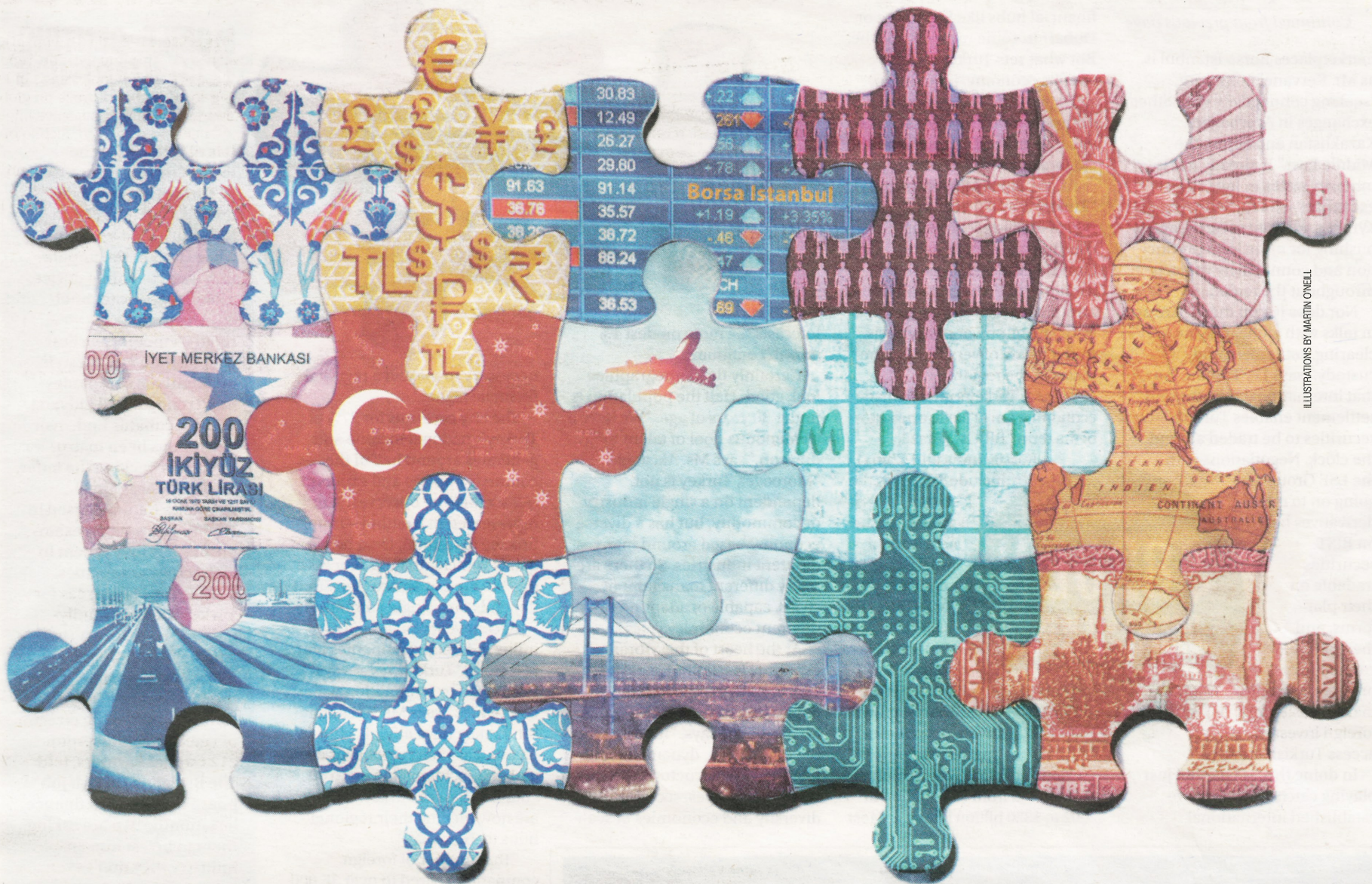


Special Advertising Section

FOCUS ON TURKEY



ILLUSTRATIONS BY MARTIN O'NEILL

ISTANBUL BIDS TO BECOME GLOBAL FINANCIAL CENTER

A FAST-GROWING ECONOMY COMBINED WITH SKILLED WORKERS PROPELS CAPITAL TO THE FORE

Where Europe meets Asia, work has begun on building a new financial powerhouse: the \$2.6 billion International Financial Center on Istanbul's Asian shore. At its core is Borsa Istanbul (BI), which now encompasses not only Turkey's stock exchange but also trading in fixed income, derivatives and precious metals, all on a single platform.

"Nasdaq-OMX is the technology provider and (since the exchange became a joint stock company in December 2012) now a shareholder," observes Mike Davey, the European Bank for Reconstruction and Development's director for Turkey. "Some banks are relocating there already."

At last month's groundbreaking ceremony for the Borsa

Istanbul Finance and Technology Campus, which will bring together the newly integrated financial exchange, the central registry agency and Takasbank under a single roof, BI's chairman and chief

"ALL SECTORS ARE REPRESENTED IN ISTANBUL... WE ARE NOT AN ECONOMY THAT DEPENDS ON A SINGLE COMMODITY."

executive officer Dr. Ibrahim M. Turhan declared, "We are working to make Borsa Istanbul a center of excellence." The aim is to create a financial hub that will serve not only Turkey's

fast-growing economy but also the entire region, from southeast Europe to the Middle East and Central Asia.

"There is a growing need in the region for a financial center as well as increasing project finance and investment for big-ticket infrastructure projects," says Hakan Binbasgil, CEO of Akbank, one of Turkey's largest and most profitable private-sector banks. And these are areas where he believes "Turkey prevails with its know-how and well-developed market economy."

Such ambitions only became possible after the enactment of the Capital Market Law, which gave both Borsa Istanbul and the new overarching regulatory body, the Capital Market Board, independence from government. The CML aligns Turkey's financial regulation and practices with those in the

European Union, although it has drawn on best practice elsewhere in the world, including the United States.

"There have been huge improvements recently to the institutional framework and to the regulatory and supervisory regime," says Selim Kervanci, HSBC's head of capital Middle East and North Africa and Turkey.

"New commercial codes, amendments to capital markets law and disclosure requirements, have all made it easier for providers of capital to operate."

"The bulk of the legislation and regulatory framework is

now in place," says Mr. Davey. But that is only the enabling mechanism. Turkey's bid to become the region's pre-eminent financial center—and in due course a global player—is backed up by its size, its skills and its geographic situation.

"Turkey enjoys a strategic position as a bridge between East and West, and trade has been passing through it since the days of the Silk Road," observes Serra

Akcaoglu, Citi's chief country officer in Turkey. It remains a vital transport corridor, for goods, people and ideas, as well as oil and natural gas. And in today's electronic

50%
THE PROPORTION OF
TURKEY'S POPULATION
BELOW THE AGE
OF 30

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marketplaces Borsa Istanbul is, as Mr. Kervanci points out, "seeking connectivity with other exchanges in Azerbaijan, Kazakhstan and across the Middle East." It already holds minority stakes in four stock exchanges—Baku, Sarajevo, Kyrgyz and Montenegro—and is pushing for more joint production and connectivity projects throughout the region.

Nor does it stop there. "We are in talks with global players in clearing, settlement and custody," says Dr. Turhan, "so that international clearing and settlement enables Turkish securities to be traded around the clock. Negotiations with the LSE Group are going on to make derivatives based on BIST securities tradable on their platforms, and there are connectivity projects that will make it easier for foreign investors to access Turkish markets."

In doing this, is Istanbul just playing catch-up with more established international

financial hubs like Singapore or Dubai? In some respects, maybe. But what sets Turkey apart is size. Its economy, population, skills pool and the volume of domestic financial transactions tower over those of financial centers based in city-states.

As Mr. Binbasgil points out, "Turkey is a G20 economy and one of the fastest growing countries in its region. It is currently the 16th largest economy in the world and would rank sixth in Europe on a purchasing-power parity basis. And it is one of very few democracies in the region."

Indeed, Turkey's growth made economist Jim O'Neill, originator of the term "BRICs" (Brazil,

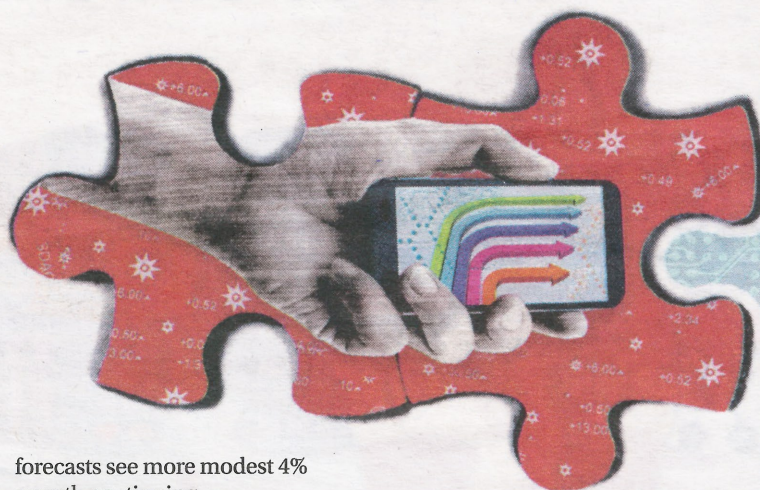
Russia, India and China), include Turkey as the

"T" in his acronym for the next wave of world-beaters, the MINTs (Mexico, Indonesia, Nigeria and Turkey.) With economic growth averaging 5% over the past decade, gross

domestic product has more than tripled from \$232 billion in 2002 to \$820 billion last year. Most

\$820BN

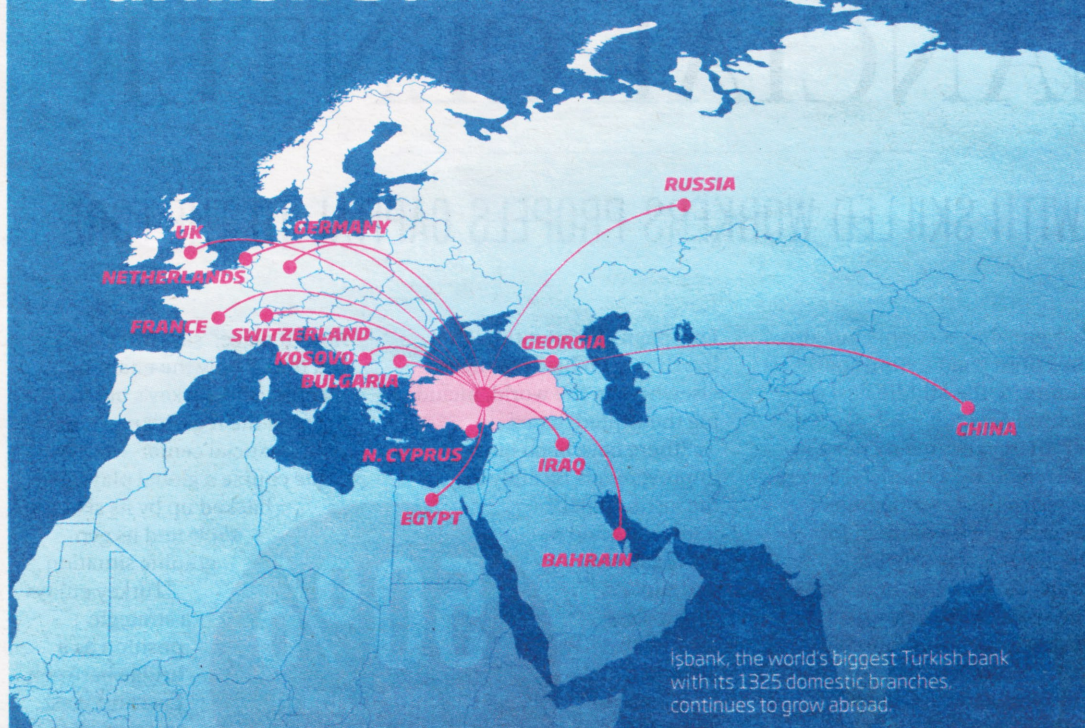
TURKEY'S GDP IN 2013,
WHICH HAS MORE THAN
TRIPLED FROM \$232BN
IN 2002

MOBILE-CENTRIC
TECH START-UPS
TAKE OFF

It is early days for the technology start-up market in Turkey, but these days the talk is of "Digital Bosphorus." In a country where 84% of the population owns a mobile device, mobile-centric technology—especially in retail—emerged earliest with fashion and lifestyle e-commerce companies like Trendyol and Lidyana. Local incubator Endeavor Turkey has been instrumental in backing the latter, while business angel Aslanoba Capital, based in Istanbul, has set an example of early investment in technology companies.

These are new areas for Turkey's largely family-based private investors, who have traditionally looked to real estate, gold or the stock market. As Ali Karabey, managing director of venture-capital group 212 Capital Partners, told The Bridge, a Turkish job board dedicated to finance, last month, "We are asking them to invest into an industry they don't even know exists." He hopes Aslanoba's example will draw in more players, "Success stories are the best way to intrigue people to go into the market."

—Jonathan Gregson

The world's biggest*
Turkish bank

İşbank, the world's biggest Turkish bank with its 1325 domestic branches, continues to grow abroad.

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2 Branches in Kosovo	Representative Office in Egypt	Representative Office in Shanghai, China	13 Branches in Russia**	13 Branches in Germany**
Branch in Amsterdam, Netherlands**	Branch in Paris, France**	Branch in Sofia, Bulgaria**	Branch in Zurich, Switzerland**	

*The Banker magazine's July 2014 ranking of the "Top 1000 World Banks."

**Branches at Russia, Germany, Netherlands, France, Bulgaria and Switzerland are the branches of İşbank's subsidiary banks.

İŞBANK

forecasts see more modest 4% growth continuing.

Certainly the demographics look good. Half the population is under 30 years of age. "We have a tremendous pool of talent to draw on," says Ms. Akcaoglu. "Moreover, Turkey is not dependent on a single industry or commodity, but has a diverse economy based around many different industries. So there are many different management styles, capable of adapting to different economic cycles."

At the heart of this vibrant economy is Istanbul, a city of 14.1 million people and the country's commercial capital. As Mr. Binbasgil says, "It possesses the population, dynamism and financial infrastructure, the human resources, sectoral diversity and economies of scale

necessary to make it a regional financial center."

The city accounts for 27% of Turkey's national income and generates around half of the country's imports and exports. "All sectors," he observes, "are represented in Istanbul—from finance to fashion, from heavy goods vehicles to food processing. We are not an economy that depends on a single commodity."

Recent years have seen an influx of foreign companies and investors. "Turkey has always been open to multinational companies," says Ms. Akcaoglu, "and many have already chosen Istanbul as their regional or even global hub, managing up to 80 countries out of Turkey. Others are now moving their regional hubs to Turkey."

"The number of foreign companies soared to over 36,000 last year, from 5,600 in 2002."

Given its still undeveloped capital markets, both domestic and international banks remain crucial to financing Turkish companies and consumers. The banking sector saw "strong but healthy growth in the last decade," says Mr. Binbasgil. Assets grew on average 21% per annum, loans and deposits 31% and 19% respectively, between 2002 and June 2014.

ROBUST BANKING SYSTEM

This growth in lending has been matched by a strengthening of the banks' capital bases and improved risk management. Ms. Akcaoglu notes that the average rate of non-performing loans is just 2.8%.

And there are strong prospects for the banks to grow further. Around 17 million Turks remain unbanked and average household debt at 22% of GDP is relatively low. Mortgages represent just 7% and pension funds a tiny 1.7% of national output. "The relatively low penetration of most banking products implies opportunities," says Mr. Binbasgil.

Among them is Islamic banking, which currently has a share of around 7% banking activity in Turkey and is expected to grow. "In terms of cash management and financing, Islamic banking is part of the solution," says Ms. Akcaoglu. Dr. Turhan highlights the state's "pioneering role in Islamic

finance by undertaking several Sukuk issuances—a critical step to secure Turkey's position as a regional financial center."

Turkey's bond market ranked third largest across all emerging markets last year with volumes of more than \$520 billion, and is rapidly broadening the range of instruments traded. "We believe we will see asset securitizations from Turkish banks soon," says Mr. Binbasgil. And while "the bond market was started by banks and financials, we believe now is the time for private companies. They will reach cheaper, longer term and more diversified funding through this channel."

New corporate debt issues jumped to \$29 billion last year from \$1.4 billion in 2010, while the combined market capitalization of Istanbul-listed companies has risen from \$34 billion in 2002 to more than \$295 billion. But Turkey's low savings ratio means that much of the demand comes from outside. "What is needed now," says Mr. Davey, "is a much deeper domestic institutional investor base, primarily pension funds and life insurance. Longer-term savings in Turkey are still at a relatively low level, but work is being done to change that."

| FOCUS ON TURKEY |

Pipelines Help Supply Southern Europe

TURKISH TERRITORY IS BECOMING A NEXUS FOR TRANSPORTING NATURAL GAS

The Trans-Anatolian Pipeline, or TANAP, will make Turkey a key part of the "Southern Corridor" bringing alternative supplies of natural gas from the Caspian Sea to Europe. Initial capacity will be 16 billion cubic meters, although as Stephen O'Rourke, gas analyst at Scottish energy and metals consultancy Wood Mackenzie, points out, "If they added five compressor stations fairly early that could be increased to 30 billion cubic meters."

Fed through Greece and Albania to the Trans-Adriatic Pipeline, or TAP, and on to Italy, this Southern Corridor will, he says, "be a significant new source of supply for Southern Europe."

As Turkey will retain 6 billion cubic meters to help meet domestic demand, only 10 billion cubic meters will reach

"TURKEY COULD BECOME A REAL ENERGY HUB—NOT JUST A TRANSIT CORRIDOR."

Europe. But as Ilya Zaslavskiy of London-based think tank Chatham House says, "that really matters at hours of peak consumption." He also notes that "Gazprom will no longer be the only supplier to Bulgaria."

Mr. O'Rourke points out that Turkey imports nearly half of its gas from Russia through Bulgaria or pipelines under the Black Sea, and a further 8 billion cubic meters from Iran. Given the sharp rise in domestic demand (every year distribution companies sign on another million customers) and a desire to reduce dependence on Russian gas, he sees Turkey looking to other sources such as northern Iraq, additional supply from the Azeri fields in the Caspian Sea and possibly more from Iran.

But will more pipelines by themselves make Turkey an energy hub? Aura Sabadus, Turkey energy market specialist at U.K.-based energy consultancy ICIS, says, "If what you mean by an energy hub is that a nexus of pipelines and transmission lines meet on Turkish territory, then that is likely to happen by the end of the decade. But if you mean a marketplace for a large number

of buyers and sellers, then for this to develop further changes must occur."

"Gas has to change hands many times for there to be a meaningful hub," says Mr. Zaslavskiy. "It will be a decade before a proper gas hub with a fully-functioning spot market emerges."

Ms. Sabadus contrasts progress made in opening electricity generation to the private sector, where new entrants such as German energy group RWE have helped more than double Turkey's generating capacity over 12 years to 69

gigawatts as state ownership declined from 74% in 2001 to around a third today, with the situation in natural gas—where state-owned gas giant BOTAS still controls about 75% of the market. Government subsidies to



gas consumers and cross-subsidization further deter private-sector entrants.

"Given its size, growing domestic demand and proximity to three-quarters of the world's conventional oil and gas reserves," she says, "Turkey could become a real energy hub—not just a transit corridor, but also a traded hub

that could establish itself as a counterweight to the energy hubs of northwestern Europe."

16BN
INITIAL CAPACITY IN CUBIC METERS OF NATURAL GAS VIA THE TRANS-ANATOLIAN PIPELINE

The text of this Special Advertising Section is written by Jonathan Gregson, a freelance financial journalist and author of three books on South Asia.

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