REPUBLIC OF TURKEY

PRE-ACCESSION ECONOMIC PROGRAMME 2007

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TABLES

FIGURES

BOXES

ABBREVIATIONS

ADSL	Asymmetric Digital Subscribers Line
AIS	Automatic Identification System
APL	Applicable Program Loan
ARIP	Agricultural Reform Implementation Project
BAĞ-KUR	Social Security Organization of the Self-Employed
BASEL-II	International Recommendations on Banking Laws and Regulations Issued by Basel Committee on Banking Supervision
BEL-DES	Project for Supporting Infrastructure of Municipalities
BO	Build-Operate
BOT	Build-Operate-Transfer
BOTAŞ	Petroleum Pipeline Corporation
BRSA	Banking Regulation and Supervision Agency
CBRT	Central Bank of the Republic of Turkey
CMB	Capital Markets Board
CPI	Consumer Price Index
CRD	Capital Requirements Directive of EU
SCF	Coherence Strategy Framework
DHMİ	State Airports Authority of Turkey
DIS	Direct Income Support
ECB	European Central Bank
ECOFIN	Economic and Financial Affairs Council
EIA	Environmental Impact Assessment
EMRA	Energy Market Regulatory Authority
ESA 95	European System of Accounts 1995
ETS	European Telecommunications Standards
EU	European Union
EU-15	The EU Member Countries Before Enlargement on May 1, 2004.
EU-25	The EU Member Countries After Enlargement on May 1, 2004.
EUROSTAT	European Union Statistics Office
FED	The Federal Reserve, The Central Bank of USA
FSAP	Financial Sector Assessment Program
FX	Foreign Exchange
GDBI	Government Domestic Borrowing Instrument
GDP	Gross Domestic Product
GMPCS	Global Mobile Personal Communications by Satellite
GNP	Gross National Product
GSM	Global System for Mobile Communications
HIA	Household Labour Survey
IACS	Integrated Administration and Control System
IDKK	Internal Audit Coordination Board
ILO	International Labour Organization
IMF	International Monetary Fund
IPA	Instrument for Pre-Accession Assistance
IPARD	IPA Rural Development Funds
ISE	İstanbul Stock Exchange
IT	Information Technology
İŞKUR	Turkish Employment Organization
KOSGEB	Small and Medium Industry Development Organization
KÖY-DES	Project for Supporting Infrastructure of Villages
LPG	Liquefied Petroleum Gas
M&A	Mergers and Acquisitions
MEB	Ministry of National Education
MEDA	Euro-Mediterranean Partnership

MLSS	Ministry of Labour and Social Security
MoU	Memorandum of Understanding
NABUCCO	Natural Gas Pipeline of Turkey-Bulgaria-Romania-Hungary-Austria
NAIRU	Non Accelerating Inflation Rate of Unemployment
NFRS	National Farmer Registration System
NUTS	Nomenclature of Territorial Units for Statistics
OECD	Organization for Economic Co-operation and Development
PA	Privatisation Administration
PEP	Pre-Accession Economic Programme
PETKİM	Petrochemical Corporation
PHARE	Poland and Hungary: Action for the Restructuring of the Economy
PSSP	Privatisation Social Support Project
QIS	Quantitative Impact Study
R&D	Research and Development
RIA	Regulatory Impact Analysis
SARUT	Standard Interconnection Reference Fee Tariffs
SCT	Special Consumption Tax
SDIF	Savings Deposit Insurance Fund
SDR	Special Drawing Right
SEEs	State Economic Enterprises
SGDP	Social Security Support Premium
SMEs	Small and Medium Sized Enterprises
SPO	State Planning Organization
SSI	Social Security Institutions
SSK	Social Insurance Institution
TAEK	Turkish Atomic Energy Authority
TBMM	Turkish Grand National Assembly (TGNA)
TCDD	Turkish State Railways
TEDAŞ	Turkish Electricity Distribution Company
TEİAŞ	Turkish Electricity Transmission Company
TEKEL	General Directorate of Tobacco, Tobacco Products, Salt and Alcohol Enterprises
TETAŞ	Turkish Electricity Trading and Contracting Company Inc.
TFP	Total Factor Productivity
TINA	Transport Infrastructure Needs Assessment
TR31	İzmir Province
TR52	Karaman and Konya Provinces
TR62	Adana and Mersin Provinces
TR72	Kayseri, Sivas and Yozgat Provinces
TR82	Çankırı, Kastamonu and Sinop Provinces
TR83	Amasya, Çorum, Samsun and Tokat Provinces
TR90	Artvin, Giresun, Gümüşhane, Ordu, Rize and Trabzon Provinces
TRA1	Bayburt, Erzincan and Erzurum Provinces
TRA2	Ağrı, Ardahan, Iğdır and Kars Provinces
TRB1	Bingöl, Elazığ, Malatya and Tunceli Provinces
TÜBİTAK	Scientific and Technological Research Council of Turkey
TURKSTAT	Turkish Statistical Institute
UCTE	Union for the Coordination of Transmission of Electricity
UKKS	National Rural Development Strategy
VAT	Value Added Tax
VEDOP	Tax Office Full Automation Project
YOİKK	Coordination Council for the Improvement for the Investment Environment
YÖK	Higher Education Council
YTL	New Turkish Lira

1. OVERALL POLICY FRAMEWORK AND OBJECTIVES

Responding to the request of the Economic and Financial Affairs Council (ECOFIN Council) dated 26/27 November 2000, Turkey has prepared the Pre-Accession Economic Programme (PEP) and has submitted to the European Commission since 2001. The 2007 PEP covering the 2008-2010 period is the seventh program that has been prepared under the coordination of the Undersecretariat of State Planning Organization[1] with the contributions of relevant ministries and institutions. The 2007 PEP has been adopted by the decision of the High Planning Council[2] No.2007/71. Furthermore, the 2007 PEP was prepared according to the new outline suggested by the European Commission General Directorate of Economic and Financial Affairs to the candidate countries. Thus, the 2007 PEP was given a similar structure to the Stability and Convergence Programmes prepared by member states.

Along with the conclusions of the European Council in Copenhagen in June 1993, in its evaluation of the economic developments in candidate countries, the European Commission has determined existence of a functioning market economy and the capacity to cope with the competitive pressures and market forces within the union as basic criteria.

In the 2005 Progress Report, the European Commission has confirmed that the Turkish economy could be considered as a functioning market economy, and has mentioned that Turkey could cope with the market forces and competitive pressures in the Union in the medium term, on the condition that the stabilization policy and structural reforms are to be continued. Furthermore, in the 2007 Progress Report, it was stated that towards the strengthening of the market economy, economic policies agreed with the international financial institutions were largely adhered as the stand-by agreement with the IMF and the revised Country Assistance Strategy conducted with the World Bank in 2006. Besides, the same Report mentioned the positive developments recorded in recent years to strengthen the market economy, however it also pointed at areas that required further development.

In this context, the 2007 Pre-Accession Economic Programme covering the 2008-2010 period lays out the economic policy framework that will ensure permanence of macroeconomic stability and growth, and the structural reform agenda that is required to strengthen the market economy and eliminate potential risks in areas that may lead to macroeconomic imbalances in the future.

The general framework of stability oriented macroeconomic policies being implemented in the recent years will be maintained in the 2007 Pre-Accession Economic Programme period. In this context, the basic objective of economic policies is to create an environment conducive to economic growth, through ensuring price stability, maintaining fiscal discipline and implementing an incomes policy compatible with macroeconomic stability.

In the existing policy framework, the fiscal policy will continue to have dual roles. Improvement of fiscal balances and reduction of debt stock will be considered on one hand, and the disinflation process will be supported on the other. In this context, the basic objectives of the fiscal policy are to reduce fiscal deficits and the ratio of the public debt stock to gross domestic product permanently, to attain a balanced budget structure and to support the disinflation process. In order to achieve these objectives, giving high primary surplus policy will be continued.

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[1] The 2007 Pre-Accession Economic Programme was prepared under the coordination of the Undersecretariat of State Planning Organization (SPO) with the contributions of Ministry of Finance, Ministry of National Education, Ministry of Health, Ministry of Transport, Ministry of Agriculture and Rural Affairs, Ministry of Labour and Social Security, Ministry of Industry and Trade, Ministry of Energy and Natural Resources, Undersecretariat of Treasury, Undersecretariat of Foreign Trade, Central Bank of Republic of Turkey, Privatization Administration, Capital Markets Board of Turkey, Turkish Competition Authority, Banking Regulation and Supervision Agency, Savings Deposit Insurance Fund, Telecommunications Authority, Energy Market Regulatory Authority, Council of Higher Education, Revenue Administration, Social Security Institution and Turkish Employment Organization.

[2] The High Planning Council is a board composed of the Prime Minister as chair and eight Ministers and the Undersecretary of the State Planning Organization.

The basic objective of the monetary policy is to ensure price stability. In the 2007 PEP period, the monetary policy will be conducted within the framework of explicit inflation targeting regime that was introduced by the Central Bank at the beginning of 2006. In this context, the Central Bank will continue to use short term interest rates as the basic policy instrument. Considering the structural transformation in the economy, transition from high inflation to low inflation and the convergence process to developed countries, an inflation target of about 4 per cent in the medium term was determined. In order to attain inflation target, the monetary policy will continue to be supported by the fiscal policy, incomes policy and structural reforms.

The floating exchange rate regime being implemented since 2001 will be maintained in the 2007 KEP period. Foreign exchange rates will be determined by supply and demand conditions in the market as in the previous years, however, the Central Bank may intervene in the foreign exchange market to prevent actual and potential excess volatility in the foreign exchange rates. Additionally, in order to accumulate reserves, the Central Bank may hold foreign exchange purchase auctions in a pre-announced schedule considering the developments regarding balance of payments and currency substitution.

Structural reforms, which have been implemented with determination in the recent period, will also be continued in the 2008-2010 period. These structural reforms will serve to strengthen the market mechanism, increase competitiveness, reduce the share of the public sector in the economy through privatization, strengthen the functions of regulatory and supervisory agencies, develop the intermediary capacity of the financial sector to meet funding requirements needs of the enterprise sector, improve labour qualifications according to today’s conditions, strengthen the link between the labour market and the education system, improve the effectiveness of public services, eliminate the deficiencies in health and social security systems, increase R&D activities and innovative capacity, improve transportation and energy infrastructure, ensure regional development and increase productivity in agriculture.

The 2007 Pre-Accession Economic Programme consists of four main chapters. In the second chapter following the overall policy framework and objectives, recent economic developments in the Turkish economy are evaluated by considering the developments in the world economy, and macroeconomic forecasts for the 2008-2010 period are presented. In the third chapter, firstly the current situation is assessed and then fiscal policies for the 2007 PEP period are put forward together with forecasts and analyses regarding budget and debt management. Additionally, in this chapter the quality and institutional features of public finances are covered. The fourth chapter includes evaluations on developments in structural reforms, budgetary impacts of them and reform agenda.

2. MACROECONOMIC OUTLOOK

The world economy has captured a significant growth momentum in recent years contributed by high growth rates of developing economies. Keeping inflation rates under control in the world made a positive contribution to maintaining macroeconomic stability. The world economy, which grew by 5.4 per cent in 2006, is expected to grow by 5.2 per cent in 2007.

Despite the positive developments in global growth, volatility in financial markets increased in 2007. Due to the impact of fluctuations experienced in financial markets, negative expectations regarding the world economic growth in 2008 have arisen. According to the International Monetary Fund (IMF) forecasts, the world economic growth rate in 2008 is expected to decline compared to the year of 2007, and to be realized as 4.8 per cent. Particularly, the US economy is estimated to slow down in 2008. These forecasts are based on the assumption that the credit shortage problem in the international financial markets will be overcome in the coming months, and market conditions will turn out to be normal. Furthermore, other risks that might threaten the world economy in the short term are inflationist pressures due to increasing energy and food prices, fluctuations in oil prices and probable negative effects of capital flows on emerging market economies.

In the 2007 PEP, assumptions regarding the world economy used in macroeconomic analyses and forecasts are based on the most recent forecasts of the European Commission and the IMF.

Assumptions regarding the world economy have special importance on all macroeconomic variables, mainly export, import and growth performance. Based on the consideration of the forecasts of the aforesaid organizations, it is assumed that the world imports will grow by 7.2 per cent annually on average in the period of 2008-2010. The world import price index is assumed to increase by 1.5 per cent in 2007. In the period of 2008-2010, it is predicted that the world import price index will rise by 1.2 per cent annually on average. In the period of 2007-2010, it is assumed that the EU and the US consumer price indices will rise by 1.2 per cent and by 2.4 per cent, respectively, annually on average. On the other hand, in the period of 2008-2010, the dollar/euro parity is assumed to be 1.42, at a value above that of 2007. All assumptions used in the PEP forecasts are presented in Appendix Table 7.

2.1. Recent Economic Developments

The Turkish economy, which has grown considerably fast since the first quarter of 2002, maintained its performance in 2006 as well and the economic growth rate was realized as 7.2 per cent annually on average in the period of 2002-2006. The main determinants of this high growth performance were structural reforms implemented in Turkey, and the confidence environment established in parallel with the macroeconomic policies as well as the positive circumstances in international markets. In addition, the ongoing tight monetary and fiscal policies did not have any restrictive impact on economic growth; on the contrary, it contributed significantly to the economic growth with the help of improving public balances and sustaining price stability.

However, due to the fluctuations in the international markets in the second quarter of 2006, the risk premium for Turkey increased as it did for other emerging markets. The Central Bank responded to these fluctuations, which were envisaged to create an upward pressure on inflation, by raising the short term interest rates by 425 basis points. Accordingly, the GDP growth rate receded to 5 per cent in the second half of 2006, which was realized as 7.5 per cent in the first half. In the second half of 2006, limited increases in the private consumption and investment expenditures appeared as factors reducing the growth rate. On the other hand, contributions of public sector consumption expenditures and exports to growth became salient. Thus, the GDP growth rate in 2006 estimated to be 6 per cent in the 2006 PEP was realized as 6.1 per cent.

On the other hand, when the realizations in 2006 are analyzed, some discrepancies are observed between the demand components of the GDP realizations and those of the 2006 PEP projections. The increase in exports of goods and services in the 2006 PEP was estimated to be 6.7 per cent for 2006, but realized as 8.5 per cent. On the other hand, despite the high growth rate in

2006, the increase in imports of goods and services was 7.1 per cent, much lower than the projection. Thereby, the net contribution of exports of goods and services to growth, which was estimated as -1.6 points in the 2006 PEP, was realized as 0.3 points in 2006. Private consumption expenditures were realized a bit lower than the 2006 PEP projections, while the private sector investments were higher than expectations.

Analyzing the components of growth by sectors, it is observed that value-added increases in agriculture, industry and services sectors in 2006 were 2.9 per cent, 7.4 per cent and 6.1 per cent, respectively. On the other hand, value-added increase in construction sector was recorded as 19.5 per cent in 2006.

One of the remarkable indicators of structural change in the Turkish economy in the period of 2002-2006 was the productivity increase. The partial productivity per worker in production has recorded high increases since 2002, and became an important factor supporting GDP growth. In 2006, the productivity increase was realized as 4.7 per cent in overall economy, and 6.3 per cent in the manufacturing industry. On the other hand, the partial productivity increase in manufacturing industry was 2.7 per cent in the first half of 2007. It is observed that productivity increases continued since 2002 have decelerated in recent period.

Table 2. 1: Growth Rates and Demand Components

(Annual Percentage Change, at 1987 Prices)

			By Quarters						
	Annual		2006				2007		
	2005	2006	I	II	III	IV	I	II	I. Half
Agriculture	5.6	2.9	7.6	-0.4	0.5	9.7	4.4	-1.1	0.9
Industry	6.5	7.4	4.5	11.1	7.2	6.5	7.5	3.2	5.2
Services	8.2	6.1	7.6	7.8	5.4	3.9	6.8	4.7	5.7
GDP	7.4	6.1	6.7	8.3	4.8	5.2	6.9	3.9	5.3
GNP	7.6	6.0	6.4	9.3	4.3	4.6	6.8	3.9	5.2
Total Consumption	8.1	5.6	8.3	12.2	3.3	0.2	2.6	0.4	1.5
Public	2.4	9.6	10.1	18.3	14.8	0.7	9.0	7.4	8.1
Private	8.8	5.2	8.1	11.5	2.3	0.1	2.0	-0.3	0.8
Gross Fixed Capital Formation	24.0	14.0	32.1	14.0	11.3	4.4	3.0	10.0	6.9
Public	25.9	-0.2	32.8	-11.9	-4.1	1.8	9.1	33.9	25.1
Private	23.6	17.4	32.1	18.4	15.0	5.6	2.5	6.9	4.9
Total Final Domestic Demand	12.1	8.0	14.1	12.7	5.3	1.4	2.7	3.4	3.1
Total Domestic Demand	8.8	5.6	8.2	10.6	1.4	2.7	2.4	2.6	2.5
Exports of Goods and Services	8.5	8.5	6.8	9.1	11.5	6.2	14.7	12.7	13.6
Imports of Goods and Services	11.5	7.1	10.0	13.7	3.6	1.0	4.3	8.4	6.5

Source: TURKSTAT

The economy grew at a rate of 6.9 per cent in the first quarter of 2007. In the second quarter, growth rate declined to 3.9 per cent, which has been the lowest rate in the last 16 quarters. However, the economy grew continuously in the last 22 quarters.

In the first half of 2007, the uncertainty in domestic markets due to the general elections held in 2007 and the increasing real interest rates in 2006 had negative effects on the economy. In this period, the growth of private final consumption at such a low rate as 0.8 per cent was the main determinant for the limited GDP growth. Similarly, a limited increase of 4.9 per cent was realized in the private fixed capital investments. On the other hand, the public sector fixed capital investments and consumption expenditures increased more than the GDP growth in the first half of 2007. Thus, the total domestic demand increased by 2.5 per cent in the same period.

In the first half of 2007, particularly in the second quarter, while YTL appreciated significantly in real terms, exports of goods and services increased by 13.6 per cent. The increase in imports of goods and services was limited to 6.5 per cent due to the slowdown in the domestic demand. Thereby, net contribution of exports of goods and services to the growth was 2.6 points.

In the first half of 2007, the sectoral value-added increases in agriculture, manufacturing and services were realized as 0.9 per cent, 5.2 per cent and 5.7 per cent, respectively. Moreover, the value-added in the construction sector increased by 16.1 per cent.

It is observed that the rising trend in the industrial production since 2002 has continued during 2007. The industrial production grew by 4.9 per cent in the January-September period of 2007, compared to the same period of the previous year.

Considering the developments in the labour markets, it is observed that total employment increased by 1.3 per cent in 2006. While the agricultural employment contracted by 405 thousand persons, the industrial sector employment expanded by 123 thousand persons and the services sector employment expanded by 567 thousand persons in 2006. Thereby, despite a 6.2 per cent contraction in the agricultural sector employment, the non-agricultural employment went up by 4.4 per cent and the increase in total employment was recorded as 285 thousand persons in the economy. Employment increases in trade, social services, financial institutions, and manufacturing industry played a significant role in this development.

The labour force participation rate receded to 48 per cent in 2006, with a decline of 0.3 points compared to the previous year. Related to this decline, the labour supply increased by a limited amount in 2006. Thereby, the unemployment rate decreased by 0.4 points from the previous year and declined to 9.9 per cent in 2006. The declining trend in the unemployment rate is observed in subcategories as well. In 2006, the unemployment rate in the non-agricultural sectors declined to 12.6 per cent, by a 1 point decrease from the previous year, and the youth unemployment rate went down to 18.7 per cent by a 0.6 points decrease.

Table 2. 2: Developments in the Labour Market

(15+ Age, Thousands of Persons)

	Annual		2006			2007		
	2005	2006	Feb.	May	Aug.	Feb.	May	Aug.
Working Age Population	50,826	51,668	51,371	51,561	51,770	52,203	52,415	52,644
Labour Force Participation Rate (Per cent)	48.3	48.0	45.5	48.6	49.5	46.3	48.8	49.3
Labour Force	24,565	24,776	23,400	25,075	25,622	24,158	25,574	25,931
Employed	22,046	22,330	20,604	22,860	23,279	21,398	23,309	23,548
Unemployed	2,520	2,446	2,796	2,215	2,343	2,760	2,265	2,383
Employment Rate (Per cent)	43.4	43.2	40.1	44.3	45.0	41.0	44.5	44.7
Unemployment Rate (Per cent)	10.3	9.9	11.9	8.8	9.1	11.4	8.9	9.2
Non-Agricultural Unemployment Rate	13.6	12.6	14.8	11.5	12.0	14.2	11.5	11.9
Unemployment Rate Among Young People	19.3	18.7	21.9	16.4	17.5	21.7	17.5	19.2
Employment by Sectors								
Agriculture	6,493	6,088	5,167	6,488	6,809	5,337	6,488	6,591
Industry	4,280	4,407	4,209	4,277	4,531	4,346	4,451	4,496
Services	11,269	11,836	11,229	12,095	11,939	11,716	12,412	12,461

Source: TURKSTAT

Analyzing the data for 2007 in comparison to the respective periods of 2006, the most remarkable point is that there is no significant contraction in the agricultural sector employment in 2007 in contrast to previous years. On the other hand, the employment figures of industrial and services sectors indicate strong employment increases. When the realizations in 2007 are examined, it is expected that there will be a stronger increase in employment in the entire year compared to the previous years. Thereby, an increase in the employment rates will be observed as well. On the other hand, labour force participation rates showing an upward movement, is expected to partially restrict the decline in unemployment rates.

When the labour market developments are compared to the 2006 PEP forecasts, the realizations in general are better than projections.

When the wage increases in 2006 are analyzed, while average nominal worker wage in public sector increases were realized as 6.6 per cent in line with the incomes policy, average nominal worker wage in private sector increased by 11.9 per cent. Additionally, average nominal worker wage in manufacturing industry increased by 12.6 per cent in 2006. Thereby, the nominal wage increase in the overall economy realized as 11.3 per cent in 2006.

Inflation, Monetary and Exchange Rate Policies

The downward trend in annual inflation in recent years paused in 2006, and the year-end CPI inflation increased by 1.9 percentage points compared to 2005 and realized as 9.65 per cent. Thereby, the realization significantly exceeded the pre-announced inflation target of 5 per cent. The fact that the 2006 year end inflation was above the upper limit of the uncertainty band announced for end-2006 at 7 per cent, triggered the accountability mechanism pursuant to the Central Bank Law. In this context, the Central Bank wrote three open letters to the government in July and October 2006 and January 2007 to explain the reasons behind the divergence from the targets, the recent policy response and possible future responses, and about the process towards converging back to the targets. These letters were publicly announced as a requirement of the accountability and transparency principles, and presented to the IMF as part of the program conditionality.

Analyzing the price developments in 2006, it is observed that the rise in inflation in the first quarter of the year can be attributed to a combination of adverse developments beyond the control of the monetary policy such as rising oil prices, high unprocessed food price inflation, and the sustained increases in the gold prices. In addition, relatively strong domestic demand in this period contributed to the rise in inflation. In this period, effects of supply side shocks on inflation were clearly observed, furthermore, the risk perceptions tended to deteriorate in response to adversities experienced in the global liquidity conditions in May, and the demand for financial assets of the developing countries fell down. As a result of these developments, serious fluctuations were also observed in Turkish financial markets. YTL depreciated more than 20 per cent against dollar in the period from the beginning of May through end-June, the risk premium increased about 150 basis points and inflation expectations rose.

The aforesaid developments not only caused the inflation to diverge from the uncertainty band, but also seriously deteriorated inflationary expectations and posed a serious threat to the achievement of medium term objectives. Under these circumstances, the Central Bank took a series of policy measures to curb this deterioration, to prevent the mentioned deterioration from having a permanent effect on pricing behaviour, and lastly to make the inflation objectives achievable in the medium term. In this context, firstly, the interest rates, which are the main policy tool, were raised 425 basis points in June-July 2006 period and the overnight borrowing rates were raised to 17.50 per cent. In addition, various measures were taken to stabilize the deteriorated YTL and foreign exchange liquidity in the markets. In this context, to withdraw excess YTL liquidity in the financial markets progressively, the Central Bank started one-week and two-week maturity YTL deposit purchase auctions. On the other hand, as a response to the insufficient liquidity in the foreign exchange markets, foreign exchange sale auctions on pre-announced schedules and amounts were decided to hold.

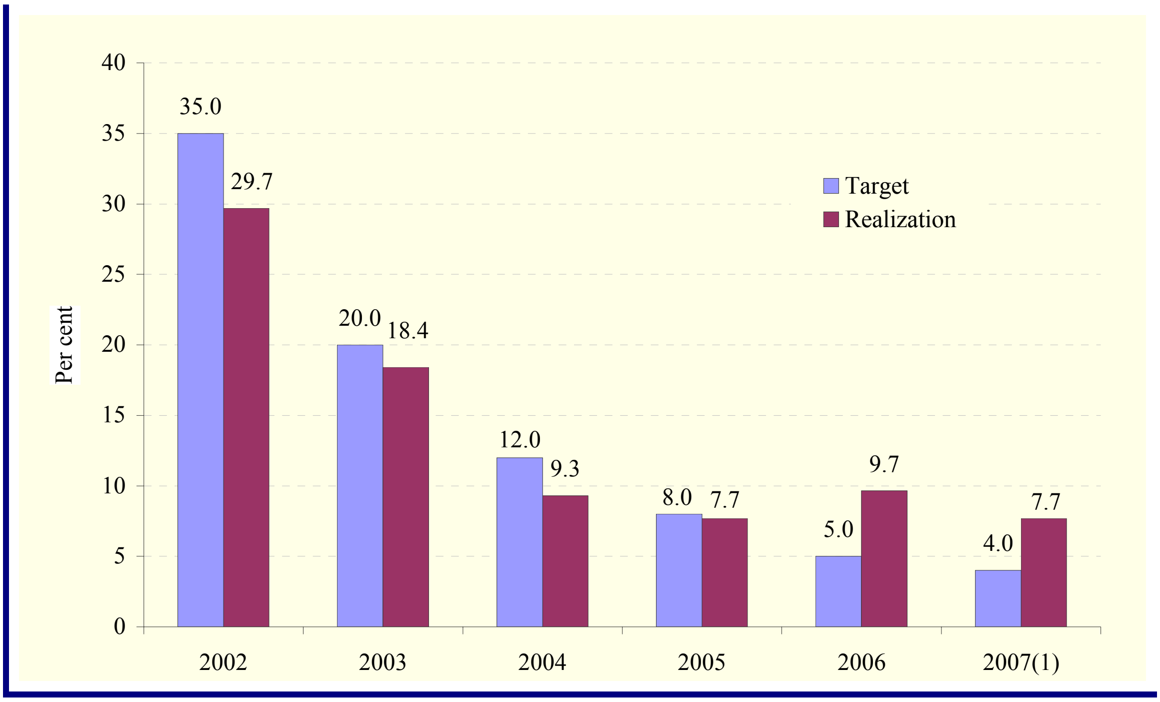
All these measures were an indication that the Central Bank was dedicated to its medium term commitments and these measures were perceived positively by the markets. Consequently, the foreign exchange markets attained a stable situation and YTL started to strengthen again. In addition, the deterioration in inflation expectations ceased as of end-July 2006, and in the rest of the year inflation expectations improved, though limited. The risk premium decreased by 100 basis points until August 2006, with the help of the positive developments in the global liquidity. In parallel with these developments, the market interest rates took a downward trend again in this period.

Despite these positive developments observed in the short term, it took a while for the effects of the policy measures taken by the Central Bank became apparent in the economy and particularly on the inflation. The annual CPI inflation rose to 11.70 per cent as of July 2006, and showed a decreasing tendency in the rest of the year, and fell again to single digits as of October. In the second half of 2006, the domestic demand was an important contributing factor to this downward trend in inflation and thus, the international liquidity conditions were improved in this period. Despite this downward trend, the existence of serious risk factors such as the inflation and inflation expectations staying significantly above the targets in the second half of the year, continuance of service price rigidities, persistence of uncertainties in oil and other commodity prices and uncertainties regarding the global risk appetite, led the Central Bank keep its tight stance, and the short term policy interest rate was kept at 17.50 per cent until the end of 2006.

Although the inflation target could not be achieved in 2006, considering that frequent revisions in targets would create adverse impacts on inflation expectations and undermine the reliability of future commitments, it was decided to preserve the inflation target of 4 per cent announced earlier for the end of 2007. In other words, the Central Bank adopted the approach of not revising the targets, as long as the medium term targets were foreseen as attainable in reasonable terms.

In the first quarter of 2007, the inflation took an upward trend again, however stood at 10.86 per cent by the end of the first quarter, and stayed in the target consistent path. In this period, the basic driving factors of the rise in inflation were the continuation of the high increases in unprocessed food prices, price increases of tobacco products, the effects of the tightening of the monetary policy not being apparent on inflation, and the degressive continuation of the lagged effects of the exchange rates. However, as of August, the annual inflation rate increased temporarily and reached 7.39 percentage level as a result of increases in unprocessed food prices particularly. Although the food prices continued to rise higher than they did in previous years, with continuation of effects of the strong monetary tightening on services and durable goods prices, the decrease in the inflation continued in September, so the annual inflation in the third quarter realized as 7.12 per cent and continued to be within the uncertainty band. The annual inflation increased to 7.70 per cent level in October due to the increases in food prices.

Figure 2. 1: CPI Targets and Realizations



(1) 2007 realization figure is as of October.
Source: TURKSTAT, CBRT

The service prices increases in the first 10 months of 2007 slowed down significantly compared to the previous years. In this period, while the energy price increases were lower than the previous years, the ongoing high increases in unprocessed food prices sustained and strengthened. The ten-month price increases in goods other than energy and unprocessed food were realized lower than the previous year's level, despite high increases in processed food prices.

Despite the overall downward trend observed in inflation in the first eight months of the year, the Central Bank did not change the policy interest rates and continued to keep them at 17.50 per cent level until the end of August considering risk factors such as the rigidity of service inflation being not fully removed, the significant continuation of backward indexation behaviours of economic agents and probable changes in global risk appetite perceptions. However, considering the downward trends in inflation and inflation expectations in this period, this fact points to progressively strengthening monetary tightening, despite unchanged interest rates throughout the period. In the end of summer 2007, having observed that fluctuations starting from the housing markets in developed countries affected financial markets worldwide, Central Bank found appropriate to keep its existing stance in that period considering these developments were not be effective on the inflation outlook of Turkey as of August. In addition, it was stressed that changes in international liquidity conditions, external demand, public expenditures and other developments affecting the medium term inflation outlook would be closely monitored and the Central Bank would change its stance, if necessary.

The Central Bank points out that it is possible to reach the medium term inflation target of 4 per cent by the end of 2008, under a scenario that interest rates are lowered moderately beginning from the last quarter of 2007. However, it is also stated that it was not a commitment, and interest rate cuts may be considered earlier as well as later depending on conditions. In fact, in the September Monetary Policy Committee meeting, it was considered that developments experienced in the global economy in this period might affect both domestic and external demand growth in a restrictive manner, and this would increase downward risks for attaining the inflation target of 4 per cent in the medium term. In this context, moderate easing process of interest rates was started earlier and it was decided to decrease the short term policy interest rates by 25 basis points. Despite the risks regarding energy and food prices and administered prices, the moderate easing of interest rates was continued in October in which the consideration that the inflation is expected to continue to decline with the lagged impact of strong monetary tightening was made, due to the effects of developments that the aggregate demand conditions continued to be conducive to the process of inflation reduction and the inflation in services sector stayed in favourable levels. In this context, the overnight borrowing rates of the Central Bank was reduced by an additional 50 basis points to the level of 16.75 per cent. Finally, for the facts that the existing figures did not differ significantly from the October outlook, and the non-food inflation was in favourable levels, the overnight borrowing rates were lowered by an additional 50 basis points in November. Within this framework, in the first eleven months of 2007, the Central Bank overnight borrowing rate declined from the level of 17.50 per cent to 16.25 per cent, decreasing by 125 basis points on aggregate.

Analyzing the results of the first quarter expectations survey in November, it is observed that annual inflation expectations of the next 12 and 24 months receded to 5.82 per cent and 5.05 per cent, respectively.

The operational framework of the explicit inflation-targeting regime was mostly preserved in 2007. In this context, inflation targets continued to be defined as the annual percentage change in CPI, and the 3-year target horizon was maintained. In addition, the uncertainty band was defined as 2 percentage points around the target and announced along with the 3-month inflation path consistent with the year-end target, also in 2007.

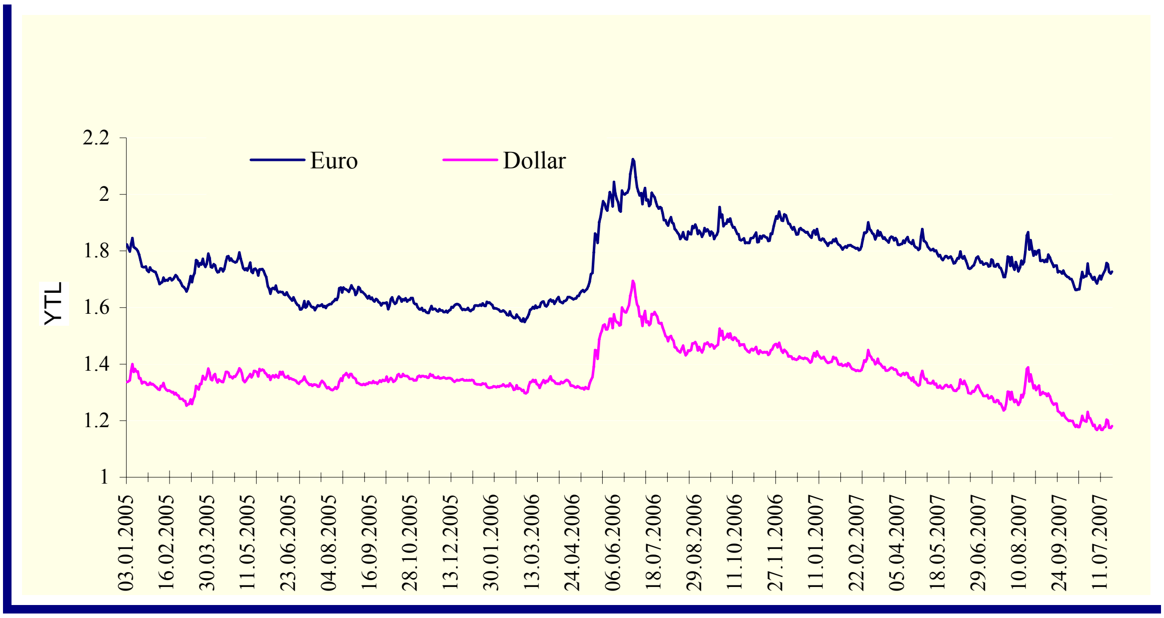
While the operational framework of the explicit inflation targeting policy was kept unchanged, a set of modifications was initiated to make communication policy and monetary policy implementation more effective. The first of the mentioned modifications was to start announcing the inflation forecasts in the Inflation Reports, which were presented earlier with a one and a half years forward time horizon, with a two-year forward time horizon starting from 2007 to help economic agents to forecast and foresee the future clearly. With this modification, creating a projection horizon comparable to the Expectations Survey and making inflation forecasts easier to analyze and evaluate were aimed. On the other hand, the practice of publishing the Monetary Policy Committee decisions on the same day with its English translation text was put into practice to facilitate more effective communication policies. In addition, the practice of publishing the Monetary Policy Committee Meeting Minutes within 8 days following the meeting along with its English translation text has started from 2007 onwards.

On the other hand, the Central Bank has been continuing to implement the floating exchange rate regime since 2001. Within the scope of this regime, the exchange rates are set by demand and supply conditions in the markets, the Central Bank does not target any level for exchange rate. However, the Central Bank reserves the right to make direct interventions of purchase or sale in the foreign exchange markets, if the exchange rates display excessive volatility or developments that may lead to excessive volatility are observed. In addition, the Central Bank may hold foreign exchange purchase auctions to accumulate reserves.

Developments before May 2006, such as the rising confidence in the economic program and policies implemented, Turkey's starting accession negotiations with EU, and developments in favour of developing countries in the international markets, led to an increase in the foreign capital inflows to Turkey. As a result of these developments, an excess supply was experienced in the foreign exchange markets and the Central Bank implemented a reserve accumulating strategy through foreign exchange purchase auctions. In this context, starting from 2005, to affect the market demand and supply conditions as low as possible, the Central Bank started holding foreign exchange purchase auctions according to the preannounced schedules and within the preannounced limits, and adopted the approach of not altering these schedules unless extraordinary deviations are observed in foreign exchange liquidity.

However, the Central Bank suspended foreign exchange purchase auctions from 16 May 2006, as a result of the excessive volatility in the exchange rates stemming from the decrease in the foreign exchange liquidity due to the changes observed in the international liquidity conditions from May 2006 based on the decrease in the risk appetite for the markets of developing countries. In addition, as fluctuations in the financial markets continued and this resulted to distortion on the inflation expectations, the Central Bank sold a total of 2.1 billion dollars foreign exchange to the markets in June 2006.

Figure 2. 2: Developments in Exchange Rates



Source: CBRT

The foreign exchange markets showed a relative stabilization, as a result of the measures taken by the Central Bank against the fluctuations in financial markets in May-June and the improvement in the global liquidity conditions. The paused foreign exchange purchase auctions resumed starting from 10 November 2006. During 2006, the total foreign exchange purchases through auctions and interventions amounted 9.7 billion dollars, and the sales amounted 3.1 billion dollars.

The foreign exchange purchase auctions aiming reserve accumulation continued in 2007 as well. In the first ten months of 2007, the total purchases through auctions amounted 8.4 billion dollars. According to September 2007 figures, Central Bank gross foreign exchange reserves have reached 71.7 billion dollars.

Table 2. 3: FX Purchases of the Central Bank

(In Million Dollars)

Years	FX Purchase Auctions	FX Sale Auctions	FX Purchase Interventions	FX Sale Interventions	Total Net FX Purchases
2005	7,442	-	14,565	-	22,007
2006	4,296	1,000	5,441	2,105	6,632
2007*	8,387	-	-	-	8,387

*As of 19 November 2007
Source: CBRT

Financial Sector

Turkish banking sector sustained its robust growth performance in 2006 and 2007; total assets of the sector reached 354 billion dollars by the end of 2006 and 409 billion dollars as of June 2007. In this period, the emphasis on loan extension activities continued. The credit volume, which was recorded as 116 billion dollars in 2005, increased by 36.3 per cent to 155 billion dollars by the end of 2006. The loan volume as of June 2007 reached 190 billion dollars.

The ratio of loans to deposits, an indicator of the development of banks' intermediation function, rose to 71.1 per cent in 2006, and 75.1 per cent in 2007 as of June. The decline of non-performing loans as a share of total credits continued in 2006 and 2007. The decrease in non-performing loans and developments in economic activities are the positive indicators that reduce credit risks.

Table 2. 4: Overview of the Banking Sector

	2001	2002	2003	2004	2005	2006	2007 June
Main Aggregates							
Assets (In Billion Dollars)	127	133	183	234	303	354	409
Loans (In Billion Dollars)	24	31	50	78	116	155	190
Deposits (In Billion Dollars)	75	86	114	147	187	218	253
Number of Banks	61	54	50	48	47	50	50
Number of Employees (Thousands)	139	124	124	128	133	151	157
Performance Indicators							
Net Profit (In Billion Dollars)	-8.2	1.8	4.0	4.8	4.4	8.0	6.1
Return on Assets (Per cent)	-7.0	1.5	2.5	2.4	1.7	2.5	2.9
Rate of Return for Equity Capital (Per cent)	-7.7	15.9	18.3	16.5	10.9	19.2	23.5
Loans/Deposits (Per cent)	32.0	36.0	43.9	53.1	62.0	71.1	75.1
Risk Indicators							
Capital Adequacy Ratio (Per cent)	20.8	25.1	30.9	28.8	23.7	22.3	18.7
FX Position in the Balance Sheet (In Billion Dollars)	-1.6	- 0.6	-0.0	-1.4	-1.9	-5.5	-7.7
Net General Position (In Billion Dollars)	-0.5	-0.4	0.3	-0.1	-0.1	0.2	-0.6
Non-Performing Loans/Gross Loans (Per cent)	29.3	17.6	11.5	6.0	4.8	3.8	3.9
Securities Portfolio/Assets (Per cent)	35.0	39.7	41.9	39.4	35.2	31.8	31.0

Note: Assets, loans, deposits and net profit figures do not include participation banks. Other data includes participation banks starting from 2006.
Source: BRSA

Loans used from abroad by firms have increased in recent periods. Despite the decrease from the previous years, the share of foreign currency loans in the loans used by non-finance companies including the loans used from the foreign financial markets is estimated to be 56 per cent as of the first half of 2007.

The ISE National-100 Index gained an upward trend following the fluctuations in the financial markets in May-June 2006. The ISE Compound-100 Dollar Index (1986=100) was 1,621 dollar at the end of 2006, and reached 2,612 dollar as of September 2007. At the same period, the market capitalization was realized as 323.7 billion YTL.

Balance of Payments

Current Account

Scrutinizing the period of 2002-2006, it is observed that the current account deficit continuously increased and reached 32.9 billion dollars in 2006 from its level of 1.5 billion dollars in 2002. The current account deficit in 2006 was realized as 2.1 billion dollars more than the 2006 PEP projection. The higher than expected increases in imports and lower than expected tourism revenues were influential in this difference. In the January-September period of 2007, the current account deficit realized as 26.1 billion dollars.

Table 2. 5: Balance of Payments

(In Billion Dollars)

	Annual		January-September	
	2005	**2006**	**2006**	**2007**
Current Account	-22.6	-32.9	-24.5	-26.1
Trade Balance	-33.5	-41.3	-32.2	-34.4
Total Exports	76.9	91.9	65.9	80.6
Exports (fob)	73.5	85.5	61.4	76.2
Total Imports	-110.5	-133.3	-98.1	-115.0
Imports (cif)	-116.8	-139.6	-102.4	-121.5
Balance on Services	15.3	13.4	11.3	12.1
Credit	26.6	24.5	19.5	22.3
Tourism	18.2	16.9	13.7	14.6
Debit	-11.4	-11.1	-8.2	-10.1
Balance on Income	-5.8	-6.6	-4.8	-5.2
Credit	3.7	4.5	3.4	4.7
Debit	-9.5	-11.1	-8.2	-9.9
Current transfers	1.5	1.7	1.2	1.3
Capital and Financial Account	20.4	35.1	25.8	25.5
Financial Account	20.4	35.1	25.8	25.5
Direct Investment	8.9	19.0	12.8	13.5
Direct Investment in Turkey	10.0	20.0	13.1	15.3
Direct Investment Abroad	-1.1	-1.0	-0.3	-1.8
Portfolio Investment	13.4	7.4	3.1	3.9
Other Investment	15.9	14.8	14.8	16.0
Assets	0.3	-12.4	-5.8	-3.2
Liabilities	15.6	27.2	20.6	19.2
Trade Credits	3.1	2.6	2.4	3.5
Credits	11.7	19.7	17.2	20.8
Monetary Authority	-2.9	0.0	0.0	0.0
General Government	-4.6	-5.2	-3.6	-3.3
Banks	9.2	5.8	5.7	4.4
Other Sectors	10.0	19.1	15.2	19.7
Currency and Deposits	0.5	4.6	0.7	-5.4
Monetary Authority	-0.8	-1.3	-0.9	-1.1
Banks	1.3	5.9	1.7	-4.3
Other Liabilities	0.3	0.3	0.3	0.3
Official Reserves	-17.8	-6.1	-4.9	-7.9
Net Errors and Omissions	2.2	-2.3	-1.3	0.6

Source: CBRT

The high growth trend in exports volume continued in 2006 as well. Exports, which grew by 16.3 per cent in 2005, increased by 16.4 per cent in 2006 and reached the level of 85.5 billion dollars. The continuation of buoyancy in the world economy in 2006 and the appreciation of euro against dollar were the external factors positively affecting the exports performance. On the other hand, the depreciation of YTL in 2006, increase in labour productivity and the raises in export prices were the other determining factors of the high export performance in 2006. As a result of these developments, the value of exports in 2006 was realized 2 billion dollars higher than the 2006 PEP projections.

During the January-September period of 2007, exports increased by 24.1 per cent compared to the same period of the previous year and reached 76.2 billion dollars. The main contributors to this development were increases in exports of motor vehicles and parts and accessories, iron-steel and machinery, mechanical devices and boilers.

In 2006, imports increased by 19.5 per cent compared to the previous year and reached 139.6 billion dollars. Imports of intermediate goods made the highest contribution to the increase in imports in 2006. In the mentioned period, the increase in industrial production was the determining factor in the increase of intermediate goods imports. The slowdown of the domestic demand and the depreciation of exchange rate were the limiting factors for the increase in imports in 2006. In the January-September period of 2007, imports increased by 18.6 per cent compared to the same period of the previous year and reached 121.5 billion dollars.

The ratio of trade volume to GDP, which was 52.4 per cent in 2005, increased to 55.9 per cent in 2006. Thus, Turkish economy’s integration with the world economy has improved.

Analyzing the foreign trade with EU countries in 2006, it is seen that the share of EU countries in Turkish exports decreased by 0.3 per cent to 56 per cent, and the share of EU countries in Turkish imports decreased by 2.6 per cent to 42.6 per cent. The energy bill paid by Turkey for imports from non-EU countries was influential on the decrease in the share of imports from EU countries. In the January-September period of 2007, the share of exports to EU countries in total exports was 56.6 per cent, while the share of imports from EU countries in total imports was realized as 40.3 per cent.

Table 2. 6: Foreign Trade by Countries

(In Million Dollars)

	Annual					January-October				
	2005	Per cent Share	2006	Per cent Share	Percentage Change	2006	Per cent Share	2007	Per cent Share	Percentage Change
Merchandise Exports	73,476	100.0	85,535	100.0	16.4	61,401	100.0	76,201	100.0	24.1
European Countries (EU-27)	41,365	56.3	47,935	56.0	15.9	34,456	56.1	43,122	56.6	25.2
Other Countries	29,138	39.7	34,633	40.5	18.9	24,735	40.3	30,951	40.6	25.1
Turkish Free Zones	2,973	4.0	2,967	3.5	-0.2	2,210	3.6	2,128	2.8	-3.7
Merchandise Imports *	116,774	100.0	139,576	100.0	19.5	102,432	100.0	121,506	100.0	18.6
European Countries (EU-27)	52,696	45.1	59,401	42.6	12.7	43,821	42.8	48,912	40.3	11.6
Other Countries	63,318	54.2	79,231	56.8	25.1	57,947	56.6	71,709	59.0	23.7
Turkish Free Zones	760	0.7	944	0.7	24.2	664	0.6	884	0.7	33.2

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

The surplus in services balance, which was 15.3 billion dollars in 2005, declined by 12.4 per cent to 13.4 billion dollars in 2006. The decrease in tourism revenues from 18.2 billion dollars in 2005 to 16.9 billion dollars in 2006 was the most significant factor in this decline. Avian influenza, political tensions in countries neighbouring Turkey, and the World Cup organized in Germany contributed to the decrease in tourism revenues in 2006. Consequently, tourism revenues in 2006 were realized 1.2 billion dollars less than the 2006 PEP forecasts. Tourism revenues in the January-September period of 2007 went up by 6.5 per cent compared to the same period of the previous year and reached 14.6 billion dollars.

The incomes balance, which had displayed a 5.8 billion dollars deficit in 2005, ran a deficit of 6.6 billion dollars in 2006. In the January-September period of 2007, the incomes balance deficit, which was above the level of the same period of the previous year, realized as 5.2 billion dollars. The increase in interest expenditures was effective in this development.

The current transfers reached the level of 1.7 billion dollars in 2006, and was recorded as 1.3 billion dollars in the January-September period of 2007.

Capital and Financial Account

In recent years, significant capital inflows took place as a result of continuation of sustained stability and positive prospects in the economy. The capital and financial account displayed a surplus of 20.4 billion dollars and 35.1 billion dollars in 2005 and 2006, respectively. In the first nine months of 2007, this account gave a surplus of 25.5 billion dollars and the reserve accumulation realized as 7.9 billion dollars in the same period.

While 30.8 per cent of the net 43.6 billion dollars inflow in the capital and financial account (excluding IMF credits and reserves) were portfolio investments in 2005, this ratio went down to 16.1 per cent in 2006. In this development, portfolio outflows resulting from the fluctuations in the financial markets were the determinant factor. In 2006, the net inflow in the capital and financial account was 45.8 billion dollars.

The net capital inflow excluding IMF and reserve assets was recorded as 36.7 billion dollars in the January-September period of 2007. In this period, direct investments and long-term loans were the main sources of finance.

Similar to 2005, the continuation of privatization and M&A in 2006 resulted in attaining high levels of foreign direct investments. In 2006, with net foreign direct investments amounting 19 billion dollars, Turkey became one of the top emerging market economies attracting foreign direct investments. Real estate purchases accounted for 2.9 billion dollars of this figure. The high increase in the foreign direct investments, which is a non-debt creating item in capital account, maintains its importance regarding the financing and sustainability of the current account deficit. As a matter of fact, in the January-September period of 2007, net foreign direct investments were realized as 13.5 billion dollars.

Analyzing the capital flows in 2006, it is observed that the share of short-term capital flows in the total financing kept declining compared to the previous year.

The decisively implemented macroeconomic stability program helped the creation of a favourable environment for investments by reducing uncertainties and risk premium in the economy. In this context, in parallel with the increase in the domestic investment expenditures, the net long term loans obtained by the non-banking private sector from foreign markets continued to expand and were realized as 18.6 billion dollars in 2006. Increasing significantly in the January-September period of 2007, the same figure reached the level of 2006 and realized as 18.7 billion dollars.

In the January-September period of 2007, while 4.4 billion dollars of debt repayments were made to the IMF, 1.1 billion dollars were borrowed from the IMF. Thus, net 3.3 billion dollars were repaid to the IMF.

When the January-September period of 2007 is compared to the previous years, it is seen that the high share of private sector items kept increasing in the financing of the current account deficits.

2.2. Medium-Term Macroeconomic Scenario

The main objective of the policies to be implemented in the 2008-2010 period is increasing the welfare of the society. Towards this objective, the basic priority of macroeconomic policies to be implemented in the 2007 PEP period is sustaining economic growth by strengthening macroeconomic stability, thereby maintaining the convergence process of per capita income to the EU average. Social policy practices will also be continued within the budgetary means.

The fiscal policy in the 2007 PEP period will be a continuation of the policies in effect, which have resulted in significant improvements in the public fiscal balance. Efforts to increase tax revenues by expanding the tax base and reducing informal economy and to ensure efficiency in public expenditures will be continued, and thus the tight fiscal policy targeting the primary budget surplus will be maintained. In this context, the fiscal policy will be an important tool for permanently reducing the public deficits and the ratio of the public debt stock to the national income, reaching a balanced budget structure, contributing to a sustainable growth environment, and supporting anti-inflationary efforts.

In the 2007 PEP period, the monetary policy will be executed in the framework of explicit inflation targeting, the policy that was adopted by the Central Bank at the beginning of 2006. In this period, implementation of floating exchange regime will be continued. As it was in the previous years, exchange rates will be determined by market supply and demand conditions, however the Central Bank would intervene to the foreign exchange market to prevent, observed or possible, excessive fluctuations. Taking the developments in balance of payments and currency substitution issues into account, the Central Bank may also continue to holding foreign currency purchase auctions to accumulate reserves within a program to be announced in advance.

Setting of the incomes policy in harmony with the inflation target is important for bringing the gains of anti-inflationary efforts to a permanent situation. In this context, the public sector wage policy will be maintained within a forward looking indexation framework in the 2007 PEP period.

2.2.1. Real Sector

The high growth performance recorded in the Turkish economy in recent years is expected to continue in the forthcoming period. However, in parallel with the increasing uncertainty in the international markets and concomitant downward adjustment for world growth forecasts, it is projected that the average annual growth rate in the 2007 PEP period will be less than that of the period of 2002-2006.

Exports and private sector investments are expected to be the most important driving factors of the GDP growth in the period of 2007 PEP. Despite a mild slowdown in the world demand, high export performance is expected to be sustained as a result of productivity increase recorded in the industry sector, maintaining the diversity of export markets attained in recent periods, and supporting the exports by new investments.

Evaluating the developments in domestic demand, the trends arising in 2006 are expected to continue in the period of 2007 PEP. In this period, the domestic demand is not foreseen to be as strong as it was in the period of 2002-2005 due to the expectation that YTL will not appreciate further. Similarly, compared to the period of 2002-2005, more restricted import demand growth is expected. Thereby, foreign demand is anticipated to make positive contribution to growth in the period of 2008-2010.

In the period of 2007 PEP, it is expected that the partial productivity per worker in production will continue to increase. However, in this period compared to the period of 2002-2005 in which restricted increase in employment was created, productivity increases are expected to be lower. In the period of 2007 PEP, it is forecasted that a significant number of new employment will be created particularly in the non-agricultural sectors.

Demand Components of Growth

The economic growth was realized at a high level of 6.1 per cent in 2006. On the other hand, due to the financial fluctuations in the international markets in the second quarter of the year, an increase in risk premium of Turkey occurred, and accordingly, the borrowing interest rates moved upwards. Negative impacts of these developments were observed particularly in the first half of 2007.

Scrutinizing the national income figures for 2007, it is observed that the growth rate was realized as 5.3 per cent in the first half of 2007. In this period, while the contribution of the domestic demand to growth decreased significantly, the foreign demand made positive contribution to growth. The domestic final demand increased by 3.1 per cent and its contribution to growth was realized as 3.3 points, in the first half of 2007.

In the second quarter of 2007, in spite of the real exchange rate appreciation of 15.9 per cent, the domestic demand failed to gain momentum. In this development, uncertainties brought by general elections held in July 2007 and rising interest rates in 2006 were effective. In the first half of 2007, while private consumption expenditures increased by 0.8 per cent, private sector fixed capital investment expenditures showed a limited increase of 4.9 per cent. Similarly, the private sector machinery and equipment investments, which rose by 13.9 per cent in 2006, increased only by 1.5 per cent in the first half of 2007. On the other hand, the growth rate of public sector consumption and investment expenditures were higher than the economic growth rate in the first half of 2007 due to the general elections.

Table 2. 7: Demand Components of Growth

(Percentage Changes, at 1987 Prices)

		Forecast				
	2006	**2007**	**2008**	**2009**	**2010**	**2008-2010 Average**
Total Consumption Expenditure	5.6	4.2	4.6	4.5	4.6	4.6
Private	5.2	4.0	4.8	4.7	5.0	4.8
Public	9.6	6.5	3.4	2.7	1.3	2.5
Total Investment Expenditure	5.5	7.4	5.3	5.5	5.5	5.4
Gross Fixed Capital Formation	14.0	6.5	5.7	7.4	6.4	6.5
Private Fixed Investment	17.4	7.4	7.5	7.5	7.5	7.5
Public Fixed Investment	-0.2	2.3	-3.9	7.2	0.2	1.1
Change in Inventories (1)	-2.1	0.5	0.1	-0.4	-0.2	-0.2
Exports of Goods and Services	8.5	11.2	8.3	8.5	8.5	8.4
Imports of Goods and Services	7.1	10.7	6.7	6.7	6.9	6.7
Domestic Demand	5.6	5.2	4.8	4.8	4.9	4.8
Domestic Final Demand	8.0	4.9	4.9	5.3	5.2	5.2
Gross Domestic Product	6.1	5.0	5.5	5.7	5.7	5.6

(1) Contribution to GDP growth.
Source: SPO, TURKSTAT

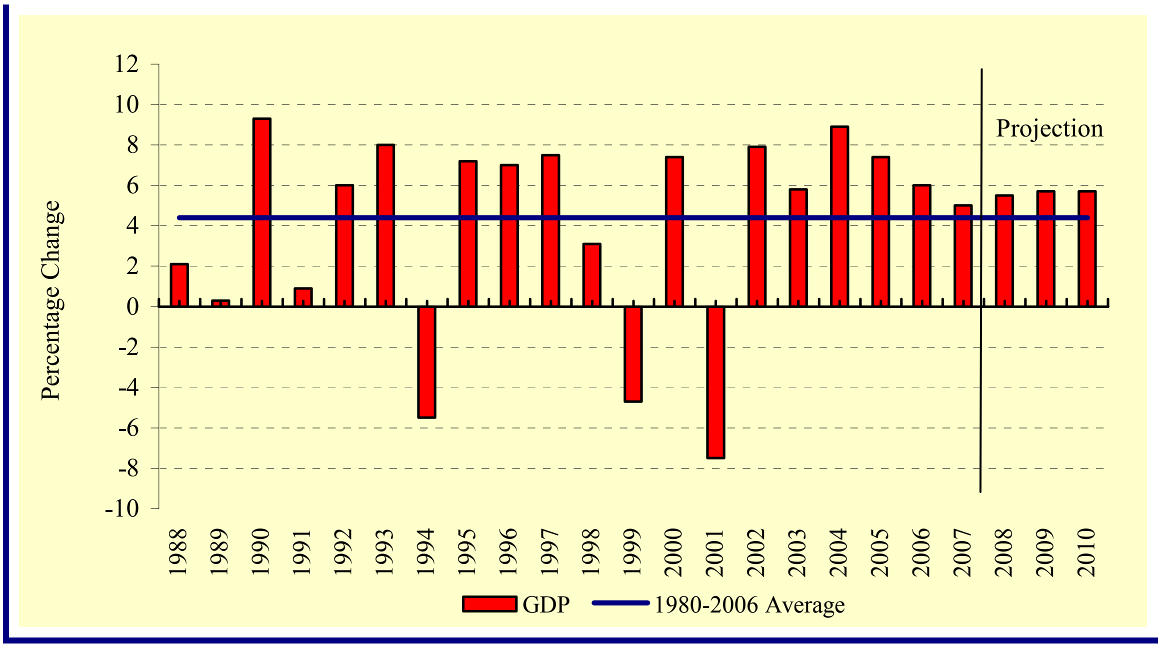
The contribution of the external demand to growth reached positive levels in 2006, and continued the similar trend in 2007, and became the main determinant of growth in the first half of 2007 despite appreciation of the reel exchange rate. In this context, the external demand's contribution to growth was realized as 2.6 points in the first half of 2007.

In the second half of 2007, the uncertainties related to general election disappeared and domestic demand displayed an increasing trend. Automotive sales, which decreased by 29.1 per cent in the second quarter of 2007 compared to the same period of the previous year, increased by

13.2 per cent in the third quarter. On the other hand, the increase in imports of capital goods was realized as 15 per cent in the third quarter of 2007. In this context, private sector consumption and investment expenditures are expected to rise in the second half of the year.

As a result of these developments, private sector consumption and private fixed capital investment expenditures are estimated to increase by 4 per cent and 7.4 per cent, respectively, in 2007. Taking into account the strengthening trend of domestic demand and the anticipated appreciation of the real exchange rate in the second half of 2007, imports of goods and services are expected to increase higher in 2007 compared to the previous year, and to increase by 10.7 per cent. On the other hand, as a result of the high export performance attained, exports of goods and services are expected to increase by 11.2 per cent in 2007. It is forecasted that public investment and consumption expenditures will slow down in the second half of 2007, and rise by 2.3 and 6.5 per cent respectively, in the entire year of 2007. Thereby, in line with the 2006 PEP, growth rate of GDP in 2007 is estimated as 5 per cent in the 2007 PEP. When the demand components of the 2007 PEP are compared with those of the 2006 PEP, it is observed that consumption, investment and import growth forecasts are slightly higher for 2007.

Figure 2. 3: GDP Growth Rate



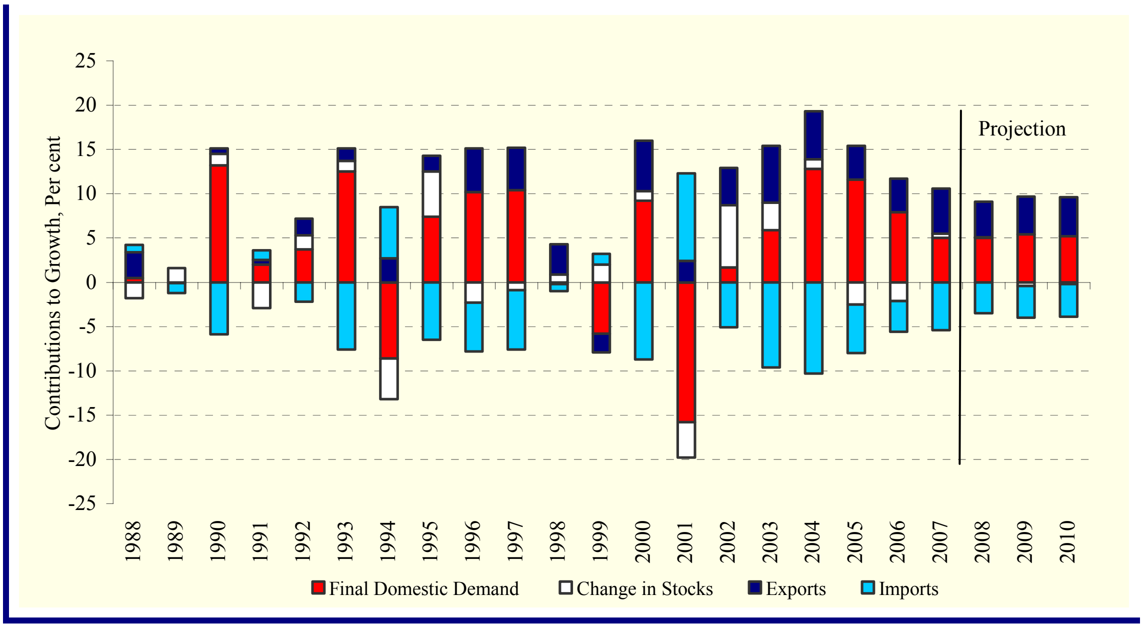
It is expected that the GDP growth will be around its potential and growth rate of GDP will realize as 5.6 per cent annually on average in the period of 2008-2010. Growth is expected to be private sector investments and exports driven in the 2007 PEP period, as it was in the 2006 PEP period, and the external demand will have a positive contribution to growth.

Tight monetary and fiscal policies implementation will be continued decisively in the 2008-2010 period. Within the scope of the expectations that the real exchange rate appreciation trend observed since 2002 will end in the 2007 PEP period, the increase in private sector consumption expenditures is forecasted to be below economic growth rate. In this context, the increase in private sector consumption expenditures is expected to be 4.8 per cent annually on average.

Expected decrease in debt stock and interest rates as a result of tight fiscal policy to be implemented, is estimated to have a positive impact on private fixed capital investments in the 2008-2010 period, and the investments growth will be at 7.5 per cent annually on average, well above the growth rate. On the other hand, forecasts for the annual average increase for public investments and expenditures in this period are 1.1 per cent and 2.5 per cent, respectively.

In the 2007 PEP period, under the assumptions that product variety will rise, reaching to new markets will continue, the increase in productivity will sustain and real exchange rate appreciation will not continue, exports of goods and services will maintain its high performance. On the other hand, in parallel with the increase in investments and exports in particular, it is forecasted that the share of capital goods and intermediate goods imports in total imports of goods and services will be high and the growth rate of imports will be realized as 6.8 per cent annually on average. In this context, it is estimated that the contribution of external demand to growth will be 0.5 point, 0.7 point and 0.6 point for the years of 2008, 2009 and 2010, respectively.

Figure 2. 4: Contributions to GDP Growth



Investment-Savings Balance

In 2007, any change is not expected in the share of private sector fixed capital investments in GDP compared to 2006. The most important factor behind the non-increasing of share of private sector investments is the continuance of the high levels of real interest rates. In the period of 2008-2010, on the other hand, in parallel with the decline in real interest rates, it is expected that the share of private sector investments will increase and reach 18.1 per cent in 2010.

Table 2. 8: Total Savings-Investment Balance

(Per cent of GDP, at Current Prices)

	Realization	Forecast			
	2006	**2007**	**2008**	**2009**	**2010**
Total Investment	24.9	25.0	24.7	24.4	24.0
Fixed Capital Formation	21.9	21.7	21.5	21.8	21.8
Public	4.5	4.2	3.8	3.9	3.7
Private	17.5	17.5	17.7	18.0	18.1
Change in Stocks	3.0	3.3	3.2	2.6	2.2
Total Savings	24.9	25.0	24.7	24.4	24.0
Domestic Savings	16.9	17.9	17.5	17.5	17.5
Public	5.9	2.5	2.7	3.6	4.1
Private	11.0	15.4	14.8	13.9	13.4
Foreign Savings	8.0	7.1	7.2	6.9	6.5

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

The share of public fixed capital investments in GDP is estimated to be 4.2 per cent in 2007. However, at the end of the 2007 PEP period, this share is expected to decrease to 3.7 per cent with the effect of privatization of some of the SEEs. In this context, the ratio of total investments to GDP is predicted to decline from 24.9 per cent in 2006 to 24 per cent in 2010.

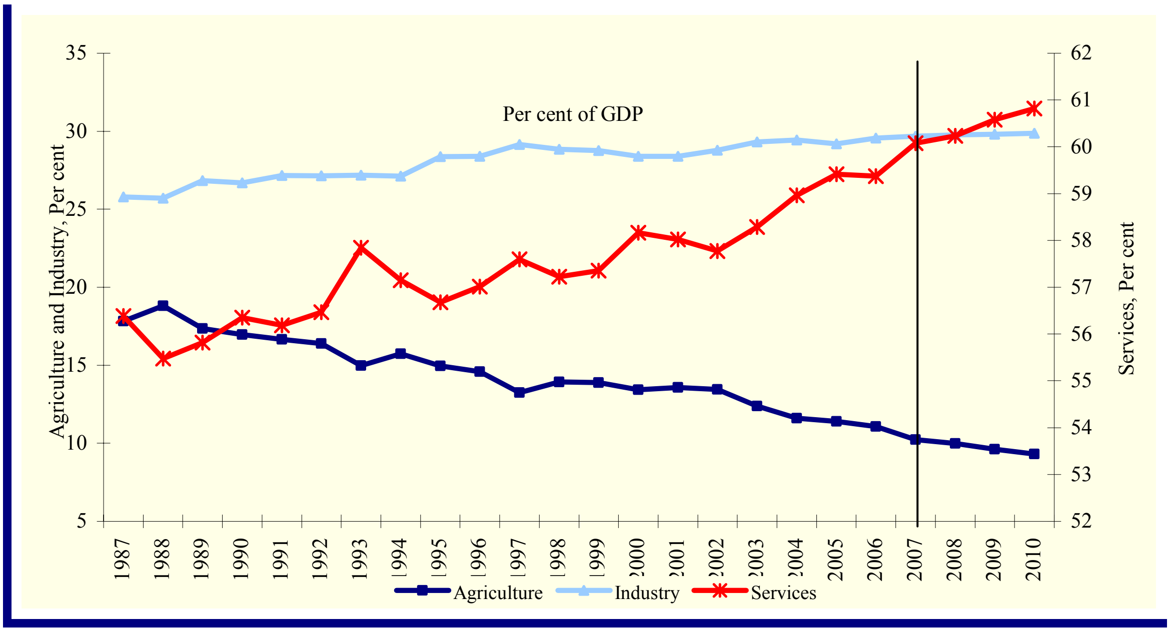
The ratio of the foreign savings to GDP, which was 8 per cent in 2006, is expected to decrease to 6.5 per cent at the end of the 2007 PEP period. However, the ratio of domestic savings to GDP is expected to increase from 16.9 per cent in 2006 to 17.5 per cent in 2010.

From 2007 onwards, it is anticipated that the share of public disposable income and public savings in GDP will significantly rise by continuing tight fiscal policy implementation. As a result of this, with the effect of the decline in the ratio of private disposable income to GDP, the ratio of private savings to GDP is forecasted to recede from 15.4 per cent in 2007 to 13.4 per cent at the end of the 2007 PEP period.

GDP Growth by Sector

The ratio of value added in agriculture sector to GDP, which was 11.1 per cent in 2006, is expected to recede to 10.2 per cent in 2007 due to the drought. At the end of the PEP period, it is predicted that the share of agriculture sector in GDP will decline to 9.3 per cent, parallel to its historical downward trend.

Figure 2. 5: Production by Sectors



In the period of 2008-2010, private fixed capital investments and high export performance are expected to become the factors supporting the industry sector growth. In this period, it is anticipated that the growth rate of the industry sector will be higher than the growth rate of GDP. In this context, the share of the value added of the industry sector in GDP, which was 29.6 per cent in 2006, is estimated to be 29.9 per cent in 2010. It is expected that the value added of the services sector growth will be 5.9 per cent annually on average and that the services sector's share in GDP will reach 60.8 per cent in 2010.

Table 2. 9: Value Added Growth by Sectors

(Percentage Change, at 1987 Prices)

	Realization	Forecast				
	2006	2007	2008	2009	2010	2008-2010 Average
Agriculture	2.9	-3.0	3.0	1.6	2.5	2.5
Industry	7.4	5.5	5.7	5.8	5.9	5.8
Services	6.1	6.2	5.9	5.9	6.0	5.9
GDP	6.1	5.0	5.5	5.7	5.7	5.6

Sources of Growth

In 2006, the increase in employment was realized at low levels and the contribution of employment to growth stayed at a limited level. Therefore, the main determinants of 2006 growth were increases in the physical capital stock and the total factor productivity. In 2007, the facts that the growth elasticity of employment reaches above the its long term value and that high increases in the private sector fixed capital investments accelerate the physical capital stock, give the signal that the contribution of these two production factors to the economic growth will be significantly larger.

Table 2. 10: Growth Rates of Factors of Production

(Per cent)

Period	GDP	Capital Stock	Employment	TFP
2005	7.4	2.7	1.2	5.5
2006	6.1	4.3	1.3	3.5
2007	5.0	5.4	2.8	1.1
2008	5.5	5.2	2.1	2.1
2009	5.7	5.3	2.1	2.2
2010	5.7	5.4	1.9	2.2
2008-2010	5.6	5.3	2.0	2.2

The growth rate of physical capital stock in 2007 is expected to continue in the 2008-2010 period as well. On the other hand, the employment increase, which is expected to be at 2.8 per cent in 2007, is foreseen to decrease slightly and to be realized as 2 per cent in the PEP period. As a result of these projections, the GDP growth in the 2008-2010 period is expected to be supported mainly by the increases in physical capital stock and total factor productivity. On the other hand, the forecast that the contribution of the employment increase to growth will be higher than the 2006 PEP forecasts indicates that regarding the contribution of production factors to growth, a more balanced structure will arise. In this context, it is estimated that the contributions of capital stock, total factor productivity and employment increases to growth will be 39.6 per cent, 39.1 per cent and 21.3 per cent, respectively, annually on average.

Table 2. 11: Contribution to Growth by Factors of Production

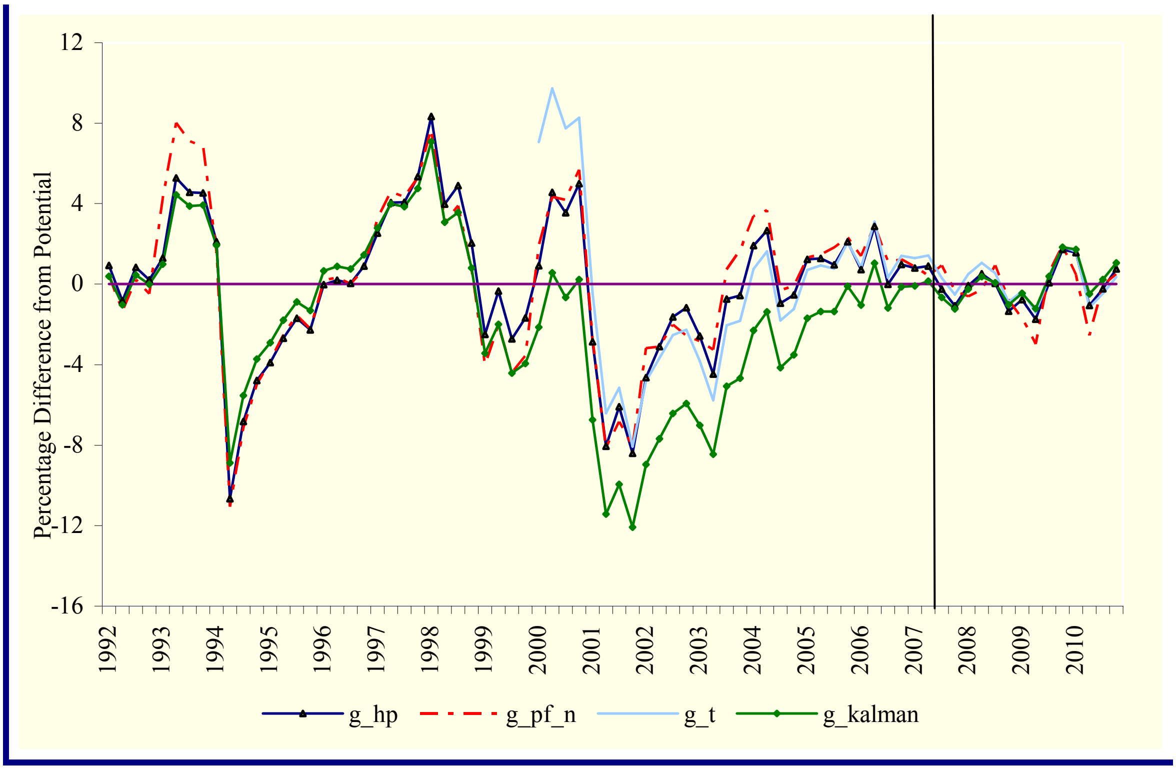
(Per cent)

Period	Capital Accumulation	Employment Increase	TFP Increase
2005	15.8	9.5	74.7
2006	30.0	12.5	57.4
2007	45.3	32.7	22.0
2008	39.5	22.3	38.2
2009	39.0	22.1	39.0
2010	40.3	19.6	40.1
2008-2010	39.6	21.3	39.1

Potential Output

In the 2007 PEP period, the output gap estimates obtained by alternative methods indicate that the level of projected production will be around the potential output. Output gap series calculated based on four different methods, namely the linear method, the Hodrick-Prescott method, the production function method and the Kalman filter method are presented in Figure 2.6.

Figure 2. 6: Output Gap



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

Besides the linear method[3], when the output gap estimates calculated by the production function method, Hodrick-Prescott method and Kalman filter method are examined, it is observed that the values of output gap move similarly in 2008-2010 period. All three methods indicate that the production level displays small fluctuations around the potential, however there is no sign of serious overheating in the economy. Therefore, the projected growth path is not expected to have any inflationary impact in the 2007 PEP period.

Labour Market

In 2006, while employment increased by 4.4 per cent in the non-agricultural sectors, a 6.2 per cent contraction was experienced in the agricultural employment, and the overall employment increase in the economy remained at 1.3 per cent.

Analyzing the figures for the year 2007, it is observed that the contraction trend in agricultural employment had a temporary stall, and that there was a strong employment increase in the non-agricultural sectors. Consequently, the agricultural sector employment is projected to preserve its 2006 levels in 2007, and there will be an increase of 3.8 per cent in the non-agricultural employment. Thereby, the total employment increase in 2007 is expected to follow a stronger trend compared to recent years and be realized as 2.8 per cent.

Another important change observed in 2007 is the upward movement in the labour force participation rate. The labour force participation rate, which had shown a downward trend in recent years, is expected to increase about 0.4 points in 2007. As a result of these developments, the unemployment rate is expected to recede by 0.2 points in 2007, and realize at the level of 9.7 per cent.

[3] Considering the structural break experienced in the Turkish economy from 2000 onwards, the output gap estimates are calculated by the linear method starting from the year 2000.

Table 2. 12: Developments in the Labour Market

(15+ Age, Thousands of Persons)

	Realization	Forecast			
	2006	2007	2008	2009	2010
Working Age Population	51,668	52,532	53,441	54,359	55,279
Labour Force Participation Rate (Per cent)	48.0	48.4	48.6	48.8	48.9
Labour Force	24,776	25,413	25,960	26,515	27,008
Employment	22,330	22,955	23,436	23,933	24,382
Agriculture	6,088	6,096	6,021	5,934	5,819
Non-agricultural	16,242	16,859	17,414	17,999	18,564
Unemployed	2,446	2,459	2,524	2,582	2,625
Employment Increase (Per cent)	1.3	2.8	2.1	2.1	1.9
Agriculture	-6.2	0.1	-1.2	-1.5	-1.9
Non-agricultural	4.4	3.8	3.3	3.4	3.1
Employment Rate (Per cent)	43.2	43.7	43.9	44.0	44.1
Unemployment Rate (Per cent)	9.9	9.7	9.7	9.7	9.7
Employment by Sectors (Per cent)					
Agriculture	27.3	26.6	25.7	24.8	23.9
Non-agricultural	72.7	73.4	74.3	75.2	76.1

In the period of 2008-2010, it is expected that the employment in the agricultural sector will continue to decrease, and that there will be strong employment increases in the non-agricultural sectors. In this period, the employment in the non-agricultural sectors is projected to increase by 3.3 per cent annually on average. Despite expected employment contraction in the agricultural sector, total employment is expected to increase by around 1.4 million in the 2007 PEP period. As a result, the employment rate would increase, though moderately.

In parallel with the expected increases in employment, it is anticipated that the number of discouraged workers, who are not participating in the labour force due to being hopeless of finding a job, will decrease and the labour force participation rate will increase slightly. The unemployment rate in the 2007 PEP period is forecasted to remain at 2007 levels, with the effect of the increase in the labour force participation rate.

2.2.2. Inflation, Monetary and Exchange Rate Policies

Establishing price stability at a low level of inflation will continue to be the main objective of the monetary policy in the 2007 PEP period also. In this framework, the Central Bank will continue to implement the explicit inflation targeting policy that was started at the beginning of 2006. In this context, the Central Bank will use short-term interest rates as the main policy instrument, to direct expectations and affect funding costs. The Central Bank will continue to focus on the medium term inflation outlook when formulating monetary policy decisions. An inflation target of about 4 per cent in the medium term has been deemed appropriate, considering the structural transformation in the economy, transforming from high inflation to low inflation and the EU convergence process. In this context, while the inflation targets for 2007 and 2008 were kept as 4 per cent, the target for 2009 was announced as 4 per cent as well.

Table 2. 13: Price Targets and Exchange Rate Policies

(Percentage Change)

	2007	2008	2009	2010
CPI(1)	4.0	4.0	4.0	....(2)
GDP Deflator(3)	7.2	4.9	4.4	3.9

(1) End-year target.
(2) CBRT has not set the target for 2010 yet.
(3) Projections for average annual increase.

As observed in monetary policy practices in 2006, the Central Bank responds to the deviation of inflation from the medium term targets, not to the temporary fluctuations in inflation. In the October 2007 Inflation Report, the Central Bank perceives it possible to achieve the 4 per cent target by the end of 2008. In the scope of the mentioned report, at 70 per cent probability inflation is forecasted to be between 2.5 to 5.7 per cent (mid-point 4.1) at the end of 2008, and between 1.7 to 5.5 per cent (mid-point 3.6) in the third quarter of 2009, under the assumption that the policy interest rates are to be lowered moderately in the rest of 2007 and first months of 2008 and held constant for a while afterwards.

The aforesaid forecasts are made under the assumptions that the support provided by the demand conditions to the decline of inflation will continue in the medium term, food prices will show a progressive correction tendency, oil prices will realize around 70 dollars, and the risk premium will remain fixed around its recent levels. However, if any deviation from the mentioned assumptions occurs, since changes in the framework outlined for the inflation outlook will be unavoidable, the Central Bank may revise its stance.

In order to attain the medium term inflation targets, it is important to maintain fiscal discipline, to continue the incomes policy consistent with the inflation targets and decisive implementation of structural reforms, in addition to the monetary policy.

In the forthcoming period, the floating exchange rate regime implementation will be continued. Unless extraordinary changes emerge in foreign exchange liquidity conditions, the Central Bank will continue to hold foreign currency purchase auctions aiming reserve accumulation within the disclosed program. On the other hand, the CBRT may, with prior notice, suspend the auctions for a short or a long term when there is excessive volatility in exchange rates observed due to a serious exogenous shock or unforeseen extraordinary developments. Meanwhile, the volatility in exchange rates will continue to be closely monitored by the Central Bank and in the event of excessive volatility that might occur in exchange rates, direct intervention to the markets will be realized.

Box 2. 1: Fluctuations in International Financial Markets and the Impacts on Turkish Financial System

After a high growth period ongoing since 2002, the world economy has entered a period of increased uncertainties due to financial turbulence experienced in developed economies in the second half of 2007.

Signals of contraction starting in the US housing market and concomitant losses in the value of subprime mortgage backed securities caused the tension in developed financial markets to increase in the second half of 2007. Especially in July and August, the liquidity crisis that deepened upon the shut-off of credit facilities among the large financial institutions could only be overcome by intensive interventions of the FED and the ECB. On the other hand, despite the financial turbulence and liquidity crisis in developed countries, as a result of FED's and ECB's intensive efforts, sudden capital outflows were not experienced in the developing countries.

In this context, FED provided significant liquidity for financial institutions by lowering the discount rates in the second half of August and ECB injected considerable amounts of liquidity to financial markets via open market operations. While the liquidity crisis was softened in the second half of August, the facts that the deposits were dissolved in a medium scale bank in the United Kingdom (UK), and the UK Central Bank consequently guaranteed all liabilities of this bank were not enough to alleviate concerns about the sustainability of financial stability in international markets.

In order to eliminate concerns about the global financial stability, in September and October, FED lowered the policy interest rates, which had not been changed for more than four years, by 75 basis points to 4.5 per cent.

While the initial shock of the financial turbulence that started in July was left behind, the fact that the losses in the balance sheets of international financial institutions were realized more than expectations in the early weeks of November, increased doubts on depth and duration of the crisis.

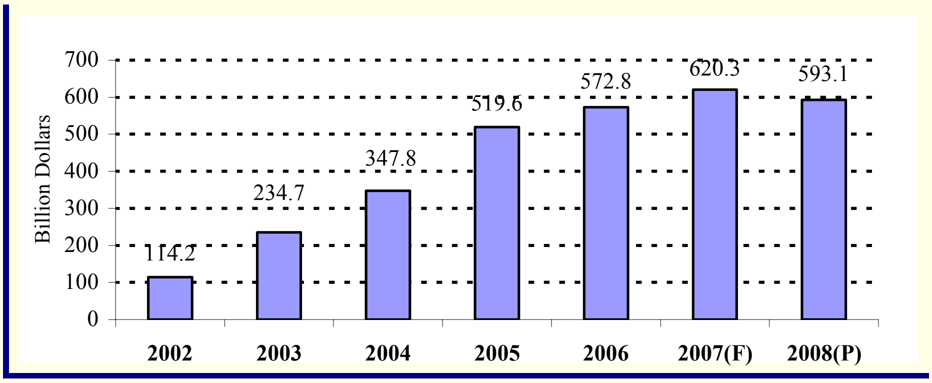
Despite this financial turbulence experienced in developed countries, the developing countries were not much affected from this turbulence contrary to past experience. As a matter of fact, according to IMF forecasts, China and India are expected to make high rates of contribution to world economic growth in 2007. In 2008, it is projected that the developing economies will maintain their strong growth trends. It is considered that these developments are reflections of the strong macroeconomic policies implemented in developing economies in early 2000's. Furthermore, the view that the world is now in the process of decoupling, and that adverse developments in the US economy will not negatively affect the growth of developing economies is being discussed.

Since the year of 2002, the net capital inflows directing to developing countries and reaching historically high levels due to the favorable environment created by the global liquidity conditions are expected to reach a new peak in 2007.

Expectations, regarding the increase in vulnerabilities of the financial systems of the developing economies and the decrease in risk appetite will cause tightening in the global liquidity conditions, are getting stronger. Therefore, the year of

2008 will be a period, in which economies like Turkey that need capital inflows to finance current account deficit will closely follow international developments. However, initial figures show that there will be a considerable amount of net capital inflow to developing countries in 2008 as well.

Figure 1: Net Capital Inflows to Developing Countries

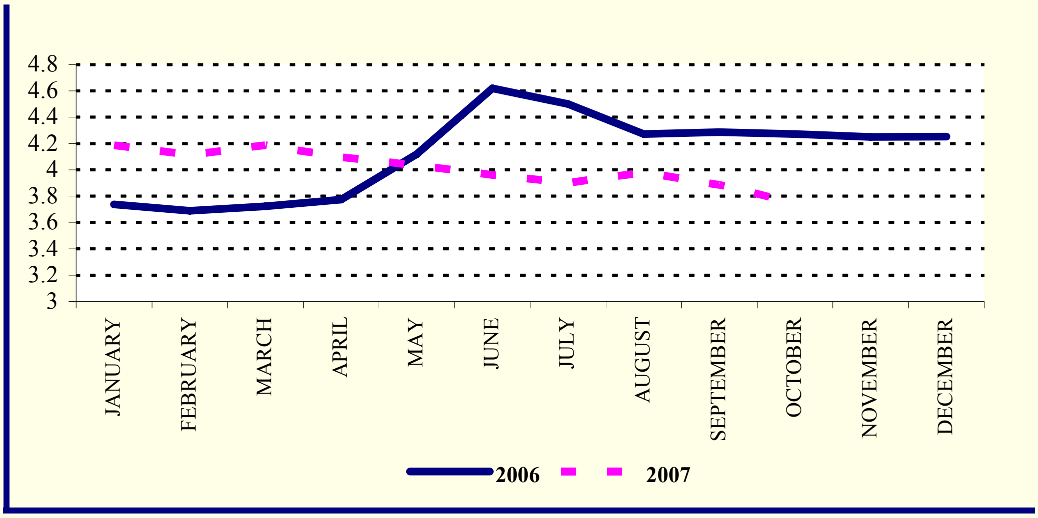


F: Realization Forecast, P: Projection
Source: The Institute of International Finance, October 2007

While the expectations regarding the changes in global liquidity conditions are of significant concern for the Turkish economy in the forthcoming period, it was observed that the Turkish financial system maintained its strong position vis-à-vis the international financial turbulence experienced in July.

Contrary to the financial volatility experienced in the first half of 2006, it is observed that the financial fluctuation in the second half of 2007 did not have any negative impact on the exchange rates and capital markets, and YTL continued to appreciate. The cautious stance of the monetary policy was effective in preventing tension to increase in the markets.

Figure 2: Developments in Exchange Rate Basket (1 Dollar+1.5 Euros)



Source: CBRT

However, signals that the liquidity conditions in the international markets will become tighter increase the importance of harmony between the monetary and fiscal policies in designing macro policies. In this context, the continuation of the fiscal discipline maintained in the past five years will be one of the most important anchors against fluctuations in financial markets. Besides, the continuation of the monetary policy framework without any change and thereby the continuation of the Central Bank's cautious stance in interest rate policy will be the other important anchor. On the other hand, structural reforms that have been implemented decisively in parallel with the EU accession process for the last five years were effective in strengthening the economic structure and thereby reducing macroeconomic vulnerability. In this context, a decisive continuation of structural reforms in the forthcoming period will be an important factor for maintaining economic stability and protecting the Turkish economy's strength against external shocks.

Furthermore, agents actively involving in economic administration have determination to monitor figures on dimensions and depth of international financial turbulence and consequently implement proactive policies in a coordinated manner.

2.2.3. Balance of Payments

Current Account

The increase in current account deficit on dollar basis, which was realized as 45.4 per cent in 2006, is estimated to be around 10.7 per cent in 2007. The favourable rise in terms of trade and the increase in tourism revenues are expected to be effective in the slowdown of the current account deficit increase in 2007.

Within the framework of the export promotion strategy, in recent years, substantial rise in exports has been recorded in the Turkish economy. Thus, the annual average increase in exports was realized as 22.2 per cent in the 2002-2006 period. This increase is owed to systematic promotion and marketing activities as well as important advances in ensuring macroeconomic stability, and productivity increases in tradable sectors. Furthermore, due to the fact that the share of EU countries in total exports is significant, the downward movement of euro/dollar parity is another factor that supported export increases in the 2002-2006 period. In addition, the favourable trend in the world output was the determinant factor of sustaining high export performance.

The high export performance continued in the first nine months of 2007, and the exports increased by 24.1 per cent. Exports are expected to increase by 21.6 per cent in the entire year, and reach 104 billion dollars in 2007.

The US economy is estimated not to be able to keep its past growth trend in years 2007 and 2008 with the effect of the contraction began in the US housing markets in 2007. However, the EU-25 growth, which was 3 per cent in 2006, is expected to be 2.9 per cent and 2.4 per cent in 2007 and 2008, respectively. Thereby, it is foreseen that exports will be one of the most important source of growth during the 2007 PEP period under the assumption that there will be no significant change in external demand conditions of Turkey. In this period, productivity increase, continuation of macroeconomic stability and implementation of structural policies targeting export increases will be the factors supporting the export performance. Furthermore, efforts for increasing export market diversification to alleviate regional dependency in exports and to create sustainable exports infrastructure have been continuing. Thus, while the number of countries that Turkey has an export value higher than 1 billion dollars was 14 in 2004, it reached 19 in 2006.

The exports are expected to be 117 billion dollars in 2008, reach 132 billion dollars in 2009 and 149.2 billion dollars in 2010.

The imports increased by 27.5 per cent annually on average in the 2002-2006 period. The increase in domestic demand, strong YTL, the necessity of imports of intermediate goods for high level of production activities, and high increases in oil prices could be considered as the most important determinants of this increase.

During the January-September period of 2007, imports realized as 121.5 billion dollars by increasing 18.6 per cent compared to the same period of the previous year. Parallel to this increase, it is estimated that the imports will increase by 18.9 per cent in 2007, and reach 166 billion dollars by the end of 2007.

In the 2007 PEP period, it is projected that the Turkish economy will grow by 5.6 per cent annually on average. Along with this growth, the import demand is projected to be 182 billion dollars in 2008, 198.4 billion dollars in 2009 and 217 billion dollars in 2010. In this context, the share of trade volume in GDP, which was 55.9 per cent in 2006, is expected to rise to 61.5 per cent in 2010.

Tourism revenues increased by 6.5 per cent in the first nine months of 2007 and rose to 14.6 billion dollars. In the first nine months of 2006, 18.4 million tourists visited Turkey, and this figure reached 21.6 million in the same period of 2007. In the light of these developments, it is expected that at the end of 2007, tourism revenues will be realized as 18.6 billion dollars. At the end of the 2007 PEP period, it is estimated that tourism revenues will reach 22 billion dollars.

In this framework, the current account deficit, which is expected to be 36.4 billion dollars in 2007, is estimated to reach 40.7 billion dollars at the end of 2010. It is foreseen that this increase in the current account deficit will be mainly affected from the deterioration in the income balance resulted from interest expenditures. The ratio of the current account deficit to GDP is expected to improve during the period and recede to 6.8 per cent in 2010, from 7.4 per cent in 2007.

Table 2. 14: Balance of Payments Forecasts

(In Billion Dollars)

	Realization			Forecast			
	2004	2005	2006	2007	2008	2009	2010
Current Account	-15.6	-22.6	-32.9	-36.4	-39.2	-39.8	-40.7
Balance on Goods	-23.9	-33.5	-41.3	-45.5	-46.9	-46.8	-46.7
Total Exports	67.0	76.9	91.9	111.8	125.5	141.3	159.2
Exports (fob)	63.2	73.5	85.5	104.0	117.0	132.0	149.2
Total Imports	-90.9	-110.5	-133.3	-157.3	-172.4	-188.1	-205.9
Imports (cif)	-97.5	-116.8	-139.6	-166.0	-182.0	-198.4	-217.0
Balance on Services	12.8	15.3	13.4	14.4	15.2	16.2	16.9
Credit	22.9	26.6	24.5	28.1	29.8	31.8	33.9
Tourism	15.9	18.2	16.9	18.6	19.6	20.7	22.0
Debit	-10.1	-11.4	-11.1	-13.7	-14.6	-15.6	-17.0
Balance on Income	-5.6	-5.8	-6.6	-7.0	-9.3	-11.2	-13.1
Credit	2.7	3.7	4.5	6.1	6.4	7.4	8.4
Debit	-8.3	-9.5	-11.1	-13.1	-15.7	-18.5	-21.5
Current Transfers	1.1	1.5	1.7	1.7	1.8	2.0	2.2
Workers' Remittances	0.8	0.9	1.1	1.1	1.0	1.1	1.2
Capital and Financial Account	13.4	20.4	35.1	33.6	39.2	39.8	40.7
Financial Account (Including Reserves)	13.4	20.4	35.1	33.6	39.2	39.8	40.7
Direct Investment	2.0	8.9	19.0	16.2	16.5	17.1	19.0
Direct Investment in Turkey	2.9	10.0	20.0	18.2	18.5	19.1	21.0
Direct Investment Abroad	-0.9	-1.1	-1.0	-2.0	-2.0	-2.0	-2.0
Portfolio Investments	8.0	13.4	7.4	4.9	2.7	2.8	4.0
Assets	-1.4	-1.2	-4.0	-3.7	-3.5	-3.9	-3.6
Liabilities	9.4	14.7	11.4	8.6	6.1	6.6	7.6
Equity Securities	1.4	5.7	1.9	5.7	2.0	3.0	3.5
Debt Securities	8.0	9.0	9.5	2.9	4.1	3.6	4.1
Other Investments	4.2	15.9	14.8	21.4	23.9	20.1	20.1
Assets	-7.0	0.3	-12.4	-1.9	0.9	-1.0	-1.0
Liabilities	11.1	15.6	27.2	23.2	23.0	21.0	21.1
Monetary Authority	-4.6	-3.7	-1.3	-1.4	-1.8	0.0	0.0
General Government	-0.3	-4.6	-5.2	-2.5	2.1	-2.0	-2.4
Banks and Other Sectors	16.0	23.9	33.7	27.1	22.7	23.0	23.5
Official Reserves	-0.8	-17.8	-6.1	-8.8	-3.8	-0.2	-2.5
Net Errors and Omissions	2.2	2.2	-2.3	2.8	0.0	0.0	0.0

Source: SPO, CBRT

Capital and Financial Account

As a result of the liquidity abundance in the global economy in recent years, macroeconomic stability attained and the improvement of the investment environment, significant amount of capital inflows to Turkey has been recorded. In 2006 PEP, the financial account for 2006 had been estimated as 31.9 billion dollars, but it realized above the projections and recorded as 35.1 billion dollars. High volume of capital inflows is estimated to continue in the 2007 PEP period.

Direct investments were realized as 13.5 billion dollars in the first nine months of 2007. It is expected that direct investments will be 16.2 billion dollars by the end of 2007, and 16.5 billion dollars by the end of 2008. In the period of 2005-2007, foreign direct investment was mostly realized in the form of privatization and M&A, but it is estimated that share of greenfield investments in the foreign direct investments will increase in 2008. The foreign direct investments are foreseen to increase in 2009 and 2010, and to reach 17.1 billion dollars in 2009 and 19 billion dollars in 2010.

Net portfolio investments, estimated to be 5.6 billion dollars in 2006 PEP, were realized as 7.4 billion dollars due to the rising demand for the government domestic borrowing instruments. In 2007 and 2008, it is expected that net portfolio investments will decrease to 4.9 billion dollars and 2.7 billion dollars, respectively. This trend is foreseen to reverse and net portfolio investment inflows are estimated to be 2.8 billion dollars and 4 billion dollars respectively, in 2009 and 2010.

In the 2007 PEP period, other investment item is expected to be in high levels. Other investments, which were 14.8 billion dollars in 2006, are estimated to reach 21.4 billion dollars in 2007 and by maintaining its level during the 2007 PEP period, to realize as 20.1 billion dollars in 2010.

As a result of these developments, it is foreseen that there will be no problem in financing the current account deficit, though net 5.8 billion dollars repayment to the IMF in 2008-2010 period. Furthermore, the capital inflows are expected to result in reserve build up in the 2007 PEP period. In this context, the reserve accumulation is projected to be as 6.5 billion dollars in the period of 2008-2010.

2.2.4. Main Risks in Projections

The macroeconomic framework projected for the 2007 PEP period may differ because of possible significant changes in the basic assumptions. In this section, factors that may pose risks to realization of macroeconomic projections in the 2007 PEP are discussed.

- An increase in the risk premium resulting from a possible fluctuation in global financial markets might drive up investment costs and particularly cause the private sector machinery-equipment investments and private durable consumption expenditures realize below the projections. As a result, global fluctuations are considered as a demand side external risk factor on growth.

- A significant increase in exports was achieved in Turkish economy in the 2002-2006 period. In this period, favourable external demand condition was one of the significant factors that promoted exports growth. A possible demand contraction in the world economy in the forthcoming period, particularly in EU economies may adversely affect the export performance of Turkey. In the second half of 2007, as a result of the sharp declines in the US housing market, uncertainty in the developed economies has increased and a liquidity contraction has been experienced. As a result of these developments, projections for the world growth deteriorated slightly. The realization of the adverse impact of the turbulence in the second half of 2007 higher than expected on the world growth and particularly on EU growth might pose a risk on Turkey's exports performance.

- The high current account deficits in recent years in the Turkish economy were financed by high amounts of capital inflows. Examining the sources of capital inflows, it is observed that the share of foreign direct investments increased considerably, compared to previous years. The quality of financing of the current account deficit improved with this increase. The foreign direct investments realizing lower than expected might pose a risk on the financing of current account deficit in the forthcoming period.

- As a result of the liquidity abundance in international markets, Turkey has become an important destination for portfolio investments. Possible adverse developments in international liquidity conditions and risk appetite are other risk factors that might adversely affect portfolio investment inflows and make the financing of the current account deficit difficult.

- Possible changes in the global risk appetite and concomitant new fluctuations in the financial markets constitute a significant risk for the medium term inflation outlook. Currently, the prevailing view is that the world economy will not sharply slow down in the medium term and no significant decrease is expected in capital flows into developing countries. However, any corrections that might occur due to global imbalances are still part of the scenarios that might adversely affect particularly developing economies. Resultant excessive fluctuations in foreign exchange markets might pose a threat on the inflation target.
- Both the high levels of crude oil prices and uncertainties in the future path of energy and food prices constitute other external risk factors for the medium and long term inflation outlook.
- In the past five years, strong fiscal policy was supportive in achieving significant results in anti-inflationary process. In this context, it is of utmost importance to support the monetary policy by fiscal policy in order to reach medium and long term inflation targets in the forthcoming period.
- In the forthcoming period, maintaining the tight fiscal and monetary policies decisively, sustaining the implementation of structural reforms determinately is of high importance in order to sustain the high growth performance achieved in the recent period. Possibility of deviations from the targets set for fiscal and monetary policies constitute a significant risk.

3. PUBLIC FINANCES

The fiscal policy continued since 2002 is based on yielding significant primary surplus to reduce the public debt stock, supporting the establishment and sustainability of macroeconomic stability and contributing to anti-inflationary efforts. In the 2007 PEP period, it is aimed to maintain the fiscal discipline and fiscal policy in the same framework.

3.1. General Government Balance and Public Debt

The general government balance is obtained by consolidating the revenues and expenditures of the central government budget, local administrations, non-budgetary funds, social security institutions, unemployment insurance fund and revolving funds. Once the general government balance runs a deficit, the necessary financing is obtained through borrowing.

3.1.1. Fiscal Policy Strategy and Medium Term Objectives

The basic objectives of the fiscal policy are to contribute to sustainability of macroeconomic stability, to support the struggle against inflation and current account deficit, to ensure the continuance of the growth environment achieved in recent years in harmony with the monetary policy and complying with the fiscal discipline, to yield a significant public primary surplus at a considerable rate of the national income with the aim of continuing the process of reducing the ratio of debt stock to the national income.

Fiscal transparency in public finances will be strengthened, and regulations and practices that would violate the fiscal transparency will be avoided. Regulations and practices that would have financial impact will be implemented by taking their short term as well as medium and long term impacts into account.

The public revenues, expenditure and borrowing policies will be implemented effectively in harmony with the aforesaid basic objectives in the period of 2008-2010.

In this context, the public revenues and expenditures policies to be implemented in the 2008-2010 period are as follows:

Revenues Policy

- Public revenues policy will be determined and implemented in harmony with the primary surplus target.
- Fight against the informal economy will be continued effectively in the context of a strategy to be prepared.
- Stability will be the basis in tax policy practices in order to assist market players to make long term economic decisions and increase predictability in taxation.
- Revenue reduction regulations such as exception, exemption and tax discount will be implemented to the extent allowed by means of public finances and by considering the macroeconomic objectives.
- Efforts will be continued to simplify the tax legislation.
- Arising income surpluses will be used in reducing the tax burden especially, transaction taxes and payroll taxes, to the extent allowed by public fiscal balances.
- The pension premium employers' share for the wage earners will be decreased by 5 points starting from 2009.

Expenditures Policy

- In determining wages and salaries in the public sector, the inflation target, public finance balance and the principle of ensuring equity of wages among employees will be taken as basis.
- Restrictions on recruitment to the public sector will be continued with the aim of reducing the over-employment in the public sector.

- Efforts will be continued to rearrange the public personnel system by a comprehensive personnel regime reform.
- Measures will be taken to effectively implement financial management, internal control and internal audit activities in public administrations.
- Works on strategic planning and performance-based budgeting will be continued.
- In order to improve the efficiency in public expenditures, expenditure programs will be revised to cancel those of no longer in priorities.
- Works towards the rationalization of public investments will be continued.
- Investments required by the ongoing efforts to implement policies and priorities introduced in the EU accession process, will be accelerated.
- Works related to increasing the effectiveness of health expenditures in the public sector will be continued. Efforts towards increasing premium collection rates and reducing health expenditures in the social security system will be continued.
- By preserving and sustaining the macroeconomic stability achieved in the recent period, efforts will be continued to alleviate the pressure of interest payments on budget expenditures.

3.1.2. Current Situation and Medium Term Perspective

Current Situation

Developments in the Central Government Budget Revenues and Expenditures

The 2006 budget was prepared and implemented, pursuant to the Law No.5018 Public Financial Management and Control, with a three-year perspective, aiming to reduce the ratio of public debt stock to the national income and yield a high primary surplus.

In 2006, no significant revenue-increasing measures were projected. The most important development in this period that affected budget revenues was one-time revenues. The amount transferred to the budget for the finalized tax, charge, fines, late payment penalty, arrears and GSM treasury share liabilities of the organizations, the management and supervision of which were taken over by the Savings Deposit Insurance Fund (SDIF), reached the level of 1.1 per cent of GDP. Further, a cash sum of 0.2 per cent of GDP, which was obtained from the privatization of Türk Telekom and decided to be transferred to the Treasury, positively affected the budget revenues.

2006 was a year in which important regulations were made in terms of the budget revenues. The Corporate Tax Law was revised and put into effect by taking into account priorities such as simplifying the tax legislation, expanding the tax base and struggling against the informal economy. With the regulation, the corporate tax rate was decreased to 20 per cent from 30 per cent, thereby the tax burden on the corporate earnings were reduced from 44 per cent to 34 per cent. On the other hand, by rearranging income tax rates and the structure of the tariffs, the practice of implementation of different tax rates to wage incomes and non-wage incomes was ended, and the number of tariffs was decreased from 5 to 4. Furthermore, the Law No.5281 that rearranges the equity capital revenue taxation system was put into effect at the beginning of 2006.

As a requirement of the tight fiscal policy implemented in 2006, important measures were taken to control the budget expenditures. In this context, the salaries and wages of public employees were determined in harmony with the inflation target, the number of public servants recruitments was limited to 80 per cent of the positions vacated due to retirement, resignation and death, the extra increase in revenues was decided to be used for contributing to primary surplus except the investment projects in prior, an upper limit was set for the primary expenditures of the central government budget and social security institutions except the transfers to the social security institutions.

Box 3. 1: IMF-Defined Primary Budget Surplus

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

Table: IMF-Defined Primary Budget Surplus

(Per cent of GDP)

	2003	2004	2005	2006
Primary Surplus	**5.12**	**6.08**	**7.71**	**7.17**
Interest Receipts (-)	0.35	0.82	1.74	0.98
Privatization Revenues (-)	0.00	0.00	0.37	0.26
Tax Arrears (+)	0.00	0.00	0.07	0.21
Risk Account (+)	0.26	0.11	0.04	0.04
Revaluation Difference (-)	0.01	0.00	0.00	0.00
SSK and BAĞ-KUR Adjustment (Previous Year Debts) (-)	0.09	0.00	0.00	0.00
SSI Adjustment (Appropriation-Cash Difference) (+)	0.00	0.01	-0.01	-0.01
Dividend Payments of State Banks (-)	0.00	0.26	0.26	0.24
Seigniorage Revenues from Coins (-)	0.00	0.00	0.11	0.02
Telekom Cash Dividend (-)	0.00	0.00	0.00	0.24
IMF-Defined Primary Surplus	**4.93**	**5.13**	**5.34**	**5.67**

Source: SPO

Pursuant to the Law No.5458 regarding the restructuring of social security premium revenues, premium restructuring revenues of 2,959 million YTL in BAĞ-KUR and 714 million YTL in SSK were obtained in 2006, and revenues from restructuring payments of 1,032 million YTL in BAĞ-KUR and 478 million YTL in SSK are expected in 2007.

As a result of these developments, the ratio of the central government expenditures to GDP was 30.9 per cent in 2006, and the ratio of the central government revenues to GDP was realized as 30.1 per cent. The ratio of the budget deficit to GDP was 0.8 per cent with a 0.9 points decrease compared to the previous year, and the primary surplus was above the target and realized as 7.2 per cent of GDP.

As in 2006, in preparation and implementation of the 2007 budget, the basic objective is adopted as to contribute to the sustainability of the public debt stock by yielding a high primary surplus. Furthermore, supporting the macroeconomic objectives takes place as one of the budget objectives.

In 2007, in the scope of the efforts for simplifying the tax system and increasing tax fairness, the tax discount for wage earners was abolished, and it was foreseen to implement the minimum subsistence allowance system from the beginning of 2008. The minimum subsistence allowance envisages leaving a certain portion of the gross minimum wage out of tax for the worker himself, non-working and non-earning spouse and each child for whom he/she is responsible. The minimum subsistence allowance may increase to the full amount of the minimum wage depending on the number of children of the wage earner.

Table 3. 1: Consolidated / Central Government Budget Balance

(Per cent of GDP)

	2004	2005	2006	2007*
Expenditures	32.8	30.0	30.9	32.4
Non-Interest Expenditures	19.6	20.6	22.9	24.0
Personnel Expenditures	6.7	6.5	6.6	6.9
Social Sec. Ins. Government Premium Expenditures	0.9	0.9	0.9	1.6
Goods and Services Purchase Expenditures	2.9	3.0	3.3	2.5
Current Transfers	6.4	7.2	8.6	9.6
Capital Expenditures	1.9	2.0	2.1	1.9
Capital Transfers	0.1	0.3	0.5	0.6
Lending	0.6	0.6	1.0	0.6
Reserve Appropriation	0.0	0.0	0.0	0.4
Interest Payments	13.1	9.4	8.0	8.4
Revenues	25.7	28.3	30.1	29.8
General Budget Revenues	25.3	27.9	29.2	29.0
Tax Revenues	20.9	21.9	23.9	25.0
Non-Tax Revenues	4.1	5.2	4.7	3.5
Capital Revenues	0.0	0.4	0.3	0.4
Grants, Aids and Special Revenues	0.3	0.3	0.4	0.1
Annexed Budget Revenues	0.4	0.5	-	-
Special Budget Administrations Self Revenues	-	-	0.6	0.5
Regulatory and Supervisory Institutions Revenues	-	-	0.2	0.2
Primary Surplus	6.1	7.7	7.2	5.7
IMF-Defined Primary Surplus	5.1	5.3	5.7	5.0
Borrowing Requirement	7.0	1.7	0.8	2.7

Note: The figures given for the years of 2004 and 2005 are based on consolidated budget (excluding shares and funds as well as returns and refunds), figures for the years of 2006 and 2007 are based on central government budget (excluding returns and refunds).

*The figures are initial appropriation.

Source: SPO, Ministry of Finance

In 2007, in order to support the tourism sector and to increase its competitiveness, the VAT rate on some goods and services related to the sector were reduced to 8 per cent valid from 2008.

In order to consolidate the distribution of resources acquired from the taxes charged on lottery games under one single organization, and ensure simplicity in practice, the Law on regulation and distribution of taxes, funds and shares was put into effect.

Financial problems experienced by energy SEEs and the privatization and asset sales revenues realized above the expectations in 2007 were the main factors that affect the budget revenues of the central government. Tax revenues were adversely affected due to the facts that the energy SEEs were unable to meet their financial obligations including taxes, and the SCT revenues could not be realized as expected. However, the revenue of 1.1 per cent of GDP from the cash payment of the remaining instalments of the privatization of Türk Telekom A.Ş. within the year and revenues from real estate sales have been the determining factors on the performance of the budget revenue.

Rapid increase in VAT rebates due to increased exports exerts a negative impact on the tax revenue collection.

The Major Taxpayers Tax Office activated in 2007 in order to enable the Revenue Administration to manage the tax system more effectively.

In 2007, in the context of the policy of increasing investments and employment, by easing the conditions for benefiting from the Law No.5084 on the encouragement of investment and employment, the minimum number of employees was reduced from 30 to 10 to benefit the incentives.

The expenditures made for the Project for Supporting Infrastructure of Villages (KÖY-DES) and the Project for Supporting Infrastructure of Municipalities (BEL-DES) aimed to support infrastructure of villages and municipalities respectively is expected to realize as 0.4 per cent of GDP in 2007.

In order to attain the targets set for the 2007 budget, appropriations for various goods and service purchase and appropriations marked for capital expenditures in the last three months of the year were blocked as of September.

The public personnel wages were determined in compliance with the inflation target in 2007, and in order to alleviate the wage imbalance, higher rates of wage increases were made to lower wage earners. The difference between the wage increase and the realized inflation was reflected to the wages.

The decrease in the revenues due to the restructuring of SSK and BAĞ-KUR premium receivables, and the increase in the insurance expenses because beneficiaries of restructuring retired and the increase in health expenditures due to easier access to health services will cause that the transfers made in 2007 from the budget to the social security institutions will be higher than budget appropriations.

Developments Regarding General Government Revenues and Expenditures

The ratio of general government revenues to GDP, which was 43.9 per cent in 2005, reached the level of 46.2 per cent in 2006. The ratio of the general government tax revenues to GDP in 2006 was realized 0.5 points below the previous year's level. In this decline, as a result of the reduction in rates, the decrease in direct tax collections was effective. In the same period, the share of indirect taxes in the total taxes rose from 67 per cent to 68 per cent. In 2006, significant increases were recorded in the general government non-tax revenues as a percentage of GDP, compared to the previous year, especially with the effect of one-time revenues.

Table 3. 2: Revenues and Expenditures of the General Government-1

(Per cent of GDP)

	2003	2004	2005	2006
Taxes	23.6	23.6	24.8	24.3
Direct	7.6	7.3	7.4	7.0
Indirect	15.1	15.6	16.6	16.6
Wealth	0.9	0.6	0.8	0.8
Non-Tax Revenues	3.1	3.1	3.4	3.7
Factor Incomes	6.4	6.9	8.0	8.4
Social Funds	6.6	7.0	6.9	7.7
Total	39.8	40.5	43.1	44.1
Privatisation Revenues	0.1	0.4	0.8	2.1
Total Revenues	39.9	40.9	43.9	46.2
Current Expenditures	17.5	17.7	17.5	19.0
Investment Expenditures	3.6	3.1	3.9	4.3
Fixed Investment	3.6	3.1	3.8	4.2
Change in Stocks	0.0	0.0	0.0	0.0
Transfer Expenditures	28.8	25.4	22.3	21.0
Current Transfers	28.1	24.6	21.7	19.5
Capital Transfers	0.6	0.8	0.5	1.6
Stock Revaluation Fund	0.0	0.0	0.0	0.0
Non-Interest Expenditure	33.1	32.8	34.1	36.1
Total Expenditures	49.9	46.2	43.6	44.3
Primary Surplus	6.8	8.1	9.8	10.1
Borrowing Requirement	10.0	5.3	-0.3	-1.9
IMF-Defined Primary Surplus	5.5	6.0	6.2	5.9
Borrowing Requirement Compatible with Fiscal Notification	11.3	5.8	0.3	0.2

Note: Return and tax refunds are not included in the figures for revenues and expenditures.
Source: SPO

The share of general government total expenditures in GDP, which was 43.6 per cent in 2005, realized as 44.3 per cent in 2006. While the primary expenditures increased by 2 points, the decrease in interest expenditures was 1.5 points. In 2006, the share of investment expenditures in GDP increased by 0.4 points.

As a result of these developments, the general government balance gave a surplus in 2006 as it was in 2005, and realized as 1.9 per cent as a ratio of GDP. In the same period, the ratio of the general government primary surplus to GDP increased by 0.3 points and realized as 10.1 per cent. The borrowing requirement to GDP ratio, in harmony with the fiscal notification decreased from its level of 0.3 per cent in 2005, to the level of 0.2 per cent in 2006.

Box 3. 2: Adjustments in General Government Balance in the Context of Fiscal Notification

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

During preparation of fiscal reporting tables;

- Revenues and expenditures (duty losses of the state banks, etc.) which are defined as such in the ESA 95 rules but not included in the budget deficit are added to the budget; and accounts which do not comply with the definition of revenue (privatisation, revaluation differences, revenue of issuing coins, etc.) or expenditure (risk account, etc.) but which are included in the 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, the differences between the two definitions are presented below.

Table: General Government Borrowing Requirement Compatible with Fiscal Notification

(Per cent of GDP)

	2003	2004	2005	2006
General Government Borrowing Requirement	**10.0**	**5.3**	**-0.3**	**-1.9**
Privatisation Revenues	0.1	0.4	0.8	2.1
Telekom Dividend	0.0	0.0	0.0	0.2
Risk Account	-0.3	-0.1	0.0	0.0
Claims and Credits (Net)	-0.4	-0.4	-0.5	-0.2
Paid and Accrued Interest Rate Differences	1.6	0.6	-0.1	0.2
Net Fund Lending	-0.1	0.0	-0.1	-0.2
Duty Loss of State Banks	0.2	0.0	0.0	0.0
Other	0.1	0.0	0.5	0.0
General Government Borrowing Requirement (Compatible with Fiscal Notification)	**11.3**	**5.8**	**0.3**	**0.2**

Source: SPO, Ministry of Finance, Undersecretariat of Treasury

Medium Term Perspective

In the forecast of general government accounts, various assumptions about revenues and expenditures were taken into consideration in addition to the macroeconomic assumptions such as economic growth, inflation, interest rates, balance of payments, terms of trade, wage increases and exchange rates for the period of 2008-2010.

Assumptions about revenues:

- The Special Provincial Administration and Municipality Revenues Law, which constitutes one of the components of the local administrations reform, is assumed to become effective in the PEP period and its financial impact is reflected on balances.
- It is calculated that the financial impact of the minimum subsistence allowance will be equal to the savings obtained from the wage earners tax reduction that was abolished.
- It was assumed that possible price changes in international energy prices would not affect the amounts of SCT on energy products.
- The impact of VAT reductions on various goods and services were taken into account.
- It is estimated that additional revenue increase will be ensured via fighting against informal economy and the effective functioning of the Revenue Administration.
- Starting from 2009, the impact of a 5 point decrease in the pension premium employers' share for the wage earners is taken into account.

The Tax Office Full-Automation Project (VEDOP), which was initiated with the aim of reducing the work load of tax offices through the realization of their transactions in digital environment, increasing productivity and efficiency in the operation and transactions of tax offices and setting up a sound administrative support and management information system infrastructure, will be continued. In parallel with this, the works for strengthening the information systems and infrastructure will be completed, and a disaster recovery center will be established for storing data backups. In this context, all units of the revenue administration will be included in the automation in the first half of 2009.

Based on the taxpayer friendly administration concept, efforts to provide the taxpayers with more services on the internet and make them benefit more from the digital means will be intensively continued. In this context, the scope of the electronic statement filing obligation was expanded. In addition, the Electronic Invoice Project will be implemented.

With the aim of rationalization and simplification of the tax system, just as in the Corporate Tax Law, works for rewriting the Income Tax Law and rearranging its systematic structure are continuing and it is envisaged that the new Income Tax Law will be put into effect in 2008.

In order to ensure effectiveness in public health expenditures, IT infrastructure of social security system will be strengthened to reduce losses and leakages in the social security system, to enable regular tracking of health expenditures by surveillance of invoices in digital environment, to enable instant access to the detailed information of all shareholders in the system such as hospital-physician-pharmacist-insuree, and to make auditing and control easier.

The maintained economic stability supported the struggle against informal economy, and various measures have been started to be taken in overall economy and at sectoral levels to reduce the informal economy. Within the framework of struggle against informal economy, for the forthcoming period:

1) Strategy for struggling with the informal economy will be prepared by analyzing causes, consequences and size of the informal economy as a whole, developing solution proposals to eradicate its causes, and scheduling the concrete steps that will be taken along with their performance indicators.
2) In order to reduce informal economy and informal employment, coordination among the public agencies will be increased. Activities will be organized that will encourage individuals to participate in formal economy and explain the negative consequences of informal economy.
3) Practices to increase strength and effectiveness of the control dimension of the fighting against informal economy, will be implemented and necessary legal regulations will be prepared. In this context, enterprises employing workers informally will be barred from public tenders for a certain time, amendments will be made to the Identification

Notification Law No.1774 to facilitate the fight against informal employment, and a call center will be established to make notices timely and easily. In addition, a Computerized Control and Risk Analysis Center will be established within the Revenue Administration. In order to ensure that documents in gas stations are recorded to actual owners and prevent informality in the fuel sector, the Vehicle Identification Unit System Project will be implemented. Recruiting tax inspection staff in large numbers will be continued.

4) It will be ensured that the causes of tax deficits by sectors will be investigated, analyzed and regularly reported.
5) In order to facilitate collection of claims, an electronic seizure system will be used effectively.

Under these assumptions, the general government revenues excluding the privatization revenues, which are programmed to be 41.9 per cent of the GDP in 2007, are estimated to be 41.6 per cent of GDP in 2008. The general government revenues including privatization revenues, which are expected to be 43.7 per cent of GDP in 2007, are estimated to be 43.2 per cent of GDP in 2008. In 2010, the general government revenues excluding the privatization revenues are estimated to be 39.6 per cent of GDP, and total general government revenues are estimated to be 40.6 per cent of GDP in 2010.

It is estimated that the share of tax revenues in the general government revenues excluding the privatization revenues will increase by 1.6 points compared to 2007 and reach 58.4 per cent in 2008, and rise to 59.5 per cent in 2010.

Assumptions about expenditures:

- The fiscal impact of possible implementation of the personnel regime reform in the program period is not reflected to the calculations.
- It is assumed that the policy of restricting the amount of public personnel recruitment will continue, and the wages and pensions will be increased in accordance with the inflation target.
- It is assumed that the eligibility conditions for unemployment insurance will be relaxed from the final quarter of 2008, and its probable cost was reflected to the balances.
- The fiscal impact of the social security reform is not reflected on the balances due to the fact that the parameters of the system, which is expected to be enacted in 2008, have not fully been determined.

As a result of the projections based on these assumptions, the share of the general government expenditures in GDP is estimated to be 43.6 per cent in 2007, 43.3 per cent in 2008, and 39.6 per cent in 2010. The share of primary expenditures in GDP is expected to recede to 34 per cent in 2010, a 1.9 point decrease from its 2007 level of 35.9 per cent.

The share of the general government fixed capital investments in GDP is expected to recede to 3.7 per cent in 2008, by a 0.4 points decrease from its 2007 level, and also keep its level in 2010.

The general government revenues and expenditures are estimated to be in balance in 2007 and 2008. In 2009 and 2010, the general government balance is forecasted to have a surplus of 0.7 per cent and 1 per cent of GDP, respectively. The ratio of the general government primary balance surplus to GDP is estimated to be 7.7 per cent in 2007, and expected to be 7.9 per cent, 7.1 per cent and 6.5 per cent in 2008, 2009 and 2010, respectively.

The projection of balanced budget that was made in the 2006 PEP regarding the general government revenues and expenditures for 2008 was kept in this PEP as well. On the other hand, while in the 2006 PEP the general government balance to GDP ratio was forecasted to run a deficit of 0.3 per cent in 2009, it was changed to a 0.7 per cent surplus by a 1 per cent revision due to the reduction especially in interest expenditures and current expenditures.

Table 3. 3: Revenues and Expenditures of the General Government-2

(Per cent of GDP)

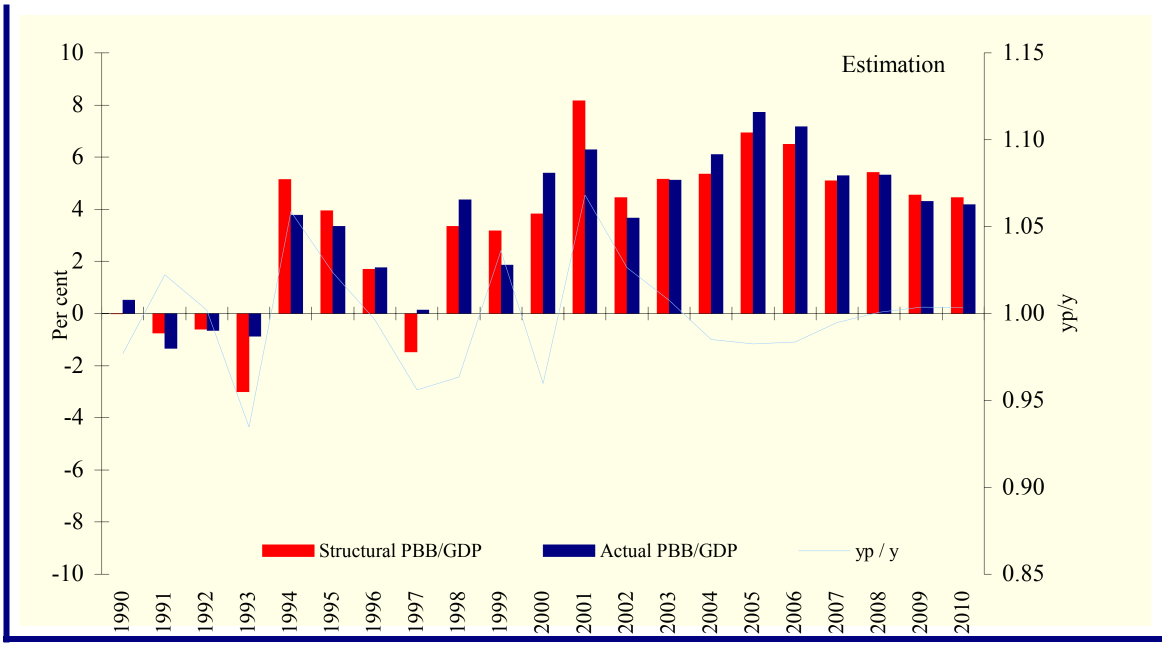
	2007	2008	2009	2010
Taxes	23.8	24.3	24.2	23.5
Direct	7.2	7.3	7.4	7.4
Indirect	15.7	16.2	16.0	15.4
Wealth	0.8	0.8	0.8	0.8
Non-Tax Revenues	2.9	2.6	2.6	2.6
Factor Incomes	7.7	7.1	6.7	6.6
Social Funds	7.5	7.6	7.0	6.8
Total	41.9	41.6	40.6	39.6
Privatisation Revenues	1.8	1.6	1.4	1.0
Total Revenues	43.7	43.2	42.0	40.6
Current Expenditures	19.4	19.0	18.7	18.1
Investment Expenditures	4.1	3.7	3.8	3.7
Fixed Investment	4.1	3.7	3.8	3.7
Change in Stocks	0.0	0.0	0.0	0.0
Transfer Expenditures	20.1	20.6	18.8	17.7
Current Transfers	19.5	19.8	18.1	17.0
Capital Transfers	0.6	0.8	0.7	0.7
Stock Revaluation Fund	0.0	0.0	0.0	0.0
Non-Interest Expenditure	35.9	35.4	34.9	34.0
Total Expenditures	43.6	43.3	41.3	39.6
Primary Surplus	7.7	7.9	7.1	6.5
Borrowing Requirement	0.0	0.0	-0.7	-1.0
IMF-defined Primary Surplus	3.8	5.1	4.7	4.5

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

3.1.3. Structural and Cyclical Consolidated/Central Government Budget Balance

The structural and cyclical budget balances for the Turkish economy and cyclical impacts on the budget were examined by the commonly used method as in the previous PEPs.

Figure 3. 1: Actual and Structural Primary Budget Balances



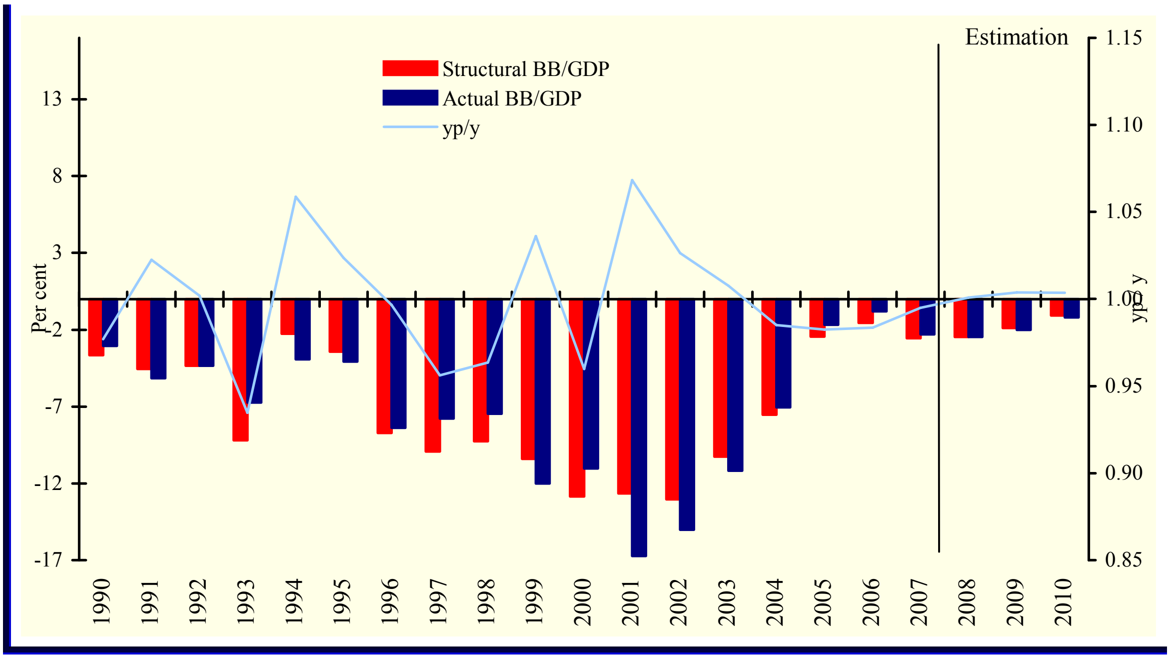
PBB: Primary Budget Balance yp/y: Potential Output/Actual Output

When the structural primary budget balance and the actual primary budget balance shown in Figure 3.1 are examined, it is observed that the actual primary budget surplus took higher values than the structural primary budget surplus in 2005-2006. In 2007, the primary budget surplus has declined slightly compared to the previous years. Furthermore, it is observed that the cyclical impact has weakened in 2007, and the structural primary budget balance and the actual primary budget balance have converged to each other.

In the 2007 PEP period, it is projected that the 2007 trends regarding the primary budget balances will change slightly and the primary budget surplus will realize around 4.5 per cent. Furthermore, a cyclical impact is not expected in this period, as in 2007.

Figure 3.2 presents the actual budget balance and the structural budget balance. In the 2002-2006 period, the positive impact of the tight fiscal policy on the budget balance is observed. Both the decline in interest payments with the decreasing interest rates, and high levels of the primary surplus were the determining factors in the decline of the budget deficit. However, the increase in the risk premium due to the impact of the financial fluctuations in the international markets was reflected to the borrowing interest rates in 2006. This situation affected the interest payments negatively in the year of 2007, as the maturity of borrowing was around 2 years. Therefore, as seen in Figure 3.2, the budget balance deteriorated slightly in 2007 compared to 2006. However, the budget is forecasted to converge to a balance in 2009-2010 with the projection that interest rates will decline starting from 2008 and tight fiscal policy implementation will continue.

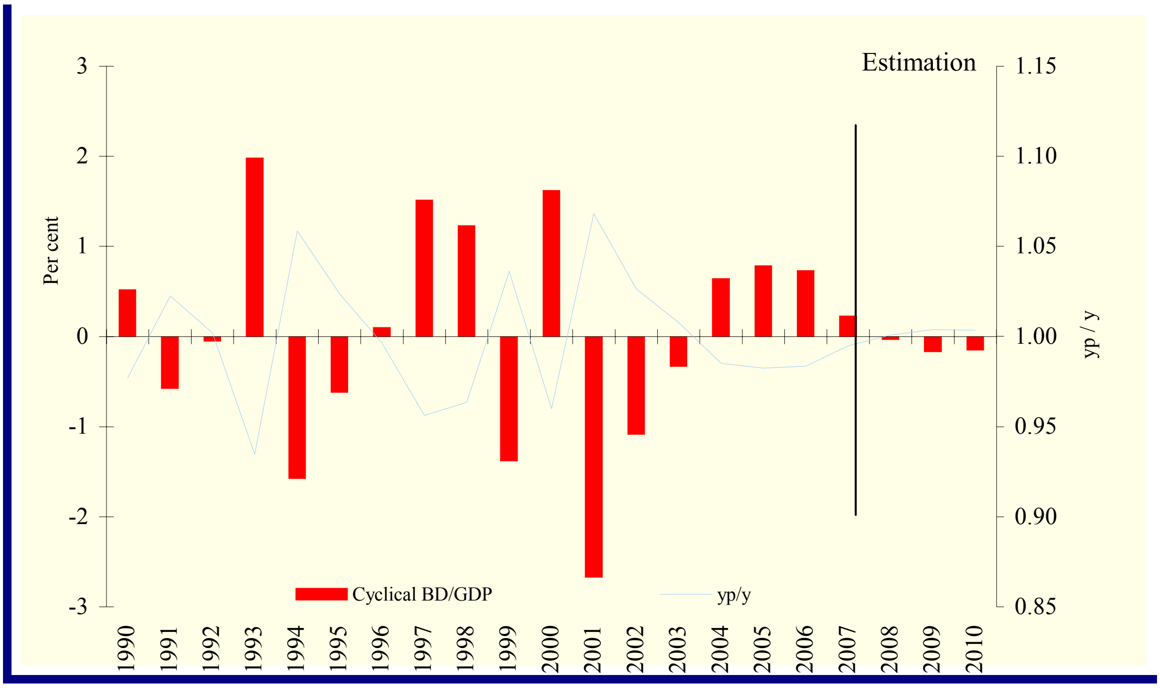
Figure 3. 2: Actual and Structural Budget Balances



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

The cyclical budget balance, defined as the difference between the actual budget balance and the structural budget balance, indicates the cyclical effects on the budget. As mentioned earlier, the cyclical impact tended to decline in 2007 compared to the previous period. In the period of 2008-2010, it is projected that there will be no cyclical impact on budget as a result of the forecast that the economic growth will be around its potential.

Figure 3. 3: Cyclical Budget Balance



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

3.1.4. Public Debt Management

Institutional Responsibilities for Debt Management and Borrowing Limits

The Undersecretariat of Treasury carries out debt management within the framework of the borrowing limit determined as required by Article 5 of the Law No.4749 on Regulating Public Finance and Debt Management promulgated on April 2002.

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

a) Following a sustainable, transparent and accountable borrowing policy that is in line with monetary and fiscal policies by considering macroeconomic balances,

b) Meeting financing requirements at the lowest possible cost in the medium and long-run, within the framework of the risk level determined by considering domestic and foreign market conditions and cost elements.

The borrowing limit is defined as the amount of the difference between the total commencement appropriations that are specified in the budget law of a certain fiscal year and estimated revenues. Within the framework of the same article of the mentioned Law, the net borrowing limit may be increased by 5 per cent taking the requirements and development of debt management into account.

Public Debt Stock

Current Situation

The economic programme being implemented since 2002, fiscal discipline and political stability have increased the efficiency of debt management. In this context, the ratio of the general government gross debt stock to GDP continued its downward trend and declined to 60.9 per cent at the end of 2006, from 69.2 per cent in 2005.

Table 3. 4: General Government Gross Debt Stock

(Per cent of GDP)

	2002	2003	2004	2005	2006
Domestic Debt Stock	54.7	54.8	52.9	51.0	44.4
External Debt Stock	34.7	25.3	21.9	18.1	16.5
Total	89.3	80.1	74.7	69.2	60.9

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

Table 3. 5: Central Government Gross Debt Stock

(Per cent of GDP)

	2002	2003	2004	2005	2006
Domestic Debt Stock	54.0	54.0	52.1	50.2	43.6
External Debt Stock	33.4	24.6	21.4	17.8	16.2
Total	87.4	78.6	73.5	68.0	59.9

Source: Undersecretariat of Treasury

The ratio of the central government's total debt stock to GDP keeps its yearly declining trend. In this context, the mentioned ratio realized as 59.9 per cent by the end of 2006, a 8.1 points decrease from 2005. In the period of 2002-2006, the total decline was recorded as 27.6 points.

The total debt stock of the central government which was 242.7 billion YTL by the end of 2002, realized as 341.5 billion YTL by the end of September 2007. Domestic borrowing constituted 75.6 per cent of the stock and the share of foreign borrowing declined to 24.4 per cent by a decrease of 13.9 points compared to 2002 year end, by the end of September. Due to the fact that the weight of the YTL denominated borrowing has increased as a result of the borrowing program, the share of YTL borrowing in the total debt stock continued to rise in years, and was realized as 67.1 per cent in September 2007. The share of foreign currency denominated and foreign currency indexed debts declined by 25.2 points compared to year end of 2002 and became 32.9 per cent in September 2007, and the share of fixed rate loans increased by 9.3 points to 54.2 per cent. This fact decreased the sensitivity of the total stock to changes in exchange rate and interest rate.

The domestic debt stock of the central government increased from 244.8 billion YTL by the end of 2005, to 251.5 billion YTL by the end of 2006. The ratio of the central government's domestic debt stock was 50.2 per cent in 2005, and receded to 43.6 per cent in 2006. At the end of September 2007, the central government's domestic debt stock realized as 258.3 billion YTL.

In the scope of the borrowing strategies followed towards alleviating foreign exchange currency risks, mostly YTL denominated borrowing was continued. The share of YTL denominated borrowing in the central government's domestic debt stock increased from 86 per cent by the end of 2006 to 89 per cent as of the end of September 2007.

Table 3. 6: Central Government Debt Stock Composition by Instruments

	2002		2003		2004		2005		2006		Sep. 2007	
	Million YTL	%	Million YTL	%	Million YTL	%	Million YTL	%	Million YTL	%	Million YTL	%
Overall Total	242,665	100	282,807	100	316,528	100	331,520	100	345,050	100	341,523	100
Fixed	109,079	45	138,116	49	170,276	54	166,106	50	186,169	54	185,259	54
Floating	133,586	55	144,691	51	146,252	46	165,414	50	158,881	46	156,265	46
YTL Denominated	101,694	42	151,790	54	185,020	58	206,852	62	216,800	63	229,311	67
Fixed	37,576	15	68,614	24	94,930	30	101,444	31	111,457	32	113,254	33
Floating	64,118	26	83,175	29	90,090	28	105,408	32	105,343	31	116,057	34
FX Total	140,971	58	131,017	46	131,508	42	124,667	38	128,250	37	112,213	33
FX Denominated	121,199	50	113,140	40	122,067	39	119,098	36	126,569	37	110,993	32
Fixed	71,037	29	69,502	25	75,346	24	64,662	20	74,712	22	72,005	21
Floating	50,161	21	43,639	15	46,721	15	54,436	16	51,856	15	38,988	11
FX Indexed	19,772	8	17,877	6	9,441	3	5,570	2	1,681	0	1,220	0
Fixed	466	0	0	0	0	0	0	0	0	0	0	0
Floating	19,307	8	17,877	6	9,441	3	5,570	2	1,681	0	1,220	0
Total Dom. Debt Stock	149,870	100	194,387	100	224,483	100	244,782	100	251,470	100	258,272	100
Total Fixed	54,390	36	85,032	44	115,572	51	111,061	45	121,053	48	124,002	48
Total Floating	95,480	64	109,354	56	108,911	49	133,720	55	130,417	52	134,270	52
YTL Denominated	101,694	68	151,790	78	185,020	82	206,852	85	216,800	86	229,311	89
Fixed	37,576	25	68,614	35	94,930	42	101,444	41	111,457	44	113,254	44
Floating	64,118	43	83,175	43	90,090	40	105,408	43	105,343	42	116,057	45
FX Denominated	28,404	19	24,720	13	30,021	13	32,360	13	32,989	13	27,742	11
Fixed	16,348	11	16,418	8	20,642	9	9,617	4	9,596	4	10,748	4
Floating	12,055	8	8,302	4	9,380	4	22,743	9	23,393	9	16,994	7
FX Indexed	19,772	13	17,877	9	9,441	4	5,570	2	1,681	1	1,220	0
Fixed	466	0	0	0	0	0	0	0	0	0	0	0
Floating	19,307	13	17,877	9	9,441	4	5,570	2	1,681	1	1,220	0
External Debt Stock	92,795	100	88,420	100	92,046	100	86,738	100	93,580	100	83,251	100
USD	37,300	40	35,723	40	38,973	42	42,245	49	49,236	53	45,353	54
JPY	7,159	8	5,222	6	3,854	4	3,095	4	3,062	3	2,699	3
EUR	24,314	26	23,328	26	23,708	26	21,089	24	25,451	27	25,191	30
SDR	22,801	25	23,365	26	24,765	27	19,662	23	15,130	16	9,405	11
Other	1,221	1	782	1	745	1	647	1	700	1	604	2
External Debt Stock	92,795	100	88,420	100	92,046	100	86,738	100	93,580	100	83,251	100
Fixed	54,689	59	53,084	60	54,704	59	55,045	63	65,116	70	61,257	74
Floating	38,106	41	35,337	40	37,341	41	31,693	37	28,463	30	21,994	26

Source: Undersecretariat of Treasury

Realization of the amortizations of an important share of non-cash bonds issued in 2001 within the recent years led to a decrease in the average maturity of the debt stock. In spite of this, the fixed and floating rate bonds with 5 years maturity, which were started to be issued in 2005, and the YTL denominated floating rate bonds with 7 years maturity in 2007, gradually increased the average maturity of the central government domestic debt stock. The average maturity of the central government domestic debt stock was 23.5 months in 2005, 24 months in 2006, and 26.6 months as of September 2007.

Table 3. 7: Maturity Structure of the Central Government Domestic Debt Stock

	2002	2003	2004	2005	2006	2007 Sep.
			Average Maturity of Stock (Month)			
Cash	12.8	12.4	11.8	19.6	22.3	26.8
Non-Cash	60.4	51.2	45.5	38.7	32.0	25.8
Total	32.1	25.1	20.6	23.5	24.0	26.6

Source: Undersecretariat of Treasury

The share of fixed rate borrowing in the central government's external debt stock continued its increasing trend starting from 2002 and realized as 74 per cent in September 2007. Furthermore, analyzing the foreign currency composition of the stock, while the share of borrowing in dollars and euros increased in the last five years, the SDR denominated borrowing declined. In this context, the share of dollar and euro denominated debts in the total external debt stock that was 40 per cent and 26 per cent, respectively at the end of 2002, increased to 54 per cent and 30 per cent, respectively, as of the end of September 2007, and the share of the SDR denominated debts receded to 11 per cent by a 13.3 points decrease.

The share of the public sector in central government total domestic debt stock, which reached the level of 66 per cent due to the bonds issued for duty losses and capital injection to public banks in 2001 and those issued to the Savings Deposit Insurance Fund for the restructuring in the banking sector, continued to decrease and declined to 30.8 per cent in 2005, 28.4 per cent in 2006 and 27 per cent as of September 2007.

Table 3. 8: Domestic Debt Stock by Lenders

	2002	2003	2004	2005	2006	2007 Sep.	2002	2003	2004	2005	2006	2007 Sep.
Total	149.9	194.4	224.5	244.8	251.5	258.3	100.0	100.0	100.0	100.0	100.0	100.0
Public	79.1	92.6	83.3	75.5	71.4	69.8	52.8	47.7	37.1	30.8	28.4	27.0
CBRT	18.4	18.4	18.4	18.4	17.8	16.2	12.3	9.5	8.2	7.5	7.1	6.3
State Banks	24.3	27.2	27.5	25.0	19.9	19.9	16.2	14.0	12.2	10.2	7.9	7.7
SDIF	11.0	15.1	8.3	4.5	4.5	3.8	7.4	7.7	3.7	1.8	1.8	1.5
CBRT (IMF Credits)	9.7	8.5	3.7	-	-	-	6.5	4.4	1.6	-	-	-
Other	15.7	23.4	25.4	27.5	29.3	30.0	10.5	12.1	11.3	11.2	11.6	11.6
Market*	70.8	101.8	141.1	169.3	180.1	188.5	47.2	52.3	62.9	69.2	71.6	73.0

*Market includes the instruments issued to SDIF for the deposits of İmar Bank.
Source: Undersecretariat of Treasury

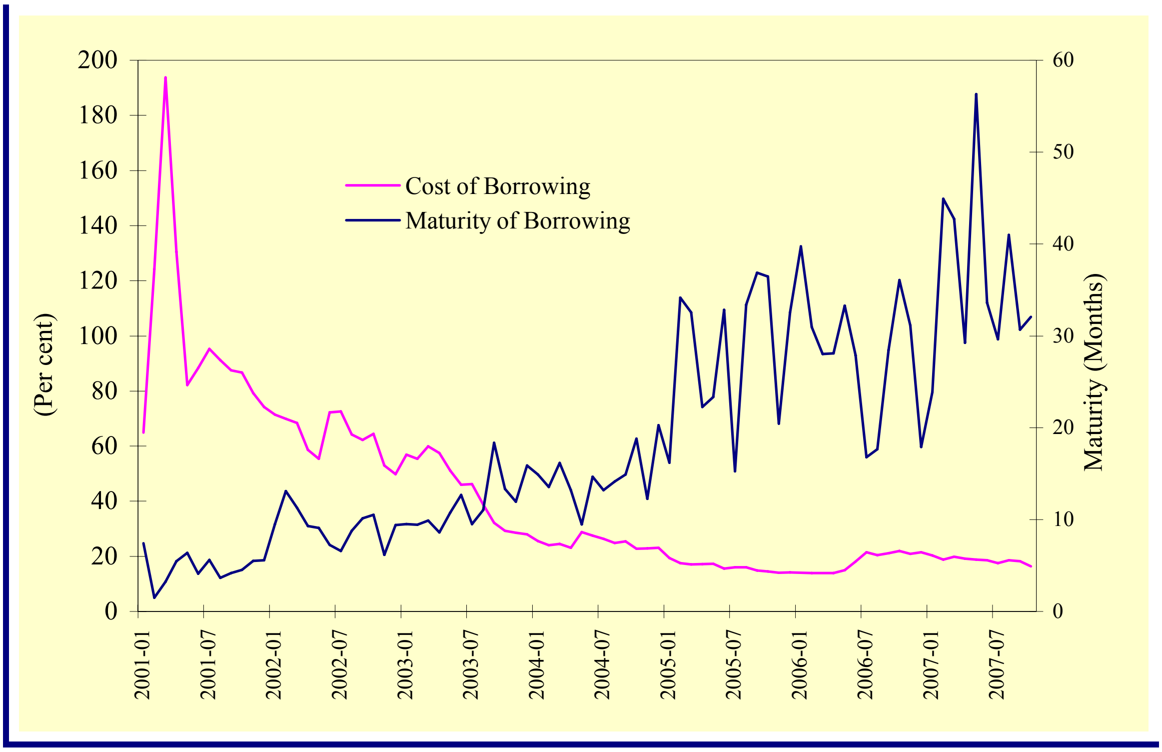
As a result of the positive atmosphere realized in the markets due to the continued structural reforms and the developments regarding fiscal policy in the scope of the economic programme being implemented, the cost of YTL denominated discounted borrowing realized as 14.2 per cent as of December 2005 and declined to 13.9 per cent as of April 2006. However, due to the fluctuations in the foreign markets since May as well as the increasing doubts about the inflation target and current account deficit, the interest rates increased, and the secondary market interest rates exceeded 22 per cent in June. In the aforesaid period, the borrowing cost increase was curbed with increasing the share of floating rate borrowing by the suspension of the fixed coupon borrowing, and curbing the debt rollover rate, the average cost of the discounted borrowing receded to 21.5 per cent in December as a result of the fiscal and monetary measures taken.

As the effects of the fluctuations in foreign markets disappeared, the prospects for 2007 became positive, and the average cost of discounted borrowing declined to 17.6 per cent in July. However, upon the global turbulence due to the risky loan markets in the USA, the interest rates increased to 18.6 per cent in August.

The average real interest rate of the domestic debt stock was 7.96 per cent as of the end of December 2005, 7.79 per cent at the end of 2006, and 10.26 per cent in August 2007.

The average maturity of the domestic cash borrowing was 27.7 months in 2005, and increased beyond 30 months in January-April 2006. On the other hand, due to the shortening of the maturity of borrowing beginning from May with the fluctuations in the markets, the average maturity of the domestic cash borrowing for 2006 realized as 28 months. In 2007, the policy of prolonging the maturity of the domestic debt was continued and thereby the average maturity of the domestic cash borrowing rose to 35.2 months in October.

Figure 3. 4: Average Maturity and Cost of Treasury's Borrowing



Source: Undersecretariat of Treasury

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

Since the end of 2002, the share of bond liabilities in general government external debt stock increased, and realized as 56.9 per cent in the second quarter of 2007. In addition to making borrowing through bonds, the repayment of credit liabilities led to an increase in the bond stock in the total debt stock.

With the crisis of 2001, the share of loans from international organizations in the general government external debt stock almost doubled, and realized as 35.7 per cent in 2001, 36.7 per cent in 2003 and 38.1 per cent in 2004. The share of the mentioned liabilities in the stock started to recede from 2005 as a result of the massive repayments and was 25.8 per cent at the second quarter of 2007, a 12 points decrease from the end of the year 2004.

The share of dollar denominated debts in the stock tends to increase in years. As a result of this increasing trend, in the second quarter of 2007, the weight of the dollar denominated debts in the stock realized as 54.7 per cent. The SDR denominated debt, which was at 25 per cent levels in the period of 2002-2004, realized as 12.5 in the second quarter of 2007 as a result of loan repayments to the IMF. The share of the euro denominated debt that tended to decline by the end of 2005, increased by 3 points to 27.1 per cent at the end of the year 2006. As of June 2007, the share of the euro denominated debt in the general government external debt stock was 28.6 per cent.

Table 3. 9: General Government External Debt Stock

	In Million Euros							Percentage Distribution						
	2001	2002	2003	2004	2005	2006	2007Q2	2001	2002	2003	2004	2005	2006	2007Q2
By Type														
Total	46,499	56,472	52,123	51,520	55,719	54,123	50,906	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Bond	22,823	22,140	21,406	21,842	26,676	28,992	28,977	49.1	39.2	41.1	42.4	47.9	53.6	56.9
Credit	23,675	34,332	30,717	29,679	29,043	25,132	21,930	50.9	60.8	58.9	57.6	52.1	46.4	43.1
By Maturity														
Total	46,499	56,472	52,123	51,520	55,719	54,123	50,906	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Short Term	0	0	0	0	0	0	0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Medium-Long Term	46,499	56,472	52,123	51,520	55,719	54,123	50,906	100.0	100.0	100.0	100.0	100.0	100.0	100.0
By Lender														
Total	46,499	56,472	52,123	51,520	55,719	54,123	50,906	100.0	100.0	100.0	100.0	100.0	100.0	100.0
International Organizations	7,659	20,153	19,121	19,620	19,019	15,753	13,124	16.5	35.7	36.7	38.1	34.1	29.1	25.8
Government Institutions	7,575	6,772	5,712	4,882	4,450	3,938	3,355	16.3	12.0	11.0	9.5	8.0	7.3	6.6
Commercial Banks	18,317	17,051	15,428	15,868	18,169	21,829	22,082	39.4	30.2	29.6	30.8	32.6	40.3	43.4
Other Private Creditors	12,946	12,497	11,862	11,151	14,081	12,603	12,345	27.8	22.1	22.8	21.6	25.3	23.3	24.3
By Currency														
Total	46,499	56,472	52,123	51,520	55,719	54,123	50,906	100.0	100.0	100.0	100.0	100.0	100.0	100.0
USD	23,807	22,755	21,103	21,805	27,074	28,405	27,826	51.2	40.3	40.5	42.3	48.6	52.5	54.7
DEM	81	-	-	-	-	-	-	0.2	-	-	-	-	-	-
JPY	4,984	4,203	2,993	2,110	1,949	1,738	1,542	10.7	7.4	5.7	4.1	3.5	3.2	3.0
EUR	14,577	14,171	13,355	13,044	13,461	14,677	14,567	31.3	25.1	25.6	25.3	24.2	27.1	28.6
SDR	526	13,385	13,389	13,557	12,386	8,586	6,353	1.1	23.7	25.7	26.3	22.2	15.9	12.5
Other	2,524	1,958	1,283	1,005	849	718	619	5.4	3.5	2.5	2.0	1.5	1.3	1.2

Source: Undersecretariat of Treasury

The average of time remaining to maturity of the central government's external debt stock realized as 7.5 years at the end of September 2007, increasing by about 6 months compared to the end of the year 2006. On the other hand, time remaining to maturity realized as 9 years in September 2007, increasing by 0.4 points compared to the end of the year 2006.

Table 3. 10: Time Remaining to Maturity of the Central Government's External Debt

	2006				September 2007			
	Stock		Time Remaining to Maturity	Time Remaining to Average Maturity	Stock		Time Remaining to Maturity	Time Remaining to Average Maturity
	Million Euros	%	Year	Year	Million Euros	%	Year	Year
Maturity	53,104	100	8.6	7.0	48,494	100	9.0	7.5
Short Term (Less than 1 year)	0	0	0.0	0.0	0	0	0.0	0.0
Medium Term (1-5 years)	1,774	3	2.1	1.3	1,304	3	2.4	1.0
Long Term (More than 5 years)	51,330	97	8.8	7.2	47,190	97	9.2	7.7
By Lender	53,104	100	8.6	7.0	48,494	100	9.0	7.5
Credit	24,112	45	7.3	3.9	19,968	41	8.2	4.5
International Organizations	15,428	29	6.2	3.5	12,097	25	7.2	4.2
IMF	8,582	56	2.7	1.4	5,475	45	3.1	1.7
Government Institutions	3,933	7	13.0	6.3	3,267	7	13.8	6.9
Other	4,751	9	6.3	3.3	4,605	9	6.8	3.6
Bond	28,992	55	9.6	9.6	28,525	59	9.6	9.6
By Currency	53,104	100	8.6	7.0	48,494	100	9.0	7.5
USD	27,940	53	10.7	9.6	26,418	54	10.6	9.5
JPY	1,738	3	14.2	6.7	1,572	3	15.0	7.7
EUR	14,443	27	7.2	5.5	14,674	30	7.8	6.1
SDR	8,586	16	2.7	1.4	5,479	11	3.1	1.7
Other	397	1	11.4	5.1	352	1	11.1	5.4

Source: Undersecretariat of Treasury

Debt Management Strategy

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

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

are being continued as the main components of the borrowing policy in 2007. Following borrowing strategies that are consistent with strategic benchmarking will be continued within the framework of risk and cost objectives during the period following 2007 as well.

The high amount of primary surplus projected, within the framework of the economic programme being implemented during the 2008-2010 period, will result in sustaining the confidence environment created in the markets and continuance of the decrease in borrowing requirement. It is projected that, with the positive impact of the decreasing borrowing requirements and the confidence environment in domestic and foreign markets on the expectations, borrowing costs will keep their downward trend; and in line with all these developments, the ratio of the public debt stock in GDP will continue to decrease during the coming period as well.

Within the framework of these benchmarks that are taken as basis in debt management, the risks to which the Treasury debt stock is exposed are being eliminated gradually and the sensitivity of the debt stock to fluctuations in exchange rate and interest rates are being alleviated. The share of foreign exchange denominated/indexed debts within the domestic debt stock of the central government budget, which was 15 per cent as of the end of 2005, receded back to the level of 13.8 per cent as of the end of 2006 and reached the level of 11.2 per cent as of September 2007. While the share of fixed rate debt stock in the domestic debt stock was 45.4 per cent in 2005, it increased to 48.1 per cent in the end of 2006 and remained at the level of 48 per cent as of September 2007.

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

In addition, within the scope of sustaining transparency in debt management, regular announcement of the financing programs, the monthly procurement programme and debt information will also be continued in the forthcoming period. Related to domestic borrowings, which constitute a major part of the annual financing requirement, it is projected that the repurchasing and clearing transactions being currently implemented as active debt management instruments will be continued in a manner consistent with strategic benchmarking with the aim of making the current amortizations more organized. Developing the GDBI investor base, through diversification of borrowing instruments to be issued according to preferences of different investors, is included among the priorities of the coming period.

Contingent Liabilities

Undersecretariat of Treasury provides repayment guarantees for purposes such as minimizing the investment financing costs of administrations and institutions that remain outside those included in schedule (I) attached to the Public Financial Management and Control Law No.5018, ensuring the sustainability of growth and meeting the funding requirements of multi-year investments. In addition, within the scope financing projects realised with the Build-Operate-Transfer (BOT) and Build-Operate (BO) models, those administrations that remain outside those included in schedule (I) attached to the Public Financial Management and Control Law No.5018, which have buy-or-pay agreements signed with the BOT/BO companies, are also provided with investment guarantees by the Treasury.

The probable undertaking of the payments of the guaranteed debts of the financially stressed organizations and the obligations under the buy-or-pay agreement, by the Treasury from the consolidated budget constitute a significant part of the explicit fiscal risks.

Under the active risk management, the Credit Pricing Model developed was put into practice from 1 January 2007 to improve the management of the contingent liabilities confronting the Undersecretariat of Treasury. In this context, the Treasury guaranteed facility limit, used in order to alleviate risks arising from contingent liabilities, guarantee fee and partial guarantee rate, is calculated based on the expected losses[4] from organizations by using this model.

In this context, the guarantee limit is defined by the budget law every year. The Treasury guaranteed facility limit, the scope of which was expanded by the Law No.4749 that became effective in 2002, was 2 billion dollars in 2005, and was specified as 3 billion dollars in 2006 and 2007. The guarantee fee is collected as one-time fee up to 1 per cent of the guaranteed amount from the guaranteed company under the Law No.4749. In the partial guarantee practice, credits except export credits obtained from the international and regional organizations and foreign Official Export Insurance Agencies (ECA), are guaranteed up to 95 per cent of the total liabilities.

Repayment Guarantees

Repayment guarantees provided by the Treasury for project financing purposes, which were monitored outside the budget until 2003 and incorporated in the budget through the determination of their potential risk amounts after 2003, have been used for keeping financing costs at the minimum level and ensuring the sustainability of economic growth.

While, the Treasury guaranteed debt stock decreased by 1.9 billion dollars as of June 2007 period, compared to 2002 and became 4.4 billion dollars, the undertaking rate fell from 52 per cent to 20 per cent.

When the repayment projection of Treasury guaranteed external debt stock is examined for the medium-term, it is observed that the repayment amounts entered to a downward trend.

Table 3. 11: Treasury Guaranteed External Debt Service Projections

(In Million Euros)

	Principal	Interest	Total
2007 (II.Quarter)	204	78	282
2008	403	142	545
2009	420	121	540
2010	414	100	513
2011-2015+	1828	303	2131

Note: Exchange rate dated on 30 June 2007 are used in the calculation.

Investment Guarantees

Apart from repayment guarantees, investment guarantees provided to established electricity power plants of which 10 BOT and 5 BO models and one energy SEE with a buy-or-pay agreement constitute important explicit contingent liabilities as well. Even though there has not been any payment obligation arising from the mentioned guarantees until now, these financial risks

[4] Expected loss indicates the expectation regarding the cost which arises from the request undertaken of institutions due to the financial inadequacy, or the condition of inability to meet their liabilities to Treasury.

must also be taken into consideration while calculating the burden that might arise from these contingent liabilities.

In addition to these, an investment guarantee was provided to a municipality within the scope of a BOT project in 1995 for its water invoice payment obligation. Within the scope of the mentioned investment guarantee, a total undertaking of 1.03 billion euros[5] was realised from 1999 until September 2007.

Treasury Receivables

When the Treasury receivable stock as of the end of September 2007 is examined, it is observed that, within the total, the share of funds, local administrations, SEEs and other receivables are 80.6 per cent, 12.2 per cent, 4.9 per cent and 2.3 per cent, respectively. All of the funds are constituted of receivables from the SDIF.

When the distribution of realised collections is examined according to their sources, payments made in cash by organizations constitute 92.7 per cent of actual collections during the 2007 January-September period. The collections consisting of the deductions made from the tax revenue shares of municipalities by the Ministry of Finance constitute 6.5 per cent and those made from the same source by the İller Bank cover 0.7 per cent of the total collections realised during this period. Collections made within the scope of the Law No.6183, on the other hand, are equal to 0.1 per cent of the total collections realised during the same period.

When the collections made in the context of Law No.6183 are compared with those of the previous year, it is observed that there is a decline in these collections. In this development, the decline in the amount of claims to be collected within the context of Law No.6183 as a result of the reconciliation efforts carried out according to the Laws No.5393 and 5216, was effective.

Risk Account

Amounts of budgetary funds transferred to Risk Account in the Central Bank, continually decreased, not only from the decline in undertakings arising from the guarantees provided but also by the increase in the collections. Use of appropriations was realized as 924.8 million YTL in 2003, 240 million YTL in 2006 and 204.3 million YTL as of September 2007.

General Government Gross Debt Stock Projections for 2007-2010 Period

During the 2007 PEP period, a significant improvement in the ratio of the general government gross debt stock to GDP is projected as a result of the stable growth environment to be achieved with the tight fiscal policy, and efficient debt management that will be implemented. In this context, the ratio of the general government gross debt stock to GDP, which was 60.9 per cent in 2006, is projected to recede to 45.6 per cent in 2010.

[5] Cross-currency rates dated 14 November 2007 were taken into acount.

Box 3. 3: Public Debt Stock Projections, 2007-2012

The net public debt stock is obtained by subtracting the Central Bank net assets, public deposits and the net assets of Unemployment Insurance Fund from the gross public debt stock, which is the summation of the central government's total debt stock, gross domestic and external debts of local administrations, SEEs and non-budgetary funds. In the calculation of the net public debt stock, liquid financial assets are also taken into account as well as financial obligations of the public sector. The mentioned method of calculation is important for correctly identifying the risks on the public debt stock and monitoring it appropriately.

In the last 5 years, as a result of the strict fiscal policy implementation, stability and confidence established and high growth rates obtained, net public debt stock to GDP ratio declined significantly. In this context, net public debt stock to GDP ratio, which was 77.7 per cent at the end of 2002, realized as 45 per cent at the end of 2006. Considering the first 9 month-realizations of 2007, this ratio is expected to recede to 39 per cent at the end of 2007.

The policy of high primary surplus, which is the most important instrument in reducing public debt stock, will also continue until 2012. In the period of 2008-2012, IMF-defined public primary surplus to GDP ratio is estimated to be 4.9 per cent annually on average. The impacts of the major reforms, such as the gradual increase in the shares transferred to the local administrations from the central government budget, lowering the employers' social security contributions by 5 points, are reflected in the calculations.

Table: Public Debt Stock Projections

(Per cent of GDP)

	2006	2007	2008	2009	2010	2011	2012
	Real.			Forecast			
General Government Gross Debt Stock	60.9	56.8	52.5	49.6	45.6	42.4	40.0
Public Net Debt Stock	45.0	39.1	36.8	34.2	30.2	27.2	25.0
IMF Defined Public Sector Primary Surplus	6.5	4.1	5.5	4.9	4.8	4.5	4.5
Public Sector Primary Balance	-2.6	0.0	-0.3	-0.8	-1.2	-1.2	-1.8
General Government Borrowing Requirement	-1.9	0.0	0.0	-0.7	-1.0	-1.0	-1.7
General Government Total Expenditures	44.3	43.6	43.3	41.3	39.6	38.1	37.1
General Government Primary Expenditures	36.1	35.9	35.4	34.9	34.0	33.7	33.3
General Government Total Revenues	46.2	43.7	43.2	42.0	40.6	39.2	38.7
General Government Revenues (Excluding Privatization)	44.1	41.9	41.6	40.6	39.6	38.9	38.4
GDP Growth Rate	6.1	5.0	5.5	5.7	5.7	6.0	6.0

Source: Undersecreteriat of Treasury, Ministry of Finance, SPO.

At the end of forthcoming 5 year period, reducing the net public debt stock to GDP ratio to 25 per cent is targeted. Medium-term fiscal policy parameters are determined in accordance with the mentioned target and the forecasts for the ratios of primary surplus, public sector borrowing requirement, primary expenditures and program defined revenues to GDP are presented in the table above.

3.1.5. Budgetary Implications of Major Structural Reforms

Countries implement the reforms they need to establish a sustainable social security system in the medium and long term by considering their special circumstances. Among the parametric amendments that could be made are increasing the retirement age and working years, lowering the replacement rates, and amending the salary calculation formula and updating coefficient. Parametric changes such as increasing the retirement age on a gradual basis, lowering the replacement rates, amending the definition of premium base for newly recruited public servants are planned in the social security reform in Turkey. Furthermore, it is envisaged that health services that are served under various norms and standards will be provided to all the insured under the same norms and standards within the universal health insurance system.

If the social security reform comes into effect with the currently specified parameters, it is expected to impose an additional burden of 203 million YTL, 338 million YTL and 379 million

YTL in 2008, 2009 and 2010, respectively, on the budget. This burden, which initially arises from the expansion of the scope of the health services, is expected to turn to savings in the long-term as a result of the effective functioning of the health system with observed impact of the health transformation program and the reflection of parametric changes in the retirement system.

To be implemented from January 2009, 5 point decrease in the pension premium employers' share for the wage earners is envisaged to decrease the financial liabilities on employment, in the context of fighting against unregistered employment. The impact of this reduction on social security balances will be observed by March 2009, with two months lag due to the notification and payment period. This implementation is expected to create an additional burden of 4.2 and 5.5 billion YTL on social security system in the years of 2009 and 2010, respectively.

If the personnel reform aiming to simplify the wage system in the public sector, to balance the imbalances and inequities in financial and other remuneration of the public personnel, to reduce the number of existing status, and to adhere to flexible employment principles were implemented in the 2007 PEP, the central government budget personnel expenditures would increase by 0.4 per cent of the GDP.

The draft bill which is prepared to strengthen the financial structure of the local administrations and to rearrange the revenues of provincial special administrations and municipalities is assumed to be enacted in the 2007 PEP period. It is estimated that the shares to be allocated to local administrations from the general budget tax revenues would rise by 0.3 per cent as a share of GDP in 2009 and 2010.

3.2. Sensitivity Analysis[6]

Under the sensitivity analysis, the impact of growth, real interest rate, primary surplus and real exchange rate changes on the general government gross debt stock is separately analyzed using accounting approach[7]. In this context, the results of the analysis obtained from the end year 2001 and 2007 June, are presented in Table 3.12 comparatively. Accordingly, it is observed that general government gross debt stock to GDP ratio's sensitivity to the mentioned parameters has declined considerably since 2001, and that the debt stock has evolved into a more sustainable structure.

While a 5 per cent real appreciation or depreciation in YTL affected the ratio of gross debt stock to GDP by 2.9 points positively or negatively in 2001, this rate receded to 0.9 points in June 2007. In the same period, the sensitivity to a 5 points increase/decrease in the real interest rate of YTL denominated debt receded from 2.3 points to 1.7 points. The effect of 2 points increases/decreases in economic growth, on the ratio of gross debt stock to GDP recedes from 2.1 points to 1 point in the same period. On the other hand, by definition the sensitivity of the debt stock to the primary surplus does not change as of years.

Table 3. 12: Change in General Government Gross Debt Stock to GDP Ratio*

	2001	2007
5 Per cent Real Depreciation/Appreciation in YTL	+ / - 2.9 Points	+ / - 0.9 Point
5 Point Increase/Decrease in Real Interest Rate of YTL Denominated Debt	+ / - 2.3 Points	+ / - 1.7 Points
2 Point Decrease/Increase in GDP Growth Rate	+ / - 2.1 Points	+ / - 1.0 Points
1 Point Increase/Decrease in Primary Surplus/GDP Ratio	+ / - 1.0 Point	+ / - 1.0 Point

* It shows the impact of scenarios on general government gross debt stock to GDP ratio by taking the end year of 2001 realized figures and stock estimations of 2007 as of June as basis.

[6] Baseline scenario estimations prepared in the context of sensitivity analyses include debt repayments and repayments arising from new borrowings planned to be made in related period. Furthermore, state guarantees are defined as explicit contingent liabilities and liabilities arising from this item is included in baseline scenario estimations via risk account. On the other hand, implicit contingent liabilities are defined as the liabilities that do not depend on any contract, and are placed under the primary surplus scenarios.

[7] The detailed information about the accounting approach is presented in Box 3.2 in Public Finance chapter of 2003 PEP.

3.3. Public Finance Risks

In the 2008-2010 period, continuation of the tight fiscal policy targeting a high rate of primary surplus, is necessary in order to reduce the ratio of debt stock to the GDP which is an indicator of the sustainability of the debt stock. The possible risks that would be encountered in achieving this objective are presented as follows:

- Foreign exchange denominated/indexed bonds and floating rate bonds within the existing domestic debt stock might be adversely affected by the possible unexpected increases that in exchange rates or interest rates.
- Because of a possible undertaking by the Treasury guaranteed loans and product purchase and input guarantees given to BOT projects constitute a risk on the budget.
- Even though wages and salaries are planned to be increased in compliance with the inflation target, requests towards increasing the welfare levels of employees constitute a significant risk element on personnel expenditures of the general budget.
- The global liquidity, which moves in response to the interest rates of the FED, might continue to be stress factor on developing country economies.
- The unexpected increase in energy prices is continuing to affect the world payments system and terms of trade adversely.
- Negative developments that would adversely affect the premium collection in social security institutions and inability to discipline health expenditures will result in an increase in the amount of transfers from the budget to social security institutions.

If the revenue decreasing regulations lead to higher than projected revenue losses, additional financing will be needed.

3.4. Quality of Public Finances

Public expenditures will be prioritized with respect to resource scarcity and their impact on potential growth in the context of economic and social benefits. Public agencies and institutions will revise their resource allocations under the specified priorities considering the budgetary means. In this context, activities and projects no longer in priority will be eliminated and created fiscal space will be allocated to expenditure priorities with growth potential.

In the calculations of the general government expenditures, regarding the transfer transactions between general government institutions, the transaction amount is neither recorded as expenditure in the accounts of the institution making transfer, nor recorded as revenues in the accounts of the institution receiving transfer. Thereby, any public revenue is written as revenue in the account of the institution, which firstly receives the revenue, and recorded as expenditure in the account of the institution which makes final spending. The functional distribution of the general government expenditures is also calculated according to this framework. Based on the calculation method, for example, while the shares and funds from the general budget revenues are recorded in the expenditures for general public services when the functional distribution of the central government budget are made, they are recorded in related functional expenditure codes of the related administrations when the functional distribution of the general government expenditures are made.

Examining the functional distribution of the general government expenditures, it is observed that expenditures for general public services constitute the highest share in total general government expenditures. The share of the expenditures on general public services in the total general government expenditures was 26 per cent in 2006, and is expected to recede to 22 per cent due to the effects of the decrease in interest expenditures. The share of the expenditures on social security and social assistance services in total general government expenditures, which was 22.1 per cent in 2006, is expected to increase to 25 per cent in 2010. Similarly, the shares of the expenditures on economic affairs and services, health and education in total general government expenditures were realized as 16.5 per cent, 10.8 per cent and 9.2 per cent respectively in 2006, and are expected to be 15.7 per cent, 12.2 per cent and 9.8 per cent respectively in 2010.

KÖY-DES introduced in 2005 and BEL-DES introduced in 2007 will be continued in 2008 as well. The mentioned projects were developed to meet common local needs such as potable water, sewage and roads. In this context, for these two projects, expenditure is expected to realize as 2.3 billion YTL in 2007 and a 800 million YTL appropriation is allocated to them for 2008.

With the regulations made in incentive system, the scope of incentives for development priority regions was expanded and eligibility conditions for incentives were improved. In this context, the amount of incentives to be covered by the Treasury under the Law No.5084 is expected to realize as 300 million YTL in 2007. For 2008, an amount of 300 million YTL has been allocated for the mentioned incentives.

An expenditure of 500 million YTL is estimated in 2007 for R&D supports which are provided through the Scientific and Technological Research Council of Turkey (TÜBİTAK) to encourage domestic industries to allocate more resources to R&D, encourage cooperation and partnership between industrial entities and universities, and an amount of 450 million YTL has been allocated for these supports in 2008. Further, an amount of 105 million YTL is expected to be spent in 2007 for the supports provided through the Small and Medium Industry Development Organization (KOSGEB), and 110 million YTL has been allocated for these supports for 2008.

An amount of 200 million YTL were appropriated for 2007 for the Development Agencies which were decided to be established by the Law No.5449 that came into effect in 2006 and are still in the process of institutionalization in order to activate the local potential and support regional development. However, due to the developments in legal process, it is expected to spend a small amount corresponding to personnel and maintenance costs. With the expectation that the structuring of the agencies will be continued and problems will be overcome in 2008, a 100 million YTL appropriation has been allocated for 2008.

In this context, social expenditures aiming social infrastructure development, constituted 18.8 per cent of GDP in 2006 and this ratio is expected to increase to 19.2 per cent in 2007. It is projected that it will be 19.3 per cent, 19.1 per cent, and 18.7 per cent in 2008, 2009 and 2010 respectively.

In line with the current economic program, increasing the efficiency of public investments, directing them to infrastructure in order to meet priority social needs and support productive activities, and using public investments as an effective tool in achieving sectoral, regional and EU coherence goals are targeted. Within the framework of these policies, efforts for rationalizing the public investments and for projects of public-private cooperation to increase private sector involvement in public infrastructure investments are being continued.

Strategic planning and performance based budgeting system are being made widespread in resource utilization.

The basic objective of the tax policies to be implemented is to contribute to supporting growth and employment in accordance with macroeconomic policies, reducing informality in the economy, and creating a tax system that is simpler, fairer and with wider base.

The Corporate Income Tax Law was redrafted considering such priorities as simplifying the tax legislation, expanding the tax base and fighting with informal economy, and legislated accordingly. In this context, the corporate income tax rate was reduced to 20 per cent, and the tax burden on the corporate profits was receded to level of 34 per cent. Furthermore, the number of income tax tariffs was reduced from 5 to 4. The Major Taxpayers Office was established in order to provide major taxpayers with efficient service. By legal regulations related to VAT, tax rates in certain sectors including mainly education, health, food and tourism were reduced.

Within the means of the public finances and without compromising the fiscal discipline, it is programmed to gradually reduce the transaction taxes, the stamp duty being the major one, which constitute burden on enterprises. In addition, savings obtained from the budgetary activities will be used to alleviate the tax burden on production and employment. In order to reduce labour costs of the employers, an initial 5 points reduction is planned in the SSK employer premium rate.

3.5. Institutional Features of Public Finances

Significant structural changes are being made to improve the institutional capacity in the public financial management. In this context, some of the recent regulations and implementations are presented below.

Public Financial Management and Control Law

About 300 appointments were made to 1200 financial service specialist positions which were allocated under the Law No.5436, amending the Law No.5108 Public Financial Management and Control published in the Official Gazette dated 24 December 2005, and examinations were held on 6 October 2007 to make appointments to 425 positions. Furthermore, the by-law that determines working procedures and principles of the financial services specialists was promulgated in the Official Gazette dated 25 August 2007. It is planned that training of financial services specialists appointed to the public administrations will be completed by the Ministry of Finance till the end of 2008.

As of November 2007, 517 appointments were made to 1200 internal auditor positions allocated for the administrations which are subject to Decree Law No.190. Three-month certification training was given to the 204 appointed internal auditors.

The 2006 General Activities Report, which was prepared as a requirement of fiscal transparency and accountability pursuant to the Law No.5018, which includes a fiscal year activity results of public administrations and social security institutions under the central government and overall assessments of financial structure of local administrations, was announced. In addition, the 2007 Central Government Budget Realizations and Expectations Report, which includes the first half implementation results of central government budget, financial positions, expectations, targets and activities of the second half, was announced.

Table 3. 13: Secondary and Tertiary Legislation List of Law No.5018*

Name of the Arrangement	Legal Basis	Situation
By-Law on Procedures and Principles for Collecting Public Losses	5018 Art. 71	Published in the Official Gazette dated 19.10.2006 No.26324
Communiqué on Principles and Procedures about the Internal Auditor Appointments (No.2)	5018 Art. 65	Published in the Official Gazette dated 30.12.2006 No.26392
Principles and Procedures about Preparation, Approval, Implementation and Monitoring of Detailed Expenditure and Financing Programs	5018 Art. 20	No.3 Budgetary Practice Order is published in the Official Gazette dated 24.01.2007 No.26413
By-Law on Movable Property	5018 Art. 44	Published in the Official Gazette dated 18.01.2007 No.26407.
General Communiqué on Preliminary Payment Procedures and Principles	5018 Art. 35	Published in the Official Gazette dated 08.03.2007 No.26456
General Communiqué on Central Government Expenditure Vouchers	5018 Art. 33	Published in the Official Gazette dated 08.03.2007 No.26456
By-Law on Budgeting and Accounting of Revolving Fund Enterprises	5018 Temp. Art. 11	Published in the Official Gazette dated 01.05.2007 No.26509
By-Law on Financial Services Specialists	5018 Art. 60	Published in the Official Gazette dated 25.08.2007 No.26624
Public Internal Audit Standards	5018 Art. 67	The No.12 decision of The Internal Audit Coordination Board (IDKK) dated 20.11.2006
Public Internal Auditors Professional Code of Ethics	5018 Art. 67	The decision of IDKK dated 20.11.2006 No.12

By-Law on Working Principles and Procedures of Internal Auditors		
Public Internal Audit Charter	Art. 13	The decision of IDKK dated 22.01.2007 No.2
Public Internal Audit Reporting Standards	5018 Art. 67	The decision of IDKK dated 05.06.2007 No.10
Procedures and Principles on the Ranking Certification of Public Internal Auditors	Art. 30	The decision of IDKK dated 02.07.2007 No.11
Procedures and Principles on the Common Working of the Internal Auditors More than One	Art. 51	The decision of IDKK dated 03.07.2007 No.12
Manual for Preparing Public Internal Audit Plan and Program	Art. 40	The decision of IDKK dated 29.08.2007 No.15
Risk Assessment Guide in Public Internal Auditing	Art. 36	The decision of IDKK dated 06.09.2007 No.17

* The secondary and tertiary legislation list for 1 January 2006-19 October 2006 period was given in the PEP 2006.
Source: Ministry of Finance

Budget Accounting Code System and Fiscal Transparency

Due to the amendment made in Article 49 of the Law No.5018 which constitutes the legal basis of the By-Law on General Budget Accounting introduced on 1 January 2006, the Central Government Accounting By-Law prepared according to the mentioned amendment was put into effect on 1 January 2007.

While the By-Law on General Budget Accounting covers only the public administrations in the general budget, the By-Law on Central Government Accounting covers the special budget public administrations and regulatory and supervisory agencies in addition to the general budget public administrations.

By-Law on General Budget Accounting became effective on 1 January 2006. From 1 January 2006, the special budget administrations, regulatory and supervisory agencies, social security institutions and local administrations started to implement their accounting schemes and detailed account plans prepared according to By-Law on General Budget Accounting provided that affirmative opinion of the Ministry of Finance is taken.

Of the central government financial statements under the scope of the Law No.5018, cash based budget tables are published monthly both in digital and hard copy version, and efforts to publish the accrual based financial statements monthly and annually are continuing.

Cash based budget tables and accrual based financial statements of local administrations are published quarterly and annually.

Revenue Administration and Social Security System

Efforts are continuing to improve the implementation and auditing capacity of the Revenue Administration. In this context, the Major Taxpayers Office was activated in the beginning of 2007. The third phase of VEDOP project which constitutes the basis of the technological infrastructure of the revenue administration is continuing, and it is planned to include all units of the revenue administration under the scope of the system in 2009, and in parallel, to strengthen information systems and infrastructure and establish a disaster recovery center.

By the Social Security Institution Law No.5502 published in the Official Gazette dated 20 May 2006, General Directorates of SSK, BAĞ-KUR and Pension Fund for Government Employees were abolished and combined under the new Social Security Institution. The new institution comprises the General Directorate of Social Insurances, the General Directorate of Universal Health Insurance, the General Directorate of Non-Premium Payments and the General Directorate of Service Provision. Thereby, the retirement services, health financing and non-premium payments were united. In the same Law, it is envisaged that by establishing social security centers with full automation and organized at local level with one-stop service, the retirement and health services will be delivered more rapidly. By the mentioned law, the institutional and administrative capacity was enhanced and a new institution, which will be effective in collecting premiums and prevent abuses in retirement and health services, was established.

4. STRUCTURAL REFORMS

As a result of the structural reforms pursued with determination since the early 2000s, important progress was made in ensuring macroeconomic stability, high growth and productivity increases, and economic, social, and legislative harmonization with the EU. However, continuation of the reform process in our country with an accelerating pace and determination is of critical importance for making the progress achieved permanent. In this context, it is important to continue with the structural reforms necessary for strengthening the market economy and eliminating the possible future risks in the areas that can cause macroeconomic instabilities.

The Ninth Development Plan (2007-2013), the Government Program and the process of convergence to the EU shape the framework of basic reforms that Turkey will implement. Both Turkey's and the EU's priorities are taken into account in determining and implementing the reforms. Policies to be followed and reforms to be realized in the EU accession process are stated in the documents prepared by Turkey such as the National Program, Pre-Accession Economic Program and the Strategic Coherence Framework[8] (SCF).

The SCF has been prepared in close cooperation with the EU Commission for two of the components of Instrument for Pre-Accession Assistance (IPA) of the EU, namely Regional Development and Human Resource Development. Three of the four operational programs included in the SCF prepared for the 2007-2013 period and submitted to the High Planning Council are among the issues taken up in the structural reforms section of the 2007 KEP. Operational programs prepared on regional competitiveness, transport and human resource development under the SCF framework are supportive of the reforms on labour market, regional development and transport, included in the 2007 PEP.

In this part, basic reform areas are taken up and developments in these reform areas are assessed, related to the real sector, financial sector, labour market, agricultural sector, administrative issues, regional development, health and social security system, R&D and innovation, information and communication technologies, transportation and energy sectors in the 2007 PEP period.

With the real sector reforms, it is contemplated to continue with the privatization process, encourage private entrepreneurship by improving the investment climate, and strengthen the regulating and supervising functions of the regulatory and supervisory agencies in energy and telecommunication sectors, within the framework of strengthening the market economy and expanding the role of the private sector by downsizing the share of state in the economy.

The financial reforms focus, in the banking sector, on privatizing the public banks, dissolving the banks under the SDIF, and on the secondary legislation for full harmonization with the EU directives and international principles and standards, in the capital markets area, they are towards protecting investors in this sector in an EU compliance framework, and creating a market structure functioning in a stable and effective manner. As for the insurance sector, reforms are intended for the legislative regulations to harmonize with the EU acquis and international standards.

Concerning the labour market reforms, they focus on improving the quality of labour and strengthening the link between the labour market and the education system. In this context, it is envisioned to develop and implement projects towards making the curricula in line with today’s conditions, lowering informal employment, disseminating flexible working practices, increasing educational level of the labour, establishing a professional qualifications system, increasing the employability of women and youth, strengthening social dialogue, providing social support to

[8] SCF is a document which takes into account both Turkey's priorities and EU's priorities. In this context, the Ninth Development Plan which is the main policy document of Turkey for 2007-2013 period, serves as the basis for SCF. Furthermore, the Medium Term Program, Annual Program and sectoral strategic documents were utilized in preparing SCF. In addition, inputs were made to SCF considering EU's priorities and particularly the Multi-Annual Indicative Planning Document prepared by the EU. SCF is in line with the EU Regulation No.1085/2006 dated 17 July 2006 that regulates the Instrument for Pre-Accession Assistance (IPA), Lisbon Strategy, European Employment Strategy, Accession Partnership Document and Progress Reports.

privatization process and joint diploma programs of domestic and foreign education institutions and making the vocational and technical education system efficient.

Directing the production according to demand, and increasing the competitiveness of Turkey gains importance in agricultural sector. In this framework, the reforms focus on areas such as revising the establishment and duties of the Ministry of Agriculture and Rural Affairs, strengthening the autonomy of producers' organizations, speeding up land consolidation activities, making progress in the chapter of food safety, veterinary and phytosanitary, developing organic agriculture, creating regions free of animal diseases, strengthening agricultural statistics infrastructure, improving the institutional structure of the fisheries sector and completing institutional regulations in the sugar sector.

For rural development, in addition to legislative harmonization in this field, it is aimed to enhance the competitiveness of agricultural enterprises, increase the income level of rural population and diversify their economic activities, meet their infrastructure needs, develop human resources, disseminate the participatory structures in organizations and protect the environment. In this context, it is important to prepare the Rural Development Plan and conduct studies to build capacities for benefiting from the EU Pre-Accession Rural Development Fund.

The works about administrative reform aim to increase efficiency in public services. Basic reform works in this field focus on spreading the strategic planning and performance based budgeting practices to all public organizations, developing local administrations reform and solving the problems with the implementation of the mentioned reform.

In the 2007 PEP, harmonization with the EU, regional development projects and developing institutional capacity for regional development at both central and local levels come to the forefront for regional development.

Reforms in health aim to realize the Health Transformation Program. In this context, it is contemplated to promote family medicine, compile data from health institutions according to specified standards, restructure institutions in charge of carrying out health services, and build a new institutional structure in medicine and medical devices. Concerning social security, in addition to institutional restructuring, reforms regarding the establishment of a unique pension system and a unique health system are on the agenda.

For R&D and innovation, the emphasis is on increasing the number of technology development zones and technology centers, the programs created under the Turkey Research Area Program and tax incentives on R&D, regulating tax incentives on R&D, educating researchers inside and outside the country, and the EU Seventh Framework Program.

As for Information and Communication Technologies, the main reform agenda is the developments in the Information Society Strategy and the annexed Action Plan.

Reforms in the transport sector focus on, in addition to EU convergence, the Transport Infrastructure Needs Assessment (TINA) project, restructuring and strengthening the railway sector, enhancing maritime safety and road traffic safety, Land Transportation Automation System, and on restructuring the Regional Directorates of Transportation.

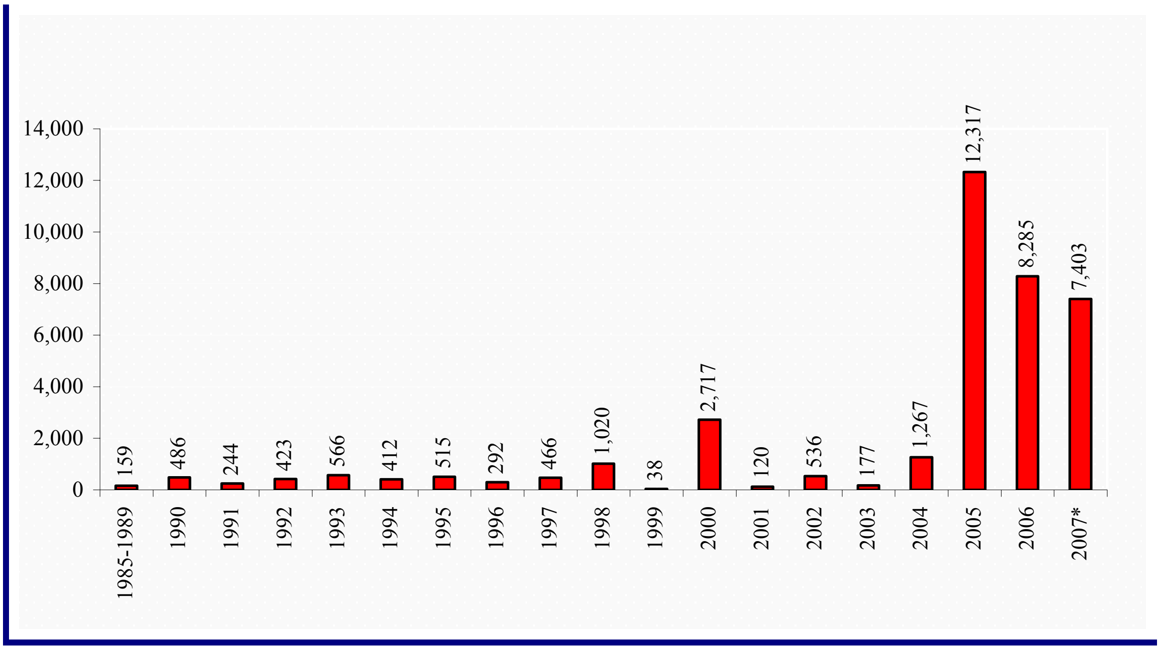
For the energy sector, basic reform areas involve completing the secondary energy legislation, privatizing public generation and distribution assets, spreading natural gas use across the country, establishing the Stock Agency, fighting illegal fuel, energy efficiency, geothermal and natural mineral water resources and renewable energy resources.

4.1. Enterprise Sector

4.1.1. Privatisation

Privatisation practices in Turkey have had a serious momentum from 2005 onwards. While the total revenues from the privatization operations for which sale/transfer processes were completed, in 2006 were at 8.29 billion dollars, it was realized as 7.4 billion dollars as of October 2007.

Figure 4. 1: Sale Revenues of Privatisation Operations as of Years (Million Dollars)



*Covering January-October period of 2007.
Source: Privatization Administration, SPO

Table 4.1 presents the list of privatization transactions for which sales/transfers were completed from November 2006 to October 2007.

The total amount, for privatization of Petrokimya Holding A.Ş. (PETKIM), TCDD Izmir and Derince Ports and various real estates, and 20-year lease of Sabiha Gökçen Airport of the Undersecretariat of Defence Industries for which tenders have been completed and sales/transfers approvals or contracts are in progress in 2007, is 6.16 billion dollars.

The following are the companies/assets included in the 2007 privatization portfolio (entities included in the privatization program):

- Bridges and highways,
- Turkish Sugar Factories Inc.[9],
- Sumer Carpet and Handcrafts Industry and Trade Inc. (SÜMERHALI),
- Doğusan Pipe Industry and Trade Inc.

In the scope of the Ninth Development Plan, it is aimed by the end of 2013 that the public sector will withdraw, as a result of privatization operations, totally from airlines and maritime transportation, locomotive and railway car production; sugar, tobacco and tea products processing, petro-chemicals industry, electricity distribution and wholesale trading; and decrease its share in electricity generation, natural gas market, coal and other mining operations as well. It is contemplated that State Economic Enterprises engaged in grain purchasing, seed production, railway transportation, electricity transmission, oil exploration, airport operations, postal services and coastal security provision will not be privatized in the plan period.

The transfer of operating rights during the process of privatization of İzmir and Derince Ports belonging to TCDD will be completed after the approval of the concession contracts by the Council of State. Furthermore, tender preparations for Bandırma, Iskenderun and Samsun Ports are continuing, and it is aimed to start the tender procedures in a short period of time.

[9] Tenders opened for Bor, Ereğli and Ilgın Sugar Factories and state held shares of Kayseri Sugar Factory were cancelled, and all factories of Turkish Sugar Factories Inc. under the privatization scope were included in the privatization program.

Table 4. 1: Privatisation Transactions Completed During the Period of November 2006-October 2007

Company	Privatisation Transaction	Sales Price (Dollars)
HMİ	Leasing of Antalya Airport for 17.5 Years	3,197,000,000
HALKBANK	Public Offering of 24.98 per cent of Public Shares	1,838,642,981
Treasury	Beşiktaş Real Estate of General Directorate of Highways	800,000,000
TCDD	Mersin Port	755,000,000
Vehicle Inspection Station	II. Region	313,250,000
Vehicle Inspection Station	I. Region	300,250,000
Sümer Holding	Real Estate in Kırklareli-Lüleburgaz	58,000,000
Pension Fund	Çelik Palas Hotel	38,900,000
TDÇİ	Deveci Iron Mine Field	21,500,000
Other	Sale and Transfer of Various Assets and Plants	161,114,396
TOTAL		**7,483,657,377**

Source: Privatization Administration

Tenders were announced for cigarette factories of TEKEL, and the tender process for Çamaltı and Ayvalık saltpans will be commenced as soon as possible.

Preparations for the privatization of electricity distribution companies have been completed to a large extent. In addition, efforts are continuing to realize the privatization of electricity distribution and generation simultaneously.

Tenders were announced for the privatization of Tercan, Kuzgun, Mercan, İkizdere, Çıldır, Beyköy and Ataköy Hydroelectric Power Plants of Ankara Doğal Elektrik Üretim ve Ticaret A.Ş., and Denizli Geothermal Power Plant. The tender process for Mazıdağı Phosphate Plant is continuing.

Preparations were completed to a large extent for the draft terms of reference for the privatization of lottery games, which is an another privatization project on the agenda of the Privatization Administration, and a draft bill that include market regulation mechanisms and rules after the privatization has been prepared. After the mentioned draft bill is legislated, the privatization transactions will be started.

4.1.2. Competition Law and Policies

Even though the Turkish competition legislation is largely in conformity with the EU legislation in terms of antitrust rules, for an efficient implementation of competition law, changes are called for in the legislation and the institutional structure in the light of the past practices and EU experience. The draft bill about which the opinions of the concerned institutions have been obtained is on the agenda of the Turkish Competition Authority.

As regards the implementation of the Law on the Protection of Competition No.4054, no distinction has been made between public undertakings and private undertakings. Within this framework, as in the case of other M&A, the transfer of public authorities to private sector is also examined and supervised by the Competition Authority. However, the fact that public monopolies have certain privileges brings a distinction between their transfer by privatization and the M&A among private undertakings. Thus, the Competition Authority carries out its supervisory function with regard to privatizations by making a different regulation. Communiqués No. 1998/4 and 1998/5 set forth the procedures and principles to be followed in preliminary notifications and authorization applications to the Competition Authority in order for the transfer transactions to be made by the Privatization Administration or other public organizations to become legally operative. These regulations are particularly important, not only in M&A, but also in respect of the duty of competition advocacy of the Competition Authority.

With the Communiqué No.2007/2 on the Amendment of the Block Exemption Communiqué on Vertical Agreements, which came into force on 1 July 2007, a market share threshold of 40 per cent has been introduced in line with the relevant regulations of the EU and within the framework of the previous experience of the Competition Board. This practice aims to prevent those undertakings with market power from establishing contracts that create barriers to entry into the market. According to the new practice, block exemption is implemented where the market share of the supplier in the relevant market in which it provides the goods or services concerning the vertical agreement is no greater than 40 per cent, or, as regards vertical agreements which include the obligation to supply a single buyer, where the market share of the buyer in the relevant market in which it receives the goods and services concerning the vertical agreement is no greater than 40 per cent.

Additionally, another amendment introduced with Communiqué No.2007/2 grants the Competition Board the authority to remove agreements containing certain restrictions in the relevant market from the cover of the block exemption, in cases where parallel networks created by vertical restraints of a similar nature cover more than 50 per cent of the relevant market. On the other hand, the wording of "a significant part of the relevant market" used in determining the market volume of the parallel networks has been replaced with the "more than 50 per cent of the relevant market" criterion. The goal of the introduced criterion is to increase legal certainty for undertakings by binding the withdrawal of the exemption to an objective criterion.

There is not a specific legislation regulating the relationships between the Competition Authority and sectoral regulatory agencies. The Law No.4054 on the Protection of Competition applies to all sectors except mergers between banks whose total assets' share in the sector exceeds 20 per cent level. In the framework of the provisions of the Wireless Law No.2813, the Competition Board firstly considers the opinion of the Telecommunications Authority and the general regulatory activities carried out by the Authority in respect of examinations, inquiries and investigations, and decisions about M&A related to the telecommunications sector. In Electricity Market Law No. 4628 and Natural Gas Market Law No. 4646, the Law No. 4054 is specially referred for antitrust issues in the related sectors.

Regulatory Impact Analysis (RIA), which represents an important innovation in terms of legislation process, has been put into effect since 2007. Impact analyses take into account whether the regulations enable firms to be in a strong or dominant position, whether their effects increase or decrease the number of firms, whether competition is restricted or not and whether competition level is strengthened or not. RIA process will be carried out with the Competition Authority. Competition impact assessment included in RIA will contribute to the strengthening and institutionalization of competition advocacy role of the Competition Authority.

On the other hand, in order to harmonize with EU legislation in the field of competition law and policy, draft law, which stipulates that a department shall be established in order to create a supervisory mechanism in order to supervise and monitor state aid in terms of competition, has been presented to the Prime Ministry and it is foreseen that it will become a law within the year of 2008.

4.1.3. Improvement of the Investment Environment

Activities to expand the role of the private sector in the economy maintain its priority in the macroeconomic stability program of the government. In this respect, efforts to improve the investment environment being undertaken since 2001 aim to rationalize the investment related procedures, and increase the volume of international foreign direct investments to Turkey.

Efforts to improve the investment environment are carried out by the Coordination Council for the Improvement of the Investment Environment (YOIKK), a national platform based on public and private sectors cooperation, and the Council functions through 11 Technical Committees[10] each assigned for a different theme of the investment environment.

[10] Company Founding, Employment, Sectoral Licenses, Investment Location, Taxes and Incentives, Foreign Trade and Customs, Intellectual and Industrial Property Rights, Investment Promotion, Foreign Direct Investment Legislation, SME, Corporate Governance.

YOIKK aims to rationalize the investment related regulations in Turkey, develop policy proposals by identifying regulations necessary to increase the competitiveness of the investment environment and generate solutions to administrative barriers confronting the national and international investors during all phases of investment including the operation period. The active participation of the private sector to the attempts for improving the investment environment in the structure of YOIKK is encouraged and thus great importance is given to include private sector representatives in each Technical Committee along with public sector representatives.

The Steering Committee, which was established in May 2005 aiming to accelerate the works under YOIKK, meets every month with its agenda on a specific draft bill or a different aspect for enhancing the investment environment, and monitors the progress in the works carried out by the Technical Committees.

Important improvements were achieved as a result of the works carried out regarding the investment environment and dealt with under the YOIKK platform since 2005.

By amendments made in 2007 to the By-Law on Opening a Business Place and Work License, significant improvements were realized regarding the sectoral licenses such as simplifying the licensing process, licensing based on declaration, Environmental Impact Assessment (EIA) Report substituting various documents.[11]

Legislative act that amended the provisions of the Land Registry Law regarding property acquisition by foreigners[12] came into effect on 7 January 2006.

Opinions obtained for the Draft Bill Amending the Coastal Act prepared by the Ministry of Public Works and Settlement are now being considered by the Ministry. Works for the Planning and Zoning Draft Bill are continuing.

It is expected that the Turkish Commercial Code draft bill, which is on the agenda of the TBMM, will be enacted in 2007. With this legislation, it is aimed to harmonize with the equity companies part of the EU Company Law legislation, provide legal infrastructure needed by trade and business actors, and increase the international competitiveness of our companies.

Efforts are continuing to get over the problems in the company closing process, to reduce costs of company establishments, and to allow establishment of companies electronically.

The SME Strategy and Action Plan that aims to implement national SME policies and increase competitiveness of SMEs was revised and approved by the High Planning Council in 2007.

Works are continuing to legislate the Draft Bill on Amending the Law No.4817 on Work Permits for Foreigners prepared by the Ministry of Labour and Social Security in order to get over the problems experienced in the implementation process related to work permits for foreigners.

The Twinning Project Toward Improving Investment Environment in Turkey: Comments on YOIKK Reform Process carried out by the Undersecretariat of Treasury and the German Ministry of Economy was completed in September 2006. Under the project, reforms realized by the YOIKK platform were reviewed in terms of possible impacts on the private sector investments and international foreign direct investment inflows to Turkey, EU legislation and principles of best practices in EU (and OECD) countries. Findings and recommendations in the project final report are considered in YOIKK process.

It is aimed to identify professions for which standards shall be established by the Professional Qualifications Institution and thus progress significantly in the process of establishing vocational qualification infrastructure by the end of 2007.

[11] Regulation on Amending the Regulation on Opening a Business Place and Work License, published in Official Gazette dated 13.04.2007, No.26492.

[12] Law amending the Law No.5444 Land Registry Law, published in Official Gazette dated 07.01.2006, No.26046.

The Corporate Governance Technical Committee was formed on 24 November 2005 under the Chair of the Capital Markets Board (CMB) in order to conduct studies within the YOIKK to implement and promote corporate governance principles in Turkey. The Committee decided that two projects should be worked on; one is to identify the best practices of corporate governance implementations for unlisted companies, and the other is to complete the legislative infrastructure to determine and implement corporate governance principles in the state owned companies and these two projects are started to be carried out. With the Corporate Governance in the Unlisted Companies Project, it is aimed to identify and promote corporate governance principles applicable to unlisted companies, raise awareness for corporate governance, to ensure their more effective participation in the economy by monitoring and improving practices. In addition, the Corporate Governance Project in State Owned Companies, which aims to implement modern corporate governance principles in state owned enterprises.

4.1.4. Utilities and Network Industries

Monitoring the developments regarding utilities and network industries is important for the functioning of the enterprise sector. In this context, energy and telecommunication sectors are assessed in terms of service level, competition, status and effectiveness of regulatory authorities and boards.

Energy

The Energy Market Regulatory Authority (EMRA), which is administratively and financially autonomous, executes the function of regulation and supervision independently in the energy market (electricity, natural gas, petroleum and LPG). The decision making body of the authority is the Energy Market Regulatory Board. The Board makes its decision without being influenced by the government or any market players. Lawsuits against the Board's decisions are undertaken by the Council of State as the court of first instance.

Access to the transmission and distribution network is subject to regulation in order to ensure the competition in the electricity market. In this context, legal entities holding licenses of transmission or distribution are obliged to provide system access and system utilization rights to real and legal entities without any discrimination. Prices, principles and procedures in accessing to system and system utilization are subject to regulation of the EMRA.

Related to the companies operating in the electricity market, all transactions such as transfer, sale, merger or change of control exceeding a certain threshold (10 per cent, 5 per cent for the corporations registered in Capital Markets Board) are subject to the Board's approval. However, the Competition Authority has the reserved right to permit M&A in the market in the scope of Article 7 of the Law No.4054 on the Protection of Competition. The total share of the market that could be owned by a private sector generation company may not exceed 20 per cent of the total electric energy power installed of the previous year in Turkey. Similarly, the total share of the market that could be owned by a private sector wholesale company may not exceed 10 per cent of the total amount of electric energy consumed in the previous year in Turkey.

For each activity in the market, the entity carrying out the said activity must keep separate account and record for each the activity, plant and region.

Analyzing the energy market in terms of tariffs, it is observed that transmission, distribution, sales to captive consumers, and the wholesale electricity tariffs of TETAŞ are subject to regulation. The basic principle for the tariffs is that the tariffs should reflect costs, and no cross-subsidies should be applied. Support to certain regions and/or certain consumer groups can be given in the form of rebates to consumers without affecting the regional tariff structure provided that the amount of support and the related principles and procedures be specified by a decree of the Council of Ministers. Furthermore, price equalization implementation on the basis of tariff groups was introduced across the country in the transition period that is expected to continue till the end of 2010. Tariffs prepared in this framework were approved by the Board. The mentioned price equalization mechanism is an instrument supporting the transition period. By this way, losses will be offset between the revenue requirements of the distribution companies without disrupting the national tariffs.

Furthermore, international interconnection lines are allocated to legal entities, which wish to make electricity export/import, through tenders by TEİAŞ. When more than one legal entity applying to use the same interconnection line exists, TEİAŞ requires license holding legal entities to participate in the tender and submit bids for the congestion management price. The capacity shall be allocated on the basis of bids submitted by the license holding legal entities. License holding legal entities utilizing the interconnection lines must pay, in addition to the congestion management price, system utilization fees to TEİAŞ and/or relevant distribution license holding legal entities in the context of the import and/or export activity. Under the condition that there is only one license holder that wishes to utilize the interconnection line, no tender will be held and the capacity of the mentioned line will be allocated to the said license holding legal entity. In this case, the said license holding legal entity shall not have to pay the congestion management price.

Telecommunication

The most important structural change in the Turkish telecommunication sector is the Law No.4502 which introduced amendments to the fundamental laws regulating the sector. By this Law, the Telecommunication Authority was established, and the functions of policy and strategy formulation and regulation and operation were separated. While the policy and strategy formulation functions were naturally left with the Ministry of Transport, the regulatory functions were entrusted to the Telecommunication Authority. The Law ensures perfect competition for the value added services and establishes a transparent licensing regime as well as sets the duration of Türk Telekom’s monopoly and provides commercial independence to Turkish Telecom by containing clear provisions on such major matters as pricing and interconnection.

The basic objective of the Telecommunication Authority is to ensure full liberalization in the sector. The Authority will serve mostly as a regulatory body in the liberalization process, then minimize its regulatory functions at the end of liberalization, however will continue its supervisory and arbitration roles in order to ensure a sustainable competitive environment in the sector. The Authority is important for ensuring continuity, order, reliability and transparency in the sector.

The effective functioning of the Authority contributes to establishing a sustainable competitive environment in the sector, thus new operators and new investors can enter into the sector and employment opportunities can increase.

Important progress was achieved in the regulations for the sector. In this context, important steps in liberalizing the sector have been taken in terms of the secondary legislations issued by the Authority. In general outlook, the sectoral infrastructure now has mostly digital technology and, in terms of the service area, services can now be served across the country. As of September 2007, the mobile penetration rate was realized as 84 per cent, the fixed telephone penetration rate was 25 per cent and broadband penetration rate (DSL, cable, ISDN, leased line, satellite) was 5.8 per cent.

For the regulatory area, sectoral regulations are mostly made by the Telecommunication Authority. Nonetheless, the Authority takes into account the views of the sector and relevant agencies in its regulations and decisions. In this context, the Telecommunication Authority consults the views of the Competition Authority pursuant to Article 6 "Market Analysis" third paragraph, (c) subparagraph, of the Regulation on Procedures and Principles for Identifying Operators with Effective Market Power, dated 7 November 2007. The Competition Authority also consults the views of the Telecommunication Authority pursuant to Article 7 of the Law No.2813.

Operators with effective market power are obliged to prepare reference access and/or interconnection proposals and submit them to the Authority. The mentioned proposals are issued when approved by the Board. Currently, the reference offers of all the mentioned operators are placed on the internet website of the Authority.

The basic document for access to the local network, as in the case of interconnection, is the reference offer prepared by the incumbent operator and approved by the Authority. The reference offer that includes basic issues on technical, administrative and financial matters, serve as the basis of contracts to be signed among the operators, as in the case of interconnection. Approved reference offer was announced on the internet website of the Authority on 1 August 2007.

When the relevant operators fail to agree within the maximum three months time following the access request including the interconnection, any party can request from the Authority to apply the settlement procedure. In this context, settlement procedures were applied and concluded in 2007 upon the settlement requests of various operators filed to the Telecommunication Authority.

The Telecommunication Authority, when necessary publishes the Standard Interconnection Reference Fee Tariffs (SARUT), and the mentioned tariffs remain in effect until the new one is issued by the Authority. In this context, the SARUT for Türk Telekom and the GSM Operators with Effective Market Power (EMP) was issued on 15 January 2007, as presented in Table 4.2.

Table 4. 2: Standard Interconnection Reference Fee Tariffs

Implementation Date	Tariffs for the Call Starting and Ending in the Network of Türk Telekom (New Turkish Kuruş/Min.)		Call Ending Tariffs in GSM Networks (New Turkish Kuruş/Min.)		
	Inside Area	Outside Area	Turkcell Communication Services A.Ş.	Vodafone Telecommunication A.Ş.	Avea Communication Services A.Ş.
01.01.2007	2.0	3.7	14	15.2	17.5
01.03.2007	1.89	3.0	13.6	14.5	16.7

Source: Telecommunication Authority

In the European Union Accession Partnership Document in 2003, two major priorities were specified as the harmonization with the EU legislation in telecommunication and information technologies, and the preparation of markets for the full liberalization, and in this context, it was deemed appropriate to provide support to our country by the Technical Assistance Project on Developing Access Framework in the Turkish Telecommunication Market. The mentioned project aims to earn the Telecommunication Authority experience and competence on the accounts separation principles needed for cost based access pricing required in the EU regulatory package and cost models. The project is planned to be initiated in December 2007.

4.2. Financial Sector

4.2.1. Banking Sector

Within the framework of the public banks' privatization strategy, state-owned shares of Halkbank are put under the privatization scope and program by the Privatization High Council Decision No.2007/8 dated 5 February 2007. About 25 per cent of the bank's shares were privatized through public offering in May 2007. In light of the Halkbank experience, a privatization strategy for Ziraat Bank will be formulated.

The efforts have been continuing towards minimizing the burden imposed by the process of dissolving the banks under SDIF on the public. In this context, between the date of transfer to SDIF and June 2007, a total of 15.3 billion dollars was collected from claims under legal prosecution, claims restructured for an agreed payment plan, sales of participations, affiliates, property, security and bank sales by SDIF. In addition, revenue of 6.9 billion dollars is expected in proceeds from the liquidation of the assets of banks transferred to SDIF. Adabank was sold on 3 July 2006 by SDIF; however BRSA did not approve the share transfer and registration because of deficiency regarding the qualification of founders. Efforts towards dissolving Adabank are continuing. SDIF is expected to dispose of the remaining assets of banks taken over by the end of 2007. Thereby, the Fund will focus on its primary mission of deposit insurance.

As of 1 November 2006, secondary legislation related with the Banking Law No.5411, which went into effect on 1 November 2005 in order to fully harmonize with the EU Directives and international principles and standards, was completed. Within the context of these regulations:

- In order to fully harmonize with the EU legislation, regulations related to banks' equity were renewed, regulations on banks' capital adequacy were renewed and the concept of operational risk is added to the calculation of capital adequacy.

- The Regulation on Banks' Internal Systems was issued, taking into consideration the international standards regarding internal audit, internal control and risk management, Basel criteria and relevant EU legislation.
- Corporate governance principles were adopted as principles that contribute to the management of banks in a manner that is more effective, sound and protective for the interests of deposit owners.
- Principles and procedures were laid down for banks regarding fulfilling and maintaining adequate liquidity levels.
- Provisions regarding the establishment and activities of rating organizations were laid down.
- The scope of non-performing receivables was expanded, general provisions for new cash and non-cash loans were doubled in order to strengthen financial structures of banks, and a practice was developed to calculate the new ratios over the exceeding amounts on the basis of cash and non-cash loan amounts subjected to general provision practice prior to the effective date of the regulation.
- Establishment and operational principles of financial leasing, factoring and consumer financing companies, on which BRSA now holds responsibility for supervising and monitoring, were integrated in a single regulation to ensure uniformity, and regulations similar to those of the banks were laid down.
- For financial statements and reporting, implementation of the Turkish Accounting Standards, which are fully in compliance with the International Accounting Standards, is decided.
- Principles of independent auditing that are significantly in compliance with the International Auditing Standards was put into practice
- Risk focused auditing practice has been initiated.
- Principles and procedures were set regarding the auditing of banks' information systems and financial data generation related processes and systems by independent auditing organizations.
- The Banking Ethics Principles is issued and put into effect in order to ensure continuity of existing social respect for the banking profession and stability and confidence in the banking sector.
- The principles and requirements for all announcements and advertisements of banks via communication devices or any other means were set by the Banks Association of Turkey.

Discussions regarding the implementation of the Financial Sector Assessment Program (FSAP) in Turkey, which is jointly conducted with IMF and World Bank and where the compliance of the financial sector with international standards and best practices is assessed, were completed in March 2007.

The legislative infrastructure for restructuring the SME debts to the financial sector, known as the "Anatolian Approach" was completed and put into effect in 2007. This approach works on the basis of voluntary participation as in the Istanbul Approach, and is not expected to make any adverse impact on the market discipline and competition.

With the integration of Basel-II provisions into the EU acquis, radical changes occurred in the calculation of the capital adequacy of banks. Various quantitative impact studies (QIS) were conducted to examine the impact of clauses of Basel-II and relevant EU directives on the capital adequacy of banks in the Turkish banking sector. Firstly, the QIS-3 study conducted by the Basel Committee in 2003 was participated. Following that study, the first domestic quantitative impact study QIS-TR1 was conducted with 23 banks that constitute about 95 per cent of the sector, in 2004. Finally, the second domestic quantitative impact study QIS-TR2 was conducted with 31 banks representing about 97 per cent of the sector, based on September 2006 data. With the effect of the changing portfolio structures of banks, this study revealed better results compared to the previous QIS studies. According to the results of the study, while the capital adequacy ratios of the participant banks was 19.3 per cent under the legislation in effect, this ratio receded by 5.6 percentage points to 13.7 per cent under CRD/Basel-II. The increase of the risk weight of the foreign currency denominated government securities, which were classified in the public portfolio and trade accounts, to 100 per cent, was the most important factor in the decrease of the banks' capital adequacy ratios. Following the negative effect of public portfolio, the second highest negative impact on the sector's capital adequacy stem from inclusion of the operational risk and corporate portfolio.

In the relevant directives of EU (CRD), as in the Basel-II documents, it was required that the operational risk aspects should be included in the calculation of capital adequacy in addition to the credit and market risks; the assessment of the credit risk should be based on rating results not on the nature of the collateral; and the member states should complete their national legislation by the end of 2006 and put them into effect on 1 January 2007. Pursuant to the regulation issued on 1 November 2006, capital adequacy calculation by including the operational risk aspect, one of the two fundamental changes introduced by CRD, would start in June 2007 in the Turkish banking system, taking into account the considerable improvement in the banks’ advanced technology infrastructure, qualifications and capital adequacy levels. Thereby, the capital adequacy calculation partially compliant with CRD was commenced about six months earlier than the schedule indicated in the Basel-II road map announced by BRSA. However, it was concluded that the rating based credit risk evaluation in the bank capital adequacy calculation should be postponed to the beginning of 2009 and the rating based calculation would only be done for indicative purposes.

4.2.2. Capital Markets

At the end of 2006 and in 2007, 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 EU-Supported Technical Assistance Project for Building up Capacity for the Capital Markets Board was realized between December 2006 and July 2007 in order to obtain technical support from foreign experts to identify information technology infrastructure, which is necessary for implementing the legislation in line with the EU.
- In September 2006, hedge funds were included in the funds existing in the capital markets, as well. For qualified investors, investment opportunities in these funds were made more flexible and reporting requirements were alleviated.
- As a result of the goal to expand the product variety in the capital markets, the Communiqué for Establishing Funds of Funds was issued in November 2006.
- The Law on Housing Financing System was put into effect in March 2007. Following the Law, the Communiqué on Mortgage Covered Securities and the Communiqué on Principles of Housing Financing Funds and Mortgage Backed Securities were issued, and amendments were made to the Communiqué on Companies Providing Valuation Services under the Capital Markets Law in August 2007.
- In April 2007, the Communiqué on Establishment and Operations of Forward Transactions Intermediary Companies, which are expected to make positive contribution to forward transactions markets as specialized organizations, was issued.
- In May 2007, a communiqué for guaranteed funds and protected funds was issued.
- With amendments in July 2007 to the Communiqué on Principles of Licensing and Registration for Those Operating in Capital Markets, the introduction of a license examination was regulated on topics such as independent audit, credit rating and corporate governance, and the concerning principles were laid down.

The list of actions to be carried out in the period of 2007-2010 in order to increase supply and demand in capital markets, ensure confidence and stability in the markets, create a legislation in compliance with the EU, and establish infrastructure necessary to implement such legislation, are as follows:

- In the context of harmonization with the EU legislation, the project, which was prepared to benefit from the PHARE program under the 2004 Programming of Pre-Accession Financial Assistance being provided to Turkey by the EU, was initiated in February 2006. In the framework of this project, regulation drafts were prepared on market abuse, prospects, protection of investors, independent auditing, clearing and collaterals, share purchase bids, company law, and works for preparing drafts are continuing on investment funds, investment services, capital adequacy of intermediary institutions, public disclosure and other matters concerning capital markets. In the scope of this project, the guidelines for RIA were prepared, training seminars and study visits were organized, works were started to strengthen administrative capacity, and a seminar was organized in June 2007 widely participated by sector representatives and project proponents in order to inform the public. As a result of two years works, draft bill on the Turkish Capital Markets legislation compliant with the relevant EU legislation and accompanying by-law and communiqué drafts legislation will be prepared and upon completion of the works about establishing the administrative infrastructure compatible with this, the project will be completed in December 2007.
- In the context of the bilateral cooperation technical assistance provided by member states in the EU candidacy process, a two-year project was initiated in January 2007 on Establishing Effective Supervision System for Financial Reporting by Listed Companies and Establishing More Effective Remote Supervision System for Intermediary Institutions Operating in Capital Markets financed by the Dutch Government , and in the context of the project, it is aimed to set up and implement effective supervision mechanisms.
- Within the scope of amendments such as the implementation of inflation accounting and increasing minimum capital amount, works for revising the criteria for redefining total assets and capital exemptions, and cancellation of the registration from the Board and preparing a concerning communiqué draft are continuing.
- Efforts will be continued to monitor and improve corporate governance practices.
- The Communiqué on Principles for Board Registration and Sale of Foreign Capital Market Instruments will be amended in comply with EU regulations.
- Works are envisioned on facilitating the issue of loan bills and regulating structured capital market instruments.
- Efforts will be continued to create a registry system to provide timely and effective supervision of reporting requirements imposed on all independent auditing firms listed at CMB.
- It is aimed to make the existing accounting standards comply with the updated version of the International Financial Reporting Standards.
- In addition to the secondary legislation issued in August 2007 for establishing the housing finance system, works are continuing to prepare the secondary legislation on asset covered securities, asset financing funds, asset backed securities and mortgage financing entities, and these works are expected to be completed in 2008.
- Efforts are continuing to allow establishing real estate mutual funds, and expected to be completed in 2008.
- Efforts for revising the Communiqué on Real Estate Investment Trusts are targeted to be completed in 2008.
- Fund Transfer System (Fontra) works will be made to establish a sharing platform for trade of participation certificates.
- Infrastructure works will be initiated to establish Association of Real Estate Appraisal.

- Efforts will be made to allow portfolio management companies to become founder of a fund.
- Works will be started to create the licensing and training center as a joint-stock company by participation of market participants.
- In the CMB-ISE surveillance system project, aiming to compile data on ISE's session transactions, perform real time oversight via reports and screens, and detect manipulative transactions in particular, efforts are continuing for improvement and tests to realize the monitoring platform and are aimed to be completed in 2008.
- The completion of the test process for the Public Disclosure Project initiated to compile financial statements, notes, annual reports and special disclosures for ISE listed joint stock companies and intermediary institutions via the Internet securely by applying e-signature technology was scheduled for 2008 for technical reasons. On the other hand, the draft Communiqué on Principles for Signing and Transmitting Information, Documents and Disclosures in Electronic Medium within this project was prepared and is expected to go into effect in the first quarter of 2008.
- The project titled "advanced monitoring" to use artificial intelligence in the capital markets, and consider investor behaviour in the monitoring system as the next step of monitoring, the project titled "electronic data compiling, electronic application and registration" that would ensure easy, fast and secure access to data, and the project titled "strategic information systems planning" envisioned to plan the future actions in the information technologies are planned to carry out by the EU technical assistance. In this context, technical assistance was obtained from EU for identifying needs, and application process will be initiated for EU in order to realize these projects in the coming period.

4.2.3. Insurance Sector

There are 47 companies in insurance and private pension sectors, as end of year 2006. Of these companies, 25 operate in non-life, 10 in life, 10 in private pensions and life, 1 in private pension and 1 in reinsurance area. The total assets of the insurance sector in 2006 went up by 21 per cent compared to the previous year and reached 18.6 billion YTL, premium generation went up by 24 per cent to 9.7 billion YTL and the number of contracts went up by 15 per cent to 34 million pieces. Thereby, the share of the insurance sector in GDP was realized as 1.7 per cent.

The Private Pension System was put into practice in October 2003 as a complement to the public social security system. This system is expected to play a major role in the accumulation of long-term capital in the economy. The private pension sector is showing a high growth trend. As the end of 2006, the number of participants in the private pension system exceeded 1.1 million persons, the number of contracts exceeded 1.2 million and the funds collected reached 2.7 billion YTL. While the number of contracts increased by 64 per cent in 2006, the increase in savings and contributions were realized as 132 per cent.

As a result of the efforts to create a new legal basis that would meet the needs of the insurance sector, considering the need for insurance regulations' compliance with the EU legislation and international standards, the Insurance Law No.5684 was legislated on 14 June 2007.

The purpose of the mentioned Law is to re-regulate the issues regarding the principles and procedures for commencement, organization, administration, operation, activity abortion and inspection, of persons and entities subject to this law, in consideration of international developments and EU regulations. Thereby, development of insurance sector in our country, protection of rights and interests of individuals in the insurance contract, and ensuring efficient operation of insurance sector in a secure and stable environment are targeted. This law also regulates the principles and procedures for the insurance arbitration system for solving disputes arising from insurance contracts.

Efforts for the related secondary legislation of the mentioned Law are continuing in consideration with the EU legislation and international practices. The secondary legislation about the Law is required to be prepared and put into effect within a year.

4.3. Labour Market

Within the framework of employment focused sustainable growth and towards a competitive economy and information society, the basic priorities are to develop employment opportunities, reduce unemployment, enable labour market to function effectively, establish an effective relation between education and employment, shift labour exiting from the agricultural sector to other sectors, promote active labour market policies and increase resources earmarked for such policies.

Turkey is now leaving behind the period of high population growth and the impact of problems arising from population growth in the development process is diminishing gradually. According to the population projections renewed in 2005, the annual population growth rate, which is 1.21 per cent in 2007, is expected to be 1.18 per cent, 1.15 per cent and 1.11 per cent in 2008, 2009 and 2010 respectively. The mid-year population, which is 73.9 million in 2007, is expected to reach 74.8 million, 75.6 million and 76.5 million in 2008, 2009 and 2010, respectively. The aggregate fertility rate, which is 2.17 in 2007, is expected to be 2.15, 2.14 and 2.12 in 2008, 2009 and 2010, respectively.

While the share of 0-14 age group in the total population is decreasing, the share of working age population and elderly population is increasing.

Table 4. 3: Population Projections by Age Groups

(Per cent)

Age Groups	2000	2007	2010	2020
0-14	30.0	27.7	26.6	23.2
15-64	64.7	66.2	67.2	69.1
65+	5.4	6.0	6.3	7.8

Source: TURKSTAT

The employment created in Turkey in the 2000-2006 period lagged behind the increases in working age population and labour force. In this period, the employment, the working age population, and the labour force rose by 0.6 per cent, 1.9 per cent, and 1.2 per cent, respectively, annually on average. The most important reason for limited increase in employment was the decline of employment in the agricultural sector due to the structural transformation in the economy. The share of agricultural sector in the employment receded from 36 per cent to 27.3 per cent in the period of 2000-2006. Particularly after 2003, along with the high economic growth, the employment in the non-agricultural sectors went up significantly.

Among the other reasons for the low increase rate of the total employment were increases in labour productivity and working hours. Following the economic crisis, the increases in labour productivity and long hours of work required by employers limited the creation of new jobs. As a matter of fact, the weekly actual working hours, which were 43.8 hours on average in 2000 across all sectors, reached 51.4 hours on average in 2005, according to the TURKSTAT Household Labour Surveys (HIA).

The labour force participation rate in Turkey is significantly lower than EU averages. This rate was 50.2 per cent in our country, whereas it was 71.6 per cent in the EU-15, in 2006. The main reason is that women's labour force participation rate is considerably low. Female labour force participation rate is lower than that of male, both in rural and urban areas. Thus, the male labour force participation rate is 70.8 per cent in the urban areas, and 72.2 per cent in the rural areas, whereas these ratios are 19.9 per cent and 33 per cent, respectively, for female.

Table 4. 4: Basic Employment and Labour Indicators

(Per cent)

	Turkey				EU-15			
	2003	**2004**	**2005**	**2006**	**2003**	**2004**	**2005**	**2006**
Labour Force Participation Rate (15-64)	51.1	51.5	51.3	50.2	70.1	70.6	71.0	71.6
- Female	28.1	27.0	26.5	26.1	61.6	62.6	63.2	64.1
- Male	74.0	76.1	76.2	74.4	78.6	78.6	78.9	79.2
Employment Rate (15-64)	45.5	46.1	45.9	45.9	64.3	64.5	65.2	66.0
- Female	25.2	24.3	23.7	23.9	56.1	56.5	57.4	58.6
- Male	65.9	67.9	68.2	68.1	72.6	72.4	72.9	73.5
Unemployment Rate (15-64)	10.8	10.6	10.5	10.1	8.2	8.4	8.3	7.9
Unemployment Rate (15+)	10.5	10.3	10.3	9.9	8.1	8.3	8.2	7.8
- Rural	7.3	5.9	6.8	6.5	-	-	-	-
- Urban	14.3	13.6	12.7	12.1	-	-	-	-
Non-Agricultural Unemployment Rate	13.8	14.3	13.6	12.6	-	-	-	-
Youth Unemployment Rate (15-24)	20.5	19.7	19.3	18.7	16.1	15.5	16.2	16.7

Source: TURKSTAT, EUROSTAT

After migrating to the urban areas, women, being employed as unpaid family worker in the rural areas, fall out of the labour force because they have insufficient qualifications for jobs, and children, elderly or disabled care in the family becomes a problem.

Informal employment continues to be one of the significant problems of the labour market. According to the TURKSTAT HIA figures in 2006, about 48.5 per cent of the civil employment is informal, where as this figure is 33.9 per cent in the non-agricultural sectors. The high rates of informal employment create a dual structure in the labour market and lead to unfair competition among enterprises.

Efforts were commenced to alleviate the high non-wage labour costs that emerge depending on the number of workers employed, and is one of the main causes of informal employment.

Flexible working conditions prevalent in EU countries cannot be applied effectively in Turkey. Disseminating flexible working conditions aiming to increase employment, reduce unemployment and informal employment, and increase employment of women and disadvantaged groups in the context of social inclusion is of particular importance. In order to disseminate flexible working conditions in the labour market, it is important to identify problems arising primarily from the Labour Law No.4857 and other legislation and remedy such problems, encourage flexible working conditions, and establish their relation with social security.

Table 4. 5: Trends in Gross Schooling Rates

(Per cent)

Level of Education	**1998-1999** (1)	**2005-2006**	**2006-2007**
Pre-School (2)	10.2	19.9	24.0
Primary Education (3)	94.3	95.6	96.4
Secondary Education (3)	57.1	85.2	86.6
- Standard High Schools	32.2	54.3	54.8
- Vocational-Technical High Schools	24.9	30.9	31.8
Higher Education Total (4)	16.3	43.4	46.0
- Formal	9.0	27.5	29.1

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

Increasing schooling rates is of great importance regarding the fact that labour force participation rates increase along with education level. Analyzed by periods, it is observed that the schooling rates increased significantly.

In Turkey in 2006, 66 per cent of the labour force, 66.7 per cent of the employment, and 59.9 per cent of the unemployed are made up of those with less than high school education including the illiterate. Insufficiency in the quality of labour force leads to low labour productivity and mismatch between labour supply and demand, and thus decreases the effectiveness of labour market.

Table 4. 6: Education Level of the Labour Force in 2006

(Per cent)

	Labour Force	Employed	Unemployed	Labour Force Participation Rate	Employment Rate	Unemployment Rate
Total	100.0	100.0	100.0	48.0	43.2	9.9
Illiterate	5.0	5.3	2.2	20.3	19.4	4.4
Pre-High School	61.0	61.4	57.7	46.9	42.5	9.3
High Schools and Equivalents	21.6	20.9	28.1	57.0	49.7	12.8
- Vocational and Technical High Schools	---	---	---	65.5	57.9	11.6
Higher Education	12.4	12.4	12.0	78.5	71.0	9.5

Source: TURKSTAT, HIA

Access to education and required education quality which are not at desired levels, inadequacy of vocational education quality, lack of in-service and lifelong education as well as inadequacies in capital accumulation and technological renewal cause that labour productivity in our country remain low compared to the EU and developed countries.

Table 4. 7: Comparative Labour Productivity Indicators in 2006

Country	Productivity per Employed(1) (in 1000 Dollars)				Productivity per Hour Worked (2) (Dollar)	Average Annual Hour Worked
	Overall	Agriculture	Industry	Services		
USA	88.1	54.8	97.3	85.8	44.0	2002
Japan	64.0	24.7	65.9	64.0	31.1	2057
Korea	48.3	18.2	64.5	45.3	19.8	2439
Belgium	80.8	55.6	78.0	80.5	45.9	1760
Germany	63.9	25.6	62.5	60.5	37.1	1723
Poland	38.8	5.0	41.4	45.9	20.1	1866
Romania	23.1	6.0	28.9	29.1	12.4	1864
Turkey	28.8	11.7	33.5	36.1	13.5	2129

(1) According to purchasing power parity, GDP/ Employment.
(2) According to purchasing power parity, GDP/Employment/Hours Worked.
Source: IMD World Competitiveness Yearbook 2007

National and international markets increasingly demand labour that is creative, has high analytic thinking abilities and can quickly adapt new skills and access information. In this context, the new curriculum prepared in line with today's conditions so as to increase education quality, was started to be implemented in primary education. The works of the curriculum preparation for vocational and technical secondary schooling have been completed to a large extent. Works are continuing to update curricula in general secondary schooling and vocational education programs under the Secondary Education Project aiming at secondary schooling reform.

The Primary Education Project that was started in 1998 and cost 600 million dollars was completed in 2007 and improvements were achieved in the physical infrastructure of primary education within the context of this project. In order to improve the education environment, classrooms are being constructed through "A Hundred Per Cent Support to Education Campaign" with the contribution of the private sector in addition to public resources.

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. Broadband internet access services have been provided to 29,000 schools and other educational institutions for effective use of Information Technology (IT) classes, and efforts are continuing to disseminate this service to all schools and educational institutions.

In order to make the occupational and technical education more effective, vocational and technical education programs at secondary level that were prepared according to the modular education system for 42 broad areas and would allow horizontal transitions were introduced across Turkey since the beginning of the 2006-2007 academic year.

It is of utmost importance to effectively direct occupational and technical education to meet qualified intermediate labour required by the labour market. While the share of vocational and technical education was 42.3 per cent in secondary education in 1995, this rate receded to 32.3 per cent due to the effect of different coefficient applications among school types at university entrance in the 2002-2003 academic year. However, with the effect of non-exam entry to vocational high schools introduced in 2002, this rate started to pick up again and reached 36.8 per cent in the 2006-2007 academic year.

Efforts continue to build up the capacities of Professional Qualifications Agency established in 2006 to create and operate the national professional qualifications system.

The draft of educational outcomes being prepared under the National Qualifications Framework based on defining associate, baccalaureate and postgraduate levels in tertiary education and knowledge and skills that students must have according to educational outcomes on the basis of programs at such levels will be completed by the end of 2007.

In 2007, it was decided by YÖK to transform Technical Education Faculties (except two) to Applied Technical Science Faculties in order to allow vocational school graduates to continue baccalaureate education in their own track and vocational high schools associate degree holders to switch to baccalaureate programs by vertical transition examinations. These faculties where applied education will be provided shall contribute to training qualified labour force demanded by the business world and alleviating "on the job training" costs because graduates will already have received practical training.

In order to support the development of SMEs and strengthen their competitiveness in the Eastern and Southeastern Anatolian Regions, The Human Resources Support via Vocational Education Project, that aims to develop human resources by modernizing and updating vocational education in selected provinces, was initiated by the Ministry of National Education and YÖK in 2007.

The By-Law on Building Joint Education and Training Programs by Higher Education Institutions with Foreign Higher Education Institutions which would allow the education institutions in our country and in foreign countries to operate joint diploma programs was put into effect in 2006.

Within the context of developing active labour market policies, The Active Employment Measures and Local Level Support to Turkish Employment Agency Project aimed to increase employability of women and youth and strengthen the institutional capacity of İŞKUR, which covers 28 provinces and is financed jointly by Turkey and EU was initiated in 2007.

A total of 5,673 persons were provided vocational education in 284 courses for employment guarantees and for starting up own business in various occupations by İŞKUR under vocational education to the unemployed in 2006. By financing obtained through fining business places, which failed to employ disabled and ex-convicts, 1,884 disabled persons and 1,664 ex-convicts were provided vocational education. Besides, a total of 1,687 unemployed persons were provided vocational education in 118 courses financed from the Unemployment Insurance Fund under the placement of unemployed persons on unemployment insurance in new jobs.

In 2006, by the Communiqué on Procedures and Principles for Those Who Take the Central Examination for Being Recruited as Workers to Permanent Positions in Public Agencies and Organizations and Those Who Are Not Included in the Central Examination due to Educational Levels and Their Placement, the acts and actions for job placement in the public organizations were simplified and gender discrimination was abolished in public organization worker requests in order to provide equal opportunity to women for entering the labour market. In addition, restrictions on age, gender, military service status discrimination for labour requests from public organizations, and in announcement of labour requests gender discrimination from private sector were abolished by İŞKUR. Besides, 12,743 unemployed women registered with İŞKUR were placed in jobs in 2005, and 16,424 in 2006. There was an increase by 28 per cent in placing unemployment women in jobs in 2006 compared to 2005. This increase indicates that some positive outcomes were achieved in projects and programs that aim to integrate women with the labour market.

An increase was recorded in 2006 compared to 2003 in the employment of the disabled, another group having difficulty in entering the labour market. While İŞKUR placed 12,481 disabled persons in jobs in 2003, it placed 23,781 disabled persons in 2006.

The Project for Strengthening Institutional Structure of İŞKUR, an Enhanced Employment Strategy for the Disabled and Vocational Rehabilitation was initiated in 2007 with the partnership of the Dutch Ministry of Economic Affairs and the Turkish Ministry of Labour and Social Security. By this project, which aims to develop a coding and registration system defining the individual skills, existing potentials and functional capacities of the disabled and place them in appropriate jobs and increase their employment, it is aimed to attain EU standards.

Under the Privatization Social Support Project (PSSP) I Re-employment component, a total of 25,184 persons benefited from 773 projects on consulting, formal training, on the job training and social work program services in the 2001-2006 period. 11,701 out of 22,230 successful participants in the project programs were employed. In addition, by small-scale business start up consulting services provided under the project, 414 small-scale enterprises were established and 1,230 persons were employed in such enterprises. Under the PSSP II, a total of 5,228 persons in 254 projects as of October 2007 were provided with consulting, formal training, on the job training and social work program services, and of the total, 2,791 persons were employed.

The Employment Status Report was prepared in 2003 under the works of harmonization with European Employment Strategy in the EU accession process. The Joint Assessment Paper, specifying the priorities and policies in employment, is expected to be completed by the end of 2008.

The Social Dialogue Project initiated on 1 February 2006 and implemented by the Ministry of Labour and Social Security under joint financing by Turkey and EU was completed in November 2007. Within the context of the project, a database was set up, three working groups formed, training programmes provided, conferences organized, and a grant program created to increase joint working culture between social parties and 26 projects were supported under the program.

Table 4. 8: Matrix of Policy Commitments: Labour Market

(In 1000 Euros)

	2006	2007	2008	2009	2010
1. Privatisation Social Support Project II					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-25,779	-27,750	-26,971	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-25,779	-27,750	-26,971	---	---

2. The Active Employment Measures and Local Level Support to Turkish Employment Agency Project					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	---	---	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	---	---	---	---
3. Basic Education Programme					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-820,806	-668,997	-764,700	-897,000	-950,000
B.1. Direct Effect on Budgetary Revenues(1)	165,850	200,000	220,000	260,000	280,000
B.2. Direct Effect on Budgetary Expenditures(2)	-986,656	-868,997	-984,700	1,157,000	1,230,000
Total Net Budgetary Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-846,585	-696,747	-791,671	-897,000	-950,000
B.1. Direct Effect on Budgetary Revenues	165,850	200,000	220,000	260,000	280,000
B.2. Direct Effect on Budgetary Expenditures	-1,012,435	-896,747	-1,011,671	-1,157,000	-1,230,000

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

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

4.4. Agricultural Sector

The basic objectives of agricultural policies are; by taking food security into account, to ensure balanced and adequate nutrition and to provide accession to quality and safe food for the increasing population; to create an agricultural structure that is economically, socially and environmentally sustainable, is well-organized, highly competitive and harmonized with the EU policies, and to ensure the effective use and development of natural resources.

In this context, while the policy instruments are being implemented to convert agricultural production to a more consumer-based pattern, high priority will be given to the necessary transformation of the agricultural structure in order to compete in the Union after Turkey's accession to the EU. In this respect, important items of support provided to contribute to the structural transformation in the agriculture sector are given in Table 4.9. In addition, projects for basic activities regarding the abovementioned priorities including technical support provided under the EU Financial Cooperation are given in Table 4.9.

The Law on the establishment and duties of the Ministry of Agriculture and Rural Affairs will be revised in order to ensure the functional organization as required for main issues like the harmonization with the EU legislation, implementation of agricultural R&D and extension services in a comprehensive manner as well as for land protection and use.

It is envisaged that provisions regarding establishment permits, monitoring, control and inspections in the legislation for the agricultural producers' organizations is to be amended with an integrative view for strengthening the autonomy of producers' organizations and regulations regarding the independent audits will be completed. Furthermore, regulations will be prepared for the Agricultural Sales Cooperatives and Unions, which are important entities for organizing producers, to have sustainable financial and administrative structures and necessary amendments will be made in the related legislation to strengthen their independence as well.

In the context of the redesigned legislation, it is aimed to solve the problem of fragmented and small agricultural lands as well as to accelerate land consolidation activities for reducing investment costs in irrigation projects and expropriation costs.

In order to make progress in the chapter of food safety, veterinary and phytosanitary, and to ensure that the public services on plant and animal health, and food safety are provided in a holistic framework, it is expected that draft legislation being prepared to include food, feed, veterinary services and general hygiene rules will be issued after the review and assessments among the institutions. In addition, under the works being carried out with the purpose of strengthening the institutional capacity to effectively implement the mentioned legislation, priority areas are to improve the control and inspection infrastructure including laboratories, and accelerate the relevant accreditation process.

Payments are made under the scope of Direct Income Support (DIS) which is expected to get the largest share with 44 per cent from the support budget in 2007, according to 16.3 million hectares of land and about 2.6 million of farmers registered in 2006. Since 2005, in addition to the basic payment per area, additional payments have been made to the farmers who have their soil analyzed and are engaged in organic agriculture.

According to the Agricultural Insurance Law No.5363, which was enacted in 2005 to compensate losses of farmers and breeders as a result of realized risks and uncertainties threatening the crop production and animal husbandry in Turkey, state support was provided to the related risks for animal assets in addition to hail and frost risks in the plant production with the implementation starting from 2006.

Considering the target of the Ninth Development Plan increasing the share of areas allocated for organic agriculture to 3 per cent in 2013, the program for developing organic agriculture is being continued, and technical assistance was obtained in 2006 under the EU Financial Cooperation to support convergence with the relevant EU legislation.

In order to establish a competitive structure in the livestock sector, it is aimed to increase fodder crop production, develop breeding cattle farming, promote artificial insemination, prevent animal diseases and make progress for regions free of animal diseases. Furthermore, establishment of a bovine animal identification system is at the final stage. In addition, in the context of ovine and caprine identification, works for determination of a method by examining the EU regulations have been started and for project preparation on this issue has been initiated.

Quality and quantity problems relating to agricultural statistics will be eliminated, and for the implementation of agricultural policies, the information system and administrative structure will be improved. In this context, preliminary studies were completed for establishing an integrative administration and control system, and the activities to build the infrastructure are programmed in such a way to obtain technical assistance in the framework of EU Financial Cooperation. In addition, National Farmer Registration System (NFRS), which is being used for DIS payments and expected to be a part of the Integrated Administration and Control System (IACS) in the future, was designed to be a frame so that all support payments can be monitored and reported and made effective as of 2007. Furthermore, while legislative works continue, related to the Farm Accountancy Data Network, which is foreseen to be established to monitor the development of farm holdings and to contribute policy making, a pilot implementation will be started.

In the fisheries sector, priority will be given to improving the institutional structure, increasing the effectiveness of resource management in capture fisheries; ensuring environmentally friendly production and developing alternative fish species in aquaculture. In this context, amendments will be made in the Fisheries Law, and construction of offices at the harbours will be continued in order to conduct controls effectively at the landing points, and the infrastructure for the information systems regarding the sector, mainly the fleet registration and monitoring system will be completed and works to disseminate the practice will be continued. Furthermore, in order to establish the fisheries resource management system, efforts will be initiated towards necessary legal and institutional structuring.

The privatization process of the public sugar factories is in progress and it is envisaged that legislative work for completing the institutional structuring in the sector and making quota management and monitoring effectively will be concluded by the end of 2008.

Rural Development

In order to contribute to the implementation of national regional development policy which aims to decrease the development disparities between the rural and urban, and among regions, and to solving the adjustment problems in rural areas resulted from the rapid transformation in the agricultural structure, the rural development objectives were determined as follows in the Ninth Development Plan (2007-2013):

- Increase competitiveness of agricultural enterprises
- Increase income level of the rural population and diversify economic activities
- Improve social and rural infrastructure services
- Develop human resources
- Disseminate the participatory structures in organizations
- Protect the environment.

While agricultural activities have an important role in rural development in Turkey, the importance of non-agricultural activities in rural development policies increases because of the low economic and social development levels of rural areas and the declining agricultural employment.

In order to contribute to the goals of Development Plan, the activities for development of rural areas will have been realised on the following principles: ensuring the harmony of rural development policies with sectoral and spatial policies, taking up the rural development and agricultural development as a whole, harmonizing with the agricultural and rural policies of the EU, taking into account the differing characteristics, needs and potential of the rural areas in the country, strengthening coordination and cooperation among the relevant organizations responsible for the implementations of all rural development projects, incorporating local administrations, the non-governmental organizations and beneficiaries in the decision making and the implementation processes.

In the EU membership process, works on programming and implementation are continuing with the main goal of increasing harmonization with the EU Common Agricultural Policy legislation and of providing support to the agricultural sector and sustainable development of rural areas.

On the other hand, the preparations for rural development program initiated to benefit from the EU 2007-2013 Pre-Accession Rural Development Fund (IPARD Fund), were carried out with the technical support project provided within the context of the Turkey-EU Financial Cooperation. The draft rural development program (IPARD Program) prepared in line with the National Rural Development Strategy (UKKS) document and other IPA components has been submitted to the European Commission.

Works are continuing to develop institutional capacity for managing the EU rural development funds set aside for Turkey in the 2007-2013 period. The Law No.5648 on Establishment and Duties of the Agricultural and Rural Development Support Organization which will conduct the implementation and payment functions for IPARD funds was promulgated in the Official Gazette dated 18 May 2007. The twinning project under 2005 Turkey-EU Financial Cooperation Programming aiming at supporting the establishment of the aforementioned Agency, and works for the secondary legislation needed for establishment of the Agency are continuing.

Works are continuing for the preparation of the Rural Development Plan that will be in harmony with the National Rural Development Strategy which is in effect since 2006. The plan is being prepared to include all rural development programs, projects and activities financed by national and international resources, establish the monitoring-evaluation infrastructure, and is designed as a dynamic action plan that lays down general principles of rural development practices.

Many rural development projects were implemented in Turkey, mostly financed by foreign resources, and some are still continuing. Of these projects, Ordu-Giresun Rural Development

Project (1995-2007) was completed, Sivas-Erzincan Rural Development Project (2004-2012), Anatolian Water Basins Rehabilitation Project (2004-2012) and Diyarbakır-Batman-Siirt Rural Development Project (2007-2012) are continuing.

Two different grant programs are implemented with national and international resources in order to serve the basic goals of increasing income level in the rural areas, strengthening the integration between the primary agricultural activities and agricultural industries, creating alternative revenue sources in the rural areas, developing irrigation infrastructure and improving agricultural mechanization. It is expected that these grant programs will increase the level of benefiting from rural development funds both in the pre-accession period and during membership and the project development capacity.

Of these grant programs, the Agricultural Reform Implementation Project is being implemented in 16 pilot provinces under the name of Village Based Participant Investment Program (2005-2008) under the rural development component. The Rural Development Investments Support Program (2006-2010) being a continuation of the above program has been implemented in other 65 provinces with financing from national resources. The scope of the grant programs covering the economic activities and agricultural infrastructure components was expanded by the Machinery and Equipment Acquisition Support subprogram in 2007.

KÖY-DES introduced in 2005 in 79 provinces except Istanbul and Kocaeli provinces, and BEL-DES introduced in 2007 in all provinces to provide for infrastructure needs of municipalities with population less than 10,000 are continuing. For the KÖY-DES Project, 2.36 billion euros was allocated in 2005-2007 period and for the BEL-DES project 186 million euros was allocated in 2007.

Table 4. 9: Matrix of Policy Commitments: Agriculture

Significant Developments in Agriculture Support

(In 1000 Euros)

	2006	2007	2008	2009	2010
1. Agricultural Reform Implementation Project (ARIP) (1)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-55,525	-47,464	-35,790	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-55,525	-47,464	-35,790	---	---
2. Direct Income Support (2)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-1,449,905	-1,429,871	-1,324,690	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-1,449,905	-1,429,871	-1,324,690	---	---
3. Pursuant to the Decree 2005/8503 on Supporting Livestock Sector					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-358,403	-395,793	-379,150	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-358,403	-395,793	-379,150	---	---
4. Support for Rural Development Investments					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-27,152	-50,171	-50,006	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-27,152	-50,171	-50,006	---	---

5. Agriculture Insurance					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-10,861	-27,873	-28,527	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-10,861	-27,873	-28,527	---	---
Total Net Effect on Budget					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-1,901,846	-1,951,172	-1,818,163	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-1,901,846	-1,951,172	-1,818,163	---	---

Significant Projects in Agriculture (3)

(In 1000 Euros)

	2006	2007	2008	2009	2010
1. Plant Health–Project to Eradicate Plant Diseases and Pests (4)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-1,575	-1,700	-1,771	-1,941	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-1,575	-1,700	-1,771	-1,941	---
2. Animal Health–Project to Eradicate Animal Diseases and Pests					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-2,715	-13,100	-13,004	-13,033	---
B.1. Direct Effect on Budgetary Revenues	8,146	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-10,861	-13,100	-13,004	-13,033	---
3. Restructuring the Border Inspection Points Project					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	3,375	3,375	---	---
B.1. Direct Effect on Budgetary Revenues	---	5,000	5,000	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-1,625	-1,625	---	---
4. Controlling of Rabies Project					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	3,162	3,162	---	---
B.1. Direct Effect on Budgetary Revenues	---	4,552	4,552	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-1,390	-1,390	---	---
5. Controlling of Foot-and-Mouth Disease Project					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	10,906	10,906	10,906	---
B.1. Direct Effect on Budgetary Revenues	---	16,359	16,359	16,359	---
B.2. Direct Effect on Budgetary Expenditures	---	-5,453	-5,453	-5,453	---
6. Avian Influenza and Human Pandemic Preparedness and Response					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	238	-7,769	-8,100	-9,268	---
B.1. Direct Effect on Budgetary Revenues	1,650	1,095	1,095	270	---
B.2. Direct Effect on Budgetary Expenditures	-1,412	-8,864	-9,195	-9,538	---

7. Improving the Seed Sector in Turkey, and Alignment with the EU [(5)]					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	420	1,075	210	---
B.1. Direct Effect on Budgetary Revenues	---	420	1,390	210	---
B.2. Direct Effect on Budgetary Expenditures	---	---	-315	---	---
8. Introduction of Stock Assessment to the Fisheries Management System of Turkey					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	---	450	1,630	120
B.1. Direct Effect on Budgetary Revenues	---	---	450	1,630	120
B.2. Direct Effect on Budgetary Expenditures	---	---	---	---	---
9. Restructuring and Strengthening of Food Safety and Control System in Turkey					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-403	1,809	2,910	---	---
B.1. Direct Effect on Budgetary Revenues	265	3,969	4,700	---	---
B.2. Direct Effect on Budgetary Expenditures	-668	-2,160	-1,790	---	---
Total Net Effect on Budget					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-4,455	-2,897	-997	-11,496	120
B.1. Direct Effect on Budgetary Revenues	10,061	31,395	33,546	18,469	120
B.2. Direct Effect on Budgetary Expenditures	-14,516	-34,292	-34,543	-29,965	---

(1) It includes all spending under the Agricultural Reform Implementation Project including investments and transfer (excluding cadastral works).

(2) They represent spending from the budget in the current year and exclude payments related to the respective year. The amount is the projected value for 2007.

(3) In EU-funded projects, impact on budgetary revenues result from EU contributions with grant and investment component in the related projects.

(4) No amount was spent by the EU and Turkey under the projects as the bidding process related to the EU project has yet to be completed. Figures recorded as budgetary spending represent spending related to the national project, which is being implemented under the Investment Programme and also comprises the EU Projects.

(5) Improving the Seed Sector project is financed from national budget starting from 2001, as a sub-component Alignment with the EU project will be started in 2008.

4.5. Administrative Reform

Strategic Planning and Performance Based Budgeting

The increasing and diversifying demands of people as a result of the rapid and multi-faceted transformation processes being experienced in the world and in Turkey brought to agenda necessitated a radical restructuring in management concept. In order to improve management quality in public administrations, it was decided that all local or central public administrations should prepare strategic plans to shape the management decisions with a medium and long term view, develop goal-based and results oriented management approach and budgeting, increase responsiveness in public service supply to user demands, and establish participation and accountability.

In this context, pursuant to the Decisions of the High Planning Council No.2003/14 and No.2004/37, strategic planning pilot studies for which SPO assumed the role of guidance, monitoring and evaluating were completed in 2006 in eight public administrations.

Based on the results obtained from the pilot studies and the Strategic Management Survey realized in cooperation with TURKSTAT, the legislative efforts were made to spread the practice to all public institutions. In this context, the By-Law on the Procedures and Principles of Strategic Planning in Public Administrations was promulgated in the Official Gazette dated 26 May 2006.

In this context, works are in progress to establish strategic planning and performance based budgeting in the public administrations under the Public Financial Management and Control Law No.5018. The practice is being expanded in the transition program indicated in the aforesaid By-Law until 2010. Within this framework, as of September 2007, out of 48 central public administrations which are under the obligation of preparation of strategic plan and performance programme, 46 have prepared strategic plans and 22 administrations have prepared performance programmes.

In the forthcoming period, strategic planning and performance based budgeting works at institutional level will be continued to expand within the said transition program. Preparation works are in progress as required by the process, in the 100 public administrations that must prepare strategic plans and performance programmes in 2008 and 2009.

The Performance Based Budgeting Guidelines will be published in 2008 to enable the institutions to conduct their works for performance based budgeting, and the concerning By-Law will be completed by the Ministry of Finance in 2009.

The budget will be structured to indicate the cost of the policies and the performance of public administrations by considering the costs of the policies to be implemented, the groups affected by these policies and the opportunity costs. .

In order to apply the strategic management effectively, it is necessary to build up theoretical and practical knowledge. For this purpose, SPO will carry out a program to encourage cooperation between public administrations, universities and civil society organizations, realize training, research and publication activities, and in this context, develop coordination between central public organizations.

Strategy Development Units

With the aim of building organization for implementing the strategic management approach in the public administrations, the problems encountered by the strategy development units established in the beginning of 2006 in performing their functions effectively and adequately were identified by carrying out the Strategy Development Units Research.

In order to implement the strategic plan and performance programmes successfully, it is aimed that the strategy development units should make studies towards developing methods and tools for measuring, monitoring and evaluating the implementation results.

Local Administration Reform

In the context of Local Administration Reform, which is a significant part of the Public Administration Reform, legal regulations were made for strengthening and restructuring the local administrations. However, deficiencies regarding financial and managerial efficiency and qualified human resources continue in local administration units. A draft bill was prepared to regulate the revenues of provincial special administrations and municipalities to create a fiscal structure, which would allow the local administrations to discharge effectively their increased duties and responsibilities under the new legislation. With the mentioned bill, it is expected that the transfers from the general budget tax revenues to the local administrations will rise by 0.3 per cent of GDP in 2009 and 2010.

Regulatory Impact Analysis

Article 24 of the By-Law on Procedures and Principles Regarding Legislation Preparation enforced on 17 February 2006 upon promulgation in the Official Gazette, introduces the regulatory impact analysis. Except for the issues related with the national security, and budget and final accounts laws and decrees, it is mandatory since 17 February 2007 to make regulatory impact analysis for laws and decrees, and any other regulations as approved by the Prime Ministry, whose effect might exceed 10 million YTL, if put into implementation. In this context, the Regulatory Impact Analysis Guidelines which the public agencies and organizations should follow were promulgated in the Official Gazette dated 3 April 2007 No.26482, in the annex to the Prime Ministry Directive No.2007/6.

4.6. Other Reform Areas

4.6.1. Regional Development

One of the five development axes defined in the Ninth Development Plan of Turkey covering the period of 2007-2013 is Ensuring Regional Development.

In this context, the Twinning Project: Support to the State Planning Organization General Directorate of Regional Development and Structural Adjustment for Strengthening Institutional and Administrative Capacity was completed as of 25 January 2007, which provides a basis for sharing important experiences about improving institutional and administrative infrastructure for more effective use of resources allocated for local/regional development and development and institutionalisation of joint decision-making processes in the field of regional development..

The Law on the Establishment, Coordination and Duties of Development Agencies, which was enacted on 25 January 2006 was put into effect and Development Agencies commenced activities in two NUTS II Regions (TR31 İzmir and TR62 Adana and Mersin). However, works were suspended in line with the decision of the Council of State because the Law and some secondary legislation were taken to the Constitutional Court. Depending on the conclusion of the legal process, it is expected that legislative and capacity building studies needed for the activation of the technically qualified regional development units will be continued.

In order to harmonize regional development policy and practices with EU and activate local development potentials and initiatives at identified priority regions, special regional development programs, which have been implemented in the scope of Turkey-EU financial cooperation with joint financing, are continued.

The total budget of the regional development programs mostly coordinated by SPO will have reached 259 million euros at the end of 2007, with the DOKAP program and the GAP program coordinated by the GAP Administration. The said programs cover 42 provinces and along with the Turkey-Bulgaria Cross-Border Cooperation Program covering 2 provinces with 19.5 million euros, a total of 1,400 projects are supported.[13]

On the other hand, revision is needed upon the Commission's insistence in the project with 19.5 million euros budget aimed at purchase of goods and services included in the 2005 Financial Cooperation Programme. However, despite various adjustments made in the Project File, agreement could not be reached with the Commission, and the project is no longer applicable at the present stage.

In addition, Yeşilırmak Basin Development Project works were completed, which is an example of regional development projects financed from the public budget.

Considering the implementation period of the regional development projects prepared and started, financial assistance amount set aside for programs, and the capacity of regional and central organizations in project generation and implementation, it is thought that the contribution of regional programs to economic development will be limited particularly in the pre-accession period. However, in this period, it is expected that as a result of capacity building activities in the center and regions, project generation, implementation and monitoring capacity will be enhanced at the regional and central level particularly by effective use of funds in the long run, and an income and employment effect, though limited, may be obtained in the program regions.

[13] Calls for proposals, which were in the scope of the DOKAP Program under the 2005 Financial Cooperation Programme, were made on 9 April 2007 and a total of 1,619 project applications were received. Evaluations for the said projects will be finished as of November 2007, then the number of supported projects will increase further.

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

(In 1000 Euros)

	2006	2007	2008	2009	2010
1. Regional Development in TR82, TR83 and TRA1 NUTS II Regions					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-9,655	-2,414	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-9,655	-2,414	---	---	---
2. Turkey-Bulgaria Cross Border Cooperation Programme					
A. Implementation rofile	---	---	---	---	---
B. Net Effect on Budget	-300	-303	-949	-1,413	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-300	-303	-949	-1,413	---
3. Regional Development in TRA2, TR72, TR52 and TRB1 NUTS II Regions(1)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	-20,970	---	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-20,970	---	---	---
4. Regional Development in TR90 NUTS II Regions					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	---	---	-6,000	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	---	-6,000	---	---
5. EU Regional Programmes(2)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-207	-564	-1,613	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-207	-564	-1,613	---	---
6. Regional Development Project(3)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-33	-110	-108	-103	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-33	-110	-108	-103	---
7. Allocations for Local Administrations					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-4,805	-4,812	-3,710	-3,668	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-4,805	-4,812	-3,710	-3,668	---
8. Development Agencies(4)					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-3,337	---	-53,769	-53,529	-54,862
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-3,337	---	-53,769	-53,529	-54,862
Total Net Effect on Budget					
A. Implementation Profile	---	---	---	---	---
B. Net Effect on Budget	-18,337	-29,173	-66,149	-58,713	-54,862
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-18,337	-29,173	-66,149	-58,713	-54,862

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

(1) The pre-financings of the projects under this Programme has been done in 2007 and thus the national co-financing in these pre-financings has been transferred in 2007. However, for some of the projects at risk of non-completion with several reasons, an official extension request is made and after the decision on this request, the national co-financing transfer in the final payments to the beneficiaries, who took extension, may extend to 2008.

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

(3) Yeşilırmak Project prepared by strategic planning approach.

(4) Depending on the conclusion of the legal process, the resource that might be needed for the activation of Development Agencies.

4.6.2. Health and Social Security Reform

Health Transformation Program

The Health Transformation Program aims to restructure the Ministry of Health to strengthen its regulating, planning and supervising roles, create the general health insurance system, ensure rational use of medicine and medical devices and make the health information system effective. The said program also aims at spreading the health services, increasing their quality and ensuring easy access to these services.

In the context of the Health Transformation Program, the pilot implementation of Family Medicine was initiated in 2005 with a view to strengthen primary health services and ensure efficient use of the referral chain, and the number of provinces was increased to 12 in 2007. It is planned to disseminate the practice to the whole country at the end of the year 2010.

Under the e-health project, which aims to compile, analyze and evaluate data from health institutions according to specified standards, the Family Medicine Information System is in practice in the provinces covered by the family medicine project, and the National Health Data Dictionary was prepared, and the Minimum Health Data Set was defined and issued. In this context, the pilot implementation in radiology and pathology of the tele-medicine system is to be started by the end of 2007. Pilot implementations in the scope of the Central Hospital Appointment System Project will be initiated in 3 regional centers in 2008.

In the framework of the Health Transformation Program, institutions responsible for carrying out the health services will be restructured. In this context, firstly, the organization law will be renewed in order to strengthen the planning and controlling role of the Ministry of Health, and Refik Saydam Hygiene Center will be transformed into a National Public Health Institution with international accreditation. In order to enhance service quality and efficiency, public hospitals will be made administratively and financially autonomous gradually. The Turkish Medicine and Medical Devices Agency will be established to regulate production, import, export, placing on the market, putting into service, and use of drugs, substances used in drug production and medical devices, and ensure that implementations of them will be delivered to the society safely, effectively, in good quality and in compliance with standards.

Social Security Reform

Studies related to the social security reform which aims to restructure the social security system institutionally as well as realize a unique pension system and a unique health system arrived an important stage by laws legislated in 2006. The Social Security Institution Law was put into force on 20 May 2006 prepared in the scope of the Social Security Reform. The Social Insurances and Universal Health Insurance Law No.5510 was enacted on 16 June 2006, however, because the Supreme Court cancelled various provisions of the Law on 15 December 2006, the implementation of the Law was postponed to 1 July 2007 and later to 1 January 2008 by the Law No.5655 by the Parliament.

After the Supreme Court cancelled various provisions of the Law No.5510, a new study titled "Social Security Reform: New Approach Prior to Implementation" was prepared in May 2007 by the Social Security Institution to provide a platform for discussion by social parties, academicians and all related parties on which amendments may be made to the Law. By the works carried out in October 2007, the draft for amendments to the Law No.5510 was completed to a large extent. All arrangements regarding the reform are presented below within the framework of the amendable existing draft.

By the regulations, which can be described as a parametric reform, it is contemplated to make such regulations as rising the retirement age gradually, reducing replacement rates, changing the definition of the premium basis for newly recruited public servants etc. Furthermore, after the Supreme Court cancelled various provisions of the Law, it was intended to change the regulation about the support premium, which is charged from those who restart to work while receiving old age pension.

Changes in premium rates are also envisioned with the reform. It is planned that the premium of long term insurance branches will be paid from the unemployment insurance fund while getting unemployment benefit, that the premium rate for voluntary insurance premium will be raised from 25 per cent to 32 per cent for SSK, from 20 per cent to 32 per cent for BAĞ-KUR, that Social Security Support Premium (SGDP) will be raised from 31 per cent to 36.5 per cent for those under SSK who are insured before the Law of Social Insurances and General Health Insurance was put into effect, getting invalidity and old age pension, or were paying SGDP by the time the Law was put into effect. In addition, for those who will be insured first after the enforcement of the Law, SGDP is planned to be raised to the range of 33.5-39.5 per cent depending on the vocational risk and from 10 per cent to the range of 15-22.5 per cent depending on the age groups for the insured under BAĞ-KUR.

The reform includes legal amendments to non-pension insurance branches. It is contemplated that the funeral aid will be set at twice the minimum wage for all insured persons under all three social security organizations, that the daily allowance paid in case of temporary inability to work will be set at 3/5 equally for inpatient and outpatient treatment (excluding Emekli Sandığı, including SSK and BAĞ-KUR coverage), and that the breast feeding aid at maternity will be paid for six months at the level of 1/10 of the minimum wage starting from the birth.

By the universal health insurance, which is another component of the reform, it is aimed to implement a mandatory universal health insurance that covers the entire society. In addition, despite the universal health insurance has not been in practice yet, by the Health Practice Communiqué (SUT) that regulates procedures and principles regarding the delivery of health services, the uniformity of practice for the insured under SSK, BAĞ-KUR and Emekli Sandığı was ensured in June 2007.

Considering the existing draft after the cancellation, once the universal health insurance is commenced, it is envisaged that the Ministry of Finance shall pay the premiums for those who do not have the ability to pay. It is assumed that persons not covered under any health scheme will start to pay universal health insurance premium under the name of those who are able to pay premiums, with the new Law. Furthermore, it is expected with the reform that those under 18 will benefit from the universal health insurance, and that the state will contribute at an amount equal to 25 per cent of the total premium collection for long term insurance branches and universal health insurance.

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

(In 1000 Euros)

	2006	2007	2008	2009	2010
1. Neonatal Screening Programme (Phenylketonoury, Hypothyroid)					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-1,200	-1,688	-2,150	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	-1,200	-1,688	-2,150	---	---
2. Eradication of Epidemics					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	---	-1,407	-1,565	---	---
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-1,407	-1,565	---	---
3. Health Transformation Project (1)					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-11,150	33,555	75,468	100,000	100,000
B.1. Direct Effect on Budgetary Revenues	---	50,000	100,000	100,000	100,000
B.2. Direct Effect on Budgetary Expenditures	-11,150	-16,445	-24,532	---	---
4. Avian Influenza Project (2)					
A. Implementation Profile	---	---	---	---	---

B. Net Budgetary Effect	---	-6,116	-6,076	-4,852	-3,725
B.1. Direct Effect on Budgetary Revenues	---	---	---	---	---
B.2. Direct Effect on Budgetary Expenditures	---	-6,116	-6,076	-4,852	-3,725
Total Net Budgetary Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budgetary Effect	-12,350	24,244	65,677	95,148	96,275
B.1. Direct Effect on Budgetary Revenues	---	50,000	100,000	100,000	100,000
B.2. Direct Effect on Budgetary Expenditures	-12,350	-25,656	-34,323	-4,852	-3,725

(1) Establishment of database infrastructure of social security is included.
(2) The project has two components, one of which will be funded by the World Bank and the other by the European Union.

4.6.3. R&D and Innovation

The basic objective of the science and technology policy in the Ninth Development Plan prepared for the 2007-2013 period was defined as to enhance innovative capabilities of the private sector, become competent in science and technology and transform such competence to economic and social benefit.

In our country, the share of R&D expenditures in GDP was 0.79 per cent in 2005 whereas it was 1.74 per cent for the EU average. It is aimed to raise this rate to 2 per cent in 2013. While the amount of public investments in R&D was 319 million YTL in 2003, it was raised to 903 million YTL in 2007.

Efforts are continuing to enhance innovative capability and capacity of the private sector which assumes a significant role in transforming R&D efforts to products and increasing its contribution to competitiveness. In this context, on the one hand support and incentives to R&D projects of the private sector are increased, on the other hand the number of technology development zones and technology centers was increased which were established to bring together parties that generate knowledge and use it to produce value added and allow the participant companies to benefit various incentives. Furthermore, works are continuing to legislate the draft bill prepared to regulate tax incentives on R&D.

On the other hand, programs are continuing on Academic and Applied R&D Support, Public R&D Support, Industry R&D Support, Defense and Space R&D Support, Increasing Science and Technology Awareness and Scientist Raising and Improving initiated in the scope of Turkey Research Area Program commenced in 2005 by TÜBİTAK.

Another issue as important as increasing the resources allocated is to overcome the shortage of researchers. The number of full time equivalent of R&D personnel per one thousand economically active persons was 2.23 in 2005 which was well below the EU average of 9.9 in 2004. Programs and projects were started to educate researchers inside and outside the country to overcome the shortage.

The EU Seventh Framework Program in science and technology was fully participated to increase science and technology cooperation with EU member states and become a part of the European Research Area. The memorandum of understanding signed for participation was promulgated in the Official Gazette dated 29 June 2007 No.26567.

4.6.4. Information and Communication Technologies

One of the basic objectives of the Ninth Development Plan (2007-2013) is to realize the transformation of Turkey into an information society.

Works are continuing under the Information Society Strategy and annexed Action Plan which lay down basic objectives and policies to realize this transformation and methods and tools that should be followed.

In order to implement the Strategy and Action Plan in an effective manner, e-Transformation Turkey Executive Committee has been assigned as the responsible body for formulating policies, making decisions, evaluations and directing the whole process at highest level by the Prime

Ministry Circular No.2007/7. The Executive Committee consists of the Minister of State and the Deputy Prime Minister affiliated with the State Planning Organization, Minister of National Education, Minister of Transport, Minister of Industry and Trade, Undersecretary of Prime Ministry, Undersecretary of Ministry of Interior, Undersecretary of Ministry of Finance, Undersecretary of the State Planning Organization and Chief Consultant to the Prime Minister. Representatives from relevant public agencies and civil society organizations may also participate in the meetings of the Committee.

By the same Directive, a Transformation Leaders Committee was created to provide a common platform to ensure cooperation between public institutions, implement common principles and standards, and effectively implement the strategy in the transformation process to information society. On the other hand, creation of an Advisory Board was envisaged in order to share and evaluate on a common platform the opinions and suggestions of public professional organisations, universities, private sector and relevant civil society organizations in the works for transforming Turkey into an information society, and in the process of implementing the strategy.

By protocols signed between the Ministry of National Education (MEB) and Turkish Telecom within the context of developing human resources as required by the information society, Internet access via Asymmetric Digital Subscriber Line (ADSL) was provided to MEB's 29,000 schools and institutions as of October 2007. As a result, a total of 11.5 million students including about 90 per cent of primary and 99 per cent of secondary school students were provided with broadband Internet access. TURKSAT, Inc will have provided Internet access to 5,200 schools and institutions by the end of 2007. Thereby, 34,200 schools and institutions will have Internet access by the end of 2007. The remaining 6,800 schools and institutions will have Internet access after necessary infrastructure investments are made.

With the e-School project that was introduced in May 2006 and included the Education Portal, services of concern to students and parents such as school records, MEB examination applications, monitoring school standing of students will be served through Internet, thus, student data needed in the education portal will be compiled and also data to be compiled at national level may be used for policy formulation through decision support systems. e-Register project which is a component of the e-School Project is being implemented in 16 pilot provinces.

Works are continuing to establish the technical infrastructure for the e-Government portal for which TÜRKSAT A.Ş. is responsible, and through which citizens and the business may access integrated public services from single point. It is expected that the e-Government portal will be implemented in 2008 with pilot services.

In addition to main e-Government applications that are utilized commonly, the address registry system is completed, and works are continuing to integrate address and population data. Similarly, the works on the third phase of Automation of Tax Administrations Project (VEDOP), Land Registry and Cadastre Information System (TAKBIS), and unique number system for legal persons are in progress.

The Public Agencies Internet Website Guidance was issued in the Annex to the Prime Ministry Circular No. 2007/4 aimed to ensure minimum content and design consistency of websites of all public institutions and organizations at central and local level. Besides, minimum standards were determined for operation of electronic registry systems to operate in harmony with each other and be managed effectively.

The Prime Ministry Circular No. 2007/16 was issued on effective functioning of the citizenship card project, which aims to provide citizen focused and quality public services in electronic environments on safe and reliable infrastructure, and facilitate and speed up daily actions and activities of citizens.

In May 2007, Turkey made a declaration of intention to participate in the Information and Communication Technologies Policy Support Program, which is a component of the EU Competitiveness and Innovation Framework Program.

The report on Turkey prepared under the OECD e-Government country study to assess e-Government preparation status was issued by OECD in mid-2007. Furthermore, in 2007 Turkey was included in the Benchmarking Study which included comparisons among European countries regarding the provision of 20 basic public services in electronic environment as selected by EU. According to the study, in fully on-line provision of 20 basic public services, EU-27+ average (EU-27 and Turkey, Iceland, Switzerland and Norway) was 59 per cent, whereas it was 55 per cent for Turkey. The level of maturity in providing such services in electronic environment was 76 per cent for EU-27+, 69 per cent for Turkey. The maturity of services for citizens was 70 per cent for EU-27+, 57 per cent for Turkey. As for the maturity of services provided to business, it was 84 per cent for EU-27+, and 86 per cent for Turkey, which is above the EU average.

Following the completion of the legal infrastructure for electronic signature, three organizations in 2005, and one organization in 2006 commenced operations to provide qualified e-certificates. The number of qualified e-certificates produced was 1,402 in 2005, and increased to 12,038 in 2006. Besides, a total of 15,000 requests were received at the end of July 2007 for mobile signature applications which were introduced in 2007. Currently, 32 public organizations have obtained e-signatures. In the private sector the use of e-signature by natural gas companies, and mobile signature in e-banking attained a certain level of use. With the increasing number of e-Government and e-banking implementations, it is expected that e-signature and mobile signature will become more widespread.

Regulatory works on information crimes are held in harmony with EU regulations. In this context, works are continuing on the Draft Bill for the Law on Protection of Personal Data. Besides, the Law on Regulation of Internet Publications and Combating Crimes Committed through Such Publications regarding the fight against the crimes committed in the Internet in terms of content, location and access providers was promulgated in the Official Gazette dated 23 May 2007 No.26530. This Law substitutes various provisions relating to information crimes in the previously prepared Draft Bill for the Law on Regulating Information Network Services and Cyber Crimes. Therefore, it is planned that the said Draft will be reviewed after 2009, after obtaining the practical results from the cyber crime provisions of the Turkish Penal Code and evaluating those results.

Works for liberalization and EU convergence are continuing in the electronic communications sector where competitive, widespread and affordable communication infrastructure and services will be provided in Turkey's transformation to an information society. In this context, the Draft Bill for the Electronic Communications Law, which was prepared in accordance with the developments in the sector and EU regulations in order to consolidate fragmented telecommunication legislation, was in the agenda of Turkish Grand National Assembly (TBMM) in the 22nd Parliamentary Period, but could not have been enacted. The draft specifies the general framework for regulations needed by the sector, simplifies the authorization process, and defines functions of policy formulation and regulation. It is expected that the Draft Bill will be renewed in the new Parliamentary period and be on the agenda in the first half of 2008.

After full liberalization, authorizations were issued for long distance telephone services starting from May 2004, and as of October 2007, a total of 33 operators were authorized. Further, by the annex (Annex-A14 Fixed Telecommunication Service) to the Regulation amending the Regulation for Authorizations regarding Telecommunication Service and Infrastructure promulgated in the Official Gazette dated 14 August 2007 No.26613, the regulation for authorizing fixed telecommunication services covering short distance calls was completed, and following the determination of the minimum license fee for the service by the Council of Ministers, authorization actions for the said service will be started. The number of authorized operators by service type is as follows as of October 2007:

1. National Telecommunication Services: 1
2. Global System for Mobile Communications (GSM) Mobile Phone Services: 3
3. Satellite Platform Services: 2
4. Satellite Telecommunications Services: 20

5. Global Mobile Personal Communications By Satellite (GMPCS) Mobile Phone Services: 4
6. Wired and Wireless Internet Service Providers: 76
7. Data Communications Services over Land Lines: 24
8. Joint Use Radio Services: 47
9. Infrastructure Operation Services: 13
10. Cable Platform Service: 5
11. Directory Services: 6
12. Long Distance Telephone Services: 33.

Legal and technical infrastructure works started in line with the policy of switching to digital broadcasting over land transmitters are carried out under the coordination of the Ministry of Transport. In this context, trial land digital broadcasts started in Istanbul, Ankara and İzmir in 2006 are continued. On the other hand, a company was established by the participation of public and private sector operators to implement land digital broadcasting over shared transmitters.

Postal services failed to acquire a structure compatible with the market realities, changing economic approaches and actual competition in the market. It is planned to complete the regulations in 2008 to liberalize postal services by stages in a controlled manner, and restructure the sector in a competitive manner under the relevant EU Directives.

The Laboratory infrastructure works were completed for the project being carried out under the 2003 Turkey-EU Financial Cooperation Programming in order to strengthen the Laboratory infrastructure of the Telecommunication Authority which aims to implement the Regulation on Market Supervision and Monitoring. Various tests can be performed to verify technical compliance of wireless and telecommunication equipment in the laboratory which was partially accepted on 22 December 2006.

4.6.5. Transportation

The insufficient traffic safety, mainly on highways, continues to be an important problem. Measures aiming to increase efficiency in the transportation system and to establish a balance between transportation modes were continued in end-2006 and 2007. Furthermore, in the framework of EU Accession Negotiations, Position Paper for Trans-European Networks Chapter has been submitted to the European Commission.

Transport Infrastructure Needs Assessment (TINA) project which aims to determine arteries, connections and transfer points that will constitute the extensions of Trans-European transport network (TEN-T) to Turkey and to integrate Turkey in TEN-T was completed on 2 May 2007 and will be submitted to the approval of High Planning Council in the first quarter of 2008.

In line with the action plan covering the 2003-2008 period which targets harmonization with the Community acquis in rail transport, The Project of Restructuring and Strengthening the Railway Sector was realized to establish the legal and institutional framework of the railway sector. The main components of this project were (1) Organization of Railway Sector (Twinning Project) and (2) New Organization of TCDD, Regulation of Financial Relations with the Government and Establishment of Financial Management Information System (Technical Support – Service Procurement Project).

The Twinning Project started formally on 1 February 2005 and was completed on 31 October 2006. In the scope of the project, the draft bills of General Railway Framework Law and TCDD Law to regulate the railway sector, and the complementary draft regulations on Railway Safety, Railway Operating License, Railway Interoperability and Railway Infrastructure Access were prepared and approved by the project leaders on 25 January 2007 and submitted to the Ministry of Transport, the main beneficiary of the project.

Pursuant to the Decree No.2005/9986 of the Council of Ministers and the Regulation on Procedures and Principles Regarding Legislation Preparation, completion of the works for the general rationale, article rationales and regulatory impact assessment, then taking the opinions of the Ministries, relevant institutions and organizations (including non-governmental organizations) is required for the aforementioned draft law bills. In order to complete these technical studies and obtain relevant opinions, an Action Plan was prepared by the Ministry of Transport. According to this action plan, the drafts are scheduled to be submitted to The Prime Ministry in 2008. Besides, in the Turkey's Programme for Alignment with the Acquis covering the 2007-2013 period, the said draft bills are scheduled to be legislated in the 2008-2009 legislative term.

The New TCDD Organization, Regulation of Financial Relations with the Government and Establishment of Financial Management Information System Technical Support project was formally started on 16 January 2006 and completed in June 2007. Under this project, detailed works were done and work plans were prepared for the new organizational forms of work units and subsectors contemplated following the restructuring of TCDD. A Financial Management Information System was developed to measure and monitor financial performance of work units and subsectors to be created in the new TCDD organization. Draft contracts which define and govern the Public Service Obligations between TCDD and the Government according to the EU regulations were prepared. A series of training courses were organized to improve the administrative capacity in transition process to the new TCDD organization. Knowledge obtained as a result of this project and studies, guided the preparation of draft bills that regulate the railway sector, and will continue to be used as guidance for the process after the legislation of these bills.

An Adaptable Program Loan (APL) from the World Bank will be used for the restructuring of TCDD. 300 million dollars of the total project cost of 450 million dollars will be financed by the World Bank. The APL credit will be used in two phases. The first phase amounts 221 million dollars, 184.7 million of which will be financed from the World Bank. In the first phase, the project for signalization and extension of station ways of line segments of Boğazköprü-Ulukışla-Yenice, Mersin-Adana-Toprakkale will be realized. The credit agreement was signed on 13 March 2006 between the World Bank and the Undersecretariat of Treasury. The credit agreement was approved by the Council of Ministers and promulgated in the Official Gazette dated 12 May 2006 and put into effect. The loan became effective on 19 June 2006. The tender process for the project is in progress and bids will be collected in December 2007.

Regarding maritime transport, Turkish flag carriers moved towards gray list from the black list of the Paris MoU in 2007, as a result of effective implementation of country obligations in flag, port and coast state controls and by the works done and measures taken regarding maritime safety. In order to further improve efficiency in the maritime safety, Automatic Identification System (AIS) which would ensure monitoring maritime traffic in Turkish sea areas and facilitate anti-smuggling efforts has been installed in all Turkish coasts and will be operated with all functions by the end of 2007. Further, Modernization of Maritime Communication Infrastructure will be started in 2008 within the framework of EU Financial Cooperation. The process of harmonizing Turkish maritime legislation with EU acquis and becoming a party to some important international maritime conventions will be continued according to the programme prepared earlier.

In the area of road transport, harmonization with the EU acquis has been attained to a large extent with the enactment of The Road Transport Law and a series of by-laws issued under this Law. Therefore, the sector as a whole has been provided with a law-level legal base. These legal regulations allow the creation and development of strong and efficient enterprises that have financial and professional competence, and professional reputation. Thereby, a road transport sector is being created, which is in harmony with the EU acquis, has high service quality and standards and total efficiency, which is organized, safe, rapid, economic and integrated with other transport modes.

It is aimed to increase road traffic safety by effective and sound conduct of mechanical inspection, weight and dimension controls of vehicles. In this context, the process of delegating the opening and operation of vehicle inspection stations to private sector (189 immobile and 39 new mobile stations) has largely been completed.

All operation and transactions in road transport sector are conducted electronically in real time by means of the recently developed U-NET Land Transportation Automation System. The automation system was harmonized and integrated with the other related agencies and organizations.

The Regional Transport Directorates were reorganized and administrative and technical capacities of road transportation units were strengthened. Furthermore, cooperation and power delegation were realized for the conduction of some functions of the Ministry of Transport by organizations established by special laws (The Unions of Chambers and Commodity Exchanges of Turkey (TOBB), Undersecretariat of Customs, Universities, and Governorships).

In the road transportation area, Turkish Highways Sector Support Project, which was developed for supporting the EU harmonization process financed by an amount of 5.5 million euros from the EU, and consists of three main components namely twinning, service procurement (training) and equipment procurement, was implemented. The joint Dutch-German proposal was selected for the twinning component and following the completion of necessary preparation the twining component started on 11 May 2006. The twinning project aims to improve the harmonization of the existing road transportation legislation with EU acquis and make necessary regulations in the non-harmonized areas. For this purpose, harmonization efforts are carried out under the project considering the reports and recommendations prepared by experts. The By-Law on Road Transport of Hazardous Materials prepared with the contribution of project works was promulgated in the Official Gazette dated 31 March 2007 No.26479.

The second and third components of the Turkish Road Transport Sector Support Project, service procurement and material/equipment procurement components respectively, were started on 30 November 2006.

Table 4. 12: Matrix of Policy Commitments: Transportation

(In 1000 Euros)

	2006	2007	2008	2009	2010
1. Reconstruction of TCDD and Turkish Railway Sector					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	-477	---	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	-477	---	---	---
2. Highways Sector Support Project					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	-1,500	-1,500	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	-1,500	-1,500	---	---
3. Increasing Maritime Safety in Ports and Coastal Areas of Turkey					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	-162.5	---	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	-162.5	---	---	---
4. Modernization of Maritime Communication Infrastructure					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	---	-700 (1)	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	---	-700 (1)	---	---
5. Transport Operational Programme					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	---	---	-387 (2)	-143,150 (3)
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	---	---	-387 (2)	-143,150 (3)

Total Net Budget Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	-2,139.5	-2,200	-387	-143,150
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	-2,139.5	-2,200	-387	-143,150

(1) Included in 2007 programming. Figures are indicative.
(2) Indicative figure for Know-How Support component of Transport Operational Programme. This figure will be definite when the Operational Programme is finalized.
(3) Indicative figure for the infrastructural investments under the Transport Operational Programme. This figure will be definite when the Operational Programme is finalized.

4.6.6. Energy

The basic objective is to supply the energy needed for economic and social development in a continuous, quality and secure manner at the least costs in a competitive free market environment. For this purpose, Turkey attaches great importance and gives priority to realizing energy market reforms and harmonizing the national energy legislation fully with the EU energy acquis. In this context significant reforms were made in recent years; basic sectoral laws were passed to set the legal framework and considerable progress was achieved in opening the sector to competition. Energy Market Regulatory Authority (EMRA) carries out the preparatory works to complete the relevant secondary legislation to fully implement the laws.

TEDAŞ, the public electricity distribution company, was restructured as 20 regional electricity distribution companies, and TEDAŞ signed contracts with these companies for the transfer of operating rights in their respective regions. Works are in progress for licensing and tariff approval for Kayseri ve Civarı Elektrik Dağıtım T.A.Ş. (distributing and supplying electricity to Kayseri and surrounding areas), the only private sector electricity distribution company.

Important progress was made in privatizing the public generation and distribution assets, a basic component of reform efforts. In this context, pre-privatization preparations of the distribution companies included in the privatization program were mostly completed and the tender was announced as of October 2007 for the generation company (Ankara Natural Electricity Generation and Trading Company) in the privatization program. Thus, privatizations will start in the coming year. A price equalization mechanism will be implemented to offset instant and high price differentials between regions after the privatization by the end of 2010.

It is projected that the reform process in the sector, where transitional period operations are continuing to achieve the final objective of a fully competitive free market, will be mostly completed within a few years.

With the aim of spreading the use of natural gas across the country, the EMRA held natural gas distribution tenders for 51 distribution regions so far and 48 winning companies were awarded gas distribution licenses. Of these, 45 distribution companies started investments in their regions, and 31 distribution companies started to supply gas in their regions.

Pursuant to the Law, the tender held on 30 November 2005 by the public natural gas company BOTAŞ to transfer natural gas imports to the private sector was concluded one year later, and as a result of tender, the proposals from four companies were found appropriate regarding gas contract release for a total volume of 4 billion sm^3. The first company that has completed transfer procedures was granted the import license by the EMRA in July 2007. In addition, natural gas transmission network was started to be used by third parties for the first time on 1 July 2007.

In 2007, articles for fighting illegal fuel were incorporated in the Petroleum Market Law No.5015 which aims to liberalize the petroleum market and reorganize the market in this direction.

The Stock Agency will be established instead of the National Petroleum Stock Commission which was established pursuant to the Law No.5015 in order to ensure continuity in the petroleum market, prevent risks in case of crises or extraordinary circumstances and perform obligations relating to extraordinary petroleum stocks as required by international agreements for keeping an adequate amount of petroleum stock and for stock management. For this purpose, a draft bill was prepared by the National Petroleum Stock Commission chaired by the Ministry of Energy and Natural Resources.

The Turkish Petroleum Law was passed in the TBMM on 17 January 2007 which aims to regulate the procedures and principles for regulating, directing, encouraging and controlling petroleum search and production activities in Turkey, compiling, evaluating and presenting for use the necessary information and data for search and production. The Law which was submitted to the President of the Republic for approval was returned to the TBMM for reviewing various articles. The said law regulates the procedures and principles for installing pipeline to ensure the transit passage of crude oil or natural gas over Turkey to another country without relying on any international agreement, or transmission of crude oil or natural gas to Turkey.

The secondary legislation works were mostly completed after entry into force of the Liquefied Petroleum Gas (LPG) Law No.5307 dated March 2005 prepared to regulate, direct, monitor, and supervise in a transparent, egalitarian and stable manner the market activities for supplying LPG from domestic and international sources to the users safely and in a competitive environment.

The Energy Efficiency Law No.5627 dated 2 May 2007 was put into effect which aims to provide such multiple benefits as utilizing energy and energy resources rationally, providing the national economy with saving potential, reducing environmental pollution from energy use, and creating new jobs. The preparatory works for the secondary legislation as required by the law are in progress, and it is expected that the relevant by-law will be completed in the coming year.

The encouraging atmosphere created for renewable energy generation by the Law No.5346 on Utilizing Renewable Energy Sources for Generating Electricity dated 10 May 2005 was improved further by the Energy Efficiency Law No.5627. In addition to other investment incentives, the mentioned Law introduced the base price (5 c€/kWh) in renewable electricity purchases. Besides, natural and legal persons who install co-generation facilities above certain efficiency level for their own needs and small scale generation facilities and micro co-generation facilities based on renewable sources were exempted from the obligation to obtain licenses and establish companies.

The Law No.5686 on Geothermal Resources and Natural Mineral Waters went into effect on 13 June 2007. The law aims to explore, analyze, develop, produce, preserve and put to economical and environmentally friendly use the geothermal and natural mineral waters.

Projects are continuing for Turkey's physical integration with the EU market in electricity and gas. In this context, the Turkey-Greece natural gas pipeline construction was completed in the first half of 2007, and the pipeline was commissioned for operation in November 2007. Works are continuing for the Natural Gas Pipeline of Turkey-Bulgaria-Romania-Hungary-Austria (Nabucco Project), which is planned to commence operation in 2012. Upon the implementation of these projects, Turkey will become a new route in gas supply to the EU. On the other hand, the connection will be made in 2008 to allow the Turkish electricity system to work synchronously with the EU electricity system (UCTE, Union for the Coordination of Transmission of Electricity).

Table 4. 13: Legislative Acts for Energy Market in 2007

Date	Number	Name	Description
		Electricity	
21/12/2006	Official Gazette No.26383	Communiqué on Revenue Regulation for the First Implementation Period of 20 Distribution Companies	This covers the procedures and principles for determining the Average Retail Energy Sales Price and loss-theft energy price ceiling to be taken as the basis for the distribution system, retail sales service and transmission fee revenue requirements adjustment and retail energy sales price to be applied between the transitional period of 01.01.2007 and 31.12.2010 in the context of the

			tariff proposal submitted by Türkiye Elektrik Dağıtım Anonim Şirketi for the first implementation period ending on 31.12.2010 pursuant to the Electricity Market Law.
21/12/2006	Official Gazette No. 26383	Communiqué on Price Equalization Mechanism Applicable in Electricity Distribution Regions	This covers the procedures and principles for the price equalization mechanism to be applied through 31.12.2010 in order to partially or wholly protect the consumers from price differentials existing due to cost differentials between distribution regions pursuant to the Electricity Market Law No.4628.
29/12/2006	Official Gazette No. 26391	Regulation on Electricity Market Activities of Organized Industry Districts	This covers laying down the rights and obligations of Organized Industry Districts in activities under the Electricity Market Law No.4628, supplying to participants the electricity energy they generate or obtain and supply as a free consumer, issuing licenses to them, and determining distribution fees and other service fees, and other matters.
07/01/2007	Official Gazette No. 26396	Regulation on Regulating Distribution System Investments in the Electricity Markets and Inspecting Actualizations	This regulates the procedures and principles regarding the regulation of distribution system investments and inspecting actualizations.
26/04/2007	Official Gazette No. 26504	Law No.5625 on Amending Various Laws	This law makes some amendments to the Law No.4283 on Installing and Operating Electric Energy Generation Facilities by Build-Operate-Transfer Model and Regulating Energy Sales.
02/05/2007	Official Gazette No. 26510	Energy Efficiency Law No.5627	This lays down the procedures and principles for increasing and promoting efficiency in all stages of generation, transmission, distribution and consumption of energy, in industrial enterprises, buildings, electric energy generation plants, in transport by transmission and distribution networks, raising energy awareness in the society, and utilizing renewable energy sources.
13/06/2007	Official Gazette No. 26551	Law No.5686 on Geothermal Resources and Natural Mineral Waters	This covers the procedures, principles and sanctions holding tenders for and inspecting resource utilization and preserving the source and take-out in search and operation periods of geothermal and natural water sources and geothermal gases.
21/11/2007	Official Gazette No. 26707	Law No.5710 on Installation and Operation of Nuclear Power Plants and Energy Sales	This Law lays down the procedures and principles for installation and operation of nuclear power plants and energy sales.
Natural Gas			
14/11/2006	Official Gazette No. 26346	Regulation on Amending the Regulation for National Gas Market Distribution and Customer Services	This is the regulation amendment that covers the procedures and principles regarding the selection of the company to be issued the distribution license for the urban natural gas distribution, and the natural gas distribution activities of license holding companies and customer services.
01/02/2007	Official Gazette No. 26421	Regulation on Amending the Regulation for Natural Gas Market Licenses	This covers the procedures and principles for issuing licenses to legal persons operating or to operate in the natural gas market.

		Petroleum	
30/12/2006	Official Gazette No.26392	Official Statistics Program	Within the program, the General Directorate of Petroleum Affairs, a subunit of the Ministry of Energy and Natural Resources is the agency in charge of petroleum statistics relating to market activities. Pursuant to the said, the General Directorate will prepare petroleum statistics by the end of 2007 on behalf of the Ministry of Energy and Natural Resources.
07/01/2007	Official Gazette No.26396	Regulation on Procedures and Principles for Inspections, Preliminary Investigations and Investigations in Petroleum Market	This is the final form of the regulation that lays down the procedures and principles for monitoring, supervising and sanctioning the market activities regarding the supply to users the petroleum and mineral oils supplied from domestic and international sources in an economically competitive environment.
13/02/2007	Official Gazette No.26433	Law on Amending the Petroleum Market Law	Its purpose is to take effective measures to prevent petroleum smuggling.
27/05/2007	Official Gazette No.26534	Regulation on Procedures and Principles for Finding and Liquidating Contraband Petroleum	This lays down the procedures and principles for finding, storing and liquidating the products defined as illegal petroleum.
		Liquefied Petroleum Gas (LPG)	
01/05/2007	Official Gazette No.26509	Regulation on Amending the Regulation on Liquefied Petroleum Gas Market	Its purpose is to lay down the procedures and principles for licenses to be issued to natural and legal persons, reporting to the Authority and record schemes in order to regulate, direct, monitor, and supervise in a transparent, egalitarian and stable manner the market activities for supplying LPG from domestic and international sources to the users safely and in a competitive environment.
05/06/2007	Official Gazette No.26543	Regulation on Technical Regulations Applicable in the Liquefied Petroleum Gas Market	Its purpose is to lay down the procedures and principles regarding the compliance with technical regulations and standards of the activities in liquefied petroleum gas, facilities, equipment and products marketed.

Four separate projects are in progress with the EU within the context of reforms in the energy sector:

1. The Twinning Project on Increasing Energy Efficiency in Turkey, initiated on 13 July 2005, was completed in November 2007.
2. Works are in progress to start in 2007 the Project for Raising Public Awareness on Efficient Use of Energy in Buildings supported under the EU 2005 Financial Cooperation Programming aimed to raise public awareness on efficient use of energy in buildings, and the tendering process is in the final phase. The total budget of the project is 1.07 million euros, of this amount 1.04 million euros come from EU, and 30,000 euros from the national resources.
3. The Project for Adapting the Operation Conditions for Crossborder Electric Trade in Turkey to the Best Practices in EU is being carried out by TEİAŞ under the 2006

Financial Cooperation Programming in order to make the technical infrastructure suitable for crossborder trade to integrate the Turkish electricity system with the European electricity system, and create the required legal infrastructure.

4. The Regulatory Board Information System Project being carried out by the EMRA envisages the creation of a regulatory information system structure with the aim of supporting the efficient regulation and supervision of energy markets by the EMRA. The tender regarding the project was concluded as of November 2005, the contract was signed and the implementation of the project was started. In the analysis phase of the project scheduled for completion in November 2006, problems were experienced due to differing interpretation of the specifications by the contracting firm, and the project was unilaterally suspended by the contracting firm.

Table 4. 14: Matrix of Policy Commitments: Energy

(In 1000 Euros)

	2006	2007	2008	2009	2010
1. Project for Increasing Public Awareness on Energy Efficiency in Buildings					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	-12	-18	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	-12	-18	---	---
Total Net Budget Effect					
A. Implementation Profile	---	---	---	---	---
B. Net Budget Effect	---	-12	-18	---	---
B.1. Direct Effect on Budget Revenues	---	---	---	---	---
B.2. Direct Effect on Budget Expenditures	---	-12	-18	---	---

ANNEX TABLES

Table 1.a: Macroeconomic Prospects

	ESA Code	2006	2006	2007	2008	2009	2010
		Level Bn YTL	Rate of Change				
1. Real GDP, at 1987 prices *	B 1 * g	155.7	6.1	5.0	5.5	5.7	5.7
2. GDP, at current prices	B 1 * g	576.3	18.3	12.3	10.7	10.4	9.8
Components of Real GDP							
3. Private Consumption Expenditure	P3	100.6	5.2	4.0	4.8	4.7	5.0
4. Public Consumption Expenditure	P3	10.9	9.6	6.5	3.4	2.7	1.3
5. Gross Fixed Capital Formation	P51	46.4	14.0	6.5	5.7	7.4	6.4
6. Changes in Inventories and Net Acquisition of Valuables**	P52+P53	4.8	-2.1	0.5	0.1	-0.4	-0.2
7. Exports of Goods and Services	P6	71.9	8.5	11.2	8.3	8.5	8.5
8. Imports of Goods and Services	P7	78.3	7.1	10.7	6.7	6.7	6.9
Contribution to Real GDP Growth							
9. Final Domestic Demand		---	7.9	5.0	5.0	5.4	5.2
10. Changes in Inventories and Net Acquisition of Valuables	P52+P53	---	-2.1	0.5	0.1	-0.4	-0.2
11. External Balance on Goods and Services	B11	---	0.3	-0.2	0.5	0.7	0.6

* Excluding statistical discrepancy.
** Contribution to growth.

Table 1.b: Price Developments

Percentage Changes, Annual Averages	ESA Code	2006	2007	2008	2009	2010
1. GDP Deflator		11.2	7.2	4.9	4.4	3.9
2. CPI		9.6	6.6	4.1	4.1	4.0

Table 1.c: Labour Market Developments

	ESA Code	2006	2006	2007	2008	2009	2010
		Level	Rate of Change				
1. Employment, persons (Thousands)*		22,330	1.3	2.8	2.1	2.1	1.9
2. Unemployment Rate (ILO Definition)		2,446	9.9	9.7	9.7	9.7	9.7
3. Labour Productivity, persons		---	4.8	2.2	3.4	3.5	3.7
4. Compensation of Employees		---	11.3	---	---	---	---

*+15 years-old

Table 1.d: Balance of Payments

Percentages of GDP	ESA Code	2006	2007	2008	2009	2010
1. Current Account		-8.2	-7.4	-7.5	-7.2	-6.8
- Balance of Goods		-10.3	-9.3	-9.0	-8.5	-7.8
- Balance of Services		3.3	2.9	2.9	2.9	2.8
- Balance of Incomes		-1.6	-1.4	-1.8	-2.0	-2.2
- Balance of Current Transfer		0.4	0.4	0.3	0.4	0.4
2. Capital and Financial Account (Excluding Reserves)		10.2	8.7	8.3	7.3	7.3
- Private Sector		0.7	-0.2	---	---	---
- Public Sector		9.5	8.9	---	---	---
Statistical Discrepancy		---	---	---	---	---

Table 2: General Government Budgetary Prospects

Percentages of GDP	ESA	2006	2007	2008	2009	2010
Net Lending(B9) by sub-sectors*						
1. General Government	S13	-1.9	0.0	0.0	-0.7	-1.0
2. Central Government	S1311	-2.8	-2.2	-1.6	-2.7	-3.6
3. Funds	S1311	-1.5	-1.0	-1.1	-1.5	-1.0
4. Local Administration	S1313	0.8	0.6	0.3	0.3	0.3
5. Social Security Fund	S1314	3.1	4.1	4.0	4.5	4.7
6. Revolving Funds	S1311	-0.6	-0.4	-0.5	-0.5	-0.5
7. Unemployment Fund		-1.0	-1.1	-1.1	-0.9	-0.9
General Government (S13)						
8. Total Receipts	TR	46.2	43.7	43.2	42.0	40.6
9. Total Expenditures	TE	44.3	43.6	43.3	41.3	39.6
10. Net Lending	EDP.B9	-1.9	0.0	0.0	-0.7	-1.0
11. Interest Payments	EDP.D41 incl. FISIM	8.1	7.7	7.9	6.4	5.5
General Government Debt Expenditures		0.0	0.0	0.0	0.0	0.0
12. Primary Balance		-10.1	-7.7	-7.9	-7.1	-6.5
Components of Revenues						
13. Taxes (13 a+13 b + 13 c)		24.3	23.8	24.3	24.2	23.5
13 a. Taxes on Production and Imports	D2	16.5	15.6	16.1	16.0	15.4
13 b. Currents Taxes on Income and Wealth	D5	7.8	8.2	8.2	8.2	8.1
13 c. Capital Taxes	D91	0.0	0.0	0.0	0.0	0.0
14. Social Funds	D61	7.7	7.5	7.6	7.0	6.8
15. Factor Incomes	D4	8.4	7.7	7.1	6.7	6.6
16. Other		5.8	4.7	4.2	4.0	3.6
17. Total Receipts	TR	46.2	43.7	43.2	42.0	40.6
Tax Burden		32.1	31.3	32.0	31.4	30.4
Components of Expenditures						
18. Total Consumption	P32	19.0	19.4	19.0	18.7	18.1
19. Total Social Transfers	D62+D63	8.1	8.4	8.4	8.3	8.3
19 a. Social Transfers in kind	D63	0.1	0.1	0.1	0.1	0.1
19 b. Social Transfers other than in kind	D62	8.0	8.3	8.3	8.2	8.2
20. Interest Payments	EDP. D41+FISIM	8.1	7.7	7.9	6.4	5.5
21. Subsidies(1)	D3	1.0	1.0	0.9	0.9	0.8
22. Gross Fixed Capital Formation	P51	4.3	4.1	3.7	3.8	3.7
23. Other		3.8	2.9	3.3	3.1	3.0
24. Total Expenditures	TE	44.3	43.6	43.3	41.3	39.6
Personnel Expenditures	D1	9.4	9.7	9.5	9.3	9.0

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

Table 3: General Government Expenditure by Function

Percentages of GDP	COFOG Code	2006	2007	2008	2009	2010
1. General Public Services	1	11.5	11.5	11.2	9.8	8.7
2. Defence	2	2.3	2.2	2.1	2.0	1.9
3. Public Order and Safety	3	2.0	2.0	2.0	2.0	1.9
4. Economic Affairs and Services	4	7.3	7.1	6.4	6.3	6.2
5. Environmental Projection	5	0.4	0.4	0.4	0.4	0.4
6. Housing and Community Amenities	6	1.5	1.2	1.1	1.2	1.1
7. Health	7	4.8	4.9	5.0	4.9	4.8
8. Recreation, Culture and Religion	8	0.7	0.7	0.7	0.7	0.7
9. Education	9	4.1	4.1	4.2	4.1	3.9
10. Social Security and Social Assist	10	9.8	9.3	10.1	10.0	9.9
Total	TE	44.3	43.6	43.3	41.3	39.6

Table. 4: General Government Debt Developments

Percentage of GDP	ESA Code	2006	2007	2008	2009	2010
1. Gross Debt		60.9	56.8	52.5	49.6	45.6
2. Change in Gross Debt		---	-4.1	-4.3	-2.9	-4.0
Contributions to Change in Gross Debt						
3. Primary Balance		---	-3.8	-5.1	-5.5	-5.4
4. Interest Expenditure	EDP D.41	---	7.4	7.6	6.1	5.2
5. Current GDP Growth		---	-12.0	-10.5	-10.2	-9.5
6. Other		---	4.3	3.7	6.7	5.7

Table 5: Cyclical Developments*

	2006	2007	2008	2009	2010
1. Real GDP Growth (1987 Prices)	6.1	5.0	5.5	5.7	5.7
2. Net Lending of General Government	-2.8	-2.2	-1.6	-2.7	-3.6
3. Interest Expenditure	7.0	6.8	7.4	6.0	5.0
4. Potential GDP Growth	6.2	6.2	6.2	6.0	5.6
Contributions:					
- Labour	7.9	24.8	21.7	22.4	21.1
- Capital Stock	30.2	20.5	32.2	33.7	34.1
- Total Factor Productivity	61.9	54.7	46.1	43.9	44.8
5. Output Gap (percentage difference from the potential)	1.7	0.5	-0.2	-0.5	-0.4
6. Cyclical Budget Component**	-0.7	-0.2	0.0	0.2	0.2
7. Cyclically Adjusted Balance**	1.6	2.6	2.5	1.9	1.1
8. Cyclically Adjusted Primary Balance**	-6.5	-5.1	-5.4	-4.6	-4.5

*Consolidated/Central Government budget

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

Table 6: Divergence From Previous Update

	2006	2007	2008	2009	2010
GDP Growth (Per cent)					
Previous Update	6.0	5.0	5.6	5.9	---
Latest Update	6.1	5.0	5.5	5.7	5.7
Difference	0.1	0.0	-0.1	-0.2	---
General Government Net Lending (Percentage of GDP)					
Previous Update	-2.7	0.6	0.0	0.3	--
Latest Update	-1.9	0.0	0.0	-0.7	-1.0
Difference	0.8	-0.6	0.0	-1.0	---
General Government Gross Debt (Percentage of GDP)					
Previous Update	63.4	57.7	53.1	48.4	---
Latest Update (ESA Definition)	60.9	56.8	52.5	49.6	45.6
Difference	---	---	---	---	---

Table 7:Basic Assumptions on the External Economic Environment Underlying the PEP 2007 Framework[1]

	2006		2007		2008		2009		2010
Interest Rates (Per cent)		change*		change*		change*		change*	
Domestic Interest Rate (Treasury Bill Rate, Simple)	18.6	0.6	18.1	0.1	---	---	---	---	---
Domestic Interest Rate (Treasury Bill Rate, Long Term)	---	---	---	---	---	---	---	---	---
Exchange Rates									
Exchange Rate vis-à-vis € (YTL / €)	1.8000	0.0036	1.7763	---	---	---	---	---	---
Parity (USD/ €)	1.26	0.01	1.36	0.11	1.42	0.15	1.42	0.15	1.42
Nominal Effective Exchange Rate	---	---	---	---	---	---	---	---	---
Real Exchange Rate	-0.3	-1.7	14.4	12.2	-2.2	-2.2	-3.0	-3.0	0.1
Real GDP Growth									
World (excluding EU)	5.4	-0.3	5.6	0.4	5.3	0.1	5.4	0.2	5.4
EU-27	3.0	0.2	2.9	0.5	2.4	0.0	2.4	0.0	2.4
World (IMF Forecast)	5.4	---	5.2	---	4.8	---	---	---	---
World Trade (In Real Terms)									
EU Export Market (Extra EU-25)	9.0	-0.6	8.8	0.2	7.7	0.1	7.9	0.1	7.9
World Import (Excluding EU-25)	8.9	-0.2	7.5	-0.8	7.0	-0.9	7.2	-0.7	7.2
International Prices									
EU CPI (IMF Forecast)	2.0	---	1.2	---	1.4	---	1.4	---	0.9
US CPI (IMF Forecast)	3.2	---	2.7	---	2.3	---	2.4	---	2.4
World Import Prices (Percentage Change)	6.0	5.3	1.5	1.1	1.2	---	1.2	---	1.2
Oil Prices (USD per Barrel)	64.3	-1.3	70.6	4.3	78.8	10.8	76.0	---	76.0

*Difference from 2006 PEP
[1]EU Commission's Autumn 2007 Forecasts

Table 8: Structural Reform Agenda and Developments

Measures Taken in the Last Year's PEP	Realization Status (Y/N)	Date[14]	Comments
Privatisation			
Initiation of the privatisation process for electricity distribution companies	N	---	To initiate the tender process, completion of necessary infrastructure investments is waited for.
Initiation of the privatisation process for lottery games	N	---	Waiting for the Draft Law, which includes the mechanism and the rules that regulate the market after privatisation, to be enacted.
Privatisation of public banks	Y	2007	24.98 per cent of Halkbank was privatized via public offering method.
Initiation of the privatisation process for electricity generation portfolio companies	Y	2007	Date of the tender for the privatization of Tercan, Kuzgun, Mercan, İkizdere, Çıldır, Beyköy and Ataköy Hydroelectric Power Plants and Denizli Geothermal Power Plant was announced as 7 January 2008.
Privatisation of seaports of TCDD	Y	2007	Transfer of Mersin Port and tenders of İzmir and Derince Ports were completed.
	N	2007	Privitization procedures for İskenderun, Bandırma and Samsun Ports have not been started yet.
Privatisation of vehicle inspection stations	Y	2007	The process was completed in 2007 and stations were transferred to the company which obtained the contract.
Initiation of the privatisation procedures for TEKEL cigarette factories	Y	2007	The date of tender was announced as 20 January 2008.
Initiation of the privatisation procedures for PETKİM	Y	2007	The tender was held and completion of approval and contract stages is waited for transfer.
Privatisation of sugar factories	N	2009	Tenders for Bor, Ereğli and Ilgın sugar factories and public shares of Kayseri sugar factory were cancelled.
Competition Law and Policies			
In respect of the Law on the Protection of Competition No.4054; for purposes of both enhancing enforcement efficiency and ensuring harmonization with the effective legislation in the EU, in the form of Regulations and Notices.	N	---	The text of the Draft Law for which the opinions of the institutions concerned have been obtained is on the agenda of the Competition Board.
The Communiqué No. 2007/2 on the Amendment of the Block Exemption Communiqué on Vertical Agreements	Y	2007	It was published in the Official Gazette (No. 26532) on 25 May 2007 and came into force on 1 July 2007.
Works aimed at the creation of a functionally independent state aids monitoring and supervising unit	N	2008	The Draft Bill, which was prepared in order to monitor and supervise the state aids in Turkey in compliance with the EU criteria, was submitted to the Prime Ministry and is expected to be enacted in 2008.
Improvement of the Investment Environment			
SME Strategy and Action Plan	Y	2007	SME Strategy and Action Plan, which was approved for the aim of providing national SME policy implementation and increasing the

[14] The date or foreseen date of realization.

			competitiveness of the SME's, was revised to cover the 2007-2009 period and approved by the 2007/25 numbered decision of the High Planning Council in 2007.
The Draft Bill on Amending the Law on Work Permits for Foreigners and some other laws	N	2008	Work permits process of foreigners; especially to work in the scope of vocational services and national and international projects, is aimed to be shortened.
The Draft Bill on Amending the Law on Land Registry	Y	2006	Legislative act that amended the provisions of the Land Registry Law regarding property acquisition by foreigners came into effect on 7 January 2006.
Turkish Commercial Law	N	2007	The draft Turkish Commercial Law, which is on the agenda of the TBMM, is expected to be enacted in 2007.
The Coastal Act	N	2008	The Draft Bill Amending the Coastal Act prepared by Ministry of Public Works and Settlement was submitted to the Prime Ministry in May 2006. The Ministry's evaluation process of the opinions obtained by the Prime Ministry has been continuing.
Financial Sector			
Privatisation of public banks	Y	2007	Halkbank was put into the privatization program in August 2006. 24.98 per cent of the bank's shares were privatized through public offering in May 2007.
	N	---	In light of the Halkbank experience, a privatization strategy will be formulated for Ziraat Bank.
Initiation of risk focused auditing practice by BRSA	Y	2007	The process is completed in transition to risk focused auditing practice, in which the content, scope, form, timing of auditing procedure and resource allocation is determined according to the banks' risk profile.
Completion of second quantitative impact study to examine the impact of clauses of Basel-II and relevant EU directives on the capital adequacy of banks in the Turkish banking sector	Y	2007	The second domestic quantitative impact study QIS-TR2 was conducted with 31 banks representing about 97 per cent of the sector, based on September 2006 data, and the results of the study were publicized in July 2007.
Completion of the establishment of a company to lay down the organization and infrastructure of an organized market where capital market instruments issued by SMEs will be traded and commencement of operations in the market in 2005	N	2007	Establishment of the company (Emerging Enterprises Market) which will lay down and develop the trade platform, where buying and selling will take place, and the related necessary organization is completed by the end of 2005, the works on technical and legal issues are finalized. The efforts for opening the market are continued by the company.
Continuing works on restructuring custody and clearing system	N	2007	As the dematerialization works kept its priority in the work plan of Takasbank, it took a significant amount of time and the targeted time frame for the restructuring works of the clearing system was extended. On the other hand, the subject is a part of Twinning Project held within CMB to comply with the EU acquis and this fact affected the timing of the work. Completion of the works within 2007 is targeted.

Legal and technical works for creating mortgage financing system	Y	2007	The law has come into force. The majority of the secondary legislation to establish housing finance system has been enacted in August 2007. The secondary legislations regarding covered bonds, asset finance funds, asset backed securities and mortgage finance corporations continue. These works will be completed in 2008.
Initiating the project to benefit from the Pre-Accession Financial Fund in the context of 2004 Programming for Candidate Countries in Central and Eastern Europe (PHARE) programme under the Pre-Accession Financial Assistance being provided to Turkey by the European Union	Y	2006-2007	The works of EU Twinning Project between the Capital Markets Board and the German Ministry of Finance on Support of Harmonization of Capital Markets Board to EU Capital Markets Standards has been initiated following the kick-off meeting held on 1 February 2006. Within the scope of the project, the works on compliance with the EU acquis as well as the works on education, strengthening administrative capacity and public disclosure continue.
Capital markets compliance with the Community acquis dealing with the intermediary institutions' capital adequacy following the acceptance of Basel II criteria by EU	N	2005-2009	Compliance with the EU acquis on capital adequacy is one of the working subject of the Twinning Project. For this reason, works on compliance on this issue is planned to be completed until the end of the project. However, the EU regulation framework on this issue is closely related to the banking sector. Therefore, the planned date could be changed by CMB in parallel to the agenda of the amendment to the banking legislation.
Establishing specialty courts for capital markets	N	---	No progress was made due to the need for coordinated work with other institutions.
Dematerialization of Government Domestic Borrowing Instruments (GDBI) at the Central Registry Agency (CRA) and custody and monitor on customer basis	N	2008	In the scope of continued works, GDBI's outright purchases and sales, repo and reverse repo transactions are decided to be handled separately. Primarily principles on the dematerialization of GDBI's outright purchases and sales transactions are determined and submitted to the Ministry of State in February 2006. Within these principles, the works on system development and software initiated by Central Registry Agency (CRA) was completed and training and testing period is continuing. The dematerialized system on GDBI's outright purchases and sales at CRA is foreseen to become effective in 2007, unless there are some troubles due to delays especially from banks that are unable to finish necessary harmonization works. On the other hand, the works on setting the principles on the dematerialization of GDBIs subject to repo transactions will be completed following the review of the repo legislation.
Legislation of the draft bill of Law on the Regulation and Supervision of the Insurance Transactions	Y	2007	The Insurance Law was put into force on 14 June 2007.
Labour Market			
Privatisation Social Support Project II	Y	2006-2008	Privatisation Social Support Project II is continuing as the implementations of privatisation continue.
Agriculture			
Issuance of the Law on food, feed, food hygiene and veterinary services	N	2008	It is aimed that the legislative package, which is started to be prepared with the goal of

			complying with the Community acquis, will be completed and issued in 2008.
Privatisation of sugar factories	N	2009	The privatisation process of Ereğli, Bor and Ilgın Sugar Factories could not be completed by the end of 2006. However, privatisation process of all sugar factories is planned to be completed by September 2009.
Preparation of Rural Development Plan	N	2007-2008	The preparatory work is continuing for the Plan which will cover all regional development activities financed by national and international resources within the framework of National Regional Development Strategy which is in effect since 2006. In the Plan, application guidelines of the rural development activities will be laid down, and coordination of these activities with sectoral and regional policies will be increased.
Preparation of IPARD Program	N	2007-2008	Works are in progress for the final draft of Program to be submitted to EU for approval. In the preparation of the program, technical support was provided by project no. TR0402.08 subject to 2004 financial cooperation programming.
Strengthening the institutional capacity in rural development area	N	2005-2008	The twinning component of the project no. TR0402.08, which provides support for improving institutional capacity in rural development and is subject to 2004 financial cooperation programming, was completed in 2007. The Law on the Establishment of Agriculture and Rural Development Support Institution No. 5648 has gone into effect. The Institution will function as an IPARD Agency. The endeavors both on achieving of the national accreditation of the Institution and making the EU to take the decision of conferral management of the funds is supported by the project no. TR0503.05.
Administrative Reform			
Public Financial Management and Control Law	Y	2005-2008	The Law No.5428 has ensured uniformity and consistency between the Law No.5018 and related provisions of the Constitution. With the Law No.5436 enforcement of the Law No.5018 has been improved and it was ensured that all provisions of the Law to become effective on 1 January 2006. Secondary legislation necessary for the implementation of the Law No.5018 was prepared and put into effect on 1 January 2006.
The Strategic Plan and Performance Programme	Y	2006-2009	Public administrations will carry on their strategic planning works in accordance with the transition schedule in the By-Law on the Principles and Procedures of Strategic Planning in Public Administrations. In accordance to By-Law on the Principles and Procedures of Strategic Planning in Public Administrations, 31, 60 and 40 public administrations will prepare strategic plans and performance programmes in 2007, 2008 and 2009 respectively.

Regional Development			
The Law No.5449 on the Establishment, Coordination and Duties of Development Agencies[15]	N	2007	The Law, which allows the establishment of Development Agencies in the determined NUTS II Regions and regulates the related principles and procedures, has been enacted on 8 February 2006 by Law No.5449 upon the adoption of the TBMM.
The Decision of the Council of Ministers on the Establishment of Development Agencies in certain NUTS II Regions[15]	N	2007	Development Agencies have been established in TR62 NUTS II Region (comprising the provinces of Adana and Mersin), of which the province of Adana is the center and TR31 NUTS II Region (comprising the province of İzmir), of which İzmir is the center.
Regulation on the Working Principles and Procedures of Development Agencies[15]	N	2007	Provisions on structure and bodies of Development Agencies, duties and authorities of these bodies, and the functioning of Development Agencies have been regulated.
Regulation on the Personnel Regime of Development Agencies[15]	N	2007	Human resources policy, procedures for the personnel recruitment and other related provisions for personnel of Development Agencies have been regulated.
Regulation on the Budget and Accounting of Development Agencies[15]	N	2007	Authorities and responsibilities of the personnel who will serve in the budget and accounting system of Development Agencies, preparation and implementation process of the budget of Development Agencies and the provisions for accounting system of Development Agencies have been regulated.
Principles and Procedures for determining wages, daily allowances and other social and financial rights of personnel of Development Agencies, and for the determination of amount of allowances to be transferred to Development Agencies in 2006 and 2007[15]	N	2007	Maximum and minimum level of wages, daily allowances and other social and financial rights of the personnel to be recruited in Development Agencies and allowances to be transferred from General Budget to Development Agencies established in TR62 NUTS II Region (comprising the provinces of Adana and Mersin), and TR31 NUTS II Region (comprising the province of İzmir) for the 2006 Provisional Budget and 2007 Budget were determined.
Twinning Project of Support to the State Planning Organization General Directorate of Regional Development and Structural Adjustment for Strengthening Institutional and Administrative Capacity	Y	2007	The Project, which lasted for 18 months, has finished on January 25, 2007.
Health and Social Security Reform			
Spreading the pilot implementation of Family Medicine	Y	2010	The pilot implementation of Family Medicine will be spread at 24 provinces at the end of 2007
Establishing the health information system	Y	2008	Usage of Minimum Health Data Sets and Social Security Institution's data sets will become widespread. Pilot implementation of Tele-medicine and Hospital Appointment and Referral Integration System projects will be started
Combining the social security institutions under a single organization, separating the long-term and short-term insurance branches and establishing universal health insurance.	Y	2005-2007	It was foreseen that the Social Insurances and Universal Health Insurance Law No.5510 would come into force on 1 January 2007, however, the Constitutional Court has canceled some of the provisions of the Law by its decision dated on 15 December 2006. The

			studies carried on by Social Security Institution (SGK) and the line ministries regarding the Law No.5510 continue in line with the decree of the Constitutional Court, and the Law No.5510 will be put into force on January 1, 2008.
Establishing an effective IT infrastructure by the social security reform.	N	2006-2008	Studies related to establishment of an effective, accessible, and sustainable service-providing structure in social insurance system by accomplishing fully computerized IT infrastructure are underway.
Information and Communication Technologies			
Law on Regulation of Internet Publications and Combating Crimes Committed through Such Publications	Y	2007	The Law, which aims to combat some specific crimes committed through internet, entered in force with promulgation in the Official Gazette dated May 23, 2007, No.26530.
Electronic Communications Law	N	2008	The Draft Law, which was prepared to align with the Directives 2002/22/EC, 93/13 /EC, 2002/58/EC, 92/44/EEC, 92/382/EEC, 2002/19/EC, 2002/20/EC, 2002/21/EC, 98/10/EC, 97/33/EC, 90/388/EEC, 90/387/EEC, was sent to the TBMM in the 22nd Legislative Term, but it was not adopted. The Draft is expected to be sent to Parliament in 2008 again.
Law on Protection of Personal Data	N	2007	The Draft Law, which was prepared to align with the Directives 95/46/EC, 2002/58/EC and Commission Decision 2001/497/EC and Council of Europe Convention ETS No.108 (919999JHA10184), was submitted to the Prime Ministry.
Number Portability Regulation	Y	2007	The By-Law aligning with the Directive 2002/22/EC on universal service and users' rights was promulgated in the Official Gazette dated February 1, 2007, No. 26421 and put into effect.
Amendment on the Access and Interconnection Regulation	Y	2007	The By-Law, which was prepared to conform to the Framework Directive 2002/21/EC, is published in the Official Gazette on June 14, 2007, No. 26552 and put into effect.
Regulation on Procedures and Principles Regarding Identification of the Operators with Significant Market Power	Y	2007	The By-Law, which was prepared to conform to the Framework Directive 2002/21/EC, is published in the Official Gazette on June 7, 2007, No. 26396 and put into effect.
Amendment on the Authorization regarding to Telecommunications Services and Infrastructure regulation	Y	2007	Published in the Official Gazette on August, 14 2007, No. 26613 and put into effect.
Amendment on the Regulation on the Authorisation in Electronic Communications Sector	N	2008	Works are underway to conform to the Authorization Directive 2002/20/EC and the Regulation will be promulgated after enactment of the Electronic Communications Law.
Regulation on processing of personal data and the protection of privacy in the electronic communications sector	N	2008	Works are underway to conform to the Directive 2002/58/EC of the European Parliament and of the Council concerning the processing of personal data and the protection of privacy in the electronic communications sector and the Directive 2006/24/EC on the retention of data generated or processed in connection with the provision of publicly available electronic communications services or of public communications networks.

Prime Ministry Circular regarding Citizen's Card Project	Y	2007	Published in the Official Gazette on July 4, 2007, No. 26572.
		Energy	
Continuation of the privatisation process for the electricity distribution companies	N	---	The privatization tenders made for 3 distribution companies were paused at the end of 2006 in order to complete the related preparatory works. The privatization process is expected to resume in the forthcoming year.
Works for privatisations in electricity sector	N	2004-2009	To start distribution privatisations, electricity distribution system has been restructured and corporatized as 21 regions and 20 of these distribution companies have been taken into privatization portfolio. It is expected that privatizations will be completed to a large extent within 2 years.
Regulatory Board Information System Project	N	2004-…	The project has been started in November 2005, but due to different interpretation of contract at the analysis stage by the contractor firm EDYN, the project was suspended unilaterally by EDYN.
Project for Feasibility Study for Turkey's Integration to UCTE Electricity System	Y	2005-2007	The project, which had been carried out by TEIAS, was completed in 2007.
Project on Providing BOTAŞ Know-How Support in Natural Gas Transmission and Transit	Y	2005-2007	Project was completed in March 2007.
Project for Increasing Energy Efficiency in Turkey	N	2005-2007	In the context of harmonization with Community acquis and EU experiences, the project aiming to implement the energy efficiency programs to improve energy efficiency performance of our country is wholly financed under the financial cooperation programs and the project is expected to finish in November 2007.
Development of Conditions for the Functioning of Cross-Border Electricity Trade of Turkey in line with the Best Practises in the EU	N	2006-2008	The twinning project, aiming to integrate the technical infrastructure of Turkish electricity system with the EU electricity system in order to enable the cross-border trading and to establish the relevant legal framework, is expected to be finished in 2008.
Safeguarding the security of electricity and natural gas supply	N	2007-2008	It became more important to set the due legal framework to safeguard and sustain the security of supply in energy markets in a deregulated environment. In this regard Electricity Market Law, Law No.4628, and Natural Gas Market Law, Law No.4646, will be strengthened in terms of ensuring supply security.
Institutional seperation of regulatory and supervisory functions in nuclear energy area	N	2007-2008	Regulatory and supervisory functions in nuclear energy will be undertaken by a new regulatory authority to be created by Nuclear Law. TAEK will retain the research, technology development and implementation roles.

[15]Although the law was put into force and Development Agencies commenced activities in two NUTS II Regions (TR31 (İzmir) and TR62 (Adana and Mersin)), works were suspended in line with the decision of the Council of State because the Law and some secondary legislation were taken to the Constitutional Court. Depending on the conclusion of the legal process by the decision of the Constitutional Court, it is expected that legislative and capacity building studies needed for the activation of the technically qualified regional development units will be continued.