

TURKEY UPDATE

By Catherine Bolgar

Turkey rose to first place as the world's fastest-growing economy, with 11% year-on-year growth in the first quarter of this year.

"This was significantly more than we had projected," says Franziska Ohnsorge, senior economist with the Office of Chief Economist at the European Bank for Reconstruction and Development (EBRD) in London. The bank forecast 6% growth for this year but is likely to raise that, she says.

"You get the sense of a rapidly expanding economy in which some sectors are pushing against constraints," she says.

Keeping the boom going, though, requires huge amounts of investment in infrastructure. Turkey's newly re-elected government knows it can't do it alone. It's counting on help from the private sector.

Ongoing projects in sectors ranging from agriculture to energy, mining and transportation required a combined 273.4 billion lira (€113.4 billion) in 2010.

Subtracting 2009 cumulative expenditures of 118.4 billion lira and budgeted 2010 government spending of 27.8 billion lira, the projects show a financing shortfall of 127.2 billion lira, according to the State Planning Organization.

"The general policy of the government left most infrastructure investment in the private sector because of budget constraints and the philosophy of the government," says Gazi Ercel, principal of Ercel Global Advisory, a financial consultancy in Istanbul, and a former central bank governor.

Public-private partnerships

Turkey has long turned to public-private partnerships to fill in the gap, a policy that dovetails nicely with its privatization program. In fact, the Prime Ministry's Privatization Administration calls PPPs a way to privatize in advance. However, laws covering private-sector involvement are a patchwork of models, including build-operate-transfer, built-operate, long-term rent, transfer of operational rights, and build-rent-transfer. A draft of a comprehensive new PPP law has been debated since 2007.

"We're hoping for a new PPP law under the new government," says Michael Davey, Istanbul-based director for Turkey for the EBRD. "Following that, we would expect to see a lot of private-sector investment."

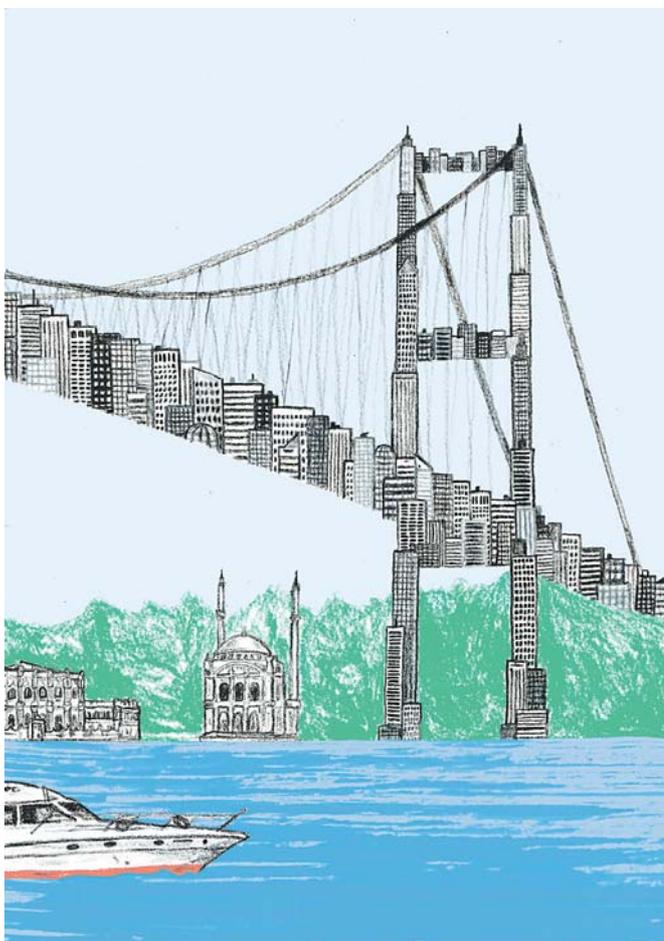
Infrastructure is important to improving Turkey's competitiveness and productivity. Turkey's average annual labor productivity growth topped 4.5% between 2002 and 2008, above the average for members of the Organization for Economic Cooperation and Development, says Rauf Gönenç, head of the Turkey desk in the OECD's economics department in Paris.

"As Turkey is not a low-labor-cost country anymore, and as the exchange rate remains exposed to long-term real appreciation pressures, improving productivity is the main avenue available for restoring Turkey's international competitiveness and external balances," Mr. Gönenç says.

Competitiveness also requires modernization and use of just-in-time processes, "but this requires a more effective logistics infrastructure," he adds.

The country has rapidly expanded its road network through the use of PPPs, with 2,000 kilometers of motorways and two Bosphorus bridges using the build-operate-transfer model. Contractors for a third Bosphorus bridge are expected to be

Country counts on the private sector to help improve its infrastructure



ALEX ROBBINS

announced by the end of this year; the \$6 billion (€4.23 billion) project includes a pathway, a car lane and a railway line on the 1.27-kilometer suspension bridge, which will link to a new motorway.

The biggest project is the Izmit Bay Crossing, which includes the world's second-longest suspension bridge, a viaduct and the Gebze-Izmir motorway. The \$9 billion build-operate-transfer project was awarded last year to a consortium of international and Turkish companies.

Roads account for 96% of passenger traffic and 92% of freight traffic, notes Mr. Gönenç of the OECD. "Although the road

infrastructure developed rapidly and road transportation companies are very competitive, congestion problems appear."

To ease congestion and address environmental concerns, the government has increased the emphasis on rail.

Most of Turkey's rail network was built in the late 19th century and is "not in very good condition," says Mr. Ercel of Ercel Global Advisory.

Turkey is working on high-speed lines: 533 kilometers between Ankara and Istanbul, 306 kilometers between Ankara and Konya, and the Marmara Project, which will connect Turkey to European high-speed

rail, with a tunnel under the Bosphorus and improvement of suburban lines.

Ports also are a constraint. Traffic in the south has increased because of trade with Iraq and Turkey needs new ports to accommodate demand, the EBRD's Mr. Davey says. Some existing ports have been privatized and "we see substantial greenfield ports planned or started."

Energy is Turkey's top priority, says Mr. Ercel. Oil imports account for 70% to 80% of the current-account deficit, one of Turkey's few economic weaknesses. At the same time, energy demand is rising quickly—6% to 7% a year, according to the Hydroelectric Plants Industry Businessmen's Association.

"Turkey needs not only energy supply, but also energy efficiency," he says.

Turkey has privatized all its electricity distribution companies, though some have come back on the table after winning bidders failed to arrange financing, says Mr. Davey of the EBRD. Small hydroelectric plants and large oil, gas and coal-fired plants also are being privatized.

At the same time, "a lot of investment is happening in renewables, medium-size hydroelectric plants and some greenfield generation plants in coal," he says. "The intention is to establish a fully liberalized market in energy."

Turkey's phone network has been completely privatized, with robust competition in mobile services. Broadband Internet access is spreading—Turkey's 2010 growth rate of 11% in broadband access was

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among the world's highest—but the country still lags OECD members in total penetration. It has 9.8 broadband subscriptions per 100 inhabitants, compared with the OECD average of 24.9.

"Broadband is a problem in the regions. The penetration of fiber optic cable networks is thin outside the large cities," says Heike Harmgart, principal economist at the EBRD's Office of Chief Economist in London.

Assorted improvements

Improving infrastructure extends even further, to health care, housing, urban transport and industrial zones.

"The authorities, generally refraining from trade protection or currency intervention, put emphasis on supply-side measures to foster productivity growth," says Mr. Gönenç of the OECD.

A full set of measures have been recently introduced to accelerate technology transfers, facilitate cooperation between research centers and enterprises, develop technological parks and clusters, and encourage research and development, including a comprehensive system of tax incentives for all innovative activities.

"Policymakers have privileged competition-neutral measures to date," Mr. Gönenç says. "It is very important to preserve this pro-competitive character of supply side policy, as opening up to competition remains the main engine of productivity growth in Turkey."

Special Advertising Section

TURKEY UPDATE

A fast-growing economy offers opportunities to foreign investors

By Helen Jones

Turkey, with a dynamic economy, a skilled and educated work force, a growing domestic market and a strategic location between East and West, is an attractive destination for foreign investors.

A United Nations Conference on Trade and Development report, published in July, says that Turkey attracted \$9.1 billion (€6.4 billion) in foreign direct investment last year and is the 27th most appealing country for investment in the world—up from 30th place in 2009. While the country has not yet returned to its performance before the global economic crisis struck—when FDI averaged \$20 billion a year—expectations for increasing levels of investment this year are high. FDI inflows more than doubled in the first five months of 2011 from the like period last year to \$5.6 billion, and Economy Minister Zafer Çağlayan recently announced that he is in discussions with two, so far undisclosed, foreign investors about \$8 billion of investment.

An open approach

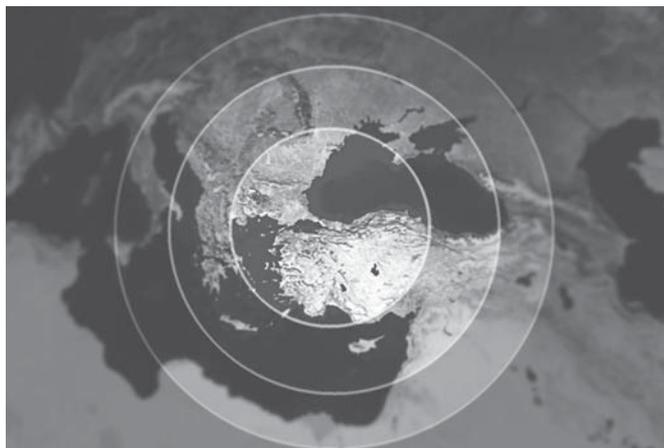
Ilker Ayci, president of the Investment Support and Promotion Agency of Turkey (ISPAT) says: “Since Turkey is interested in furthering its industries in almost all sectors, ample opportunities are available in areas such as automotive, information and communications technology, energy, renewable energy, pharmaceuticals, agro-food, petrochemicals and mining.” And, he adds: “Further privatization and developments in the energy sector will create quite lucrative opportunities for global investors. In addition, the Turkish economy is open to all avenues of investment. Global investors have the opportunity to start greenfield or brownfield ventures, as well as cooperating with the public sector through public/private partnership projects.”

Turkey’s biggest investors are from Spain, the U.S., France, Belgium and the Netherlands, and they are attracted by a number of factors. This year, Turkey became the world’s fastest-growing economy with 11% year-on-year growth in the first quarter. It also has a young, well-educated population and offers incentives such as total or partial exemption from corporate income tax in a number of industrial, technology and free zones around the country. And, in addition, its location provides easy access to some 1.5 billion customers in Europe, Eurasia, the Middle East and North Africa. As a result, a number of global companies have set up regional headquarters in Turkey. Coca Cola for example, manages 94 countries

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from Istanbul and Microsoft manages 80.

Among the companies to have a significant presence in Turkey is the food manufacturer Nestlé which has invested 85 million lira (€35 million) in a breakfast cereals production facility in Karacabey, in the west of the country. The facility, which will open later this year, will not only meet domestic demand but will export to North African and Middle Eastern countries. Hans-Ulrich Mayer, Nestlé managing director in Turkey, says that many countries competed to win the investment and adds: “This is in addition to the 325 million lira of investments we have made in Turkey in the last four years. There were other countries which vied for this investment, but Turkey surpassed all other candidates in the end. The fact that Nestlé has chosen Turkey is an indication of our belief in Turkey and the society and our long-term commitment



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in this country.”

Foreign investment in the automotive sector is also very active. U.S. engine manufacturer Cummins, which is headquartered in Columbus, Indiana, is investing \$70 million in a factory in the Aegean Free Trade Zone in Izmir—Turkey’s third largest city. It will become operational early next year and will employ over 800 people during the next five years. Ignacio Garcia, vice president and chief manufacturing officer, says that Turkey’s geographical and strategic position was a determining factor: “The expansion in Turkey allows Cummins to meet the product and service needs of the growing markets in Europe.” Cummins expects to export around 85% of what the plant produces.

In addition, the German materials and technology group ThyssenKrupp announced in December that it is investing €30 mil-

lion in a plant at Kocaeli near Istanbul that will produce chassis parts for the automotive industry. Says ISPAT’s Mr. Ayci: “Our priority is to attract investments that create high-technology and added-value. In this respect, ThyssenKrupp’s investment is of great significance as it brings chassis production—a vital technology for the automotive industry—to our country.”

R&D centers

Turkey is also attracting major international companies to set up research and development centers, including Bosch, Intel, Microsoft, Mercedes-Benz and Pfizer, which currently has over 30 international R&D projects based in the country. As Mr. Ayci explains: “Our labor force has the skills and qualifications for R&D, and Turkey offers an incentive package exclusively for R&D and innovation activities.”

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TURKEY UPDATE

Culture and history complement the sun and the sea

By Helen Jones

Turkey has long been a destination for tourists looking for sun, sea, sand and an affordable holiday, but in recent years the Ministry of Culture and Tourism has focused on the country's cultural heritage; historic sites; its ancient monuments, domes and minarets; and its natural landscapes to attract a wider range of visitors.

Tolga Tuyluoğlu, director of the Turkish Culture and Tourism Office in London, says: "Obviously, Turkey does have this appeal to the mass market, but some recent research commissioned by the Turkish Ministry of Culture and Tourism found that 71% of people who had visited Turkey had been to a historic site or museum during their stay. In all our promotional campaigns we do stress Turkey's rich and diverse history and I really think that the message is getting through."

Turkey is home to nine Unesco World Heritage sites spread across the country. These include the archaeological sites of the siege of Troy; the Göreme Valley in Cappadocia, where the wind and weather have sculpted pinnacles and peaks now known as fairy chimneys; as well as cave

"Sporting tourism is increasingly important, whether it be attending specific events, or participating in sports, such as golf."

dwellings from the fourth century, troglodyte villages and underground towns; and Safranbolu, a town on the north-west Black Sea coast, which is renowned for its charmingly well-preserved Ottoman houses, ramshackle wooden shops and 17th century baths.

Mr. Tuyluoğlu says that there is growing interest in Turkish history and culture. In 2002, there were 7.4 million visitors to the country's museums and historic sites. By 2010 this number had increased to 25.8 million. Overall tourist numbers are also up with 28.6 million visitors from abroad in 2010, compared with 13.2 million in 2002.

"Turkey has benefited from the fact that the lira offers good value for money. But at the same time, one of Turkey's great strengths is the diversity of her tourism product. Turkey is able to compete well in all of these markets—beach holidays and cultural and historic and luxury tourism—and still has huge potential for further development," he says.

Istanbul, at the crossroads of East and West, with its exotic



Turkey has nine Unesco World Heritage sites, such as the Göreme Valley in Cappadocia.

Grand Bazaar, palaces, castles, mosques, churches—and the former capital of three great empires Eastern Roman, Byzantine and

Ottoman—has always attracted visitors interested in history. But its role as a cultural destination was cemented when it became

European Capital of Culture in 2010.

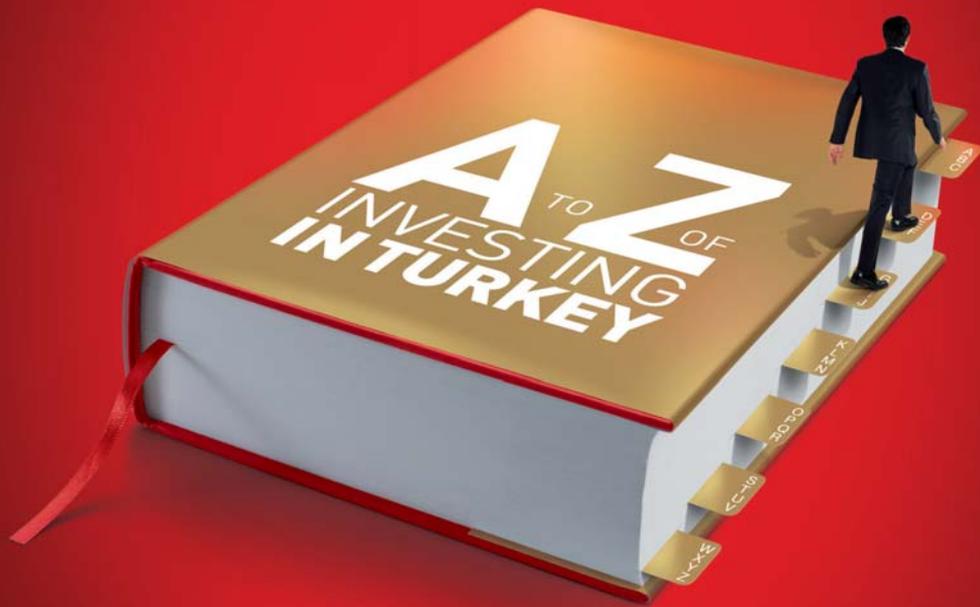
This year-long festival of events, exhibitions and performances by Turkish and international artists drew visitors from around the world. Sekip Avdagiç head of the Istanbul 2010 European Capital of Culture Agency said in a statement: "This was a long-term investment to make the beauties of the city known to everyone."

And Mr. Tuyluoğlu adds: "I think that its position as a European Capital of Culture in 2010 was significant, as it drew the world's attention to Istanbul's cultural attractions. On a practical level it also provided a focus for many new projects such as the new

Islands' Museum, which celebrates the history and culture of the Princes' Islands which are just off the coast of Istanbul in the Sea of Marmara."

The spotlight will once again turn on Turkey as Istanbul hosts the WTA Women's Tennis Championships in October and will be the European Capital of Sport in 2012. As Mr. Tuyluoğlu explains: "Sporting tourism is increasingly important, whether it be attending specific events, or participating in sports, such as golf. I hope that Istanbul's status will highlight the role which sport plays in Turkey and provide a focus for developing and promoting our world-class facilities."

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