

Turkey 2005: “Crossing the Bosphorus”

By Paul Wouters

Introduction

Turkey is the geographical and economic bridge between Europe and Asia. Taking into account the formal start of the accession talks between Turkey and the EU (3rd October 2005) and the rich history of the Ottoman Empire (giving direct access from the Middle East to Central Europe and Asia), it is clear that Turkey is destined to play a more important role on all fronts. This became clear at the Turkish–Arab Economic Forum (Istanbul, 5th–6th May 2005) and the successful 8th International Islamic Finance Forum (IIFF) (Istanbul, 26th–29th September 2005).

The sector

Although the Turkish Islamic finance market has rather modest dimensions (3% overall market share – expected to grow to 10% overall in 7–10 years), 2006 will prove to be of great importance.

Deposits end 2005 (US\$ billion)

Bank Asya	1.591
Anadolu Finans (Türkiye Finans)	2.020
Family Finans (Türkiye Finans)	
Albaraka Türk	1.296
Kuveyt Türk	1.558

Source: estimates

Recently Turkey has been gearing up to comply with international accounting and corporate governance standards. A special Basel II implementation program (Road Map for Basel II) has been activated for some time now by the Banking Regulation and Supervision Agency (BDDK).

The new Banking Law No 5411 (published on the 1st November 2005) fully takes the “participation banks” under the umbrella of the BDDK, thus denominating the so-called “special finance houses” and officially conferring bank status.

The pre-existing “Warranty Fund” (Güvence Fonu) has been absorbed by the Savings Deposit Insurance Fund (TMSF), thereby awarding participation banking the same status, supervision and insurance as conventional banking.

It is worth noting that the funds contributed by the participation banks to the TMSF will be kept separate from the contributions of conventional banks and will be directed to the funding of the interest-free sector (both domestic and abroad).

The Turkish Government is said to be currently studying the possibility of issuing a sovereign Ijarah Sukuk, provided its contents and name can be made compliant with the secular principles of the state.

Turkish Banking Sector – Deposits (1,000 YTL)			
Year	Deposit Banks	Participation Banks	Market Share %
1995	2,664,936	64,334	2.36
2000	68,442,406	1,863,000	2.65
2001	147,520,532	1,917,000	1.28
2002	142,387,988	3,206,000	2.20
2003	147,350,714	4,004,306	2.65
2004	190,996,041	5,992,159	3.04
2005/6	213,835,000	6,834,431	3.09

Source: TKBB – annual report 2005
(YTL = Yeni Türk Lirası – New Turkish Lira)
(1 YTL = approx. €1.60 or US\$1.33 – 20th Jan 2006)

Turkish Banking Sector – Credits (1,000 YTL)			
Year	Deposit Banks	Participation Banks	Market Share %
1995	1,743,685	62,560	3.46
2000	34,213,480	1,726,000	4.80
2001	57,341,438	1,072,000	1.84
2002	56,370,271	2,101,000	3.59
2003	48,018,584	3,001,313	5.88
2004	89,900,000	4,894,665	5.16
2005/6	117,131,000	5,262,006	4.29

Source: TKBB – annual report 2005
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Continued...

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At the IIFF 2004 Islamic Finance Conference in Istanbul, the Dow Jones Islamic Market Turkey Index was launched. This index includes all stocks in the Dow Jones Emerging Europe Index that are traded on the Istanbul Stock Exchange (ISE) and fulfil the requirements of the Dow Jones Islamic Market Indexes. It is reviewed quarterly in March, June, September and December.

The interest-free participation banks

The Turkish Participation Banks Union (TKBB) groups together the participation banks.

After the setback of the 2001 crisis that hit the Turkish financial industry (but which interestingly was absorbed by the participation banks without insolvencies), the sector has grown by approximately 50% over the last three years.

In December 2005, the voluntary merger of Family Finans Kurumu and Anadolu Finans Kurumu into the Türkiye Finans Katılım Bankası was announced, thereby creating the largest participation bank in Turkey. Consequently, the number of local market players was reduced to four:

- Turkish origin: Türkiye Finans Katılım Bankası and Asya Katılım Bankası (also Bank Asya – formerly Asya Finans Kurumu); and
- Foreign origin: Albaraka Türk Katılım Bankası (formerly Albaraka Türk Finans Kurumu – controlled by the Gulf-based Albaraka Banking Group) and Kuveyt Türk Katılım Bankası (formerly Kuveyt Türk Evkaf Finans Kurumu – controlled by the Gulf-based Kuwait Finance House).

Türkiye Finans

The friendly merger (probably unique in its kind in Turkey) announced on the 28th December 2005 between Anadolu Finans Kurumu (Boydak family) and Family Finans Kurumu (Ülker Family) into Türkiye Finans Katılım Bankası (Türkiye Finans Participation Bank) created the single largest participation bank in the country.

In order to create synergy, to prepare for Basel II implementation and to consolidate strategic positions, this move appeared to be prudent to the shareholders of both banks and will probably lead the way in the industry.

The first half of 2006 will be dedicated to fully absorbing this merger, although substantial plans are already developing. Branch offices total 108 (as at the end of 2005 – 42 of which are in Istanbul) and will be expanded to approximately 120 branches by the end of this year. Deposits are at the level of US\$2 billion and predicted to reach US\$3 billion in a year's time. Assets are at US\$2.02 billion and credits at US\$2.367 billion.

The Dow Jones Islamic Market Turkey Index was licensed at the end of 2005 to Bizim Menkul Değerler (part of the Ülker group).

Bank Asya

Founded in 1996, Asya Katılım Bankası (Asya Participation Bank) builds on a broad but committed shareholdership (approx 265 shareholders). An Initial Public Offering (IPO) is projected for spring 2006.

Compared to 2004, total assets grew in 2005 by 41% (up to US\$1.94 billion), total deposits by 33% (to US\$1.591 billion), and total loans grew to US\$1.568 billion. The number of branches increased from 62 (as at the end of 2004) to 70 (as at the end of 2005) and 25 new branches are planned to be opened by the end of 2006 (dispersed throughout both urban and rural areas).

Bringing in highly qualified financial experts who were made redundant by the insolvency of conventional deposit banks during the 2001 crisis and using proven traditional products, Bank Asya is a flexible niche player that strives to anticipate and quickly adapt to changing market conditions (mortgage and housing projects, privatizations, etc).

Having increased its market share more than any other participation bank and many conventional banks during 2004 and 2005, Bank Asya aims to regain leadership in the sector (presently with the Boydak Family) and to be one of the top 10 banks in the local Turkish banking market at the end of 2006.

Albaraka Türk

Founded in 1984 (with Albaraka Banking Group as its main shareholder), Albaraka Türk Katılım Bankası (Albaraka Türk Participation Bank) is the longest standing interest-free Turkish participation bank.

Deposits stand at US\$1.3 billion and net assets at US\$1.467 billion. The bank has 43 branch offices. Besides opening new branches, the main target is to raise profitability and deposits per existing branch.

Aimed at retail and corporate lending, Albaraka Banking Group wants to be a major regional player and Albaraka Türk Katılım Bankası forms a valuable part of that strategy.

The launch of a business card (corporate "compliant" credit card) is envisaged in 2006.

Kuveyt Türk

With Kuwait Finance House as its main shareholder and established in 1989, Kuveyt Türk's main focus is on wholesale banking/corporate finance. Kuveyt Türk Katılım Bankası (Kuveyt Türk Participation Bank) entered the retail business in 2000 and intends to conduct investment banking activities in 2006.

From 37 branches in 2003 it has grown to 70 branches in 2005 (of which 30 are in Istanbul); and for 2006 there are 15 new branches planned (centered in the big cities and in central Turkey).

Deposits at the end of 2005 exceeded US\$1.5 billion and assets were in excess of US\$1.75 billion.

The bank has applied to open a branch office in Dubai and also has a German representative office (in Munich – May 2004).

Continued...

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Fitch Ratings

Bank Asya	B	17/06/2995	long-term foreign
Anadolu Finans	-	-	-
Family Finans	-	-	-
Albaraka Turk	B	30/08/2005	long-term foreign
Kuveyt Türk	BB-	08/12/2005	long-term foreign

Shariah compliant activities, other market players

After the US\$60 million Murabahah that was arranged by HSBC for TAV in March 2003 (to support the expansion of Atatürk Airport terminal buildings and facilities) and the US\$100 million Murabahah arranged by the IDB and HSBC for Turkcell (Turkish mobile phone operator) in January 2004, on the financing side compliant activity was noticed at the Industrial Development Bank of Turkey (TSKB – conventional banking sector).

TSKB Bahrain Branch (launched in February 2005) signed a Syndicated Revolving Commodity Murabahah Facility worth US\$50 million in October 2005 (Maturity date – 364 days from the date of the first advance; Repayment – Bullet; Margin – LIBOR plus 45 basis points).

The Bahrain branch is the first overseas branch of TSKB. It will offer products and services to its clientele in Bahrain and across the Gulf. TSKB is reported to be eager to learn from Bahrain’s leading position in the Islamic banking sector.

In 2005 both the Dubai Islamic Bank (DIB), based in the UAE, and ABC International Bank, based in Bahrain, opened an official “representative office” in Istanbul. The acquisition by DIB of MNG Bank (at present a conventional deposit bank) is close to being finalized.

Several other conventional banks (both foreign and Turkish) are said to be considering starting interest-free banking in the near future, which would enhance visibility and credibility of the sector as a whole.

Already Turkish corporations and entities have access to Islamic finance via international syndications arranged by HSBC, Citibank and WestLB.

Fortis Bank (formerly Dişbank) has plans to offer Islamic finance products in 2006. Some domestic Turkish banks may also be willing to move forward in this area. For instance the Turkish Economy Bank (partially owned by BNP Paris Bas Bank) is believed to be interested in Shariah compliant activities.

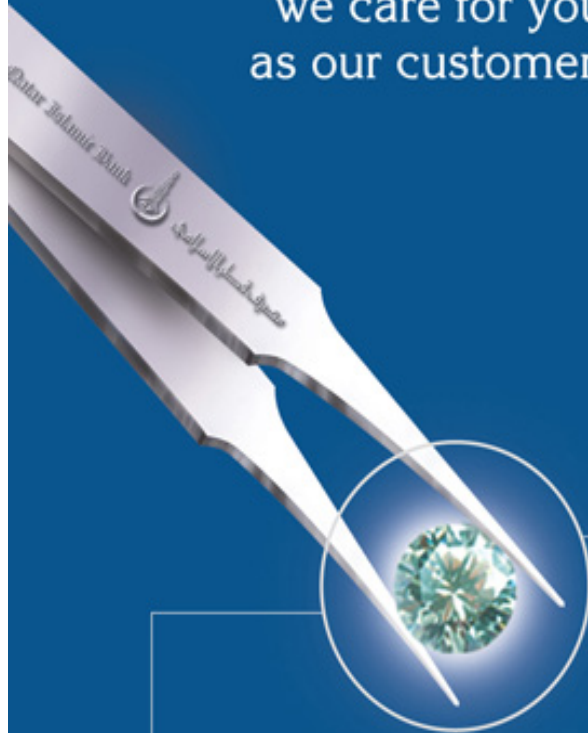
If even a small part of these plans and rumours are realized in 2006 (or other developments occur), the impact will be profound.

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