20.7	42.5	27.8	52.0	39.3	28.1	32.4	23.4	-17.6
Other Asia	10.2	7.6	10.6	6.9	3.7	9.6	6.8	10.9	7.9	14.0
Australia & N. Zealand	0.5	0.4	0.5	0.3	2.0	0.4	0.3	0.5	0.4	10.1
Other Countries	0.2	0.1	0.1	0.1	-35.7	0.1	0.1	0.1	0.1	20.6
Turkish Free Zones	2.5	1.9	2.3	1.5	-9.8	2.1	1.5	2.2	1.6	4.4
Merchandise Imports	**240.8**	**100.0**	**236.5**	**100.0**	**-1.8**	**216.7**	**100.0**	**228.5**	**100.0**	**5.4**
European Countries (EU-28)	91.4	38.0	87.7	37.1	-4.1	80.0	36.9	83.7	36.6	4.7
Other Countries	148.4	61.6	147.8	62.5	-0.4	135.8	62.6	143.6	62.9	5.8
Turkish Free Zones	1.0	0.4	1.0	0.4	0.7	1.0	0.4	1.1	0.5	20.1

Source: TURKSTAT

Services balance of 20.1 billion dollars in 2011, increased to 22.6 billion dollars in 2012 with the effect of the rise in transportation revenues. In January-October 2013 period, services balances rose by 5.8 percent compared to the same period of previous year and realized at 21.6 billion dollars.

Increase in tourism revenues, after 10.9 percent in 2011, severely slowed down and realized as 1.2 percent in 2012. It displayed a rapid recovery and increased by 12.7 percent in the first ten months of 2013. This successful performance in revenues was due to increase in both number of tourists and average spending of tourists. Number of foreign tourists increased by 12.5 percent in January-October 2013 period, although displayed a slight increase in 2012. Similarly, increase in average spending per foreign tourist in dollar terms, which was 0.8 percent in 2012, reached to 8.6 percent in the first three quarter of 2013. In this context, the average expenditure per foreign tourist, which was 696 dollars in the first three quarter of 2012, reached 755 dollars in the same period of 2013.

In 2012, income balance deficit declined to 7.2 billion dollars with a recovery of 0.7 billion dollars. In January-October 2013 period, a deterioration of 1.8 billion dollars was recorded compared to same period of previous year and the deficit increased to 8.2 billion dollars.

Surplus of current transfer, which was 1.8 billion dollars in 2011, decreased to 1.4 billion dollars in 2012. In January-October 2013 period, current transfers decreased by 0.2 billion dollars compared to same period of previous year and recorded a surplus of 0.9 billion dollars.

Box 2.1: Cyclical Effects of Gold Trade on Current Account Balance

As gold is a traditionally important store of value, domestic demand for gold in Turkey has been high in almost all periods. Together with insufficient gold production, Turkey generally has been a net importer of gold. In 2001-2011 period, the share of gold exports in GDP was 0.2 percent on average, whereas this ratio increased to 1.7 percent in 2012. In the same period, the share of gold imports in GDP was 0.7 percent on average while this ratio increased to 1 percent in 2012 and to 2 percent in the first nine months of 2013, respectively.

Significant increase in gold exports in 2012 and gold imports in 2013 brought gold trade to the forefront of the discussions on the current account balance. High level of gold export in 2012 made above-the-average contribution to trade balance. Gold exports declined significantly in the first ten months of 2013 compared to 2012 and impact of its extra contribution to export performance relatively vanished.

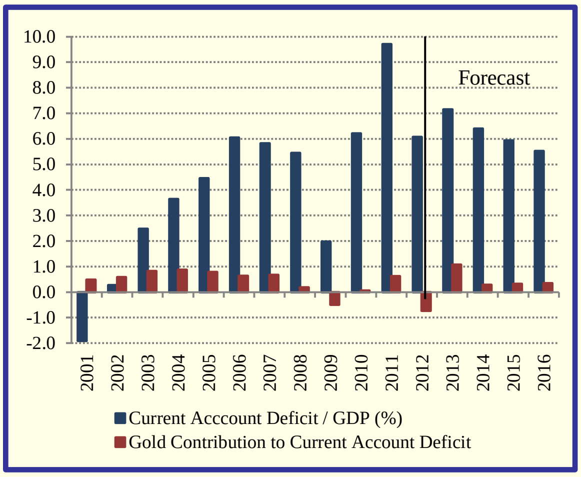
On the other hand, gold imports increased remarkably in 2013 compared to previous period. As a matter of fact, 85 percent increase in gold imports during the 2013 January-October period is noteworthy. This rapid increase in gold imports in this period might be attributed to purchases to compensate the decline in gold stocks resulting from exports in 2012 and to demand effect due to rapid decline in international gold prices.

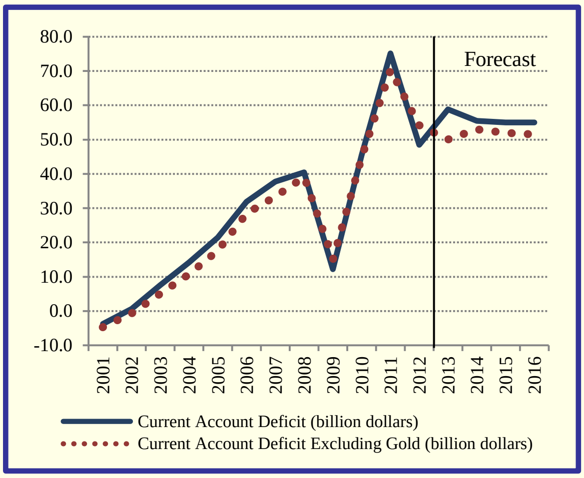
In this context, developments regarding exports and imports of gold in 2012 and 2013 had a cyclical effect on the current account deficit. In fact, the contribution gold trade to current account deficit to GDP ratio, which was around -0.5 percentage point on average in 2001-2011 period, improved to 0.7 percentage point in 2012 and declined back to -1.1 percentage points in the first three quarter of 2013. As a matter of fact, exports to imports ratio excluding gold which was 56.9 percent in 2011 rose to 60.8 in 2012, and expected to reach 62.6 percent level in 2013.

Consequently, gold trade led fluctuations in the current account deficit recently. If gold exports had realized around historical average (1.25 billion dollars), current account deficit to GDP ratio would have been 7.7 percent instead of 6.1 percent in 2012. Similarly if gold imports had been realized around historical average (3.4 billion dollars), current account deficit to GDP ratio would have been 6 percent instead of 7.1 percent.

During the Program period, no cyclical effect from gold trade is expected on the current account deficit.

Figure: Effect of Gold Trade on Current Account Balance





Source: Realization CBRT, forecast Ministry of Development

2.1.4.2. Capital and Financial Account

Net private portfolio investment flows towards emerging markets and developing economies increased to 229.9 billion dollars in 2012, from 79 billion dollars in 2011. Net foreign direct investment flows to those economies declined to 465.5 billion dollars in 2012, from 526.7 billion dollars in 2011. In other private capital flows, which is mainly consisted of credit flows, the outflow increased to 458.3 billion dollars in 2012, from 106.4 billion dollars in 2011. Thereby, total net private capital flows to emerging market and developing economies decreased from 499.3 billion dollars in 2011 to 237.1 billion dollars in 2012.

Turkish economy has demonstrated a successful macroeconomic performance on global scale in the aftermath of the crisis. As a result of this performance, foreign capital flows to Turkish economy increased rapidly despite the fluctuating global capital flows. This increase continued in 2012 as well, while the fund flows to emerging markets and developing economies decreased, and capital inflow to Turkish economy increased to 68.2 billion dollars.

Despite the increase in total capital inflows, global and domestic economic developments affected the composition of inflow. With the effect of increases in global liquidity and risk appetite in 2012, portfolio investments was the largest financing item and reached 40.8 billion dollars, representing an 85.5 percent increase compared to previous year. The decrease in funding needs with slowing growth and imports, led to lower short term credit type external borrowing. Besides, banks reduced credit type borrowing and increased bond issues due to maturity and cost advantages and thereby net other investments item decreased by 34.5 percent to 18.5 billion dollars. On the other hand, with decreasing capital flows to developing economies and ongoing economic problems in Euro Area, direct investment inflows decreased to 13 billion dollars in 2012. Direct investment inflows, which amounted 13 billion dollars in 2012, were composed of 9.9 billion dollars in capital component and 2.6 billion dollars in real estate acquisition of foreign real persons and legal entities in Turkey. Strong course of net capital inflows in 2012 led to 20.8 billion dollars of reserve accumulation.

The rise in capital inflows in 2012 increasingly continued until May 2013, in January-April 2013 period total capital inflows excluding reserves increased by 143.2 percent compared to the same period of previous year and reached 43 billion dollar. In this period, portfolio investments and other investments sustained their strong trend while direct investments tended to decrease slowly. Significant amount of capital outflow from emerging economies started in May, as FED signaled a decrease in bond purchases and expectations deteriorating accordingly. In this process, capital flows to Turkish economy continued but all external financing items decreased rapidly. With significant deterioration of expectations in June and July, outflows were recorded in portfolio investments and capital account excluding reserves also recorded a 0.3 billion dollar outflow in July. In the following period, market fluctuations declined as FED signaled a slower and gradual decrease in bond purchases in order to prevent market reactions that would adversely affect global economic balances and other economic developments; all financing items increased to positive levels again.

As a result of these developments, in January-October 2013 compared to the same period of previous year, net direct investments and net portfolio investments decreased to 7.2 billion dollars and 22.8 billion dollars, respectively. Conversely, other investments increased to 29.7 billion dollars with the continuation of rises recorded in the first four months even though at a slower pace. Thereby, in the ten months of 2013, 59.6 billion dollars of capital inflow was realized, which was 2.8 billion dollars above the amount in the same period of 2012; of this amount 11.5 billion dollars was recorded as reserve asset. Capital outflows in the first ten months of 2013 compared to the same period of the previous year resulted from the decrease in GDBI on public side and BIST sales of foreigners on private side; increases in deposits and bond exports of banks were effective on capital inflows.

Box 2.2: Macro Prudential Measures

The ongoing uncertainty in the global economy and volatility of capital flows to developing economies like Turkey brings excessive fluctuation risks in exchange rate and credit growth. In order to limit the macro financial risks regarding this situation, macro prudential measures are used for strengthening financial stability, enhancing financial soundness, making credit system work efficiently and strengthening CBRT FX reserves. In this respect:

- In November 2010, loan-to-value ceilings were set as 75 percent on housing loans and as 50 percent on purchases of commercial real estate (Loan-to-value restriction on commercial real estate was abolished in April 2013).
- With the regulations in June 2011, general provisions for consumer loans (except for vehicle and housing loans) were increased. In addition, higher risk weights based on maturity were introduced for consumer loans (except for vehicle and housing loans) similar to those implemented on credit card receivables.
- In August 2011 procedures and principles for determining interest rate risk standard ratio in the banking book are set by BRSA.
- In September 2011, amendment in deposit insurance premiums of assets, non-cash loans, liabilities and commitments in the balance sheets of credit institutions by BRSA.
- Regulations since September 2011, CBRT enabled banks to hold a certain ratio of their TL-denominated required reserves as FX and standard gold, a certain ratio of their FX-dominated required reserves in standard gold.

Besides, considering the importance of monitoring loan growth extended by financing companies and the loans in the non-banking sector for financial stability:

- With the amendment on regulation on 4 October 2013, financing companies are included in the scope of reserve requirements system within the framework of their liabilities at the same rates of banks.

Macro-prudential measures as a policy tool play an active role in averting excessive credit growth. With regulations made on 8 October 2013, amendments regarding credits are as follows:

- Definition of consumer loans was included in the regulation to cover the credit cards and overdraft deposit accounts.
- With amendments the credit card limits were related to incomes. In this context; total credit card limit for the whole credit cards of a real person having a credit card for the first time was limited to twice his monthly average income for the first year and four times for latter years.
- If minimum payment of a credit card is not made 3 times in a year it will be suspended for use of cash; if minimum payment is not made consecutively 3 times in a year that credit card will be suspended for purchase of goods and services in addition to suspension for use of cash.
- The gradually increasing risk weights based on maturity on credit card installments were increased on whole maturities.
- Credit cards minimum payment ratios were increased by 5 points on each trench.
- Credit card limit of card users whose monthly or yearly average income could not be determined and whose monthly average income are below 1,000 TL was limited as 1,000 TL. In addition to that credit card issuing institutions were obliged to prove the income above 1,000 TL and monitor the permanency of income stream.
- In calculation of capital adequacy ratio, in order to increase risk weight of vehicle credits, risk weight applied to vehicle credits with maturity of 1-2 years was increased from 75 percent to 150 percent while risk weight applied to vehicle credits with maturity more than 2 years was increased from 75 percent to 200 percent.
- In order to increase general provision rates for vehicle credits by banks, exemption of vehicle credits from calculation of general provision rates was abolished.
- In order to encourage export and SME credits, general provision rates were decreased from 1 percent to 0 percent for export credits and from 1 percent to 0.5 percent for SME credits.

In order to ensure a stable growth, increasing domestic savings, which are most reliable and permanent financing source, and directing increased savings to productive investments are aimed. Within this framework amendments introduced on 31 December 2013 are the following:

- Installment period would not exceed 9 months in purchases of goods and services by credit cards. Telecommunications, jewelry and food, petroleum products expenditures would be sold without installments.
- In vehicle credits or financial leasing, loan-to-value ratio would be applied at varying rates according to value of the vehicle.
- General maturity limitation would be implemented for vehicle and consumer credits except housing loans.
- Loan-to-value ratio with varying rates for vehicle and housing loans and general maturity limitation for vehicle and consumer credits for banks were implemented for financing companies.

2.2. Medium Term Macroeconomic Scenario

Following the 2008 global crisis, stability in the world economy has not been fully achieved yet. The uncertainties about the developed economies have been continuing, whereas the desirable growth performance has not been attained in the developing countries compared to pre-crisis period. Although the expectations about 2014 are relatively promising, uncertainties about the effects of FED’s exit strategy from monetary easing on the global financial markets and world economy still exist.

Turkish economy has quickly recovered from crisis with the help of timely macroeconomic measures, together with its strong public finance and banking sector. It became a necessity to rebalance the economy as a result of the rapid surge in domestic demand contrary to sluggish external demand and thus growth was settled to a more moderate path.

The main objective of PEP is on one hand to reduce current account deficit gradually, on the other hand to increase the growth rate through minimizing the effects of global uncertainty on Turkish economy in line with the Medium Term Programme (2014-2016). In this framework, increasing domestic savings, directing existing resources to productive areas, raising productivity level of the economy, increasing employment, reducing inflation and maintaining the strong stance in public finance will be primary intervention areas. Thereby, important progress will be ensured towards achieving the long-term development goal of the Tenth Development Plan that is to upgrade the position of Turkey in international area and enhance the welfare of citizens by structural values and expectations of the nation in a reshaping world.

The Medium Term Programme (2014-2016), which is an important instrument for attaining the objectives of Tenth Development Plan (2014-2018), was enacted as a decision of Council of Ministers and was published in the Official Gazette on October 2013. The Program, which is prepared with a three-year perspective, is the official political document that constitutes a basis for the economic and social policies in the forthcoming period. The developments realized after the publication of Medium Term Programme (MTP) do not necessarily change the medium term framework set in the MTP. In this respect, the official macroeconomic framework was preserved in PEP and recent developments were also discussed.

2.2.1. Reel Sector

2.2.1.1. Demand Components of Growth

Turkish economy, which displayed a high growth performance after the global crisis, started to slow down in 2012 with the effects of macro prudential policies implemented towards rebalancing external and domestic demand. The impact of this development on the private sector investments continued in the first nine months of 2013 as well, conversely strong increases were observed in consumption and particularly in public sector investments. Accordingly, with the increase in domestic demand an overall economic recovery was observed.

Turkish economy grew by 4 percent in the first nine months of 2013 compared to the same period of previous year. In this period, while private consumption expenditures increased by 4.7 percent, public consumption expenditures increased by 5.2 percent and public sector fixed capital formation increased by 37.2 percent and these had been main drivers of growth. In the same period, private sector fixed capital investments pulled down the growth by contracting by 1.4 percent. In the rest of the year, it is foreseen that public consumption will accelerate and increase by 7.8 percent, conversely private sector consumption increase will decline slightly and will be 3.9 percent for the whole year. Contrary to forecasted developments in public consumption, public investment increase is foreseen to reach 18.6 percent throughout the year. Private sector investments are expected to contract by 0.8 percent throughout the year despite the expected moderate recovery in the rest of the year.

Table 2.7: Demand Components of Growth

(Percentage Change, at 1998 Prices)

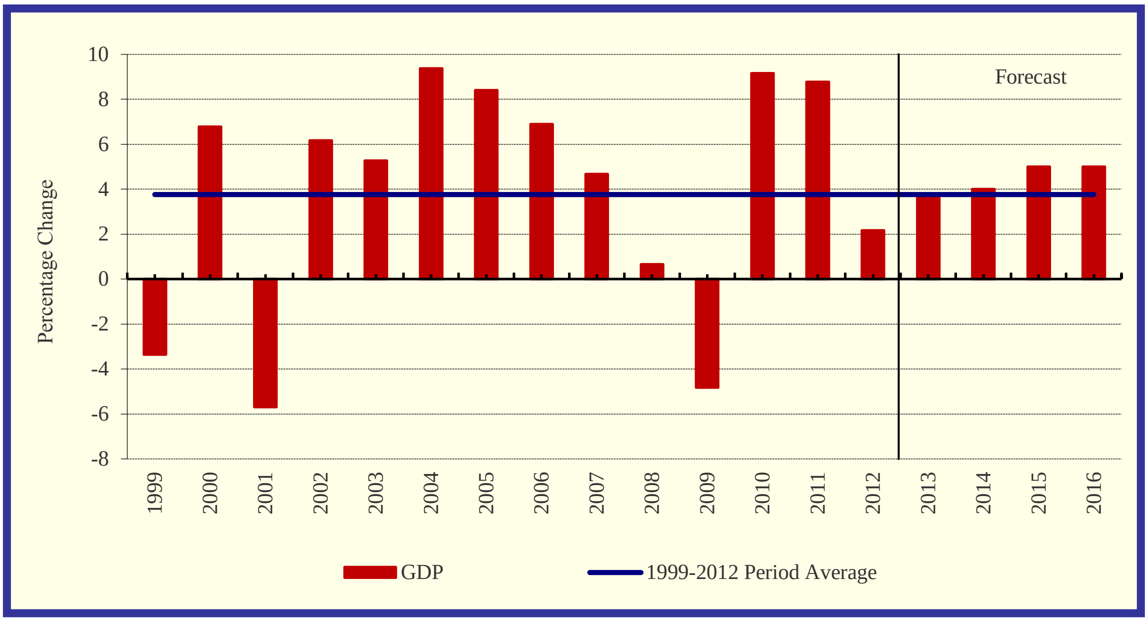
		Forecast			
	2012	**2013**	**2014**	**2015**	**2016**
Total Consumption Expenditure	0.3	4.5	3.1	3.8	3.6
Private	-0.6	3.9	3.2	3.8	3.5
Public	6.1	7.8	3.0	3.3	4.2
Total Investment Expenditure	-8.3	7.3	3.3	8.9	8.6
Gross Fixed Capital Formation	-2.7	2.4	3.9	8.6	8.3
Private Fixed Investment	-4.8	-0.8	5.7	8.2	9.2
Public Fixed Investment	9.3	18.6	-3.8	10.0	4.0
Change in Stocks [1]	-1.4	1.1	-0.1	0.0	0.1
Exports of Goods and Services	16.7	0.5	6.8	7.2	7.7
Imports of Goods and Services	-0.3	6.1	3.6	7.0	7.1
Gross Domestic Product	2.2	3.6	4.0	5.0	5.0
Domestic Demand	-1.8	5.1	3.2	5.0	4.8
Domestic Final Demand	-0.4	4.0	3.3	4.9	4.8

Source: Realization TURKSTAT, forecast Ministry of Development

(1) Contribution to GDP growth

Analyzing foreign trade side of the growth, in the first nine months of 2013, it is observed that increase in exports of goods and services was limited to 0.8 percent due to decrease in foreign demand but imports of goods and services increased by 8.5 percent in the same period with the effect of domestic demand recovery. In rest of the year, growth of exports is expected to continue to decline due to ongoing weak foreign demand and to be 0.5 percent for 2013. In addition, with the effects of slowdown in domestic demand and exchange rate depreciation in the rest of the year, imports are also expected to slow down and increase by 6.1 percent in 2013. Thus, contribution of net exports to growth is expected to be -1.6 percentage points in 2013.

Figure 2.9: GDP Growth

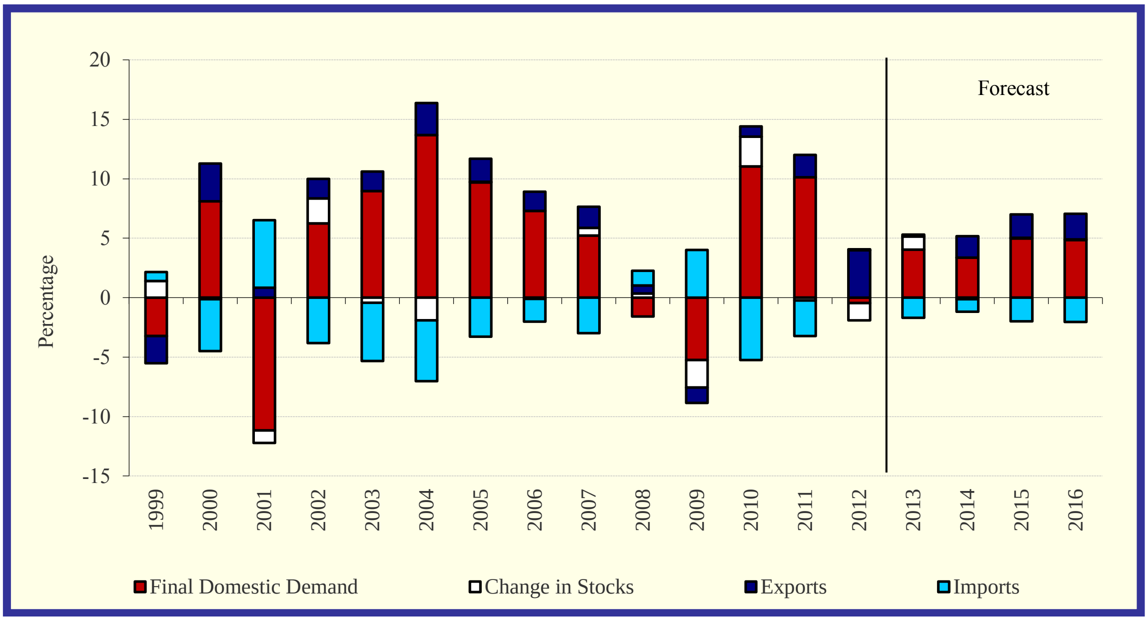


Source: Realization TURKSTAT, forecast Ministry of Development

In light of the nine months realizations and forecasts for the remaining three months, Turkish economy is foreseen to grow by 3.6 percent in 2013. The growth in 2013 will be composed of private consumption by 2.6 percentage points, public consumption by 0.8 percentage point, private fixed capital formation by -0.2 percentage point and public fixed capital formation by 0.7 percentage point. In medium term, with the contribution of increases in external and domestic demand in addition to the decrease in global uncertainties, growth is expected to continue its increasing trend and will be 4 percent in 2014. With increase in the investments rather financed more by domestic savings and directing resources to productive sectors, growth rates in 2015 and 2016 are targeted to be 5 percent.

With the impact of policies that will be implemented to rebalance the domestic and external demand and to increase savings, in PEP period private sector consumption is expected to increase by 3.5 percent annually on average, which is below the GDP growth rate. On the other hand, with the decreasing uncertainties and expected favorable external demand developments, private sector fixed capital formation is expected to increase by 7.7 percent annually on average during the Program period. Along with the public policies for preserving fiscal discipline and increasing savings in the medium term, it is anticipated that public consumption will increase by 3.5 percent and public investments will increase by 3.3 percent annually on average during the same period.

Figure 2.10: Contributions to GDP Growth



Source: Realization TURKSTAT, forecast Ministry of Development

2.2.1.2. Investment-Saving Balance

As a result of rapid deceleration of credit growth due to macro-prudential measures and ongoing global uncertainties in 2012, private fixed capital investments contracted. Consequently, the share of private fixed capital investment in GDP fell to 16.4 percent from 18 percent in 2011. The share of public fixed investments in GDP displayed a relatively stable pattern as a result of significant rise in public investments in the second half of the year and realized as 3.9 percent. On the other hand, stocks fell significantly due to negative expectations for economic activity, thus the share of total investment expenditures in GDP realized as 20.1 percent in 2012 by 3.5 percentage points decrease compared to previous period.

Table 2.8: Investment-Saving Balance

(Percent of GDP)

				Forecast			
	2010	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**
Total Investment	19.5	23.6	20.1	19.2	19.6	20.2	21.0
Fixed Capital Formation	18.9	21.8	20.3	19.8	19.7	20.4	21.0
Public	4.0	3.8	3.9	4.4	4.0	4.2	4.2
Private	15.0	18.0	16.4	15.5	15.7	16.2	16.8
Change in Stocks	0.6	1.7	-0.2	-0.6	-0.1	-0.2	-0.1
Total Savings	19.5	23.6	20.1	19.2	19.6	20.2	21.0
Domestic Savings	13.3	13.9	14.0	12.1	13.2	14.3	15.5
Foreign Savings	6.2	9.7	6.1	7.1	6.4	5.9	5.5

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

Note: Foreign savings correspond to net exports as percent of GDP

Upon falling share of total investments in GDP, required total savings subsided to 20.1 percent. With the effects of measures taken and developments in the exchange rate, the share of foreign savings in GDP declined to 6.1 percent by reducing 3.6 percentage points. In parallel to these developments, domestic savings increased slightly and the share of domestic savings in GDP realized as 14 percent in 2012.

In the first half of 2013, domestic demand started to revive and growth stemmed mainly from private and public consumption and public fixed investment. Private fixed investment continued to contract in this period. Although, leading indicators for investments display weaker outlook than for consumption expenditures, domestic demand is expected to pick up moderately in the rest of the year. In line with these developments, the share of public fixed investments in GDP is expected to reach to 4.4 percent, while the share of private fixed investments in GDP is forecasted to realize as 15.5 percent in 2013. Therefore, share of total investments is expected to decelerate to 19.2 percent compared to previous year.

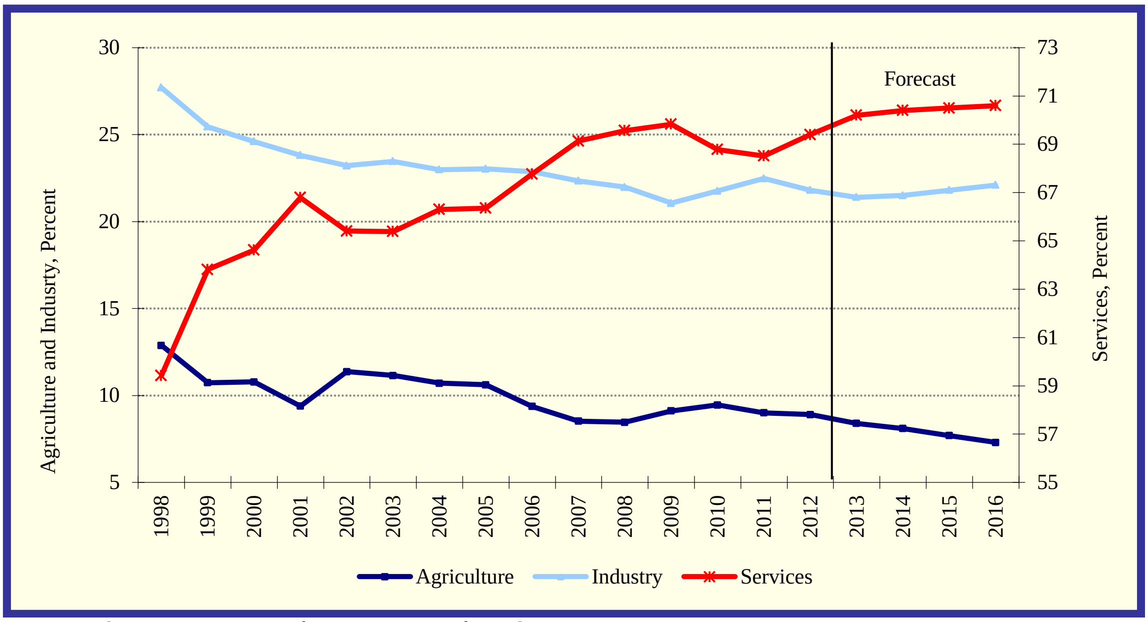
Depending on revival of domestic demand and weak global demand, imports increased more than exports, thus the contribution of net exports to growth turned negative. With the anticipation of this effect continuing throughout the year, foreign savings to GDP ratio is expected to reach to 7.1 percent. As a result, domestic savings to GDP ratio is forecasted to recede to 12.1 percent.

In the upcoming period, with the help of moderate recovery foreseen in the global economy, economic growth is targeted to converge to its potential level. In this framework, priority is given to increase domestic savings and to direct existing resources to productive areas. In addition, maintaining sound fiscal stance is another priority area. In this context, it is targeted that the share of public fixed investments in GDP is retained at 4.1 percent and this investment expenditures are rationalized in a manner to support infrastructure investments more. In parallel to positive expectations in the economy, ratio of private sector fixed capital investments to GDP is expected to rise throughout the period and to reach 16.8 percent in 2016. With the effects of measures towards increasing private sector savings, domestic savings to GDP ratio is forecasted to reach 15.5 percent at the end of the period. Thus, foreign financing need is expected to decline throughout the period and to decrease to 5.5 percent in 2016.

2.2.1.3. Growth by Sectors

Contrary to general trend, the value added in agriculture sector showed a better growth performance than other sectors and increased by 3.1 percent in 2012. Value added in agriculture sector, which increased by 3.9 percent in the first nine months of 2013, is expected to increase by 4.1 percent in 2013. On the other hand, as a result of price developments, the share of the sector in total production is projected to reach 8.4 percent with a half point decrease compared to 2012. In 2014-2016 period, the growth rate of value added in agriculture sector is expected to converge to its trend. In this framework, it is foreseen that agricultural value added will increase by 3 percent annually on average during the Programme period and the share of the sector in GDP will recede to 7.3 percent at the end of the period by gradually declining.

Figure 2.11: Production by Sectors



Source: Realization TURKSTAT, forecast Ministry of Development

Table 2.9: Value-Added by Sectors

(Percent)

	Realization			Forecast			
	2010	2011	2012	2013	2014	2015	2016
Growth Rates[1] (1998 Prices)							
Agriculture	2.4	6.1	3.1	4.1	3.0	3.0	3.0
Industry	12.8	9.7	1.9	2.3	4.4	6.2	6.0
Services	8.6	9.0	2.4	4.5	4.1	4.8	4.9
GDP	9.2	8.8	2.2	3.6	4.0	5.0	5.0
Percent of GDP[2] (Current Prices)							
Agriculture	9.5	9.0	8.9	8.4	8.1	7.7	7.3
Industry	21.8	22.5	21.8	21.4	21.5	21.8	22.1
Services	68.8	68.5	69.4	70.2	70.4	70.5	70.6
GDP	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Contribution To Growth (Percentage Points)							
Agriculture	0.2	0.6	0.3	0.4	0.3	0.3	0.3
Industry	3.4	2.6	0.5	0.6	1.2	1.7	1.6
Services	5.4	5.7	1.5	2.8	2.6	3.1	3.1
GDP	9.2	8.8	2.2	3.6	4.0	5.0	5.0

(1) Agriculture, industry and services sectors growth rate was calculated by constant prices, GDP growth rate was calculated by purchaser's prices.

(2) Sectoral shares in GDP were obtained by distributing the items of financial intermediation services indirectly measured and taxes-subsidies to sectors' shares according to the sectoral weights in GDP.

Value added of industry sector increased by 3.1 percent in the first nine months of 2013 compared to the same period of the previous year. Considering the sub-sectors of industry in the first nine months of 2013, growth rate in manufacturing sector rose to 3.5 percent from 2.5 percent in the same period of 2012. In the same period, mining sector contracted by 3.3 percent, despite 2.8 percent increase in 2012. Energy sector growth decreased to 0.4 percent from 6.2 percent. In the light of these developments, it is foreseen that value added of industry sector will increase by 2.3 percent in 2013, below previous PEP forecast. In PEP period, industry sector value added is expected to increase by 5.5 percent annually on average and its share in GDP is expected to increase gradually.

Services sector, which is mainly driven by wholesale and retail trade sector, financial intermediation sector, real estate, renting and business activities sector and construction sector, recorded a 5.2 percent growth in the first nine months of 2013 compared to same period of the previous year. With a slowdown for the rest of 2013, value added in services sector is expected to increase by 4.5 percent in 2013 above the previous PEP forecast. In 2014-2016 period, services sector value added is expected to increase by 4.6 percent annually on average. Thereby, the share of the services sector in GDP is foreseen to increase mildly during the Programme period and reach to 70.6 percent in 2016.

2.2.1.4. Sources of Growth

Scrutinizing the long-term growth structure of the Turkish economy, an unbalanced structure in terms of factors of production is observed. Growth has generally been backed by capital stock to great extent. While the contribution of employment to growth has displayed a more stable pattern in all periods, contribution of TFP to growth has stood at very limited and low level. In 1985-2000 period, the average growth rate was 4.3 percent and the contributions of capital stock, employment and TFP to this growth rate were 70.5 percent, 23 percent and 6.5 percent, respectively. On the other hand, with the impact of macroeconomic policies and structural reforms that were put into implementation following the 2001 crisis, contribution of TFP to growth increased significantly after 2002.

Table 2.10: Increases in Production Factors

(Percent)

Period	GDP Growth	Capital Stock Growth	Capital Stock Growth *	Employment Growth	TFP Growth
1985-2000	4.3	7.5	7.4	1.7	0.3
2001-2012	4.1	5.3	5.4	2.0	0.7
2002-2012	5.1	5.6	6.2	2.2	1.2
1985-2012	4.2	6.6	6.5	1.8	0.5
2014-2016	4.7	5.5	6.4	2.3	0.7

Source: Ministry of Development calculations.
* 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	70.5	23.0	6.5
2001-2012	54.0	28.5	17.5
2002-2012	51.1	25.7	23.2
1985-2012	63.6	25.3	11.1
2014-2016	56.7	29.2	14.0

Source: Ministry of Development calculations.

In 2012, the growth performance was below the forecast of the previous PEP. Similarly, capital stock increase was realized below the forecasts as a result of the contraction in investment expenditures with the impact of macro-prudential measures. On the other hand, with the ongoing effects of measures for increasing the employment after the crisis, growth rate of employment displayed a performance above the expectations. As a result of these developments, TFP growth and its contribution to GDP growth evolved more unfavorably in 2012 compared to the previous PEP forecast.

Strong employment increases continued, particularly in the first two quarters of 2013. Moreover, capital accumulation is expected to accelerate with the increase in investment expenditures in 2013. Thereby, it is foreseen that similar structure to 2012 in terms of factors of production will realize and main determinants of growth will be employment and capital stock with the impact of increase in capacity utilization rate. In light of these developments, TFP is not expected to positively contribute to growth in 2013 as well.

In PEP period, productivity increase in addition to improving the business and investment environment and making the labor market effective are of utmost importance for ensuring high and balanced growth environment. In the Tenth Development Plan, shaped with this motivation, policies regarding qualified labor force, R&D and innovation activities and labor market are included. With the support of "Program for Enhancing Productivity in Manufacturing", which is one of the priority transformation programs extensively presented in the Plan, an important step towards 2023 targets will be taken. Via the policies for increasing productivity particularly in industrial sector, the contribution of TFP to growth will be increased and shift to a more balanced growth structure in terms of factors of production will be ensured (Box 2.3). In this context, especially increasing the contribution of TFP in the Program period is critically important in terms of long-term targets.

As a matter of fact, capital stock, employment and TFP are expected to increase by 5.5 percent, 2.3 percent and 0.7 percent annually on average in PEP period, respectively. Within this growth structure, in the Program period the contribution of capital stock, employment and TFP to growth are foreseen to be 56.7 percent, 29.2 percent and 14 percent, respectively.

Box 2.3: Growth and Productivity in the Tenth Development Plan

To achieve a stable and high growth structure in Turkish economy, a productivity-focused approach is adopted in the Tenth Development Plan (2014-2018). Productivity increase in the economy will not only contribute directly to economic growth, but also will ensure effective and sustainable use of scarce resources. Therefore, productivity-led economic growth is of utmost importance for ensuring the sustainability of growth and permanent increase of social welfare in the long-term. In this context, towards achieving the goals of the Plan, productivity-enhancing policies will have priority and thus global competitive position of the economy will be strengthened. On the other hand, productivity-led economic growth will be an important factor in ensuring the long-term sustainability of current account deficit via its positive impact on competitiveness.

Analyzing the dynamics of Turkish economy, it is observed that the most important component of increasing productivity is human capital. Thus, on one hand the quality of education in general will be increased, on the other hand the harmony between education system and labor market will be strengthened by education-industry cooperation policies. In addition to increasing the qualified labor force, increasing female labor force participation will directly contribute to the economy wide productivity growth.

Another important component of increasing productivity is enhancing technology, R&D and innovation capacity. R&D and technology policies are expected to play a crucial role in establishing a higher productivity and value added structure, especially in industry sector. For innovation and innovation-friendly environment, which are the most crucial factors in the success of aforementioned policies, policies in areas such as incentives, entrepreneurship, SME, intellectual and industrial property rights, information and communication technologies will be implemented in harmony. In addition to all these, improving governance process of firms, extending firms' lives and resolving the productivity and scale problems are of utmost importance. With the scope of institutional quality; functionality of transparency, accountability and rule of law within an established legal framework will be strengthened. In the same context, combating informality and corruption will be continued, predictability and stability in tax legislation will be ensured, intellectual property and patent rights will be protected, effective operation of markets will be ensured and investment environment will be strengthened.

In Plan period, public sector will have an important role in implementing policies both in public sector and regarding the private sector in terms of increasing productivity. Savings and additional resources that will be obtained by increasing efficiency of public expenditures will be used for growth-friendly investments, incentives and R&D supports. Public infrastructure investments will increase production capacity by stimulating private sector investments; and will also contribute to productivity-focused growth dynamic.

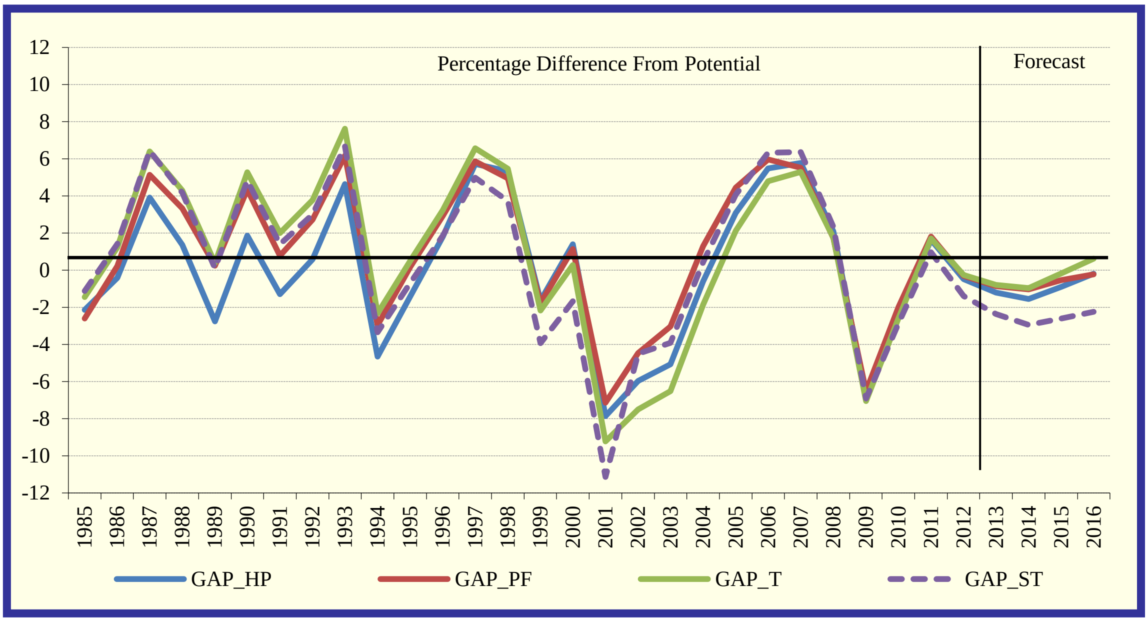
Within the framework of the new approach adopted in the Plan, priority areas of intervention were identified with the priority transformation programs towards achieving the 2023 targets. One of these programs is "Program for Enhancing Productivity in Manufacturing". With this program; strengthening productivity awareness, enhancing production processes, increasing value added and thus contributing to high and stable growth target are aimed.

2.2.1.5. Potential Output

Potential growth rate was adversely affected in 2009, when the impact of global crisis on Turkish economy was at its peak. In this year, negative output gap reached around 7 percent along with a 4.8 percent contraction in the economy. In the following years, domestic demand recovered strongly and high investment and employment increases were recorded. These developments positively influenced the potential output. The production level recaptured its potential in 2011. On the other hand, economic activity slowed down in 2012 with the effects of global developments and macro-prudential measures for rebalancing the domestic and external demand. With this slowdown, production declined below its potential level again. In the context of forecasts for 2013, a structure similar to 2012 is expected to continue in 2013 as well.

In the context of macroeconomic scenario of the PEP period, it is envisaged that potential growth rate will increase gradually as a result of foreseen developments in macroeconomic variables such as investment, employment and capacity utilization rate. In this context, output gap estimations point out that production will be below its potential during the Program period, but negative output gap will vanish in 2016. In this regard, any demand side pressure or risk in terms of inflationary dynamics is not expected during the PEP period.

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.

2.2.1.6. Labor Market

Despite the slowdown in economic activity in 2012, total employment increased by 2.9 percent, above the expectations, thanks to ongoing effects of measures taken for fighting against unemployment. In this increase, contribution of services sector employment was particularly determinant. As a result of these favorable developments in labor market, unemployment rate declined to 9.2 percent. Analyzing the developments in the first three quarter of 2013, unemployment rate is observed to follow a higher path compared to the last year. However, this situation mainly stems from the high rate of the labor force participation rate. In this period, while non-agricultural employment increased by 4.8 percent, agricultural employment shrunk by 0.2 percent; thus total employment increased by 3.6 percent compared to the same period of the previous year.

Due to revival of economic activity compared to the previous year and its positive reflection on labor markets, non-agricultural employment is expected to increase by 4.8 percent while agricultural employment is expected to decrease by 0.5 percent annually. Thus, total employment is estimated to increase by 3.5 percent throughout the year. Within the framework of current developments in the labor market, the labor force participation rate is foreseen to be 51 percent and the unemployment rate to be 9.5 percent in 2013 with a slight increase compared to previous year (Table 2.12). In 2014-2016 period, non-agricultural employment is estimated to increase an additional 1.8 million approximately based on GDP and investment growth forecast. With projected 0.1 percent annual average increase in agriculture employment, employment rate is expected to be 47.3 percent at the end of the Program period.

In PEP period, with the effects of the incentives towards increasing particularly female employment, the labor force participation rate is estimated to increase steadily. Thus, the labor force participation rate is expected to reach 51.9 percent at the end of the period. Regarding these expectations about labor market, unemployment rate is estimated to decrease gradually to 8.9 percent in 2016 (Table 2.12).

Table 2.12: Labor Market Developments

(15+ age)

	Realization		**Forecast**			
	2011	**2012**	**2013**	**2014**	**2015**	**2016**
Working Age Population (Thousand Person)	53,593	54,724	55,605	56,476	57,337	58,251
Labor Force Participation Rate (Percent)	49.9	50.0	51.0	51.3	51.6	51.9
Labor Force (Thousand Person)	26,725	27,339	28,384	28,994	29,611	30,217
Employment	24,110	24,821	25,692	26,257	26,901	27,525
Agriculture	6,143	6,097	6,065	6,089	6,089	6,089
Non-Agriculture	17,967	18,724	19,627	20,168	20,812	21,436
Unemployed	2,615	2,518	2,692	2,737	2,710	2,691
Employment Increase (Percent)	6.7	2.9	3.5	2.2	2.5	2.3
Agriculture	8.1	-0.7	-0.5	0.4	0.0	0.0
Non-Agriculture	6.2	4.2	4.8	2.8	3.2	3.0
Employment Rate (Percent)	45.0	45.4	46.2	46.5	46.9	47.3
Unemployment Rate (Percent)	9.8	9.2	9.5	9.4	9.2	8.9

Source: Realization TURKSTAT, forecast Ministry of Development

2.2.2. Inflation, Monetary and Exchange Rate Policies

The Central Bank will continue to implement inflation targeting regime in 2014, 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, convergence towards developed economies, and the rigidities in price setting behavior remaining from high inflation environment. In this context, the end-year inflation targets for 2014, 2015 and 2016 are set to 5 percent.

In 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 considers to be in line with the economic conditions. In addition, the reserve option mechanism has been effectively used since September 2011 as a complementary tool to interest rate corridor to mitigate volatility in domestic markets caused by capital flows.

The floating exchange rate regime will continue in 2014. Under this exchange rate regime, 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 case of unhealthy price formations due to possible loss of market depth, CBRT may conduct FX buying or selling auctions; or it may intervene directly to FX market in a way that does not contradict with the floating exchange rate regime. In this context, the Central Bank provided 1.45 billion dollars liquidity in 2012 and 11.76 billion dollars liquidity in 2013 to the market through FX selling auction whereas it provided 1.06 billion dollars liquidity in 2012 via direct FX intervention. On the other hand, in order to enhance the mobility of foreign exchange liquidity in the Interbank Foreign Exchange Market, CBRT 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 a view to slow down the rapid growth of the private sector's foreign liabilities and to improve 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, keeping credit growth rates at reasonable and sustainable levels are deemed important. Moreover, 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. As a result of the implementation of macro-prudential measures within this context, domestic demand contracted in 2012. Thereby, trade deficit and current account deficit decreased to 65.3 billion dollars and 48.5 billion dollars in 2012, respectively. In 2013, as a result of recovery in economy and particularly in domestic demand, with a moderate rise, trade deficit and current account deficit are expected to reach 76.8 billion dollars and 58.8 billion dollars, respectively.

During PEP period, economic growth in trade partners of Turkey is expected to be relatively higher compared to 2012 and 2013, in line with foreseen recovery in the EU. With the impact of the policies to increase exports as well, exports in nominal terms are projected to reach 202.5 billion dollars in 2016, with an annual average growth of 9.7 percent in the PEP period. Real exports of goods are expected to reaccelerate and increase by 7.4 percent in 2014 after a modest 0.6 percent decline in 2013. Real exports of goods are expected to increase by 8.7 percent and 8.2 percent in 2015 and 2016, respectively. During this period, export prices are expected to move in line with world prices and increase 1.5 percent annually on average.

Imports, which contracted by 1.8 percent in 2012 in nominal terms, are expected to increase 6.3 percent in 2013, parallel to the modest growth in domestic demand. The high rates of increases in imports during the strong economic growth periods will be replaced by mild increases with the effect of the policy measures that consider the balance between domestic and external demand in the Programme period. In this regard, imports are forecasted to reach 305 billion dollars in 2016 with an annual average increase of 6.7 percent. Real import growth is foreseen as 6.2 percent annually on average in the same period, with expected annual average import prices increase of 0.4 percent.

Energy bill will continue to constitute a significant part of the current account deficit of Turkey in the medium term. In the forthcoming period, energy and oil prices are expected to decline due to the slow increase in global economic activity. However, with the impact of expected increase in energy demand, increase in imports that arise from energy items is expected to exhibit a moderate rise. In this context, energy imports, which are expected to be 59 billion dollars in 2013, will reach 64.5 billion dollars at the end of PEP period.

Box 2.4: Policies for Sustainability of Current Account Balance in The Tenth Development Plan

In line with 2023 targets, The Tenth Development Plan (2014-2018) has revealed important policies and targets in advancing the society to high prosperity levels. In this context, keeping the current account deficit at levels that does not constitute any risk for long-term growth is of utmost importance. Strong domestic demand, low levels of private savings, high share of energy imports in total imports, import dependence of exports make current account deficit a structural problem.

The Tenth Development Plan covers many policies for high, stable and inclusive economic growth, besides issues such as the rule of law, information society, international competitiveness, human development, environmental protection and sustainable use of resources. Reforms aiming to overcome structural problems that hinder growth are important part of these policies. Contrary to macro-prudential measures aiming to smooth cyclical effects of the current account in the short term, aforementioned reforms will tackle this problem in the long term.

Policies for sustainability of the current account deficit, which is a constraint for growth, constitute also significant part of the Plan. As a matter of fact, keeping the current account deficit at reasonable levels for growth is one of the main objectives in the Plan. To serve this purpose, in addition to foreign trade and balance of payments policies, supportive policies have been designed in many areas. The first of these policies aims increasing productivity. Enhancing competitiveness through increasing productivity in the overall economy will also provide solid contribution in terms of current account deficit. Main objectives of the policies on transformation in the manufacturing industry and entrepreneurship and SMEs are increasing Turkey’s international competitiveness and its share in world exports and strengthening the production structure to achieve high value-added production structure. Within the framework of these objectives, it is expected to contribute to the reduction of the current account deficit. Investment policies, enhancing competitiveness and private sector-led production structure will also contribute to reduce the current account deficit permanently to sustainable levels. Science, technology and innovation policies, which is another important policy area in the Plan, aims at decreasing current account deficit to sustainable levels with the contributions of technological breakthroughs, innovative policies and increasing competitiveness in line with these targets. In addition to these policies, it is also emphasized in the Plan that information and communication technologies, energy, logistics and transportation policies which aim reducing energy costs, especially acceleration of knowledge-based infrastructure investment, increasing value added in technology production will contribute to sustainability of current account via strengthening infrastructure.

In addition to policies, Priority Transformation Programs are also designed in the Tenth Development Plan. The programs designed in compliance with the policies will be cure for main structural problems and were formed in a way to lead the implementation of the Plan and increase the efficiency of policies in critical areas that would contribute to transformation process. Import Dependency Reduction Program, Domestic Resource Based Energy Production Program and Energy Efficiency Improvement Program are one of these programs designed to ensure the sustainability of current account balance. With these programs, transforming the production structure in favor of high value added products, minimizing energy costs, which reveal large part of the current account deficit, reducing the dependency on imports and energy are aimed. Furthermore, programs such as: Program for Commercialization in Priority Technology Areas, Program on Enhancing Productivity in Manufacturing, Business and Investment Climate Improvement Program, Health Tourism Improvement Program and Transformation Program from Transportation to Logistics are expected to contribute indirectly to the sustainability of current account balance. With the help of these programs, supporting other programs and solving current account deficit problem are aimed via directing investments towards productive areas, enhancing production capacity, improving competitiveness etc.

In 2013, a 2 billion dollars improvement is expected in the services balance compared to previous year, mostly stemming from tourism revenues. As a matter of fact, increase in the number of tourists visiting Turkey has accelerated in 2013. This tendency is expected to steadily continue in the forthcoming period and thus tourism revenues are expected to be 29 billion dollars in 2013, and reach 34.5 billion dollars in 2016 with a 6 percent annual average increase.

Considering these developments, the current account deficit to GDP ratio is projected to recede gradually towards sustainable levels during the Program period. In this context, current account deficit to GDP ratio is expected to be 6.4 percent, 5.9 percent and 5.5 percent in 2014, 2015 and 2016, respectively. The policies in the context of the Tenth Development Plan and Medium Term Program towards strengthening fiscal discipline, increasing domestic savings, slowing down credit growth rate and decreasing high import dependency of production will remarkably contribute to this performance.

2.2.3.2. Capital and Financial Account

The global economic crisis emerged in 2008; most intense phase of it, globally and in Turkey, was experienced in 2009. Although five years have passed over this phase, as the financial losses incurred were extensive, effects of the crisis have continued at various intensities and forms around the world. Despite the possibility of a total collapse was out of agenda, uncertainties have continued in 2012 and 2013; market agents wanted to use the excess liquidity supplied against the crisis in new investments, but they were also prudent to risks and price bubbles. Similarly, the aim of policy makers to pursue pro-growth policies conflict with their sensitivity about formation of price bubbles and risk accumulation in some sectors. These conflicts in the decision-making processes faced by market actors and policy makers affect the expectation formation process in economies and markets, result in fluctuations and sudden direction changes and make long run forecasting difficult.

The performance of economies in this five-year period after the most intense phase of the crisis highlighted their structural problems. In this context, even if the US was the main source of the crisis, it has achieved economic growth process with rapid decision making processes. On the other hand in the Euro Area, which could not run decision making processes in same speed and has an aging population problem, growth has been pretty weak. Emerging economies continued their high growth performances with a slight slowdown in 2013.

In this process, Turkish economy showed a successful economic performance on global scale with its sound public finances and financial markets and has become an important alternative market for investors. Despite capital inflows to emerging economies which was 572 billion dollars in 2010, decreased to 499.3 billion dollars in 2011 and further decreased to 237.1 billion dollars in 2012, capital inflows to Turkish economy has increased continuously both in absolute amounts and as a share of total flows to emerging markets. Capital inflows to Turkish economy were realized as 56.9 billion dollars in 2010, 63.9 billion dollars in 2011 and 68.1 billion dollars in 2012.

In 2013, portfolio investment flow to emerging markets and developing economies is expected to decrease to 154.3 billion dollars and net direct investment flows is forecasted to decline to 423 billion dollars. On the other hand, net other investments outflows is expected to decrease to 179 billion dollars, thereby total private financial capital flows are expected to increase to 398.4 billion dollars, despite fluctuations throughout the year. In 2013, the FED signaled decreasing bond purchases in the short term and ending monetary expansion and this led to fluctuations in global capital flows and also significantly affected capital flows to Turkish economy. In this context, it is expected that CBRT’s tight monetary policy implementations will restrict economic activities in the last quarter of 2013; therefore current account deficit will not show a significant deterioration and financing requirement of Turkish economy will be flawlessly met. Total fund inflow throughout this year is estimated to reach 62.7 billion dollars; with a composition of 7.8 billion dollars in direct investments, 21.3 billion dollars in portfolio investments and 33.6 billion dollar in other investments items; 8.8 billion dollars of reserve accumulation is foreseen.

For 2014, total private financial capital flows to emerging markets and developing economies is forecasted to slightly decline to 366.6 billion dollars while the composition of these flows is estimated to remain almost the same. Besides the process followed by the FED in reducing monetary expansion, policy reactions of other central banks will be determinants of short and medium term global liquidity conditions and capital flows in 2014 and afterwards, likewise 2013. In this period, policy makers and market actors are expected to continue acting prudently and both total global fund flows and the flows towards emerging markets and developing economies are estimated to realize at lower levels.

Turkish economy, which has managed to continuously increase its share from global capital flows and has succeeded to increase amount of foreign fund use even in years when the capital flows to emerging markets and developing economies decreased to half, is expected to have a decreasing foreign financing need parallel to declining current account deficit in the 2014-2016 period, thereby meet the external fund requirement without any difficulty in a period with lower global fund flows.

Table 2.13: Balance of Payments Forecasts

(Billion Dollars)

	Realization			Forecast			
	2010	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**
Current Account	**-45.4**	**-75.1**	**-48.5**	**-58.8**	**-55.5**	**-55.0**	**-55.0**
Balance on Goods	-56.4	-89.1	-65.3	-76.8	-73.8	-74.6	-77.7
Total Exports	120.9	143.4	163.2	166.0	179.2	197.6	216.6
Exports (fob)	113.9	134.9	152.5	153.5	166.5	184.0	202.5
Total Imports	-177.3	-232.5	-228.6	-242.8	-253.0	-272.2	-294.3
Imports (cif)	-185.5	-240.8	-236.5	-251.5	-262.0	-228.0	-305.0
Balance on Services	16.7	20.1	22.6	24.9	26.2	27.4	30.5
Credit	36.3	40.7	43.2	47.8	50.5	52.9	57.3
Tourism Revenues	22.6	25.1	25.3	29.0	31.0	32.0	34.5
Debit	-19.6	-20.5	-20.5	-22.8	-24.3	-25.5	-26.8
Balance on Income	-7.2	-7.8	-7.2	-8.2	-9.0	-9.0	-9.0
Current Transfers	1.5	1.8	1.4	1.2	1.2	1.2	1.3
Workers' Remittances	0.9	1.0	1.0	1.0	0.9	0.9	0.9
Capital and Financial Account	**44.0**	**65.7**	**47.3**	**53.8**	**55.5**	**55.0**	**55.0**
Capital Account	-0.1	0.0	0.0	-0.1	-0.1	-0.1	-0.1
Financial Account (Excl. Reserves)	56.9	63.9	68.1	62.7	54.7	54.9	54.9
Direct Investment	7.6	13.7	8.9	7.8	10.1	15.0	14.9
Direct Investment in Turkey	9.0	16.0	13.0	10.8	13.0	18.0	18.0
Direct Investment Abroad	-1.5	-2.3	-4.1	-2.9	-2.9	-3.0	-3.1
Portfolio Investment	16.1	22.0	40.8	21.3	14.4	17.2	21.2
Assets	-3.5	2.7	2.7	3.0	-0.7	-1.1	-1.5
Liabilities	19.6	19.3	38.1	18.3	15.1	18.3	22.7
Other Investment	33.2	28.2	18.4	33.6	30.2	22.7	18.8
Assets	7.0	11.1	-0.6	1.4	0.4	0.2	0.1
Liabilities	26.2	17.1	19.0	32.2	29.8	22.5	18.8
Reserve Assets	-12.8	1.8	-20.8	-8.8	0.9	0.2	0.2
Net Errors and Omissions	**1.4**	**9.4**	**1.2**	**5.0**	**0.0**	**0.0**	**0.0**

Source: Realization CBRT, forecast Ministry of Development

2.2.4. Main Risks in Projections

In 2012, global developments were not as favorable as expected. On the other hand, in 2013 positive developments have been observed and the world economy has entered a growth path, though limited. This growth performance is expected to accelerate in 2014 and 2015. The risks rooted from the developed countries at the global level, though declined, still preserve their importance. In the global economy, rebalancing process has been experienced in asset prices, money, financial and exchange markets. The global liquidity conditions that will be shaped by the timing regarding the exit strategy from the monetary expansion policy and interest rate increase in the US economy, will be determinant on the global outlook. Thereby, any possible decline in global liquidity in the forthcoming period arises as a risk factor for the Turkish economy which has high external financing need. On the other hand, in the Tenth Development Plan policies aimed for reducing the current account deficit and thereby the dependency on external financing are covered and current account deficit is targeted to decline gradually. This can be also considered as a measure for a possible decline in capital flows to developing countries and similar risks. On the other hand, with strong fiscal balances, sound financial sector, strong domestic demand and liberalized and regulated markets, Turkish economy conveys confidence to investors. As a matter of fact, increases in credit ratings of Turkey also support this fact. Thanks to this confidence environment, Turkish economy is considered as a safe haven for capital flows and is expected to be affected less from these types of risks compared to other developing countries in the PEP period.

The EU economy, which is the primary export market of Turkey and has been contracting for a while, has started to grow again in 2013 and with this; the share of EU in Turkey's trade has begun to surge. This situation is a pretty favorable development in terms of export revenues and thereby growth performance considering the export composition to the EU. On the other hand, high government debt, fragile banking structure and low growth performance in some EU countries continue to be important problems. Unless there is a progress in tackling these problems, a risk of a decline in export revenues and deterioration in current account deficit might arise in Turkish economy. This would strike a blow at the target of high and stable growth.

As a result of the measures taken for export market diversification in recent years, share of non-EU countries in exports of Turkey has increased remarkably. However, unlike the EU countries, political instabilities experienced in Middle East and North Africa countries, in which Turkey has increased its market share, threatens continuation of market diversification performance. Thereby, Turkey could be adversely affected from possible political instabilities in these regions via trade channel.

Energy costs are an important issue for Turkish economy, which has a current account deficit problem. The projection of declining trend in oil prices in the medium term is evaluated as a favorable development in terms of current account dynamics. However, geopolitical uncertainties might lead to temporary price increases. Cyclical upward movements in oil prices would have an adverse effect on inflation via the production costs and on current account deficit via the imports.

3. PUBLIC FINANCE

Fiscal policy will be carried out with an approach that will strengthen macroeconomic stability, promote private sector-led growth process and help fight against current account deficit and inflation, considering revenue, expenditure and debt stock amounts prescribed in the Medium Term Program. 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 (2014-2016) are based on Medium Term Programme (2014-2016) and 2014 Annual Program.

3.1. General Government Balance and Public Debt

The general government balance, produced 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 the 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 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: 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 communicated 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, 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 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 2014-2016 are as follows:

3.1.1.1. Revenue Policy

- The main objective is securing the public revenues from buoyant and permanent sources. Tax policy will be implemented in a way to improve income distribution, contribute to sustainable development and increase competitiveness of the economy and domestic savings.
- Predictability in taxation and stability in implementation of tax policies are of essential.
- Studies on revision of the basic tax laws in order to make them simple and applicable for taxpayers will be continued taking into account economic and social policies.
- Implementation results of revenue policies will be disseminated to public regularly in details.
- In order to prevent unfair competition, enhance competitiveness of the economy and increase public revenues, an efficient struggle against informal economy will be waged.
- The tax base will be expanded in a way to ensure that taxation is fairer and serves properly in terms of its fiscal functions.
- Necessary administrative and judicial measures regarding preventing the tax evasion in e-commerce will be put into practice.
- Transaction taxes on commercial activities will be reduced as public fiscal balances permitted.
- In the determination and implementation of tax policies, priorities concerning climate change and efficiency in energy consumption will be taken into account.
- In order to effectively, efficiently and economically use the public immovable, all alternatives including sales of assets will be taken into consideration.
- In order to strengthen the fiscal capacity of local administrations, own revenues of local administrations will be raised taking into account of urban rents.

3.1.1.2. Expenditure Policy

- In order to strengthen accountability and increase efficiency in public financial resource management, before implementing new spending initiatives, pilot programs will be devised, impact assessments will be performed, and existing programs will be reviewed in terms of effectiveness and efficiency.
- In the budgeting process, during determination of appropriations for current expenditures except personnel expenditures, zero-based budgeting approach shall be applied.
- Spending programs will be conducted strictly in line with their predefined objectives and only within their predefined timelines.
- Compliance of institutional strategic plans with objectives of Development Plan will be pursued. Strategic plan objectives will be more efficiently reflected to budget preparation and implementation process.
- In order to strengthen implementation of public financial management reforms, a budget structure based on program approach will be adopted gradually.
- Impact of contractual liabilities on public finances will be considered in planning of public-private partnership investments.
- Effectiveness of existing policies about procurement of services in the public sector will be reevaluated with cost and benefit analysis.
- Agricultural subsidies will be determined in line with the objectives of increasing efficiency, productivity and value-added.
- In the allocation of public R&D expenditures, priority will be given to directing private investments to industrial sub-sectors with high trade deficit.
- Education will continue to be priority sector in allocation of public expenditures.
- Deductions from the general budget tax revenue shares of the local administrations on the account of their liabilities to the public sector will continue regularly.
- Without compromising the quality of health services, medicine and treatment expenditures will be rationalized to prevent unnecessary drug and service usage.
- 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.
- Measures will be taken to overcome the structural problems of university hospitals.
- Efficiency of social programs will be assessed; multiple utilizations and duplications will be prevented in these programs.
- Premium restructuring that threatens the actuarial balance of the social security system will not be allowed except extraordinary conditions such as economic crises or natural disasters.
- Implementations that have negative repercussions on the financial sustainability of the social security system will be reviewed.

3.1.1.3. Public Borrowing Policy

- Borrowing policies based on strategic benchmarks will be maintained.
- To the extent possible within market conditions, borrowing will be made mainly in TL denominated and with fixed rate instruments to manage exchange rate and interest rate risks, while policy of keeping sufficient cash reserves and extending the average maturity of the borrowing will be maintained in order to reduce the liquidity risk.

- Switching and the buy-back auctions may be used to ensure a balanced debt redemption calendar and to increase the price efficiency in secondary market.
- Policies towards ensuring an efficient secondary market yield curve and providing liquidity in trading of Government Domestic Borrowing Instruments through re-issuance strategy will continue to be implemented.
- In order to expand the investor base of the government borrowing instruments, efforts on new instrument development will continue.
- Primary Dealership System will be continued.
- Information about borrowing such as financing programs, domestic borrowing strategies and procurement announcements will continue to be announced on a regular basis.

3.1.1.4. Public Financial Management and Audit

- Consistency among strategic plans, budgets and performance programs will be strengthened, efficient and coordinated functioning of internal and external audit systems will be ensured and efficiency of internal control systems will be enhanced.
- Compliance of public administrations with the internal control and internal audit standards will be enhanced.
- Quantity and competency of human resources in public financial management will be enhanced to strengthen management responsibility in public administrations.
- In order to ensure an effective external auditing in public sector, the implementation capacity of Court of Accounts will be strengthened.

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 the global financial crisis, economic growth was strong and affected the budget revenues positively. However, there was a moderate growth environment in 2012 and this slowdown in growth rate had partially unfavorable effect on budget revenues. On the other hand, increases in the dividends from the Central Bank, interest revenues, shares from people and agencies, and as a result of the revenue increasing measures increase in SCT collections, and due to the robust performance in the registered employment and high profits in the banking sector, increases in personal and corporate income tax resulted in an increase of 0.6 percentage point in the central government budget revenues and its share in GDP was realized as 23.5 percent.

In 2012, central government primary expenditures increased by 1.2 percentage points as a ratio to GDP, and interest spending rose by 0.2 percentage point. Central government budget total expenditures were realized as 25.6 percent of the GDP. Current expenditures played a major role in the increase of primary expenditures, as it did in the recent years, while capital expenditures, as a ratio to GDP, were at the same level as compared to 2011. In this regard, total personnel expenditures increased by 0.5 percentage point as compared to 2011, and realized as 7.1 percent of the GDP due to the general wage/salary increases, inflation compensation and increase in public employment. Transfers to the social security system were 4.5 percent of the GDP with an increase of 0.4 percentage point.

Parallel to the aforementioned developments, central government budget deficit was recorded as 2.1 percent of the GDP, while primary surplus ratio was 1.3 percent.

In 2013, with the contribution of developments in domestic economic activities and one-off revenues, central government revenues to GDP ratio is expected to increase by 1.3 percentage points compared to the previous year and to realize as 24.8 percent. 1.2 percentage points of this increase stems from the rise in tax revenues.

In 2013, overdue payments of some public institutions in addition to their current tax liabilities have become a determining factor on the favorable performance of tax revenues. In this context, BOTAŞ has paid 3.3 billion TL of VAT arrears and TEDAŞ has also paid 2.6 billion TL as part of the arrears that it assumed according to the related act. In addition, Cabinet Decisions 2012/3735 and 2012/4116 on tax rates in September 2012 and January 2013, have increased the SCT revenues from petroleum products and motor vehicles and the collection of stamp duties and fees.

Although corporate income tax revenues have been affected negatively by the fluctuations in exchange rate and interest rates starting from the second half of the year, it is estimated to realize parallel with the budget targets with the help of the arrear payment made by TEDAŞ. Additionally, personal income tax revenues are expected to realize as 0.7 billion TL above the budget target.

As an important part of the budget revenues, SCT collection is expected to realize above the budget target by 3.5 billion TL with the contribution of the increase in SCT revenues from petroleum products and motor vehicles. In this context, share of SCT revenues in general government total tax revenues are estimated to rise by 0.9 percentage point compared to 2012 and reach 26.7 percent.

In 2013, compared to the budget targets, VAT revenues are expected to realize above the target by 1.3 billion TL as a result of the recovery in domestic demand and 0.7 billion TL amount of payments from TEDAŞ and BOTAŞ. Additionally, with the effect of the tax rate increases in January 2013, stamp duty and fee collections are expected to be above the target by 1.3 billion TL and 1.8 billion TL at the end of the year.

In 2013, non-tax revenues to GDP ratio is expected to realize above the budget target by 0.7 percentage point which also means above the target in nominal terms by 9.9 billion TL. In this development, privatization revenues expected as 8.3 billion TL compared to the 4 billion TL budget target and unbudgeted dividend payments from EÜAŞ and Central Bank amount of 2.1 billion TL and 2.4 billion TL respectively are the main determining factors.

Revenues from the sale of the degraded forest land in scope of the 2B regulation are expected to realize around 3 billion TL in 2013, 1.8 billion TL below the target.

In 2013, primary expenditures are estimated to realize as 22.8 percent of the GDP with an increase of 0.7 percentage points as compared to the previous year while interest spending is projected to be 3.2 percent with a decrease of 0.2 percentage point. In this regard, with an increase of 0.5 percentage point as compared to the previous year, central government total expenditures are foreseen to rise to 26.1 percent of GDP in 2013.

Total personnel expenditures are estimated to be 7.3 percent of GDP by an increase of 0.1 percentage point. General wage and salary increases were 3 percent, in each, in the first and second halves of the year, in addition to that public personnel received 0.14 percent and 1 percent additional wage and salary increases in the first and second halves of this year in line with the inflation realizations.

Budgeted as 33.4 billion TL, purchases of goods and services are expected to be 36.9 billion TL with an increase of 3.5 billion TL. Shift in the recording of lightening spending of streets and avenues from current transfers to purchase of goods and services, increases in the transportation spending in education, and additional needs of various public agencies were the main causes in the aforementioned development. As a result, initially programed as 2.1 percent, purchases of goods and services are now expected to be 2.4 percent of the GDP.

Expenditures for health, retirement and social aids are estimated to realize 935 million TL lower than its initial budget appropriation in 2013. Minimum wage and wage/salary increase for public personnel higher than their initial projection, and the rise in the volume of active insured played a major role in that situation. In this regard, in comparison to their initial budget appropriation, while social security deficit financing is estimated to decrease by 4.6 billion TL, social security contributions made by the government are estimated to increase by 447 million TL. Furthermore, payments upon receipts are estimated to realize 312 million TL lower of its initial budget appropriation; while other transfers are estimated to surpass its initial appropriation by additional 2.4 billion TL due to the fulfillment of overdue General Health Insurance premium payments in this year by government for those in need and by additional 1.1 billion TL due to incentive spending.

Table 3.1: Central Government Budget Balance

(Percent of GDP)

	2011	2012	2013*	2014**
Expenditures	**24.2**	**25.6**	**26.1**	**25.4**
Primary Expenditures	**21.0**	**22.1**	**22.8**	**22.4**
Personnel Expenditures	5.6	6.1	6.2	6.4
Social Sec. Ins. Government Premium Expenditures	1.0	1.0	1.1	1.1
Goods and Services Purchase Expenditures	2.5	2.3	2.4	2.2
Current Transfers	8.5	9.1	9.6	9.5
Capital Expenditures	2.4	2.4	2.6	2.1
Capital Transfers	0.5	0.4	0.5	0.4
Lending	0.4	0.7	0.6	0.4
Reserve Appropriation	0.0	0.0	0.0	0.2
Interest Payments	**3.3**	**3.4**	**3.2**	**3.0**
Revenues	**22.9**	**23.5**	**24.8**	**23.5**
Tax Revenues	19.6	19.7	20.9	20.3
Non-Tax Revenues	2.9	3.4	3.0	2.5
Capital Revenues	0.2	0.2	0.8	0.5
Grants, Aids and Special Revenues	0.2	0.3	0.1	0.1
Primary Surplus	1.9	1.3	2.0	1.1
Programme Defined Primary Surplus	1.2	0.3	0.9	0.5
Borrowing Requirement	**1.4**	**2.1**	**1.2**	**1.9**

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

In 2013, payments for duty losses of SEEs and public banks are projected to realize 537 million TL lower than their initial budget appropriations. Similarly, as a result of the shift in the recording of lightening spending of streets and avenues as the purchase of goods and services, Treasury aids to the local governments are expected to be 612 million TL less than its initial appropriation. In addition, other Treasury aids are estimated to realize 565 million TL less than its initial budget appropriation due the lower realization of transfers to Social Assistance and Solidarity Fund.

In line with these developments, current transfers are estimated to be 2.1 billion TL lower than its initial budget appropriation, and realize as 149.2 billion TL in 2013. As a ratio to GDP, this spending item is projected to be 9.6 percent of the GDP with an increase of 0.4 percentage point compared to the previous year.

In 2013, capital spending, which was projected 33.5 billion TL in the budget process, is estimated to realize as 40.1 billion TL with an increase of 6.6 billion TL, and as a ratio to GDP capital spending is expected to be 2.6 percent with an increase of 0.1 percentage point compared to the previous year. Supplemental increases for various transportation projects are the main reason behind this development.

Capital transfers are projected to be 0.5 percent of the GDP and realize as 2.1 billion TL higher than its initial budget appropriation in 2013. Undertaken 1.5 billion TL portion of capital transfers by the Ministry of Transport Maritime Affairs and Communication, which was projected to be made by the Treasury to the Turkish State Railways and recorded under lendings item, additional 1.1 billion TL spending to Ministry of Interior and Special Provincial Administrations and additional allocation of 0.3 billion TL for KÖYDES project are the main reasons behind this aforementioned situation. In addition, transfers to the development agencies and North Cyprus are estimated to realize 0.4 billion TL less than their initial appropriations for each item.

In 2013, lendings are estimated to realize 2.1 billion TL under its initial budget appropriation, 0.6 percent of the GDP with a decrease of 0.1 percentage point compared to the previous year, due to some portion of transfers to Turkish State Railways are realized as capital transfers and downwards revision of capital transfers for SEEs.

As a result of the above-mentioned developments, central government budget deficit, which was estimated as 34 billion TL in the budget process is now revised to 19.4 billion TL. Similarly, initial budget deficit estimation of 2.2 percent of the GDP is now revised to 1.2 percent of the GDP with a decrease of 0.8 percentage point compared to the previous year. In addition, program-defined central government budget surplus, which was 0.3 percent in 2012, is estimated to rise 0.9 percent of the GDP in 2013.

3.1.2.1.2. Developments Regarding General Government Revenues and Expenditures

General government deficit raised to 5.5 percent of GDP in 2009 as a result of global financial crises and stimulus packages introduced to mitigate the effects of global crisis on economy. High growth rates recorded in the aftermath of crises has affected public sector balances positively, strong increase in domestic demand and foreign trade contributed to rise in tax and social security premium collections substantially. Moreover, in 2011 important amount of additional revenues was obtained within the context of the regulation regarding to restructuring of some public receivables. As a result the ratio of general government deficit to GDP decreased to 3 percent in 2010 and 0.4 percent in 2011.

Table 3.2: General Government Revenues and Expenditures - 1

(Percent of GDP)

	2009	2010	2011	2012
Taxes	18.5	19.7	20.1	20.2
Direct	6.0	5.6	5.9	6.1
Indirect	11.8	13.4	13.5	13.4
Wealth	0.6	0.7	0.7	0.7
Non-Tax Revenues	2.0	1.8	1.8	2.1
Factor Incomes	6.2	5.5	5.0	5.7
Social Funds	7.4	8.1	9.2	9.4
Total	34.2	35.1	36.1	37.4
Privatization Revenues	0.5	0.4	0.3	0.5
Total Revenues	**34.6**	**35.5**	**36.4**	**37.8**
Current Expenditures	17.7	17.1	16.6	17.5
Investment Expenditures	3.3	3.4	3.3	3.5
Fixed Investment	3.3	3.4	3.3	3.5
Change in Stocks	0.0	0.0	0.0	0.0
Transfer Expenditures	19.1	18.0	16.8	17.9
Current Transfers	18.1	16.8	15.9	17.0
Capital Transfers	1.0	1.2	0.9	0.9
Stock Revaluation Fund	0.0	0.0	0.0	0.0
Total Expenditures	**40.1**	**38.5**	**36.8**	**38.9**
Borrowing Requirement	**5.5**	**3.0**	**0.4**	**1.0**
Borrowing Req. Exc. Privatization Revenues	**5.9**	**3.4**	**0.7**	**1.5**
Primary Expenditures	34.4	33.9	33.4	35.4
Primary Surplus	0.3	1.5	3.0	2.5
Program Defined Primary Surplus	-1.7	0.0	1.8	0.7

Source: Ministry of Development

In 2012, as a result of moderate economic growth, general government revenues increased slightly while general government expenditures increased by 2.1 percentage points compared to previous year due to particularly current-type expenditures, therefore the general government deficit was realized as 1 percent of GDP.

3.1.2.1.3. Medium Term Perspective

In the calculation of the general government figures, assumptions made about revenues and expenditures for the period of 2014-2016 are as follows:

- Lump-sum taxes and fees will be updated by taking the general economic environment into account.
- SEE prices will be determined in line with the programme targets.
- Salary and wage increases of public servants have been determined by Collective Agreement as 175 TL lump sum pay rise in 2014 and 3 percent increases for the first and second half of 2015.
- Measures will be taken in order to make medicine and treatment expenditures more rational without compromising the quality of health services.
- Efficiency of social programs will be assessed and arrangements will be made to increase the effectiveness of social assistance.

In 2013, general government tax revenues to GDP ratio is expected to rise by 1.2 percentage points. While direct taxes is expected to decline slightly, rise in the indirect taxes due to tax regulations introduced at the end of 2012 and payments regarding to past tax arrears of some public enterprises has been affective on the mentioned improvement. In addition, general government privatization revenues are expected to rise by 0.2 percentage point compared to previous year. In addition, as a result of increase in registered employment in 2013, social funds are expected to rise by 0.7 percentage point and reached to 10.1 percent of GDP. As a result, general government revenues are expected to rise by 1.9 percentage points compared to the previous year, and will be 1.8 percentage points above previous program estimate.

General government primary expenditures are expected to rise by 2 percentage points compared to the previous year, and will be 1.5 percentage points higher than the previous program estimate. Mentioned development was caused by 0.5 percentage point increase in current expenditures, 0.6 percentage point increase in capital expenditures and 0.4 percentage point increase in transfer expenditures compared to the previous program estimates. Thus, the ratio of general government primary expenditure to GDP is expected to rise 37.4 percent in 2013.

On the other hand, with the decline in government debt and borrowing interest rates, 0.2 percentage point decrease in interest expenditure is expected, thus the general government expenditures is expected to amount 40.8 percent of GDP. In this context, general government is expected to run 1 percent of deficit and 2.3 percent of primary surplus in 2013.

In 2014, general government tax revenues to GDP ratio are estimated to be 20.9 percent with a decrease of 0.5 percentage point compared to previous year, as a result of the decline 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 0.8 percent respectively.

In 2014, general government non-tax revenues to GDP ratio is expected to be at the same level of 2013 and to realize as 1.9 percent, likewise social funds is expected to be close to previous years amount and will be 10.2 percent of GDP. Whereas, factor incomes, which increased to 5.7 percent of GDP in 2013 due to one-off nature revenues, is expected to decline to 4.9 percent as a result of disappearance of one-off revenue effects in 2014. In this regard, in 2014, general government total revenues is estimated to decreased by 1.3 percentage points compared to the previous year and is expected to be 38.4 percent of GDP.

Table 3.3: General Government Revenues and Expenditures - 2

(Percent of GDP)

	2013	2014	2015	2016
Taxes	21.4	20.9	20.8	20.5
Direct	5.9	5.9	5.9	5.9
Indirect	14.8	14.2	14.0	13.8
Wealth	0.7	0.8	0.9	0.8
Non-Tax Revenues	1.9	1.9	2.0	2.2
Factor Incomes	5.7	4.9	4.7	4.6
Social Funds	10.1	10.2	10.2	10.2
Total	39.1	37.9	37.7	37.5
Privatization Revenues	0.6	0.6	0.4	0.2
Total Revenues	**39.7**	**38.4**	**38.1**	**37.7**
Current Expenditures	18.2	18.1	17.6	17.4
Investment Expenditures	4.0	3.6	3.8	3.7
Fixed Investment	4.0	3.6	3.7	3.7
Change in Stocks	0.0	0.0	0.0	0.0
Transfer Expenditures	18.6	17.9	17.6	17.1
Current Transfers	17.5	17.3	16.9	16.3
Capital Transfers	1.0	0.6	0.7	0.8
Stock Revaluation Fund	0.0	0.0	0.0	0.0
Total Expenditures	**40.8**	**39.6**	**39.0**	**38.2**
Borrowing Requirement	**1.0**	**1.1**	**0.8**	**0.5**
Borrowing Req. Exc. Privatization Revenues	**1.6**	**1.7**	**1.2**	**0.7**
Primary Expenditures	37.4	36.4	36.0	35.6
Primary Surplus	2.3	2.0	2.1	2.0
Program Defined Primary Surplus	0.8	0.9	1.1	1.3

Source: Ministry of Development

In 2014, general government primary expenditures is expected to decrease by 1 percentage point particularly due to the decline in central government budget capital expenditures and current transfers of extra budgetary funds. In the same period, interest expenses is expected to maintain the declining trend and decrease by 0.2 percentage point compared to the previous, as a result, total general government expenditures is expected to decline 39.6 percent of GDP.

As a result of the developments expressed above, general government deficit is expected to be 1.1 percent and general government primary surplus is estimated to be 2 percent of GDP in 2014.

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 general government balance analyzed in public finance chapter, actual general government balance does not cover the privatization revenues and one-off revenues and expenditures. 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.

In 2012, the expenditures of central government budget, social security institutions and local governments increased more than their revenues. In the same year, the negative effects of slower growth rate especially on revenues were corrected partially due to some measures taken. At the same time, increases in budget expenditures, mainly increases in personnel expenditures, good and services purchases, current transfers, interest payments, domestic lending, were effective on the rise of the actual general government deficit by 0.8 percentage point compared to previous year.

Considering the developments on the structural general government balance calculated by eliminating impact of conjuncture, it is observed that the ratio of the structural general government deficit to potential GDP have ameliorated to some extent. Similar to the situation of actual deficit, balances of social security institutions, local governments and central government budget were determinant behind the developments of the structural general government deficit.

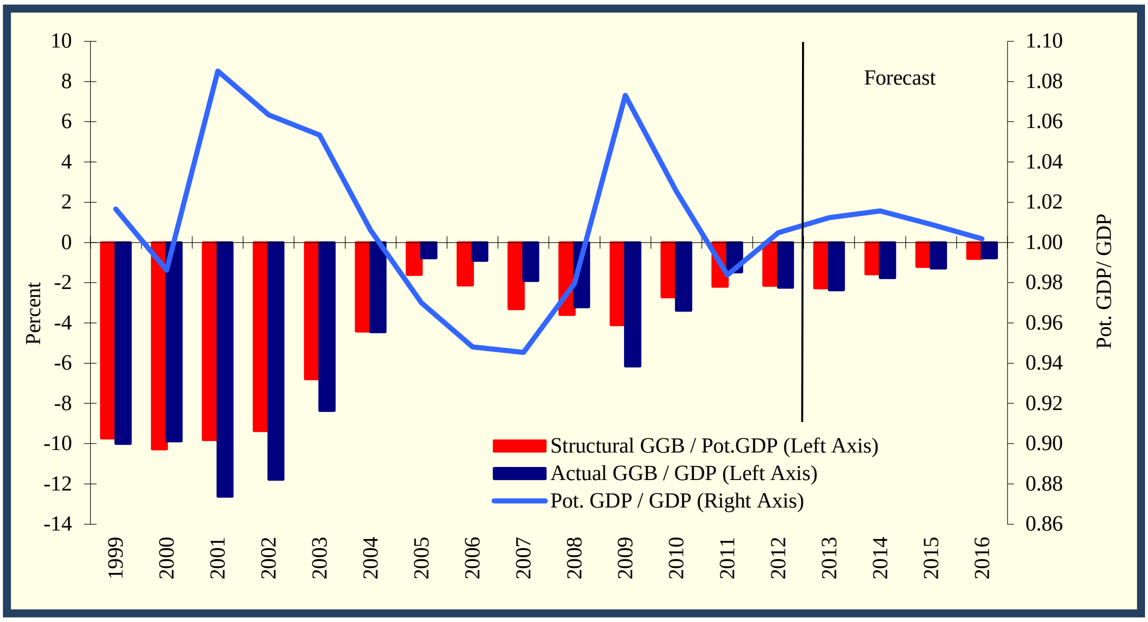
Table 3.4: General Government Balance Analysis [1]

	Output Gap (Y/Y^p) [2]	General Government Balance / GDP		Primary General Government Balance / GDP		Cyclical Balance / GDP
		Actual Balance	Structural Balance [3]	Actual Balance	Structural Balance [3]	
1999	-1.63	-9.99	-9.73	1.25	1.32	-0.09
2000	1.40	-9.87	-10.27	3.17	2.95	0.25
2001	-7.85	-12.63	-9.81	4.91	6.35	-1.98
2002	-5.96	-11.78	-9.36	3.49	5.00	-1.83
2003	-5.07	-8.37	-6.78	4.93	5.84	-1.22
2004	-0.60	-4.44	-4.42	5.89	5.86	0.00
2005	3.10	-0.77	-1.59	6.40	5.80	0.78
2006	5.48	-0.90	-2.13	5.24	4.35	1.11
2007	5.77	-1.90	-3.30	3.97	2.90	1.22
2008	2.09	-3.21	-3.59	2.21	1.94	0.31
2009	-6.81	-6.15	-4.09	-0.42	1.25	-1.75
2010	-2.48	-3.37	-2.71	1.15	1.70	-0.59
2011	1.65	-1.47	-2.19	1.89	1.22	0.69
2012	-0.48	-2.23	-2.13	1.29	1.38	-0.09
2013	-1.21	-2.36	-2.26	0.99	1.05	-0.07
2014	-1.54	-1.76	-1.56	1.37	1.53	-0.18
2015	-0.89	-1.28	-1.21	1.62	1.67	-0.07
2016	-0.18	-0.76	-0.80	1.78	1.74	0.04

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

The actual and structural general government deficits, which have started to display upward trend in 2012, are expected to decrease in 2014-2016 period, with the additional measures taken. This expected improvement in structural balance will result from the amelioration of balances of extra-budgetary funds, social security institutions and local governments in 2014, and it will be stemmed from the improvement in balances of social security institutions and central government budget for the years 2015 and 2016. Thus, the ratio of actual and structural general government deficit to GDP and potential GDP consecutively, are expected to realize as 1.3 percent and 1.2 percent on average in the period of 2014-2016 (Figure 3.1).

Figure 3.1: General Government Balance

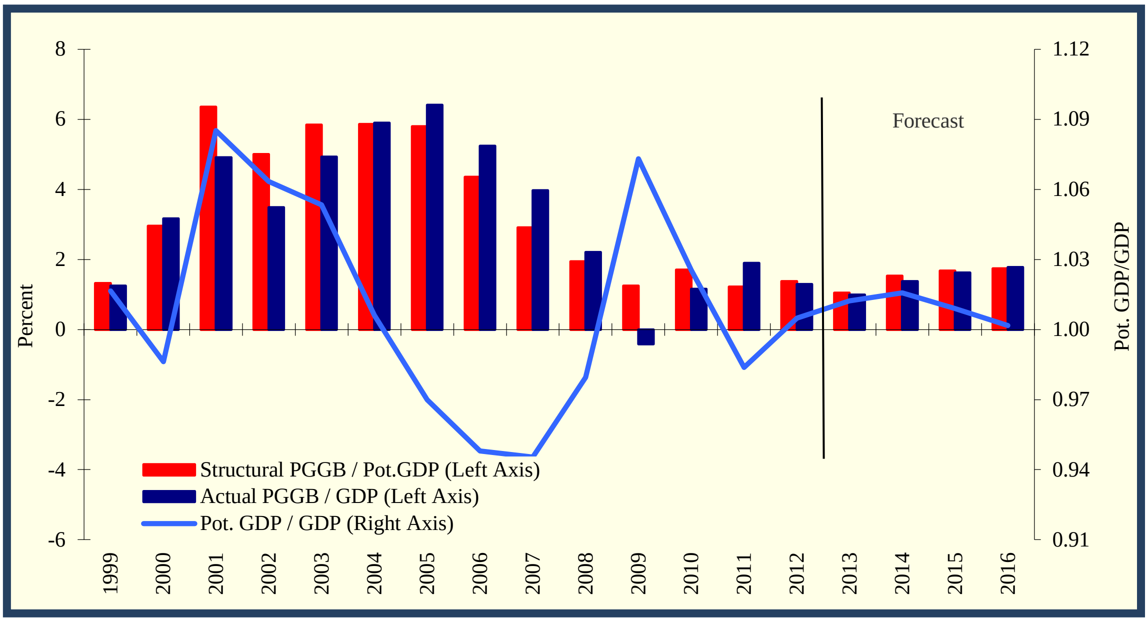


GGB: Public Claims Restructuring, Privatization, 2B Revenues and Other One-Off Revenues and Expenditures Excluded General Government Balance
Pot. GDP: Potential GDP

In 2013, deficit of social security institutions and central government budget decreased consecutively due to the increase in current premium revenues and the indirect taxes which were influenced positively by tax measures taken. On the other hand, it is expected that spendings, supposed to increase as a result of local elections, led to rise in local governments deficit and extra-budgetary funds balance, which run a surplus in the previous year, is predicted to turn into a deficit because of the increases in its expenditures. As a result of these developments, the ratio of actual general government deficit to GDP is estimated to realize as 2.4 percent with 0.1 percentage point deterioration compared to previous year. Correspondingly, the ratio of structural general government deficit to potential GDP is expected to deteriorate by 0.1 percentage point.

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 2013 (Figure 3.2). As from 2014, 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 1.6 percent annually on average in 2014-2016 period.

Figure 3.2: Primary General Government Balance

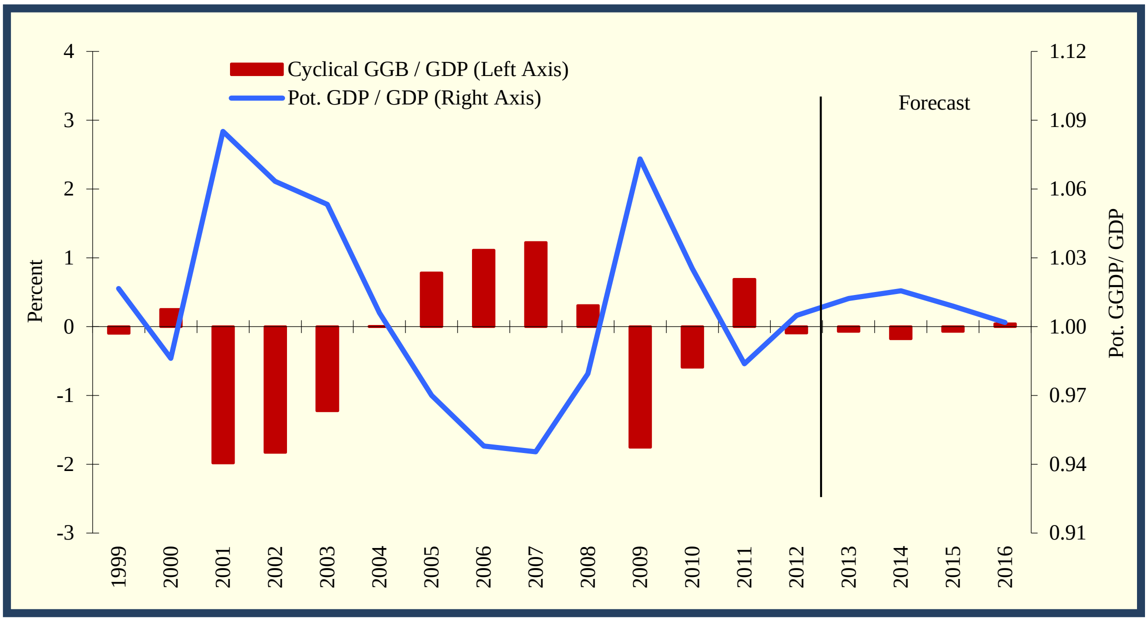


PGGB: Primary General Government Balance
Pot. GDP: Potential GDP

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 and expenditures are excluded in the calculations of structural and actual general government balances, cyclical balance only reflects the impacts of conjunctural developments.

It is observed that the cyclical effect has declined 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

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, the following measures were taken as the main pillars of the borrowing policy in 2013:

- To borrow mainly in TL,
- Using fixed rate TL instruments as the major source of domestic borrowing and decrease the share of debt which has interest rate re-fixing period less than 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 upcoming periods.

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. With a 41.7 percent decrease, the ratio of EU defined general government debt stock to GDP, which was 77.9 percent in 2001, declined to 36.2 percent at the end of 2012.

Central government total debt stock increased by 13.8 billion TL compared to its 2011 level and reached 532.2 billion TL by the end of 2012. As of September 2013, debt stock reached 576.2 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 0.5 points compared to its 2011 level and reached 59.8 percent at the end of 2012 and this ratio has been 60.7 percent as of September 2013.

Table 3.5: EU Defined General Government Debt Stock

(Percent of GDP)

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
EU Defined General Government Debt	67.7	59.6	52.7	46.5	39.9	40.0	46.1	42.3	39.1	36.2

Source: Undersecretariat of Treasury

Compared to its 2011 level, central government domestic debt stock increased by 17.8 billion TL and reached 386.5 billion TL by the end of 2012. As of September 2013, it reached 407.9 billion TL. When the ratio of the respective stock to GDP is considered, it is seen that it descended to 27.3 percent in 2012, from 28.4 percent in 2011.

Table 3.6: Central Government Gross Debt Stock

(Percent of GDP)

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Domestic Debt Stock	42.7	40.2	37.7	33.2	30.3	28.9	34.6	32.1	28.4	27.3
External Debt Stock	19.4	16.5	13.4	12.3	9.3	11.1	11.7	11.0	11.5	10.3
Total	62.2	56.6	51.1	45.5	39.6	40.0	46.3	43.1	39.9	37.6

Source: Undersecretariat of Treasury

The central government foreign debt stock has been 168.2 billion TL as of September 2013. Considering the interest composition of foreign debt stock, the share of fixed rate debt has been 80.2 percent of foreign debt stock as of September 2013.

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

(Million TL)

	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	201,866	108,367	76,309	116,190	29,467
2013 Sept.	214,897	101,324	91,725	134,956	33,283

	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	318,056	137,834	76,309	532,199	59.8	25.9	14.3	100.0
2013 Sept.	349,853	134,608	91,725	576,185	60.7	23.4	15.9	100.0

Source: Undersecretariat of Treasury

Thanks to the decrease of short term securities share 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 to 5.3 as of September 2013 while it was 2.9 years at the end of 2005.

Analyzing the borrowing realizations in 2013, the average cost of fixed rate domestic borrowing, which was 8.7 percent and 8.8 percent in 2011 and 2012 respectively, declined to 7.5 percent in January-October 2013 period. The average maturity of cash domestic borrowing increased to 60.8 months in 2012 and 74.1 months in the period of January-October 2013 from its 2011 level of 44.7 months.

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

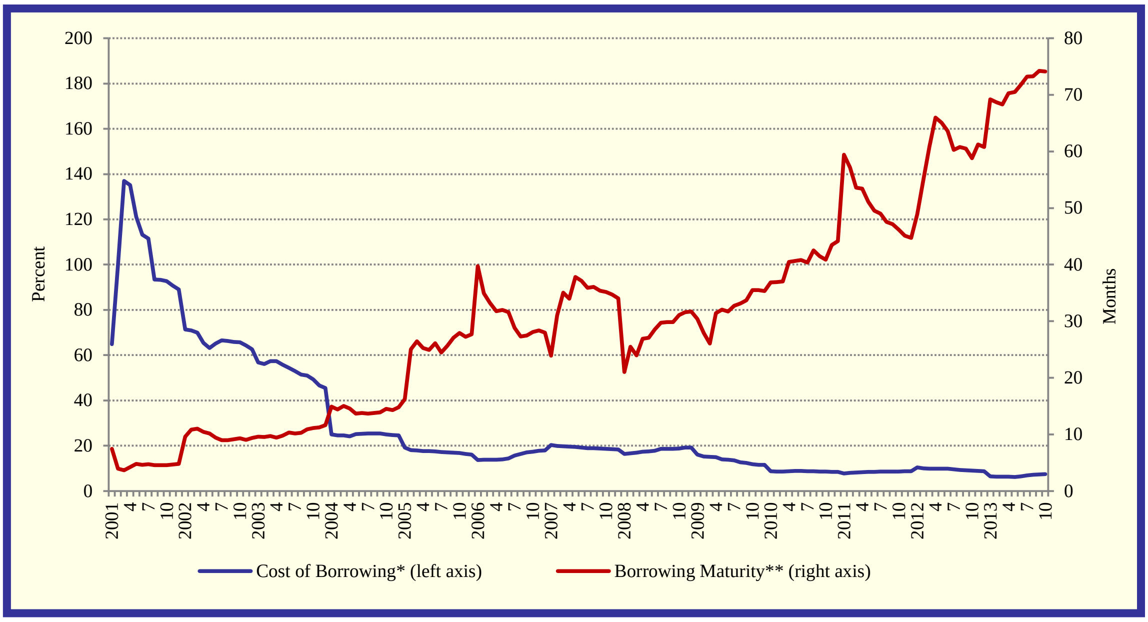
(Year)

	2005	2006	2007	2008	2009	2010	2011	2012	2013 Sept.
Domestic Debt Stock	2.0	2.0	2.1	2.0	2.0	2.6	2.6	2.8	3.6
Foreign Debt Stock	5.7	7.0	7.7	7.9	7.9	8.8	9.0	9.4	9.6
Total	2.9	3.4	3.4	3.6	3.5	4.1	4.4	4.6	5.3

Source: Undersecretariat of Treasury

In order to broaden the investor base and to diversify the borrowing instruments, lease certificates were issued for the first time in 2012. Turkish Treasury raised 3.3 billion TL through the issuances in February and August in domestic markets and 1.25 billion dollars in October through issuance in international markets in 2013.

Figure 3.4: Average Time to Maturity of 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

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.

These operations can create obligations (contingent liabilities) whose timing and magnitude depend on the occurrence of some uncertain future events which are not under the control of the Undersecretariat of Treasury. Internal 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 1 January 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. In addition to this guarantee opportunity starting from 2009, on-lent foreign financing was included in the scope of this limit and it has been determined as 3 billion dollars since 2010. 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 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 and budget appropriation was started to be allocated every year as of this date in order to eliminate the disruptions in the cash and debt management caused by the amounts paid by the Treasury due to Treasury guarantees. As the repayments to the Risk Account is sufficient for the undertakings realized from the account budgetary allocations, which is one of the items of the revenues of the account, has not been used since 2009.

3.1.4.3.3. Repayment Guarantee

The repayment guaranteed debt stock has slightly increased from its level of 9.7 million dollars in 2012 to 9.8 million dollars by end of second quarter of 2013. Guarantees provided to public banks and private investment and development banks have the biggest share within the repayment guaranteed debt stock.

Despite the increase in repayment guaranteed debt stock since 2007, the undertaking ratio decreased in the same period and it was 5.3 percent as of end of October 2013.

Analyzing 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 Euros)

	Principal	Interest	Total
2014	579	114	693
2015	696	103	799
2016	712	98	809
2017+	5,284	465	5,749

Source: Undersecretariat of Treasury

(*) Based on drawings; as of June 2013, provisional

3.1.4.3.4. Investment Guarantees

Undersecretariat of Treasury has provided investment guarantees to energy and infrastructure sectors besides the repayment guarantees. Within the context of investment guarantees provided 2 billion dollars has been undertaken in total as of October 2013.

3.1.4.3.5. Treasury Receivables

As of September 2013, the local administrations have 64.8 percent, SEEs have 16 percent and other receivables have 19.2 percent shares in the Treasury's receivables stock.

In January-September 2013 period, cash payments of the institutions (43.5 percent) have the highest share within the collections. In the same period, collections from privatization has a share of 35.5 percent of the total collections whereas deductions made from tax income shares of the Municipalities by the Ministry of Finance and by İller Bank constitutes 16.5 percent and 2 percent of total collections, respectively. Lastly, collections made pursuant to the Law No. 6183 and transfers from other institutions are 2.5 percent of collections in the mentioned period.

3.1.4.3.6. General Government Gross Debt Stock Projections for 2014-2016 Period

As a result of the prudent fiscal policies implemented, efficient borrowing strategies and strong growth performance in the last decade, the ratio of the general government debt stock to GDP has decreased significantly. However, due to the economic contraction after global crisis and budget deficit increase, 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 36.2 percent at the end of 2012. On the other hand, it is anticipated that the stock ratio will tend to decrease in the period of 2013-2016 and fall down to the level of 30 percent at the end of 2016.

Table 3.10: Projections of EU Defined General Government Debt Stock

(Percent of GDP)

	2012	2013	2014	2015	2016
	Realization	Forecast			
EU Defined General Government Debt Stock	36.2	35.0	33.0	31.0	30.0

Source: Medium Term Programme (2014-2016)

3.1.5. Budgetary Implications of Major Structural Reforms

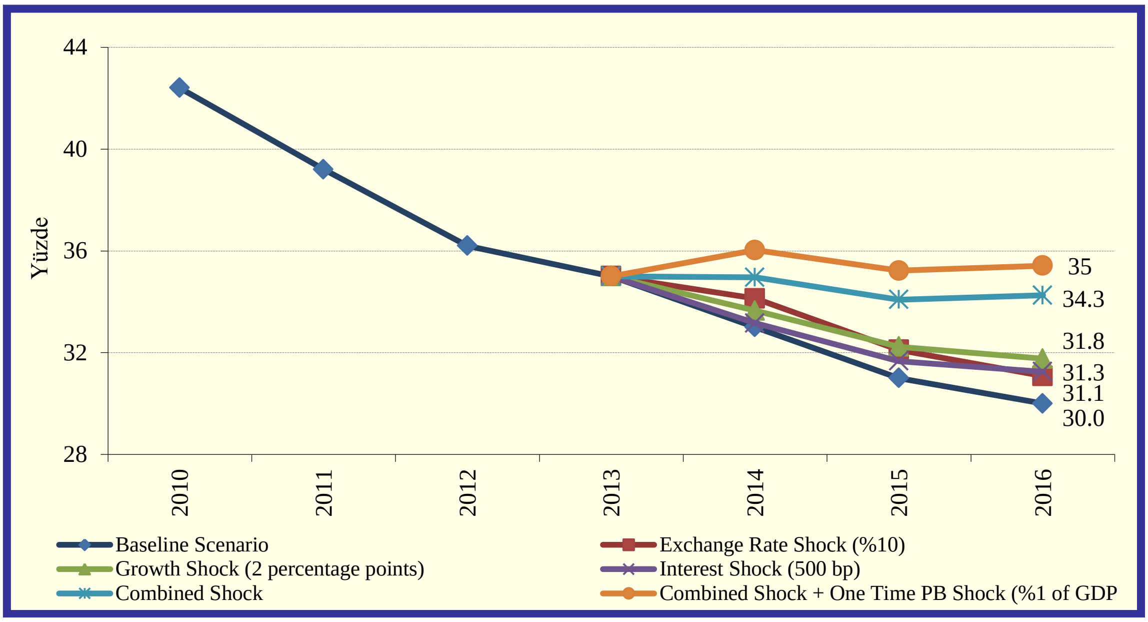
The five-point discount in disability, old age and death premiums of the employer to be paid by the Treasury in accordance with the Law No. 5763 for those who are working on an employment contract is expected to create an additional burden of 0.37 percent, 0.35 percent, 0.36 percent and 0.39 percent (as a ratio to GDP) on the social security balances in 2009, 2010, 2011 and 2012 respectively. The ratio of the related magnitude to the GDP for 2013, 2014, 2015 and 2016 is expected to place a burden of 0.44 percent, 0.45 percent, 0.46 percent and 0.47 percent on GDP, respectively.

3.2. Sensitivity Analysis

Thanks to the sound fiscal policies and debt management practices based on strategic benchmarks implemented since 2002, the resilience of the public debt stock against shocks has significantly improved. In this regard, sustainability analysis regarding the course of public debt stock against various macroeconomic shocks in the period of 2014-2016 is presented below.

Figure 3.5 illustrates medium term course of EU defined general government debt to GDP ratio under different scenarios. In these scenario analyses, impacts of 10 percent upward shift in the exchange rates, 2 points downward shift in the real growth rate and 500 base points upward shift in the real interest rates over the analysis period compared to the base scenario in each year have been separately and jointly assessed. In a new shock scenario, one time primary balance shock is applied to the first year of the analysis period in addition to the combined shock scenario. In this scenario, it is assumed that primary balance performs 1 percent of the GDP lower than the baseline scenario. In this way, impact of possible risks such as contingent liabilities, which may lead to increase the financing needs is analyzed. Compared to the baseline scenario, the debt ratio will record an increase of 1.1 percentage points under the exchange rate shock; 1.3 percentage points under the interest rate shock and 1.8 percentage points under the growth rate shock in 2016. In the combined shock scenario in which all shocks are taken into consideration together, it is expected that the debt ratio may increase by 4.3 percentage points compared to the baseline scenario. When primary balance shock is added to the combined shock, debt ratio rises to 5.4 percentage points compared to the baseline scenario. Even though the size of interest rate shock is assumed same as the previous year's sustainability scenarios, its impact at the end of the analysis period is substantially lower than the previous year's result (1.7 percentage points). This indicates benefits of debt management practices based on strategic benchmarks in general, and borrowing mainly via longer term and fixed coupon securities, specifically.

Figure 3.5: Sustainability Scenarios



Source: Undersecretariat of Treasury

3.3. Public Finance Risks

In the 2014-2016 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.
- Persistency in upward trend of primary expenditures in medium term might vanish budget flexibility and narrow down the fiscal space to be used for discretionary policies when required.
- Decline in liquidity and rise in interest rates in international markets might lead to increase in domestic borrowing interest rates leading to government interest expenses to rise.
- 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.
- The fluctuations in exchange rates and interest rates will adversely affect the revenue performance.

- 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

Turkey has made great strides in reducing government deficit and debt stock over the last decade. In this regard, generating primary surplus in the public sector to improve the fragile saving-investment balance and to reduce the need for external saving flows for sustainability of current account balance has been among one of the most important pillars of the economic program. With this strategy, it was also targeted that the private sector would focus on the employment generating reel sector activities and there would be a private-sector oriented growth rather than speculative activities dominating private sector emanated from high-reel interest rates.

Interest expenditures, which was 17.6 percent of the GDP reduced to 3.5 percent in 2012 with a 14.1 percent decrease. In this regard, the share of general government interest expenditures in total decreased to 9.1 percent from 41.2 percent within this period. Fiscal space generated was used primarily in financing social spending. In this regard, the share of social expenditures of the budget 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 be around 19.6 billion TL in 2013.

Especially during the recent years substantial increases were recorded in the investment spending. In 2013, 6.6 billion TL was added over the initial capital spending appropriations in order to expedite especially the projects regarding transportation infrastructure. In 2014-2016 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. Between 2014 and 2016, education sector will get the biggest share of total investments with a 26 percent rate. In the same period, education will be followed by transportation and communications sector and agriculture with approximately 22 percent and 16 percent rates, respectively.

For the R&D supports managed by TÜBİTAK, 841 million TL for 2013 and a total of 3.1 billion TL for 2012-2014 periods is projected 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 effective 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 1 April 2008. 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 is also regulated.

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, has been put into force. In this new incentive system, in addition to the advantages previously granted to investors, income tax withholding support and VAT refund is 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 be also paid by Ministry of Economy.

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 addition, with the amendment made in 2012, utilization period was extended to 31 December 2015. During the period between July 2009 when the said support became operative and September 2013, 1.819 million TL credit was provided for 3.396 SMEs.

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 Program, it is estimated that a total resource of 904 million TL will be used in the period of 2013-2016.

The Project for the Support of the Infrastructure of Villages (KÖYDES), 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 the forthcoming period. Accordingly, it is programed that 1.1 billion TL will be allocated to this project in the period of 2014-2016. For the program initiated to help financing of drinking water and sewage projects of municipalities, Water and Sewerage Infrastructure Project (SUKAP), 1.8 million TL is allocated for the 2014-2016 period.

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, 360 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 "Public Internal Control Guide" issued as a draft in order to guide the public administrations in implementing the new financial management and control system brought by the Financial Management and Control Law No. 5018 has been reorganized in line with the opinions and suggestions of the public administrations and planned to be issued before the end of 2013. Moreover, the studies on improving the Financial Management and Control Centre Harmonization Unit Manual carry on.

The trainings which have been asked to fulfill the responsibilities of the public administrations brought by the Law No. 5018 for establishing an effective financial management and control system continue to be organized.

The works on the amendments planned to be made in the Law No. 5018 continue.

Regulations amending the Regulations on Determining Internal Auditor Candidates, Training and Certificate", "Regulations amending the Regulations on Working Principles and Procedures of Internal Auditors" and "Decision amending the Principles and Procedures of Rating the Public Internal Auditor Certificate" were published in the Official Gazette.

Under the World Bank grant, BT Audit was carried out in the pilot administrations, Social Security Institution and Undersecretariat of Treasury with the consultancy provided by Ernst&Young Company.

The External Evaluation Expertise training program was held in March and 22 internal auditors were assigned as external evaluation experts at the end of the training.

The Public Internal Audit General Communique was published and put into effect in April, while the Public Internal Audit Guide was published and put into effect in September.

The Provisional Article 21 included in the Law No. 5018 which regulates the terms and conditions of being appointed to the internal auditor positions without being subjected to any exams was published in the Official Gazette No. 28622 on 18 April 2013 and the Basis and Procedures on Implementing the Provisional Article 21 were published in the Official Gazette No. 28656 on 24 May 2013.

The Cabinet Decision on Assigning Internal Auditor Personnel was published in the Official Gazette No. 28649 on 16 May 2013 and the Cabinet Decision on Appointing Internal Auditor Personnel to the Local Administrations was published in the Official Gazette No. 28663 on 31 May 2013.

A training program was organized for the internal auditors of the public administrations in 5 groups during May and June. A total of 670 internal auditors participated in the stated training program.

The 2012 General Report of Public Internal Audit was published in September and submitted to the Minister of Finance.

4. STRUCTURAL REFORMS

4.1. Enterprise Sector

4.1.1. Privatization

The total amount of privatization of which sales/transfer operations were completed was about 3 billion dollars in 2012. As of December 2013, this amount reached to 12.5 billion dollars. The main privatizations are block sales of Başkent Natural Gas Distribution Company and Hamitabat Electricity Generation Company, sales of Kangal and Seyitömer Thermal Power Plants belonging to EÜAŞ, sales of Boğaziçi, Gediz, İstanbul Anadolu Yakası, Akdeniz, Dicle, Vangölü, Aras and Toroslar Electricity Distribution Companies belonging to TEDAŞ, transfer of operating rights of some river power plants belonging to EÜAŞ, and sales of various immovable properties belonging to other institutions in this term.

The total amount of privatization implementations which are at the stage of approval/contract is 1 billion dollars and such implementations include Salıpazarı Port belonging to TDİ, three group of river power plants belonging to EÜAŞ, and immovables belonging to various state entities.

The privatization implementations for which transfer operations were completed in 2013 (as of December) are shown in Table 4.1.

Table 4.1: Privatization Transactions Completed in 2013

Company	Privatization Transaction	Sales Price (Dollars)
EÜAŞ-Seyitömer Thermal Power Plant	Sale of Plant/Asset	2,248,000,000
TEDAŞ-Boğaziçi Electricity Distribution Company	Sale of Plant/Asset	1,960,000,000
TEDAŞ-Toroslar Electricity Distribution Company	Sale of Plant/Asset	1,725,000,000
TEDAŞ-Gediz Electricity Distribution Company	Sale of Plant/Asset	1,231,000,000
TEDAŞ-İstanbul Anadolu Yakası Elec. Dis. Comp.	Sale of Plant/Asset	1,227,000,000
Başkent Natural Gas Distribution Company	Block Sale	1,162,000,000
EÜAŞ-Kangal Thermal Power Plant	Sale of Plant/Asset	985,000,000
TEDAŞ-Akdeniz Electricity Distribution Company	Sale of Plant/Asset	546,000,000
TEDAŞ-Dicle Electricity Distribution Company	Sale of Plant/Asset	387,000,000
TEDAŞ-Aras Electricity Distribution Company	Sale of Plant/Asset	128,500,000
TEDAŞ-Vangölü Electricity Distribution Company	Sale of Plant/Asset	118,000,000
Hamitabat Electricity Generation Company	Block Sale	105,000,000
EÜAŞ-10 group of river power plants	Transfer of Operating Rights	194,020,000
Others	-	463,217,003
TOTAL		**12,479,737,003**

The tender announcements have been published in order to privatize Derince Port belonging to Turkish State Railways, Çatalağzı, Kemerköy, and Yeniköy thermal power plants, and games of chance through license granting.

Privatization tender of some motorways and bridges, by the method of “transfer of operation rights”, was cancelled.

The completion of privatization procedure of TCDD Derince Port, TDİ Salıpazarı Port, some electricity generation plants belonging to EÜAŞ and national lottery games are foreseen in 2014.

4.1.2. Competition Law and Policies

In 2013, Guideline on Horizontal Cooperation Agreements, Guidelines on Elaborating the Leniency Regulation and Guideline on Assessment of Horizontal and Non-horizontal Mergers and Acquisitions were put into effect and thus, significant progress has been achieved in aligning national legislation with that of EU regarding the competition code.

Efforts to revise Law No. 4054, The Act on the Protection of Competition, are about to be completed and the draft is expected to be brought into the agenda of Grand National Assembly of Turkey. Work on the Guideline on Competitiveness Impact Assessment, which is part of the regulatory impact assessment process and which facilitates preparation of regulations in a way that least constrains competition, is completed and the draft Guideline is passed to the Prime Ministry.

4.1.3. Improvement of the Investment Environment

The Action Plans for 2013-2014 period of the Investment Climate Improvement Coordination Committee (YOİKK) are approved and announced on 17 July 2013.

Law on Mediation in Civil Disputes, which was approved by Grand National Assembly of Turkey in 2012, was put into practice on 22 May 2013. Regulation as to the Law was published in the Official Gazette on 26 January 2013.

Work and residence permits were consolidated in accordance with the Law on Foreigners and International Guard that was published in the Official Gazette on 11 April 2013. The Law shortens the time elapsed between the granting of the work permit and starting of the employees to work. The law will be put into practice on April 2014.

The preparatory work for the Action Plan for the Transformation Program on Improvement of Business and Investment Environment, which was designed to eliminate uncertainties and problems faced by investors by focusing on priority areas of Business and investment environment and to increase investments by improving existing mechanisms in that respect, has started. The program is planned to be implemented upon its approval by the High Planning Council in 2014.

4.1.4. Utilities and Network Industries

4.1.4.1. Energy

The studies for the liberalization of the energy market have been carried on also in 2013. 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 finally the realization of the renovation and expansion investments by the private sector.

As of September 2013, the share of private sector in electricity generation has reached to 66 percent. The increasing share of private sector in electricity generation is expected to continue in the coming years. As of the end of 2013, all of the privatization of the electricity distribution companies has been completed. Similarly, total 2.276 mw installed power capacity including 63 mw small HPP and 2.213 mw thermal power plants (Hamitabat, Seyitömer, Kangal) transferred to private sector. Preparatory works for tender of thermal power plants in state ownership power of 1.980 mw (Çatalağzı, Kemerköy, Yeniköy, and Yatağan) continue.

In consequence of the transfer of a number 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 approximately 80 percent in 2013. In this context, increasing the share of the private sector in wholesale market will provide a significant contribution to the development of competition.

4.1.4.2. Telecommunication

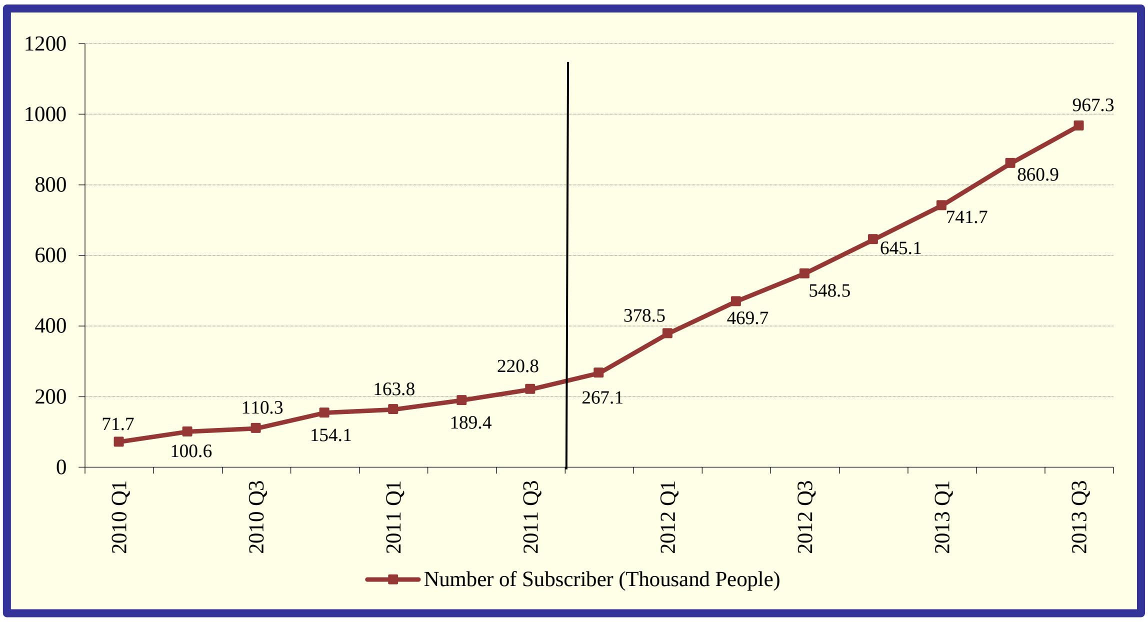
Law No. 4502, which was put into force in 2000 and amended the Telegraph and Telephone Law No. 406, paved the way to liberalization process in the telecommunications sector in Turkey and Telecommunications Authority was established as the independent regulatory body. On the other hand, in accordance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

According to Electronic Communications Law No. 5809, and Law No. 2813, on the Establishment of Information and Communications Technologies Authority (ICTA) 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.

The third round market analysis (Mobile Call Termination, Mobile Network Access and Mobile Call Origination, Wholesale Broadband Access Market Including Bitstream Access, Physical Network Infrastructure Access, Call Termination on Fixed Network, Wholesale and Retail Leased Lines, Call Origination on Fixed Network and Call Transit on Fixed Network) was completed by ICTA by April 2013. ICTA imposed ex-ante obligations on significant market power (SMP) operators to establish and maintain effective competition in relevant markets. However, ICTA evaluated that in the Market of Call Transit on Fixed Network, SMP determination and ex ante regulations are not required, and competitive environment has been developed. Based on the result of previous market analysis the obligations on Turk Telekom A.Ş, which is an SMP operator, were abolished and the related market has been deregulated. On the other hand, based on the Board Decision dated 19 December 2012 and 2012/DK-10/633 analysis results of the two markets, which received extended validity period (Market of Access to the Fixed Telephony Network and Market of Call on the Fixed Network), will be presented to public opinion till the end of 2013.

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. According to the signed Protocol, the second ordinary annual meeting, hosted by ICTA, was held on 22 January 2013. Moreover, in 2013 consultations on 15 different areas (competition infringements on the preliminary research / analysis, investigation processes, mergers/acquisitions references) were carried out between the two institutions until now.

Figure 4.1: Number of Fiber Internet Subscribers



Source: Information and Communication Technologies Authority

As a result of the Board Decision, dated 10 March 2011 and 2011/DK-10/511, which allows a partial exemption in the field of fiber access and relevant broadband market analyses (and in this context the regulatory operations made) in the last two years, a significant increase in the number of fiber subscribers were observed. As it can be seen from the Figure 4.1, the number of fiber broadband subscribers increased to 967 thousand in the third quarter of 2013, from 221 thousand subscribers in the third quarter of 2011. The aforementioned Board Decision, with the incentive effect of investments in next generation networks, is considered to have contributed to this improvement.

ICTA has completed sectorial 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 determined. 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	3.70	14.00	15.20	17.50
1 March 2007	-	1.89	3.00	13.60	14.50	16.70
1 April 2008	-	1.71	2.70	9.10	9.50	11.20
1 May 2009	1.39	1.71	2.70	6.55	6.75	7.75
1 April 2010	1.39	1.71	2.24	3.13	3.23	3.70
1 July 2013	1.39	1.71	2.24	2.50	2.58	2.96

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 an ICTA board decision 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 (WLR) implementation is effective since the beginning of February 2012. Within the scope of WLR practices, a total of 1,053,830 users received services by the end of October 2013.

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 and Communication Technologies 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, in 2011 disabled people and in 2012 first degree relatives of veterans and martyrs was granted 25 percent discount on some DSL tariff packages. In 2013, the scope of discounted tariffs, for people with disabilities, relatives of veterans and martyrs, has been extended to cover fiber internet tariffs and all DSL tariff packages in relevant reference offers.

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 July 2010. Prices for access to the local loop for the last six years are shown in the following table.

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
2013	38.55	5.49

Source: Information and Communication Technologies Authority

As of September 2013, in terms of fixed telephony revenues share of alternative operators is 21 percent in fixed telephone services market and 24 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.

Additionally in 2013, according to authority regulation entitled “Facility Sharing Requirement and Practice” all operators authorized to establish and operate fixed electronic communications infrastructure obligated to facility sharing in related communications infrastructure and network (pipes, ducts, eyes, etc.) as of 1 September 2013. With this practice, the operators, requested Facility Sharing, will finalize the requests they receive by taking into account the principles and procedures determined by the Authority.

On the other hand, changes regarding addition of Partial Leased Lines services to “Reference Leased Line Offer” (RLLO) offered by Turk Telekom was approved by ICTA to be effective on 1 June 2013. With the change, delivery of Partial Domestic Leased Lines and Partial TTUNEL service delivery have provided 25 percent discount compared to counterparts in the delivery of end to end services.

Within the scope of the churn regulation which came into force after the approval of the Authority in 2010, a total of approximately 978 thousand subscribers changed the service provider as of the end of September, 2013 and with the contribution of this regulation, alternative DSL internet service providers has reached 14 percent market share. In addition, the number of subscribers of Naked DSL service which allows DSL subscription without subscription to the PSTN has reached 998 thousand after a two-year implementation period.

4.2. Financial Sector

4.2.1. Banking Sector

As fundamental sub-regulations on banking sector were completed extensively in the previous years, 2013 regulations have complemented the previous ones. Within this scope, by the regulations made in 2013, in general, amendments have been made to the current regulations on measurement and evaluation of capital adequacy of banks, loan transactions, internal systems, support service procurement and supervision.

For providing high and stable growth, in order to increase the domestic savings which is the most reliable and permanent financing source and control the increasing of consumer credits, which has a negative impact on current account deficit, macro prudential measures are made. With regulations published in the Official Gazette on 8 October 2013, limitations made on consumer credit usage for both credit users and credit institutions (Box 2.2).

In order to increase domestic savings and to control consumer loans increase which negatively affects current account deficit, macro-prudential regulations was taken by the amendments published in the Official Gazette dated 8 October 2013. Hence, credit cards minimum payment was increased and the credit card credit limit was limited up to 4 times of income. Additionally, the suspension of use of cash was ruled in credit cards if credit cards minimum payment is not made 3 times in a year. Besides the suspension of use of cash, the purchase of goods and services will be suspended if credit cards minimum payment is not made consecutively 3 times in a year. On the other hand, the risk weights applied on credit card installments were increased by 25 points between 1-6 months and the remaining were increased by 50 points based on their maturities. The general provision rates and risk weights applied on vehicle loans were also increased. Besides these, credit cards and overdraft accounts of deposit were included in consumer credits and additional provision rates are revised upon this. To support reel sector and exports, general provision rates were decreased from 1 percent to 0 percent for export credits and from 1 percent to 0.5 percent for SME credits. Eximbank insurance policies for export credits were enabled to be counted as credit risk reduction techniques so that they can be transacted as Treasury guarantee.

On the other hand, “Regulation on Own Funds of Banks”, “Regulation on Making Amendments to the Regulation on Measurement and Evaluation of Capital Adequacy of Banks”, “Regulation on Capital Protection and Cyclic Capital Buffers” and “Regulation on Measurement and Evaluation of Leverage Levels of Banks” which are arranged within the scope of the studies for effectuating the reform recommendations known as Basel III in public and published by the Basel Banking Supervision Committee following the global crisis started in 2007 have been published and the above-mentioned regulations are foreseen to be put into force as of 1 January 2014.

4.2.2. Capital Market

At the end of 2012 and in 2013, 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:

- The new Capital Markets Law drawn up 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 entered into force upon its publication in the Official Gazette on 30 December 2012.
- In relation to the implementation of the provisions of the CML, a total of 30 communiqués and by-law were published as of 5 November 2013, it is targeted to complete most of the ongoing studies on secondary legislation by the end of 2013.
- With secondary legislation, conditions were laid down with regard to the classification of financial services in line with the EU acquis and providing flexibility in the organization of financial intermediaries to ensure that client needs are better met; regulations with regard to rating, auditing and financial reporting were amended; principles were set on investment services, institutional investors, implementation of corporate governance principles, public disclosure, dematerialization of securities, capital requirements of intermediary institutions, exchanges and market operators, investor compensation center, central clearing agencies and central counterparties as well as the setting up of Takasbank as a central counterparty.

- Borsa İstanbul was established as a joint stock corporation and the merger of the Futures and Options Exchange (VOB) with the Futures and Options Market (VIOB) of Borsa İstanbul was competed. Furthermore, İstanbul Gold Exchange has continued its operations under the Precious Metals and Diamonds Market of Borsa İstanbul.
- The CML lays down the legal infrastructure with regard to central counterparty applications and provides legal ground for the use of central counterparties for transactions conducted in both organized and over the counter markets. The use of a central counterparty has initially been allowed for the stock lending market operated by Takasbank.
- The Investor Compensation Centre, replacing the existing Investor Protection Fund, was established and related legal infrastructure was laid down in order to meet claims arising from the failure of cash payment or security delivery obligations owed by banks or intermediary institutions to clients in relation to investment services and activities or ancillary services. Under the CML the scope of payments from the Investor Compensation was extended to cover receivables due to all capital market instruments as well as cash and shares and the maximum compensation amount was raised to 100,000 TL.
- With the purpose of meeting the growing needs of the debt instruments market, which has been growing rapidly in recent periods, regulations in relation to the issues of shares, real estate certificates, warrants and investment firm warrants entered into force, and prospectus regulations were updated considering problems related to implementation as well as regulatory harmonization in the EU candidacy process.
- With respect to cooperation with foreign regulatory and supervisory authorities a memorandum of understanding has been concluded with the Turkmenistan Ministry of Finance. Furthermore a memorandum of understanding with respect to information sharing on the supervision of alternative investment funds was concluded between the CMB and securities regulators of 16 European countries.
- Five internationally regulated forms of Sukuk (lease certificate) were regulated in June 2013. Furthermore in the context of the new regulations on private pensions, pension funds that invest exclusively in interest-free products and also with the investment fund regulation published in June 2013 “Participation Funds” investing exclusively in interest-free instruments were introduced to the markets.
- CMB has prepared a draft national strategy and an action plan regarding financial literacy and presented it to the FSC. Furthermore with the purpose of contributing to capital market development, studies have been carried out on financial inclusion and financial training in the context of the “Capital Market Institutions Investor Mobilization Cooperation Protocol” that had been signed among related institutions.

The list of actions to be carried out in the period of 2014-2016 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:

- Relevant activities will be conducted in order to conclude prospectus equivalency studies being carried out with the European Securities and Markets Authority (ESMA) with the purpose of facilitating securities issues in European Union countries for issuers and to get the approval of ESMA on the equivalency of Turkish prospectus standards with the EU.
- Regulations currently being drafted in line with the Capital Markets Law with respect to investment companies with variable capital are planned to be put into force in 2014.
- The “Implementing Principles Guideline for Investment Fund Legislation” is planned to be prepared and put into effect in 2014.

- The legal infrastructure to enable the trading of investment fund shares in a central fund distribution platform has been laid down, and the final stage has been reached in related technical studies. The project is planned to be completed in the first half of 2014.
- Further memoranda of understanding will be concluded and bilateral cooperation opportunities will be explored with foreign regulatory authorities and cooperation with international institutions will be continued.

4.2.3. Insurance Sector

Strengthening Solvency Supervision Project has been started between World Bank and Undersecretariat of Treasury in 2012. The Project is planned to be finished by 2014 and a pilot study is planned to take place afterwards. The Project covers studies related to redesigning or an early warning system, developing new risk evaluation methods, designing stress/scenario testing mechanisms, integrating Solvency II's capital adequacy calculation methods into Turkish Insurance Sector and developing a legal framework on group basis supervision. After the pilot study in 2014, the outcomes of the Project is planned to be applied to the insurance sector in Turkey in 2015 or in 2016.

In order to develop insurance awareness, workings on the subjects of insurance promotion and awareness programs have been carried out by using written and visual means of communication. National Insurance Symposium: "Motor Insurance" was organized during the "National Insurance Week" that took place between May 27 and June 2, 2013. During this week, awareness programs for various parties (traders, craftsmen, industrialists and university students) are organized to improve public awareness on insurance throughout Turkey with the help of all stakeholders in insurance sector. In the last quarter of 2013, a media strategy has been prepared and informative spots/programs in the local TV channels and radios will be broadcasted in the near future.

4.3. Labor Market

Within the framework of jobs focused sustainable growth, 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 programs are the main priorities.

As of 31 December 2012, 56.8 million people out of a total population of 75.6 million are at working age in Turkey. While the share of 0-14 age group within the total population is decreasing, the share of working age population and elderly population is increasing.

The positive impacts of both rapid GDP growth and the measures aiming to improve employment and working life continued in 2012. According to Household Labor Force Survey, labor force participation rate increased to 50 percent in 2012, and reached the highest level since 2002. In 2012, employment growth rate, which was 2.9 percent, was higher than the GDP growth rate.

Unemployment rate that ascended 14 percent due to the impacts of the global crisis emerged during the last period of 2008 decreased to below the pre-crisis level in 2012 with 9.2 percent of unemployment rate. As of August 2013, seasonally adjusted unemployment rate realized as 10.1 percent. Turkey's performance was very strong among OECD countries in terms of reducing unemployment from the peak level of 2009. Similar positive developments were also observed in non-agricultural unemployment and young unemployment figures as well. Non-agricultural unemployment rate declined from 12.4 percent in 2011 to 11.5 percent in 2012 and young unemployment rate decreased from 18.4 percent to 17.5 percent in the same period. As of August 2013, these rates were realized as 12.3 percent and 18.7 percent, respectively.

In 2012, the population out of labor force increased by 1.9 percent. This increase was mainly due to the increases in the number of pensioners and students. Moreover, the number of people who are ready to work but not looking for job increased by 2.5 percent in 2012.

Table 4.5: Basic Employment and Labor Indicators

(15 + Age, Percent)

	Turkey			EU-28		
	2010	**2011**	**2012**	**2010**	**2011**	**2012**
Labor Force Participation Rate (LFPR)	48.8	49.9	50.0	57.3	57.3	57.6
Female	27.6	28.8	29.5	50.3	50.5	50.9
Male	70.8	71.7	71.0	64.8	64.6	64.7
Employment Rate	43.0	45.0	45.4	51.8	51.8	51.6
Female	24.0	25.6	26.3	45.5	45.6	45.6
Male	62.7	65.1	65.0	58.6	58.5	58.0
Unemployment Rate	11.9	9.8	9.2	9.6	9.4	10.2
Female	13.0	11.3	10.8	9.7	9.7	10.4
Male	11.4	9.2	8.5	9.6	9.2	10.0
Rural	7.3	5.8	5.5	-	-	-
Urban	14.2	11.9	11.1	-	-	-
Youth Unemployment Rate (15-24)	21.7	18.4	17.5	20.3	20.0	21.4
Non-Agricultural Unemployment Rate	14.8	12.4	11.5	-	-	-

Source: TURKSTAT, EUROSTAT, OECD

In Turkey, the total labor force participation and employment rates are lower than the EU averages, but displaying increasing trends. While these rates are close to EU averages for men, they are far below EU average for women. In 2012, female labor force participation rate increased from 50.5 percent to 50.9 percent in EU, and it increased from 28.8 percent to 29.5 percent in Turkey. During the same period, female employment rate increased by 0.7 percentage point in Turkey while it did not change in EU countries. Despite the recent remarkable improvements, female labor force participation rate and employment rate are still lower than the EU level. Through migration from rural to urban areas, women, who were previously employed in agricultural activities in rural areas, cannot participate to the labor force due to the insufficiency of their qualifications for urban jobs. Besides, those women generally working in the informal sectors are paid low wages when they are employed. These facts prevent women from joining to the labor market.

Scrutinizing the employment by sectors, it is observed that the higher number of jobs, respectively, was created in service sector among the non-agricultural sectors. In 2012, the growth rate of value added in industry was 1.9 percent, in construction was 0.6 percent, in services sector was 2.6 percent and in agriculture was 3.1 percent. On the other hand, employment growth was 1 percent in industry, 2 percent in construction and 5.9 percent in services sector, and agricultural employment decreased by 0.7 percent. The shares of agriculture and construction sectors in total employment, which showed an increasing trend since 2007, declined in 2012. On the other hand, share of services sector in total employment increased in 2012.

Table 4.6: Employment Share by Sector

(Percent)

	2011	**2012**
Agriculture	25.5	24.6
Industry	19.5	19.1
Services	48.0	49.4
Construction	7.0	6.9

Source: TURKSTAT, NACE Rev 2.

In line with the improvements in the labor market, informal employment rate was realized as 39 percent in 2012 by 3 percentage points decline, and informality rate in non-agricultural sectors was realized as 24.5 percent in 2012 by a 3.2 percentage points decline.

The main determinants of favorable developments 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. This law includes significant amendments regarding labor market. It provides voluntary right for part time workers to benefit from unemployment insurance. Moreover, the daily amount of short-time working payments and the scope of program were increased. Law No. 6111 allowed green card entitlement to be suspended, instead of being abolished, when green card holders attend labor market training programs financed by public resources. It is also enabled that under certain conditions, employers' social security contributions for new employees, hired in addition to existing number of employees, are paid from Unemployment Insurance Fund for 6 to 48 months until 2015.

Table 4.7: Trends in Gross Schooling Rates

(Percent)

	2010-2011	2011-2012	2012-2013
Pre-School (1)	45.3	46.4	44.0
Primary Education (2)	107.6	108.4	107.6
Secondary Education (2,3)	89.7	92.6	96.8
Standard High Schools	50.6	51.9	52.8
Vocational-Technical High Schools	39.1	40.7	43.9
Higher Education Total (4)	72.5	81.6	92.1
Formal	38.2	42.9	47.6

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

Although labor productivity increased in the recent periods in Turkey, it is still lower than the level of EU countries due to 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 International Labor Organization (ILO) figures, labor productivity, which is calculated as the purchasing power parity adjusted GDP per hour worked, increased from 10 dollars to 24.3 dollars over 2002 and 2012. On the other hand, this figure is 55.9 dollars in France, 46.3 dollars in Italy, 48.4 dollars in Spain, 42.6 dollars in England and 44.8 dollars in Germany as of 2012. Turkey's labor productivity figure was 23.9 dollars in 2011, and Turkey's position receded to 42 in 2012 from 39 in spite of increase in labor productivity.

Occupational Health and Safety Law No. 6331 came into force at 30 June 2012, and preparation of secondary legislation has been continued. For the first time, occupational health and safety issues are covered as a separate law. This law targets all employees in Turkey regardless of working in public or private sector. Moreover, Law No. 6311 was prepared in a precautionary perspective rather than a remedial one.

Considering the fact that labor force participation rate increases 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 is crucial for labor market, increased in the recent years with the reforms especially at the secondary level education.

As of 2012 in Turkey, 61.5 percent of the labor force, 62 percent of the employed people, and 55.9 percent of the unemployed people have less than high school education, or they are illiterate. The mismatch between labor supply and demand resulted from the low productivity and quality level 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 2012

(Percent)

	Labor Force	Employed	Unemployed	Labor Force Participation Rate	Employment Rate	Unemployment Rate
Illiterate	4.3	4.5	1.8	19.7	18.9	3.9
Pre-High School	57.2	57.5	54.1	47.6	43.5	8.7
High Schools	10.4	10.1	13.3	51.9	45.8	11.8
Vocational and Technical High Schools	9.8	9.7	10.8	64.6	58.1	10.1
Higher Education	18.3	18.1	20.0	79.1	71.1	10.1
Total	**100.0**	**100.0**	**100.0**	**50.0**	**45.4**	**9.2**

Source: TURKSTAT

Active labor policies are still important. Goals of these policies are to improve skills of the individuals who have low qualifications and having difficulties for joining the labor market, to create jobs and to train the labor force. 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 1,103 million TL in 2012. In 2013, İŞKUR has spent 704 million TL as of August 2013.

In order for İŞKUR to implement active labor market policies more effectively and efficiently, 3,914 career and occupation counsellors were employed.

In 2012, 464,645 unemployed people received training in 27,351 training courses organized by İŞKUR. Also, 191,998 people were benefited from Public Works Programmes. Entrepreneurship training was provided to 25,475 people for starting up their own business. Besides, 6,272 disabled and 4,483 convict persons and 198 ex-convict unemployed were provided vocational training by İŞKUR.

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	306,366	213,852
2010	392,644	211,627
2011	408,597	250,016
2012	1,102,864	464,645
2013 (1)	703,991	255,990

Source: İŞKUR

*As of 30 August 2013

Progress was observed in terms of job placement for women having problems regarding joining the labor market in 2012. For example, while 101,708 unemployed women registered in İŞKUR were placed in in 2011, this figure increased to 165,608 in 2012. In terms of disabled persons who are another group having problems joining the labor market, 35,351 were placed in jobs in 2012.

Based on the analysis of labor market needs conducted since 2007, there is still need for designing and implementing active labor market programs in accordance with the labor market conditions. Moreover, evaluating the impact of active labor market programs of İŞKUR, especially Public Works Programmes are still essential.

Within the Instrument of Pre-Accession Assistance (IPA), Improving Quality of Public Employment Services, Encouraging Employment of Young People and Women Employment Support Operations, held by İŞKUR during 2008-2013, were completed.

Preparation efforts of National Employment Strategy aiming at improving labor market, decreasing unemployment and enhancing skilled employment have continued under the coordination of Ministry of Labor and Social Security (ÇSGB) with the contribution of relevant partners. This strategy is especially targeting to improve flexicurity perspective in working life.

Domestic and international markets increasingly demand for labor that is creative with high analytical thinking abilities and foreign language skills, and can quickly adapt to new skills while using information technology effectively. Additionally, there is more demand for those who are innovative with strong discernment, and can transform the information to economic/social benefits.

In this context, 12 years of compulsory education system has been established. With the aim of increasing the education quality, curriculum has been prepared and updated in accordance with the contemporary requirements. However, the number and quality of the activities of in-service training for teachers are inadequate, and the efforts for enhancing the number and effectiveness of in-service training are ongoing.

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 technology accession of students and teachers has been 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. In this context, the need of providing the integration of IT to the curriculum and making impact evaluations by developing qualitative and quantitative indicators has been continuing, too.

In order to meet the need of qualified intermediate staff demanded by labor market, it is vital to make effective counseling and guidance within the vocational and technical education. The share of VET in secondary education rose to 45 percent in 2012-2013 academic calendar.

Formation of a programmatic structure rather than a structure based on different types of school is important. In order to establish such a system following approaches are crucial: i) Facilitating transitions between the different educational levels in order to reduce drop outs from the system ii) Compensating students' failures under an understandable and encouraging system. To address this approach in an integrated manner, and to carry out practices within the vocational and technical education, Vocational Education and Training Strategy (2014-2018) are being prepared. Also, efforts to make post-secondary VET more efficient are in progress.

Efforts continue to develop the capacities of Professional Qualifications Agency established to manage the national professional qualifications system. The Professional Qualifications Agency, which is an important part of the national competences system, began to develop the professional standards by considering the needs of labor market and to make certification through 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.

Draft Lifelong Learning Strategy Document 2014-2018, followed by LLL Strategy Document 2009-2013, has been completed. In this context, efforts to disseminate the LLL activities to provinces, recognition of prior learning and raising awareness have been still continuing. The LLL web portal has been established and is currently active.

An effective Monitoring and Evaluation Board established in the context of the "Action Plan for Enhancing the Relation between Employment and Vocational Education (İMEİGEP)", 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, to implement active labor market policies effectively with a perspective of lifelong learning, to increase employability of the labor force by means of overcoming the problems of vocational competence. By considering recent requirements, IMEIGEP has been revised and developments have been monitored in regular periods. With the content of Action Plan, relevant institutions have been continuing to work on secondary legislation process.

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

In addition, in the context of cooperation with private sector, with the amendment of Law No. 5580 Private Education, training aid, no more than 1.5 times the cost of a student in a public schools (by school type), is provided for each student in the vocational and technical schools which is opened in Organized Industrial Zones. This development has become a vital step for enhancing cooperation between public-private sectors.

Flexible working conditions prevalent in EU countries are not practiced very effectively in Turkey. Expanding 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 support 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:

- In order to facilitate women's labor market participation and to harmonize work and family life, regulations that will enable and extend to flexible working forms such as tele-working, telecommuting, job-sharing and flexible working hours model will be made.
- Severance Pay Fund will be established thereby preserving the acquired rights of workers and competiveness of enterprises.
- The Economic and Social Council will be restructured in order to increase the effectiveness 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 effectively, 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 efforts on regulations that enable these agencies to make temporary employment contract will be finalized.
- Sub-contracting will be reviewed by taking into account the acquired rights of workers and problems related to implementation and legislation will be fixed.

Table 4.10: Matrix of Policy Commitments: Labor Market

(1000 Euros)

	2012	2013	2014	2015	2016
1. Encouraging Employment of Young People Operation					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-863	-100	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	863	100	---	---	---
2. Improving Quality of Public Employment Services Operation					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-631	-375	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	631	375	---	---	---
3. The Women Employment Support Operation					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-50	---	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	50	---	---	---	---
Total Net Budgetary Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-1,544	-475	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	1,544	475	---	---	---

4.4. Agriculture Sector

4.4.1. Agriculture

4.4.1.1. Agriculture and Rural Development

The basic objectives of agricultural and food policies are; to ensure food security and safety and to form a sustainable and competitive agricultural structure that is harmonized with the EU. With the Tenth Development Plan, that will be put into effect by 2014, in order to improve food security conditions and to maintain stable growth of agriculture in Turkey the need for new policy implementation; on land fragmentation, effective use of agricultural holdings considering their scales, producer organizations, collection of reliable data on agriculture, product marketing infrastructure, increasing self-sufficiency of production, decreasing unregistered production, maintaining safe food supply and demand, support policies considering product-region-producer and water resources and preventing market fluctuations have been emphasized.

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. In order to increase the benefits of supports to reach a sustainable agricultural structure and considering the technical supports given via EU Financial Cooperation, there are several ongoing projects. However, the number of projects and the financial allocations to these projects has been decreasing in the last few years. In addition, the retention and change in ongoing projects, or delays in grants are seen as important problems considering the use of EU funds.

A total of nearly 9 billion TL (3.6 billion Euros) support budget is allocated in 2013 for agriculture. The share of area-based payments in total support budget is estimated to be 27.1 percent by the end of 2013. Product-based deficiency payments are given to oilseeds, tea, cereals and lentils. The share of deficiency payments in the support is to be 29.7 percent. Livestock supports are implemented on an annual basis since 2008. The share of livestock supports in total support budget is estimated to be 32.5 percent in 2013.

Within the framework of EU harmonization studies, the establishment of Land Parcel Identification System (LPIS), which is the main instrument of Integrated Management and Control System, has been ongoing as part of public investment program.

The share of Supports Program for Rural Development Investments, which is implemented in order to establish institutional capacity for implementation of EU Rural Development Policies, including national co-finance contribution for rural development program in the EU Pre-Accession Financial Instrument, is increased in 2013 at a great extent. While it is essential to consider the complementarity of this program with similar policy implementations within the scope of the EU Financial Cooperation, it is also important to increase the absorption capacity of EU grants for rural development by including rural infrastructure investments.

In this context, taking into consideration the requirements of EU accession process; the ultimate goal will be the preparation of a support strategy with a schedule that would enhance predictability, leading a subsidy system based on registered agricultural holdings with the capability of area-based administration and control and, hence, ensuring efficiency and quality improvement through registration that will enable structural transformation in animal husbandry and transforming livestock to pure culture breed.

The activities in order to eliminate problems related to the quality and reliability of agricultural statistical data and to improve information infrastructure and administrative structure are programmed in a way to obtain technical support in the scope of the EU Financial Cooperation. In this framework, having an ultimate goal of Farm Registration System; Farm Accounting Data Network is programmed to be established for monitoring the development of agricultural enterprises and contributing to policy making process, projects related to establishing Land Parcel Identification System and improvement of statistical capacity of the Ministry of Food, Agriculture and Livestock have being implemented.

4.4.1.2. Food Safety, Veterinary and Phytosanitary

The Law No. 5996 on Veterinary Services, Plant Health, Food and Feed was issued in June 2010 in order to ensure compliance to the EU in the fields of food, feed, food hygiene, phytosanitary and veterinary services. Along with the issuance of the Law, criteria of Chapter 12 titled Food Safety, Veterinary and Phytosanitary were completed and this Chapter was opened.

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 efforts.

Compliance of animal originated food processing enterprises to EU food legislation is primarily considered within the framework of Law No. 5996 and secondary legislation. The upgrading of food enterprises in accordance with their modernization plans have being implemented since 2012. After the assessment of the results of this implementation in 2014, new measures would be put into force.

For the enhancement of organic farming at the national level, a strategy and an action plan have been prepared and put into action in 2013 by the Ministry of Food, Agriculture and Livestock.

In the field of pythosanitary, the registration of plant protection products including imported ones, the reinforcement of the infrastructure for the current monitoring and control system used to detect biological impacts of registered products, raising awareness of the producers and extending early warning systems are some of the priority areas.

In addition to the cattle identification system, Tagging and Vaccination of Sheep and Goats Project was started in 2009 by using the EU grants for identification of sheep and goats, second phases of Rabies Control Project and Foot and Mouth Disease Control Project were launched in 2011. The work related to these projects is still in progress. However, “Control of Foot and Mouth Disease - 2nd Phase” project that was envisaged to be implemented all over the country was limited to only the Thrace Region by an arrangement made in 2012 and budget re-allocation studies are ongoing. Besides, Restructuring of Border Inspection Posts Project is completed by the end of

2013. Furthermore, by the use of national budget the physical infrastructure investments of 14 Border Inspection Posts have been planned to be finalized in 2014.

In 2014, Veterinary Strategy Document and Animal By-Products Strategy Document will also be prepared and a project on Electronic Tagging and Registration of Sheep and Goats will be started.

4.4.1.3. Fisheries

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, the work and investments 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.

A 1 million Euro project namely, Capacity Building Project for the Fishery Products Producer Organizations will be started in 2014 using EU funds.

Table 4.11: Matrix of Policy Commitments: Agriculture (Important Projects in Agriculture)(1)

(1000 Euros)

	2012	2013	2014	2015	2016
1. Controlling of Rabies Project (2)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	360	28	0	0	0
B.1. Direct Effect on Budgetary Revenues	443	50	0	0	0
B.2. Direct Effect on Budgetary Expenditures	83	22	0	0	0
2. Tagging and Vaccination of Sheep and Goats					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	0	0	10,000	13,700	0
B.1. Direct Effect on Budgetary Revenues	0	0	12,000	16,900	0
B.2. Direct Effect on Budgetary Expenditures	0	0	2,000	3,200	0
3. Land Parcel Identification System					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	0	0	9,366	6,121	15,179
B.1. Direct Effect on Budgetary Revenues	0	0	11,373	7,433	18,432
B.2. Direct Effect on Budgetary Expenditures	0	0	2,007	1,312	3,253
4. Controlling of FMD (2)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	8,917	1,080	2,007	0	0
B.1. Direct Effect on Budgetary Revenues	10,874	1,124	2,222	0	0
B.2. Direct Effect on Budgetary Expenditures	1,957	44	215	0	0
5. Veterinary Strategy Document					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	0	0	800	1,120	0
B.1. Direct Effect on Budgetary Revenues	0	0	900	1,260	0
B.2. Direct Effect on Budgetary Expenditures	0	0	100	140	0
6. Animal By-products Strategy Document					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	0	0	225	0	0
B.1. Direct Effect on Budgetary Revenues	0	0	238	0	0
B.2. Direct Effect on Budgetary Expenditures	0	0	13	0	0
7. Capacity Building Project for the Fishery Products Producer Organizations					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	0	0	940	0	0
B.1. Direct Effect on Budgetary Revenues	0	0	1.000	0	0
B.2. Direct Effect on Budgetary Expenditures	0	0	60	0	0
Total Net Effect on Budget					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	9,277	1,108	23,338	20,941	15,179
B.1. Direct Effect on Budgetary Revenues	11,317	1,174	27,733	25,593	18,432
B.2. Direct Effect on Budgetary Expenditures	2,040	66	4,395	4,652	3,253

(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 Tenth Development Plan period (2014-2018), the main objective is to achieve a more manageable structure for rural policies. For this purpose, both the governance and institutionalization processes will be strengthened regarding to the rural policy design and implementation at central and local level. The key instrument of this objective is the monitoring committee which was composed during the Ninth Development Plan by the Prime Ministry's circular. The committee is obliged to finalize the road map for drafting the policy documents of the Plan period.

According to the figures of 2012, Turkey is a country that 28 percent of its population lives in rural areas and 25 percent of total employment is in agricultural sector. For this reason, apart from the investments and services delivered to rural areas by the line ministries and local administrations, project support to improve rural economy also compose the significant part of the public expenditures for rural areas in recent years.

Agriculture and rural development grant scheme programs, which are executed with co-financing contribution of beneficiaries are implemented by different public agencies. In this context, the leading financial instruments are Rural Development Investment Support Program implemented by the Ministry of Food Agriculture and Livestock and IPARD Program implemented by the Agriculture and Rural Development Support Institution (ARDSI); at the regional level development agencies also support agriculture and rural development. The coordination and complementarity among these programs are monitored and organized by the related public agencies both at central and local level to help increase their contributions to the national goals.

In 2013, the European Commission has granted the conferral of management decision to 22 additional provinces (to 6 provinces with conditions) within the context of second implementation phase of IPARD Program. Thus, the IPARD Program implementation is in progress in 42 provinces of Turkey in total. As of the end of October 2013, a total of 11 calls for projects have started and 10 of them have been finalized. Contracting process for the 9th, 10th calls and project application process for 11th call currently proceed. 3381 project applications have been received in the first 10 calls and up to now grant contracts have been awarded for 1792 winning projects, which cover support for about 616 million TL.

Within KÖYDES Project, rural infrastructure projects of local administrations in 79 provinces are still being supported. In 2012, 550 million TL allocated to the Project and the outputs with approximate figures are; 3,000 km stabilized roads, 5,750 km asphalted roads and 166 km concrete roads were constructed; 5,850 km roads were repaired; 1.6 million square meter roads were paved with stones. Moreover, 3,160 village drinking water and 23 village waste water projects were implemented and 900 hectare agricultural land was irrigated. In 2013, nearly 890 million TL was allocated to the Project.

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 ministries were completed and 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 Programs of 2008 and 2009 upon the Decision of the Council of Ministers. Within this scope, 14 SEEs completed their strategic plans as of November 2013 and works are in progress in the remaining four.

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 2014 in order to overcome the problems encountered and to enable the system function more effectively.

The IPA project titled as Improved Strategic Management Capacity for Central Administrations has started in 22 January 2013. The overall aims of the project are to improve the efficiency and effectiveness in public services and to ensure a transparent and robust financial management. To these ends, the project aims at building effective strategic management capacity in central public administrations. Main beneficiary of the project is the Ministry of Development. General Directorate of Local Authorities within the Ministry of Interior, General Directorate of Budget and Fiscal Control within the Ministry of Finance and The Council of Higher Education are the co-beneficiaries of the project. 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.

In accordance to the Law No. 5018, within in the context of central harmonization function, related with performance based budgeting carried out by the Ministry of Finance; it is aimed to make the system more effective in preparation, implementation, monitoring and evaluation of performance programs.

In this regard, in the process of monitoring and assessing the performance programs of the public administrations within the central government, 102 performance programs sent to Ministry of Finance in 2012 administrations were analyzed and assessed in line with defined fundamental principles by using the Performance Budget Module included in the e-budget system. The assessments were shared with the administrations in order to improve the quality of the performance programs to be prepared in coming years.

On the other hand, in the light of experiences gained, in order to enhance performance-based budgeting system, efforts for the transition to a performance based budgeting system that will concentrate on the quantity and quality of the services offered to the citizens and strengthen the accountability of the public administrations against the parliament and public about the outputs and outcomes are carried on along with the public supply used in budget request, negotiation and allocation processes. These efforts aim to develop and implement a new budgeting model that will enable to;

- Revise the current budgeting classification so that it will include a program classification showing the outputs and outcomes of public services and
- Strengthen the integration of performance information to the budgeting processes.

4.5.2. The Law on Consumer Protection

Consumer movement has gained additional momentum with the Law on Consumer Protection enacted in 1995 and with the extensive changes made in 2003. In order to ensure full compliance of these arrangements with the European Union (EU) legislation, the Law on Consumer Protection No. 6502 came into force on 28 November 2013.

The law defines the rights for consumers and sanctions for the firms, which disobeys the rules in many different areas such as the contracts related with credit cards, card membership fees, and mortgage contracts with down payment, return policy for defective goods, subscription agreements, and advertisements. Also with the Law, various EU Directives and EU Recommendations related with consumer rights was harmonized to the national law.

4.6. Other Reform Areas

4.6.1. Regional Development

Regional development policy is covered under the heading Livable Cities, Sustainable Environment in the Tenth Development Plan (2014-2018) of Turkey. The Tenth Development Plan reserves main objectives which have guided regional policy in the Ninth Development Plan period and develops a more substantial and focused policy framework on the realization of these objectives. Main objectives of the regional policy follow:

- Disseminating welfare across the country in a balanced way by reducing regional development disparities,
- Increasing regions' contribution to national growth and development by mobilizing regional potential and increasing regional competitiveness,
- Directing inter-regional migration propensity towards intra-region to support balanced spatial distribution of the population,
- Establishing a healthy urbanization structure,
- Reducing socio-economic development disparities between urban and rural areas by strengthening rural-urban linkages and enhancing welfare in rural areas,
- Making central-level policies more compatible and effective,
- Increasing institutional capacity at local level.

Regional Development Supreme Council is the superior decision-making body with regard to regional development issues. Chaired by Prime Minister, it has been established to strengthen governance by ensuring compliance and coordination of regional development policies with other central level policies in decision making, programming, implementation and monitoring. A Regional Development Committee has also been established to analyze regional development policies at technical level and to develop suggestions for the Council. Committee is composed of high level representatives of the ministries of the Council.

Preparatory 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. Strategy document has been drafted in cooperation with relevant stakeholders and consultations with the stakeholders are continuing. In addition, in all NUTS 2 level regions, regional development plans to cover 2014-2023 period have also been drafted under the coordination of development agencies.

The Research on Socio-Economic Development Ranking of Provinces and Regions (SEDI-2011) was completed; this research constituted the base for the regional supports under the new Support Scheme announced in 2012; and the technical report of the research was released in 2013.

Regional Development Administrations for Eastern Anatolia Project (DAP), Konya Plain Project (KOP) and Eastern Black Sea Project (DOKAP), were established in 2011, respectively. Having concentrated on institutionalization, these administrations are primarily preparing action plans in order to expedite public investments and strengthen coordination in the implementation process.

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 2013. Pilot application of the programme has been commenced in Diyarbakır in 2008. The total fund allocated for Diyarbakır is 68.65 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 38.49 million TL to Van in 2010 and 2011. Budget of the programme for 2012 is 80 million TL and 25 million TL of this amount was transferred to Erzurum. Budget of the programme for 2013 is 84 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, 2012 and 2013; 3 billion TL, nearly 4 billion TL, 4.3 billion TL, 4.2 billion TL and 5.2 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 Action Plan, 18.2 billion TL was transferred for more than 300 projects and activities and 14.7 billion of these resources have been used in the period of 2008-2012. Although the activities that were planned to be realized in this period were initiated or completed to a large extent, the action plan has been revised in order to accomplish the incomplete activities and to strengthen the development momentum gained. With the revised action plan, it is aimed to realize policies to facilitate economic and social development through more advanced infrastructure and institutional capacity with such activities applying modern irrigation techniques, enhancing the transportation and housing infrastructure, transition to generating competitive products, enlarging marketing opportunities, improving the capacities of human resources and institutions and improving natural and cultural configuration.

Development agencies are basic building blocks of new regional development policy. Agencies have focused on institutional capacity building, and awareness raising activities. The agencies have also worked on articulating determining development strategies and defining priority areas of the region and providing financial support for the projects in these areas. In addition, the agencies provide direct activity and technical support in the regions. Consolidated data for the financial support is shown in Table 4.12.

Table 4.12: Information on Financial Supports Provided by Development Agencies)

(Million TL)

Type of Financial Support	Year	Grant Amount	Project Budget (including co-financing)	Project Application	Supported Project
Direct Financial Support	2008-2012(1)	1,572	2,806	27,202	5,823
	2013-Oct.(2)	34	---	78	---
Direct Activity Support	2008-2013	42.3	47.2	2,708	908
Technical Support	2008-2013	16	16	4,037	2,557
Total	---	1,664.3	2,869.2	35,184	9,288

(1) Including call for proposals of 2013 which were announced in 2012.
(2) These amounts are announced by two development agencies, process is still ongoing.

As of November 2013, totally 947 personnel are recruited, including 756 specialists and 156 officers in the development agencies.

Table 4.13: Number of Staff in Development Agencies

(1000 Euros)

Year	General Secretary	Internal Audit	Specialist	Officer	TOTAL
2013*	23	12	756	156	947

*As of November 2013.

Project and Activity Support module in Development Agencies Management System (DAMS) developed as including monitoring processes and was brought into the use of development agencies in March 2013. Software development works are continued for other modules. Electronic Documentation and Archive Management System under DAMS were set up in all 26 agencies in November 2013. Studies to develop a system infrastructure for making electronic correspondence between the Ministry, agencies and the regional development administrations are continuing.

The technical assistance project which was implemented 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, namely Capacity Improvement in Economic and Social Cohesion Policy (ESC-II), was completed as of November 2013. Within the context of the project, capacity building activities for the institutional actors involved in the implementation of components III and IV of IPA and preparations for Structural Funds were undertaken. Furthermore, works to increase the role of development agencies in using the funds under EU financial cooperation are still ongoing.

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 8,000 users of the system in 81 provinces. Additional system development, maintenance and support activities are ongoing.

Table 4.14: Matrix of Policy Commitments: Regional Development

(1000 Euros)

	2012	2013	2014	2015	2016
1. GAP Action Plan					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-1,882,125	-2,075,351	-2,851,602	-3,318,094	-2,786,908
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	1,882,125	2,075,351	2,851,602	3,318,094	2,786,908
2. Development Agencies					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-181,261	-188,757	-184,533	-183,622	-182,616
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	181,261	188,757	184,533	183,622	182,616
3. KÖYDES					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-238,611	-350,415	-131,553	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	238,611	350,415	131,553	---	---
4. Regional Development Administrations (DAP-KOP-DOKAP)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	-57,948	-53,684	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	57,948	53,684	---	---
5. SODES					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-89,804	-82,614	-83,647	-85,164	-86,822
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	89,804	82,614	83,647	85,164	86,822
Total Net Effect on Budget					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-2,391,801	-2,755,085	-3,305,019	-3,586,880	-3,056,346
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	2,391,801	2,755,085	3,305,019	3,586,880	3,056,346

4.6.2. Health and Social Security Reform

4.6.2.1. Health Transformation Program

The first part of Health Transformation Project was completed in 2009 and carried out with World Bank in order to support the Health Transition Programme, which has implemented since 2004. 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 2015.

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 2 November 2011. Aiming to carry on works related to primary health care services, prevention and control programs for communicable diseases and non-communicable diseases, consumer and 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 diseases, 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. Moreover National Rational Drug Use Action Plan 2013-2017 was prepared in order to create awareness about rational use of drugs and ensure coordination and cooperation of activities that will be carried out. In this context, Prescription Information System that ensures monitoring and evaluation of prescriptions has been created and encompassed all physicians. 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.

Having reached 346 thousand patients so far within the scope of home health care services application, currently 80 thousand patients are under active follow-up. Within the scope of this application it has been aimed that 0.2 percent of the provincial population will be reached in 81 provinces. The provinces have reached this rate during the year and the sustainability of the service is expected to continue.

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 2012. 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.

While the ratio of public health expenditure to GDP was 3.7 percent in 2002, it was 4.4 percent 2012 and this ratio is expected to be 4.5 percent in 2013.

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.

People under the coverage of Green Card system that is allowing the citizens not having power to pay to benefit from health services have been taken under the scope of General Health Insurance from the beginning of the year 2012. Premiums' of people whose monthly income is under the one third of the gross minimum wage have been started to be paid by the government. For the current situation, nearly the whole population is under the coverage of General Health Insurance.

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

(1000 Euros)

	2012	2013	2014	2015	2016
1. Health Transformation and Social Security Reform Project					
A. Implementation Profile	---	---	---	---	---
B. Net Effect On Budget	95,900	---	---	---	---
B.1. Direct Effect on Budgetary Revenues	100,000	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	4,100	---	---	---	---
Total Net Budgetary Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Effect On Budget	95,900	---	---	---	---
B.1. Direct Effect on Budgetary Revenues	100,000	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	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 0.92 percent in 2012. However, the EU-27 average was 2.03 percent in 2011. It is aimed to increase this ratio to 1.8 percent in Turkey in 2018.

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 45.1 percent in 2012. However, considering that this rate is below the EU-27 average of 62.3 percent in 2011, 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 2013, 52 TDZs have been established, and 37 of them are operational. Investments are being done for the establishment and operation of the inactive TDZ's. The number of the companies operating in the Technology Development Zones rose to 2,247 as the same year.

Dated on 28 February 2008 and No. 5746 under the Law on Supporting Research and Development Activities as of September 2013, 142 of the company's R&D Center is located R&D Centre Certificates. The amount of total R&D expenditure in these businesses between the years 2008-2012 is 7.3 billion TL. They are employed 15,686 R&D personnel in 2013.

Another issue as important as enhancement of the resources 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 49.7 percent in 2012. At the same time, this ratio was 52 percent for EU-27 countries as of 2011.

A road map for the development of research infrastructure will be done, legislation to increase the effectiveness of research infrastructure will be completed and performance monitoring and evaluation system will be established. Technological products and brands for the detection in priority sectors' commercialization activities will be supported, the existing support programs' impact analysis will be revised and clean technologies and high value-added green products for growing R&D and innovation activities will be supported.

Quality and quantity of researcher manpower will be increased in order to encourage the qualified researchers working in foreign countries necessary arrangements will be prepared. Public procurement system will be improved to encourage innovation, domestication, environmental awareness, technology transfer and innovative entrepreneurship. The transfer of critical technologies to facilitate, internalization and improving to compete with the world peer technology will be emphasized.

In line with enhancing scientific and technologic cooperation with the EU countries and being 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 and The European Research Infrastructure Consortium (ERIC) is underway for participation.

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 renewal of Information Society Strategy 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 is expected to provide 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 2013, the ratio of individuals using the internet in the last three months is 48.9 percent, and 41.3 percent of those use the internet to interact with public agencies. According to the ICT Usage in Enterprises Survey published by TURKSTAT in November 2013, ratio of the enterprises that have internet access was 90.8 percent while ratio using the internet to interact with the public agencies was 73.7 percent among these enterprises.

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, while 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 September 2013, the total number of produced qualified electronic certificates is 992,215. 292,084 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 September 2013, the total number of active electronic certificates used in these applications is 510,044. 482,219 of these are traditional electronic certificates and 27,825 are mobile electronic certificates. The number of active mobile electronic certificate, which was 71,097 in October 2012, decreased to 27,825 in September 2013.

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. As of November 2013 three REM service providers was authorized. 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 REM is used actively in Turkey. e-Correspondence Project, which is conducted to ensure secure official correspondences among Public organizations in electronic environment, is also planned to be used as a platform for REM

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 GNAT.

Within the scope of the efforts carried out in the area of cybercrimes, Turkey signed the Cyber Crime Convention of European Council No. 185 on 10 November 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 20 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. National Cyber Security and 2013-2014 Action Plan was published and became effective on 20 June 2012, Official Gazette No. 28683.

ECL 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. ICTA has outsourced the deployment of IT infrastructure. The new system named TRABİS will be active when re-delegation process is completed.

As of September 2013, fixed telephone, mobile telephone and broadband subscriber penetration rates are 18.1 percent, 91.1 percent and 44.6 percent in Turkey, respectively. At the same date, the number of subscribers using broadband service over fiber optic connections was 967 thousand. As of the end of September 2013, the number of 3G subscribers reached 47.5 million and the number of subscribers using mobile broadband access services reached more than 25.5 million. As of November 2013, 801 authorizations were granted for 502 operators[2].

The effectiveness of alternative infrastructure operators in the market and coverage of their fiber optic networks have been increasing lately. The length of fiber optic cables these operators own reached 44,725 km in September 2013, while this figure was 9,216 km at the end of 2008. Within the scope of mobile number portability, 62.5 million subscribers ported their numbers as of November 2013. This number is 502 thousand for fixed telephone numbers.

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 Acquits, the Law No. 6112 Broadcast Services and Organizations of Radio and Televisions were entered into force after being published on the Official Gazette on 3 March 2011.

Law No. 6475, the Postal Services Law which initiated liberalization process and separated policy designation, regulation and operation functions in the postal sector entered into force on 23 May 2013 by being published at the Official Gazette. By the same Law, Information and Communications Technologies Authority were assigned as the regulator of the postal sector. Moreover, Post and Telegraph Organization was restructured as a joint stock company operating subject to Turkish Commercial Code.

[2] The number of mobile broadband subscribers has been updated for 2009-2013 period considering the number of subscribers accessing the internet that use short-term package and use no packages.

4.6.5. Transportation

Turkish Rail Transport Liberalization Law providing liberalization of the railway sector published in Official Journal No. 28634 dated 1 May 2013 and was put into force. 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 120 until the year 2018.

For withdrawal of the vehicles which have completed their life economically and technically, 103,765 old vehicles in total have been withdrawn from the market as of 28 October 2013 in line with the issued communiques.

EU technical support project “weight and dimension controls of the commercial vehicles” consist of supply and service components. Service component of the Project, which started on 16 April 2012, finished and the reports have been preparing. Supply component of the project started in 28 June 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 in 1 January 2014. By the decree Law No. 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.

The study entitled “General Analysis of Air Transport” will be commenced in 2014.

Table 4.16: Matrix of Policy Commitments: Transportation

(1000 Euros)

	2012	2013	2014	2015	2016
1. Transport Operational Programme (1)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-13,350	-10,870	-11,714	-4,945	-4,714
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	13,350	10,870	11,714	4,945	4,714
Total Net Budget Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-13,350	-10,870	-11,714	-4,945	-4,714
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	13,350	10,870	11,714	4,945	4,714

(1)Indicative amounts for Köseköy-Gebze and Irmak-Karabük-Zonguldak Railway Rehabilitation and Signalization 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 with the EU energy legislation. In this context, fundamental sectorial laws were completed at great extent and efforts for establishing a fully competitive energy market are continuing.

Turkey has carried out the synchronous-parallel trial operation with Association of European Electricity Transmission System Operators (ENTSO-E) Continental Europe Synchronous Area (CESA) since 18 September 2010.

A significant portion of domestic natural gas transmission lines was been completed and access to natural gas was realized for the fundamental consumption areas. As of 2013, as a result of investments for 12,290 km of transmission lines, 72 of 81 provinces had access to natural gas and in 65 of them residential use was commenced. Until the end of 2016, it is planned to complete gas supply transmission for residential use in all provinces.

The studies on the draft Law on Natural Gas Market which is important in terms of the liberalization of the natural gas market, consisting of a new regulation restructuring of the market activities and considering public sector in the supply side of the market, continue.

Turkey acknowledges the enhancing of energy efficiency as an important topic. In this regard, Tenth Development Plan which has been approved by Parliament in 1 July 2013 includes "Program for Improving the Energy Efficiency". Improvement of energy efficiency in industry, transportation and buildings and development of financial mechanisms and institutional capacity in the field of energy efficiency are included in the components of this program.

By means of the Regulation on Increasing Efficiency in Energy Resources and Energy Usage, the efficiency increasing project and voluntary agreement models were put into force in order to support the works for energy efficiency to be made in the industry. In 2013, it was decided to support 59 efficiency increasing projects of 27 companies.

Table 4.17: Legal Regulations Realized in Energy Market in 2013

Date	No	Name	Explanation
14 March 2013	Official Gazette No. 28603	Electricity Market Law	The purpose of this Law is to ensure the development of a financially sound and transparent electricity market operating in a competitive environment under provisions of civil law and the delivery of sufficient, good quality, low cost and environment-friendly electricity to consumers and to ensure the autonomous regulation and supervision of this market.
30 May 2013	Official Gazette No. 28674	Turkish Petroleum Law	The purpose of the Law is to ensure the exploration, development and production petroleum resources in the Republic of Turkey in accordance with national interests in a speed, continuous and effective way.

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. As of September 2013 share of renewable resources in total electricity generation is around 30 percent.

After completing legal and technical arrangements for the generation of electricity from solar energy EMRA accepted license applications between 10 and 14 June 2013.

The works for allowing usage of nuclear energy for the purpose of electricity generation have been continued in 2013. The project company has applied for Environmental Impact Assessment report to constructing a nuclear power plant (NPP) in Mersin-Akkuyu with a total installed power of 4,800 mw and the process continues. Also, field study works have been initiated for the establishment of second NPP in Sinop and an agreement was signed with the Japanese Government for the installation of NPP whose power is 4,480 mw. In the coming period, it is aimed to start field identification, pre-feasibility studies and investment preparations of third NPP whose power is 5,000 mw.

Within the framework of the reforms in energy sector, there are some projects to be carrying and carried out in the next period in the context of EU Pre-Accession Financial Assistance Program:

- The Project of Improving the Structure and Capacity of TEİAŞ: This Project proposed by TEİAŞ within the scope of Instrument for Pre-Accession Assistance (IPA-1) was approved by the EU and it was started at the end of 2012. Project has 24 months of implementation duration and budget of 2 million Euros. With the project it is aimed that establishment and operation of live care system, improving the performance of occupational safety and training, developing human resources policies and rules, renovation information processing structure and organizational structure of TEİAŞ.
- The Project of Adaptation of Grid Regulation with ENTSO-E Legislation: The project proposed by TEİAŞ within the scope of Pre-Accession Financial Assistance Programming-2010 was approved by the European Commission. Total budget of the project is 1.5 million Euros and its part to be covered by national co-financing amounts 150,000 Euros, corresponding to 10 percent of this budget. The project is expected to commence actually in 2013.

ANNEX TABLES

Table 1.a: Macroeconomic Prospects

	ESA Code	2012	2012	2013	2014	2015	2016
		Level (Mil. TL)	Rate of Change				
1. Real GDP, at 1998 prices	B 1 * g	117,675	2.2	3.6	4.0	5.0	5.0
2. GDP, at current prices	B 1 * g	1,415,786	9.1	10.1	10.2	10.3	10.6
Components of Real GDP (1998 Prices, Percentage Change)							
3. Private Consumption Expenditure	P3	78,357	-0.6	3.9	3.2	3.8	3.5
4. Public Consumption Expenditure	P3	12,583	6.1	7.8	3.0	3.3	4.2
5. Gross Fixed Capital Formation	P51	29,012	-2.7	2.4	3.9	8.6	8.3
6. Changes in Inventories and Net Acquisition of Valuables*	P52+P53	-1,643	-1.4	1.1	-0.1	0.0	0.1
7. Exports of Goods and Services	P6	32,105	16.7	0.5	6.8	7.2	7.7
8. Imports of Goods and Services	P7	32,739	-0.3	6.1	3.6	7.0	7.1
Contribution to Real GDP Growth (Percentage Point)							
9. Final Domestic Demand	---	---	-0.5	4.0	3.4	5.0	4.9
10. Changes in Inventories and Net Acquisition of Valuables	P52+P53	---	-1.4	1.1	-0.1	0.0	0.1
11. External Balance on Goods and Services	B11	---	4.1	-1.6	0.8	0.0	0.1

* Contribution to growth

Table 1.b: Price Developments

Percentage Changes, Annual Averages	ESA Code	2012	2013	2014	2015	2016
1. GDP Deflator	---	6.8	6.3	6.0	5.0	5.3
2. CPI	---	8.9	7.5	5.4	5.2	5.0

Table 1.c: Labor Market Developments

	ESA Code	2012	2012	2013	2014	2015	2016
		Level	Rate of Change, Percent				
1. Employment, persons (Thousand)*	---	24,821	2.9	3.5	2.2	2.5	2.3
2. Unemployment Rate (ILO Definition)	---	2,518	9.2	9.5	9.4	9.2	8.9
3. Labor Productivity Growth	---	---	-0.8	0.1	1.8	2.5	2.6
4. Compensation of Employees	---	---	---	---	---	---	---

*****+15 years-old

Table 1.d: Balance of Payments

Percentages of GDP	ESA Code	2012	2013	2014	2015	2016
1. Current Account	---	-6.1	-7.1	-6.4	-5.9	-5.5
- Balance of Goods	---	-8.3	-9.3	-8.5	-8.0	-7.8
- Balance of Services	---	2.9	3.0	3.0	3.0	3.1
- Balance of Incomes	---	-0.9	-1.0	-1.0	-1.0	-0.9
- Balance of Current Transfer	---	0.2	0.1	0.1	0.1	0.1
2. Capital and Financial Account (Including Reserves)	---	6.0	6.5	6.4	5.9	5.5
Statistical Discrepancy	---	0.1	0.6	0.0	0.0	0.0

Source: Realization CBRT, forecast Ministry of Development

Table 2: General Government Budgetary Prospects

	ESA Code	2012	2013	2014	2015	2016
Net Lending(B9) by sub-sectors*						
1. General Government	S13	1.0	1.0	1.1	0.8	0.5
2. Central Government	S1311	0.5	0.3	1.0	0.7	0.4
3. Funds	S1311	-0.5	-0.2	-0.5	-0.3	-0.3
4. Local Administration	S1313	0.2	0.3	0.1	0.1	0.3
5. Social Security Fund	S1314	1.6	1.3	1.3	1.0	0.8
6. Revolving Funds	S1311	-0.1	-0.2	-0.1	-0.1	-0.1
7. Unemployment Fund	---	-0.6	-0.6	-0.6	-0.6	-0.6
General Government (S13)						
8. Total Receipts	TR	37.8	39.7	38.4	38.1	37.7
9. Total Expenditures	TE	38.9	40.8	39.6	39.0	38.2
10. Net Lending	EDP.B9	1.0	1.0	1.1	0.8	0.5
11. Interest Payments	EDP. D41+FISIM	3.5	3.4	3.1	2.9	2.5
12. Primary Balance	---	2.5	2.3	2.0	2.1	2.0
Components of Revenues						
13. Taxes	---	20.2	21.4	20.9	20.8	20.5
14. Social Funds	D61	9.4	10.1	10.2	10.2	10.2
15. Factor Incomes	D4	5.7	5.7	4.9	4.7	4.6
16. Other	---	2.6	2.5	2.5	2.4	2.4
17. Total Receipts	TR	37.8	39.7	38.4	38.1	37.7
Components of Expenditures						
18. Total Consumption	P32	17.5	18.2	18.1	17.6	17.4
19. Total Social Transfers	D62+D63	7.8	8.1	8.1	8.0	7.9
20. Interest Payments	EDP. D41+FISIM	3.5	3.4	3.1	2.9	2.5
21. Subsidies (1)	D3	0.7	0.7	0.7	0.7	0.6
22. Gross Fixed Capital Formation	P51	3.5	4.0	3.6	3.8	3.7
23. Other	---	5.8	6.4	5.9	5.9	6.0
24. Total Expenditures	TE	38.9	40.8	39.6	39.0	38.2

* (+) 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	2012	2013	2014	2015	2016
Percentage of GDP						
1. Gross Debt	---	36.2	35.0	33.0	31.0	30.0
2. Change in Gross Debt	---	---	-1.2	-2.0	-2.0	-1.0
Contributions to Change in Gross Debt						
3. Primary Balance	---	---	-2.3	-2.0	-2.1	-2.0
4. Interest Expenditure	EDP D.41	---	3.3	3.1	2.9	2.5
5. Current GDP Growth	---	---	-3.5	-3.4	-3.2	-3.2
6. Other	---	---	1.3	0.3	0.4	1.7

Table 4: Cyclical Developments*

	2012	2013	2014	2015	2016
1. Real GDP Growth (1998 Prices, %)	2.2	3.6	4.0	5.0	5.0
2. Net Lending of General Government / GDP (%) **	1.0	1.0	1.1	0.8	0.5
3. Net Interest Expenditure / GDP (%)	3.5	3.4	3.1	2.9	2.5
4. Potential GDP Growth (%)	4.4	4.4	4.3	4.3	4.2
5. Output Gap (Percentage Difference from the Potential)	-0.5	-1.2	-1.5	-0.9	-0.2
6. Cyclical Component / GDP (%) **	0.1	0.1	0.2	0.1	0.0
7. Cyclically Adjusted Balance / Potential GDP (%) **	2.1	2.3	1.6	1.2	0.8
8. Cyclically Adjusted Primary Balance / Potential GDP (%) **	-1.4	-1.0	-1.5	-1.7	-1.7

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

Table 5: Divergence from Previous Update

	2012	2013	2014	2015	2016
GDP Growth (Percent)					
Previous Update	3.2	4.0	5.0	5.0	---
Latest Update	2.2	3.6	4.0	5.0	5.0
Difference	-1.0	-0.4	-1.0	0.0	---
General Government Net Lending (Percentage of GDP)					
Previous Update	1.6	1.5	1.2	0.9	---
Latest Update	1.0	1.0	1.1	0.8	0.5
Difference	-0.6	-0.5	-0.1	-0.1	---
General Government Gross Debt (Percentage of GDP)					
Previous Update	36.5	35.0	33.0	31.0	---
Latest Update	36.2	35.0	33.0	31.0	30.0
Difference	-0.3	0.0	0.0	0.0	---

Table 6: Basic Assumptions on the External Economic Environment Underlying the Pre-Accession Economic Programme (2014-2016) Framework

	2012	2013	2014	2015	2016
Exchange Rates					
Parity (USD/ €)	1.29	1.33	1.33	1.33	1.33
Real Exchange Rate (Percentage Change)*	0.5	0.2	0.2	0.0	0.0
GDP Growth**					
Euro Area (Real, Percentage Change)	-0.6	-0.4	1.0	1.4	1.5
EU (Real, Percentage Change)	-0.3	0.0	1.3	1.6	1.8
World Trade (In Real Terms)**					
World Import Volume Increase (Percent)	2.7	2.9	4.9	5.4	5.6
International Prices					
EU CPI (Percentage Change)**	2.6	1.7	1.7	1.7	1.7
US CPI (Percentage Change)**	2.1	1.4	1.5	1.8	2.0
Oil Prices ($ / Barrel)	112.0	108.8	103.2	97.6	93.1

*(+) shows appreciation, (-) shows depreciation.
** IMF, World Economic Outlook, October 2013

Table 7: Structural Reform Agenda and Developments

Measures in Previous PEP	Realization Status (Y/N)	Date[3]	Comments
Privatization			
The privatization of electricity distribution companies	Y	2013	Transfer contracts of Boğaziçi, Gediz, İstanbul Anadolu Yakası, Akdeniz, Dicle, Vangölü, Aras, and Toroslar Electricity Distribution Companies were signed.
The privatization of Başkent Doğalgaz Dağıtım A.Ş. (natural gas distribution company)	Y	2013	Transfer contract of Başkent Doğalgaz Dağıtım A.Ş. was signed.
The privatization of electricity generation plants	Y	2013	Privatization operations of Kangal and Seyitömer thermal power plants belonging to EÜAŞ, and Hamitabat Elektrik Üretim ve Ticaret A.Ş. (electricity generation company) were completed.
The privatization of river power plants	Y	2013	Privatization procedures of 10 group river power plants belonging to EÜAŞ were completed.
The privatization of some motorways and bridges	N	2013	Privatization tender of some motorways and bridges, by the method of transfer of operation rights, was cancelled.
Financial Sector			
Publication of secondary legislation following the enactment of law, to ensure compliance with EU regulations and market requirements	Y	2013	As of 5 November 2013, a total of 30 communiqués and by-laws have been published since the enactment of the Capital Market Law (CML) and most of the remaining secondary legislation studies are planned to be completed before the end of 2013.
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	Y	2013	A new classification was made and investment firms were allowed to provide ancillary services. Conditions and principles with regard to activities have been laid down in a new Communiqué and capital adequacy requirements have also been redefined for the new structure of activities. In this context, custody has been regulated as a separate service for the first time and parallel to international practices, receiving order execution and custody services from different firms was allowed and a suitability test was required for portfolio management and investment advice services. Another communiqué in relation to the establishment conditions of intermediary institutions is planned to be published before the end of 2013. To allow a transition period to intermediary institutions for compliance with the new legislation the date for the entry into force of mentioned regulations will be set as of July 2014.
Regulations for activating housing finance and introducing new products such as real estate investment fund and venture capital investment fund shall be made	N	2013	Related draft regulations have been published for public comments on 11 June 2013, 16 May 2013 and 29 August 2013, they are expected to be published in the Official Gazette at the end of 2013.
Enhancing the structure in relation to Central Settlement and Central Custody Transactions	Y	2013	The CML lays down the legal infrastructure with regard to central counterparty applications and provides legal ground for the use of central counterparties for transactions conducted in both organized and over the counter markets. The use of a central counterparty has initially been allowed for the stock lending market operated by Takasbank.

[3] The date or foreseen date of realization.

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	Y	2013	With a new regulation: 1. Principles regarding the announcement of sovereign ratings that may affect the value of capital market instruments, or investment decisions of investors, issuers and capital market institutions have been included under the CMB communiqué. 2. The review period for solicited or unsolicited sovereign ratings has been set as 6 months. 3. Principles regarding the announcement of solicited or unsolicited sovereign ratings or rating outlooks were redefined.
Implementation of a comprehensive monitoring system in relation to derivatives	N	---	The target was modified following the merger of existing exchanges under Borsa İstanbul Inc. after the adoption of the CML, as establishing a monitoring system with Borsa İstanbul Inc. to enable the simultaneous monitoring of capital market instruments being traded in different markets. On the other hand, the outcome of ongoing negotiations conducted by Borsa İstanbul with respect to a strategic partnership will alter operation and monitoring systems of the Stock Exchange, therefore studies in relation to the establishment of a monitoring system will be launched after related negotiations are concluded.
The completion of secondary legislation in line with the CML in order to increase efficiency in the detection and prevention of market abuse	N	2013	Following the enactment of the CML, four separate communiqués were drafted and published for public comments in 2013. The drafts are (1) Draft Communiqué on the Payment of Net Earnings of Managers from Transactions to Issuers, (2) Draft Communiqué on the Measures to be Implemented During Insider Trading and Market Manipulation Investigations, (3) Draft Communiqué on Reporting Obligations, (4) Draft Communiqué on Actions Involving Market Abuse. Public comments on the drafts are currently being considered and resulting communiqués are expected to be published in the Official Gazette by the end of 2013.
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	Y	2013	In cooperation with the Islamic Development Bank, a training program for public and private sector experts was organized in May 2013, followed in June by a conference with broad participation.
Further memoranda 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	Y	2013	In 2013 a memorandum of understanding was concluded with the Turkmenistan Ministry of Finance and in relation to the supervision of alternative investment funds a memorandum of understanding were signed with the regulatory authorities 16 European countries. Efforts in relation to international cooperation will be continued in the next period.
Information and Communication Technologies			
Law on Protection of Personal Data	N	2013	Draft Law will be sent again to Parliament on the 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 GNAT 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 Gazette dated on 24 July 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	2013	The privatization of electricity distribution assets was completed in 2013.
Continuation of the privatization works in electricity generation assets	Y	2013-…	In electricity generation total 2.276 mw installed power capacity including 63 mw small HPP and 2.213 mw thermal power plants (Hamitabat, Seyitömer, Kangal) transferred to private sector in 2013.
Project of Improving the Structure and Capacity of TEİAŞ	N	2009-2014	Within the scope of fortification of the institutional structure and expansion of the technical capacity of the Turkish Electricity Transmission Company (TEİAŞ), 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 Within the framework of the Pre-Accession Assistance (IPA-1), the Project proposed by TEİAŞ and approved by the EU has been started at the end of 2012. It is aimed with the project which is having 24-month implementation period and 2 million Euros budget, to establish and operate the live care system, to improve the performance of work safety and training, to develop human resources policies and rules, to revise information processing structure and organizational structure of TEİAŞ.
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 Project, whose tender process is continuing, is expected to commence actually in 2013.
Activities to provide electricity supply security	Y	2013	Necessary measures were taken to activate the licenses for investment and to complete the investments within the envisaged periods. In this context, Electricity Market Law No. 6446 is required to pre-license.
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 newly established institution, the research, technology development and implementation activities will remain under the responsibility of TAEA.