

## **The Turkish Banking Sector:**

### **The Periods of 2002-2007, 2007-2011, and After 2011**

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**Abstract:** Financial structure of the banking sector in Turkey has maintained its importance due to the high share in the financial sector for many years. The potential of banking sector that can have a huge a positive or negative impact on the economy makes it one of the most element of stability and growth of an economy. This study briefly compares the periods prior to 2002 and different periods after 2002. It is seen that banking sectors showed improvements during 2002 and 2007 due to the political stability, right financial policies, and right banking regulations. Since these positive effects on economy continued on the next period till 2011, banking sector could achieve targets. The effects of global financial crisis that started in 2008 were limited in Turkey and financial sector played an important role to overcome the negative effects of global financial crisis. However the banking sector could not outperform in terms of US dollar after 2011.

**Keywords:** Turkish Banking Sector, Turkish Economy

#### **1. A Brief Overview of Turkey's Economy Before 2002**

A closer look to the history and the industry of Turkey is important to discuss how to analyze the overall situation of the Turkish banking sector prior to 2002. Financial policies created by controlling interest rates and exchange rates began to wane during 1970s. These developments in the country started the financial liberalization policies implemented after 1980. Prior to 1980 the financial markets and regulatory control of the state was still active and that was mainly governed by repressive policies as a market emerges (Kilic, 2012, p. 109).

In 24 January 1980 government described the stability program, known as the January 24, 1980 decision which was intended transition to a free market economy. However, existence of high and volatile inflation formed the inadequacy of high public deficits and the bank control mechanisms were revealed facts of this period (Binay & Kunter, 1998). The decision of opening the competition in the banking sector was again taken in July 1980. The impact of the deepening liberalization of the financial system was also observed. These developments in the market economy in the 1980s have led to the development and growth of the banking sector. However, 1990 has taken place in our history as tough times for the economy in terms of banking. Turkey Banks Union -according to the data in the period between 2001 and 1990- declared that the average consumer price increased by 80%. Again, the average growth rate

during the same period stood at 3.2%. However, again with the same period the growth rate was followed by a broadband between  $\pm 9\%$ .

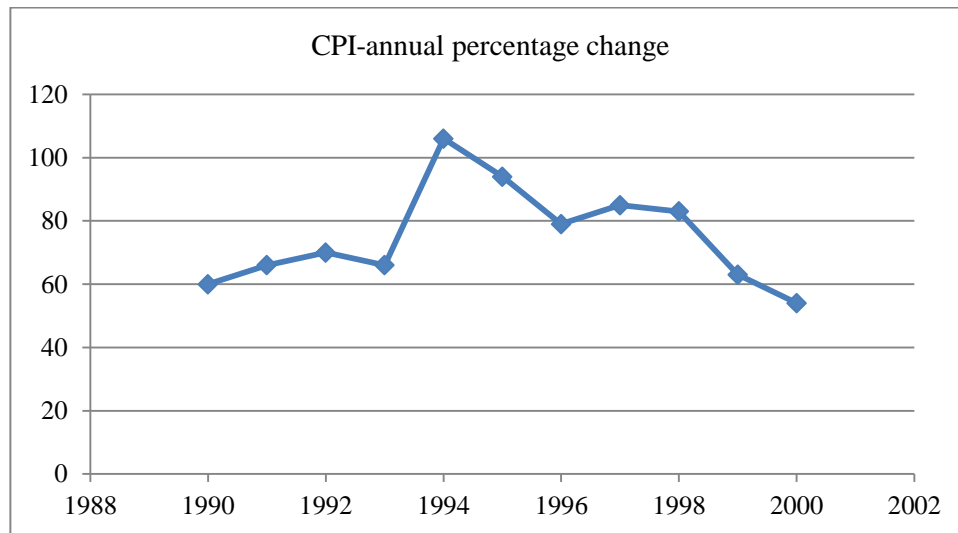


Figure 1: CPI between 1990 and 2001 (based on the 1987 prices)  
Source: Turkish Statistical Institute

Continuous and increasingly deficit balance of the savings of the public sector emerges as another important economic issue of this period. During this period, the public sector and the private sector had difficulties in meeting this deficit and has had to use outsourcing the entire period except 1994 (Banks Association of Turkey, 2008). Extra loads imposed on brokerage application still stands out as contributing to the distortion of competition during this period. In the 1990s, that policy-makers were determined in part by legislation, implementation and control approach led to administrative problems. In short, high inflation, low savings and outsourcing needs, unstable growth factors distorting competition in banking and management problems led to the banking sector experienced a difficult period which were the main negative aspects of this period.

Economic crises prior to 2002 are important events to understand the banking needs in Turkey. The first economic crisis of the 1990s took place in 1994. These are two most important causes of the crisis. The first one was in 1989 in the Treasury with the foreign banks with the liberalization of resources on capital movements funding (Binay & Kunter, 1998). After this crisis, also known as policy makers, new regulations were enacted April 5th Decisions. The most notable of these decisions is brought assurance to all saving deposits in banks. Although this decision has given positive results in the short term as one of the causes of the crisis in 2000 and 2001 took place in the pages of history. The other crisis revealed due to the high inflation, unstable growth, unsustainable debt and the uncertainty in the political environment (BRSA / Strategy Development Department, 2009).

## 2. Banking Sector 2000-2002

Total deposits during the period June 2001-December 2000 period was 58.9 quadrillion and 87.6 quadrillion respectively. The total amount of TL in the same period was 52.4% and 43.8%.

Table 1: Turkish lira Deposits and Foreign Currency Composition

|                  | December 2000 | June 2001 |
|------------------|---------------|-----------|
|                  | Shares%       | Shares%   |
| Turkish Lira     | 52.4%         | 43.8%     |
| Foreign currency | 47.6%         | 56.2%     |

Source: BRSA

When banking groups are examined the weight of the public sector banks can be seen easily. In fact, this phenomena was not only seen in this period, it was like this before this period as well.

Table 2: Public Capital and Development of Other Bank Deposits

By the end of 2000

|               | Total (Billion) | Percent |
|---------------|-----------------|---------|
| Public Banks  | 23,483          | 39.9%   |
| Private Banks | 27,030          | 45.9%   |
| SDIF Banks    | 7,896           | 13.4%   |
| Foreign Banks | 490             | 0.8%    |

Source: BRSA (Banking Regulation and Supervision Agency)

The non-performing loans (NPL) in total credit reached 4 quadrillion in mid-2000, and the end of the year 2001 the upward trend in non-performing loans was recorded during these periods. NPL ratio of loans in banks that was controlled by SDIF administration were 65.5 percent, 41.8 percent and 61.3 percent during these periods. Time periods where high percentages of NPL were same as time of the increase of the banks participating in the SDIF. The highest rates were followed by state-owned banks.

The number of banks operating in the Turkish banking sector, the banks of the number of branches and employed staff numbers in the mid-2001 and a previous period of mid-2000 showed the impact on the banking sector crisis of 2001. The number of banks operating fell from 79 to 72 during this period. When we look at the total number of branches in the same period it is seen that it decreased 3.94 percent and the total number of staff employed by the banks declined by 9.57%.

Table 3: Number of Banks, Branches, and Employee

|         | No.of Banks                  |                      | No.of Branches   |              | No.of Employee |        |
|---------|------------------------------|----------------------|------------------|--------------|----------------|--------|
|         | 2000<br>December<br>December | 2001<br>June<br>June | 2000<br>December | 2001<br>June | 2000           | 2001   |
| State   | 4                            | 4                    | 2.833            | 2.734        | 70.329         | 60.265 |
| Private | 29                           | 29                   | 3.777            | 3.832        | 71.155         | 70.391 |
| SDIF    | 11                           | 5                    | 1.076            | 877          | 20.044         | 16.439 |

Source: BRSA

February 2001 was the date where had been massively negative impact on the real sector in Turkey as well as on financial sector. During this period, particularly due to the management problems and weaknesses in the financial structure of state banks job losses and serious capital deficit were witnessed. In the same year in May, "Transition to Strong Economy Program" was introduced. The fight against inflation, the macro fundamental way on many factors such as the economy, public finance balance and transparency map had been identified. This challenge forced BRSA (Banking Regulation and Supervision Agency) to put into "Banking Sector Restructuring Program" in the same year.

The program had four main headings: (i) restructuring of state-owned banks (ii) the resolution of the SDIF banks, (iii) establishing a more healthy structure of the private banking system, and (iv) strengthening the supervisory and regulatory framework and efficiency in sector (BRSA, 2003). The main objective of this regulation was to avoid the effects of the crisis, though also aimed at harmonization with EU standards (Erdönmez, 2003, p. 38). Between 2001 and 2002, nine banks were taken over by the SDIF, 12 banks merged and a total of 5 banks were sold in this process. The resolution by the SDIF banks' deteriorating financial structure has been one of the important topics during this period.

Turkish banking sector increased by 1 percent in terms Turkish Lira as total assets compared to the previous six-month period in the middle of 2001 and it increased to 151.9 quadrillion while in terms of US dollar it declined on the basis of 18.5%, shrinking by 121.3 billion dollars. When the basis is the previous six-month period of 2001, according to the real assets of foreign banks, public banks decreased by 22.7 percent to 21.7 percent. The real assets of private banks increased by 4.3 percent compared to the same period in the previous six-month period (BRSA, 2001).

### 3. The Period of 2002-2007

This period is referred as the Turkish banking and financial sector restructuring (the Banks Association of Turkey, 2008). However, when we look at the developments in this period in industry, this process could be described as "Fight against Inflation" in 1999 and as "Transition to Strong Economy Program" in May 2001. Auditing of banks was shared between Treasury and Central Bank which was causing

conflicts. This task transferred to BRSA to avoid conflicts and eliminate disruptions before 1999. In the same year, establishments of banks and liquidation of banks were given to BRSA so that it could achieve its autonomous structure and in August 31, 2000 it began functioning (BRSA / Strategy Development Department, 2002). Historical statistics of BRSA shows that SDIF and the process called as restructuring were shaped not in this period but prior to this period. During April 2000 and March 2001 there were 45 sessions and 80 decisions. Again in this period SDIF performed 104 sessions and took 201 decisions. The process of resolution of banks taken over by the SDIF has been started prior to this period and settled largely in the same period.

1990s were a period in which Turkish economy was considered as unstable and low growth indicators could be seen. However, when 1990s were compared with 2002 and 2007, we see that the process of positive developments took place in the economy with less inflation. It was the period which produced an average rate of 7.2% a stable growth. The restructuring process of the improvement experienced in the financial sector in the economy and the banking system have begun to positively affect the recovering process that is creating opportunities for banks to strengthen their balance sheet structure and equity. The ratio of equity to total assets of the sector was 13.4% in this period. Again, control and surveillance with the arrangements provided the factors to contribute to financial stability.

The total deposits of the banking sector in 2007 reached 307 billion dollars. The GNP ratio showed a limited increase in deposits in 2007, a 2 percent rate when it is compared with 2002. In contrast, there was an increase of 18 percent over the same period considering the ratio of loans to GDP. Turkish lira loans increased by 21 percent of GDP that was recorded a decline of loans by 3 percent.

Conversion ratio of deposits to loans in parallel with the growth and diversification in loan growth has been recorded in this period. GNP ratio of deposits and loans increased again in the period 2002-2007. One of the important indicators related to the functioning of the banking sector as a data that reflects the positive developments experienced in this period was the conversion of deposits to loans. By the end of 2001 the ratio of deposits to loans conversion was 35 percent; however an increase of 40 percent was seen then it reached to 85 percent level in 2007.

The ratio of loans to total assets has increased steadily between 2002 and 2007. Considering the percentage share of loans for the same period there has been significant differentiation. The ratio of corporate loans to consumer loans was six in 2002 however this ratio became two as we came to 2007. However, SMEs were received 29 percent of corporate loans in 2007. When 2007 is compared to 2002 in terms of individual credits, it is seen that there is an increase in mortgage, car credits and the number of credit cards by 17 percent, 10 percent, and 1 percent respectively.

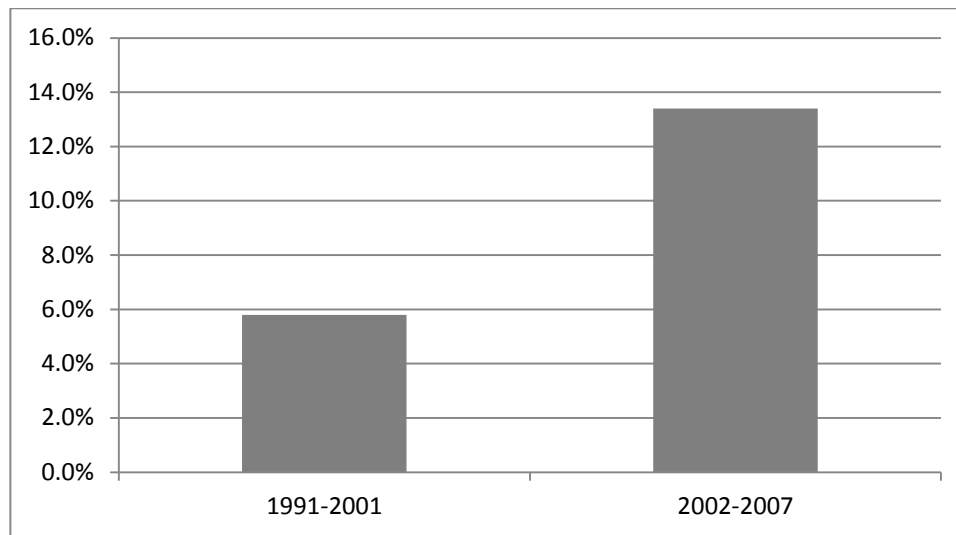


Figure 2: Equity/Total Assets (average)  
Source: BRSA

The positive developments seen in the sector in terms of deposits and loans were seen in equity too. Equity between 2002 and 2007 reached the level of 73 billion TL from 26 billion TL, an increase of nearly three times. Moreover, the average capital adequacy ratio of the sector has reached 19.1 percent in 2007. The ratio of non-performing loans and these loans have shown a steady decline between 2002 and 2007 as it was 1,695 million in 2002 and in 1,365 million TL in 2007. The ratio of non-performing loans in total loans was 3.3 percent in 2002 and this ratio became 0.5 percent level in 2007 (TBA, 2008). When the net profit in 2002 was 1.4 percent in total assets, this ratio reached 2.6 percent when it is compared to 2007. In the same period, net profit / equity reached the level of 19.5 percent from 11.2 percent. Nevertheless, net interest income / total assets ratio declined to 4.6 percent from 6 percent in 2002 when we come to 2007.

When the period between 2002 and 2007 is compared in terms of number of banks, it is seen that there is a decline. Although the total number of banks decreased from 54 to 46, there was an increase in terms of number of branches and personnel. During this period, TL gained value, interest rates have fallen, and inflation targets were met. During this period, financing has not suffered problems and showed an increase in Central Bank reserves more than estimated value. This growth has been an important source of finance and the money that its source is known developments in financial targets (the Banks Association of Turkey, Banking and Research Group, 2003). These improvements accompanying with increased demand for financial services have contributed positively on the financial structure.

#### 4. The Period of 2007-2011

Turkish financial sector with the contribution of the policy and political stability has continued to evolve during 2007-2011 like with the positive developments in 2002-2007. Banking sector's total assets reached 947.8 billion TL at the end of 2008 that means an increase of 23.1 percent based on the previous year. At the end of 2011 this value became 1.2 trillion TL. As in earlier periods of the financial sector, banking sector had the largest to share in the financial sector in this period. Assets of the banking sector

reached 1.2 trillion TL and total share in financial sector was 86 percent in the sector at the end of the period of 2007-2011.

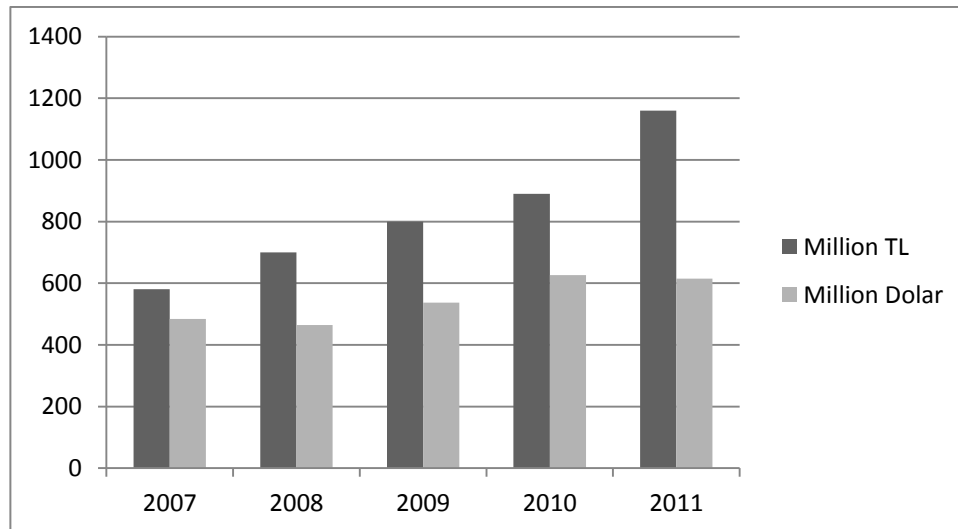


Figure 3: Total Assets in Banking Sector  
Source: BRSA

As it is seen from figure 3, the total assets of banking sector in terms of US dollar was 484 billion dollar at the end of year 2007. It became 626 billion dollar and 615 billion dollar at the end of years 2010 and 2011 respectively. There was a decline in interest income of banks each year in this period. In the same period interest expenses of banks declined like interest expenses except in year 2011. When we look at net profit and there is a slight decline in 2008, next year a recovery is observed, and it is seen that there is a similar data recorded the last two years. It began in the US mortgage market in 2006 and later became financial crisis deepened starting at the end of 2007 then the impact of the economic crisis that has become global in 2008 was seen limited in Turkey. Although crisis in 2000 and 2001 affected the Turkish banking sector very seriously, the Turkish banking sector was not been affected from the global financial crisis as it can be seen from some research results (Afsar, 2011, p. 169).

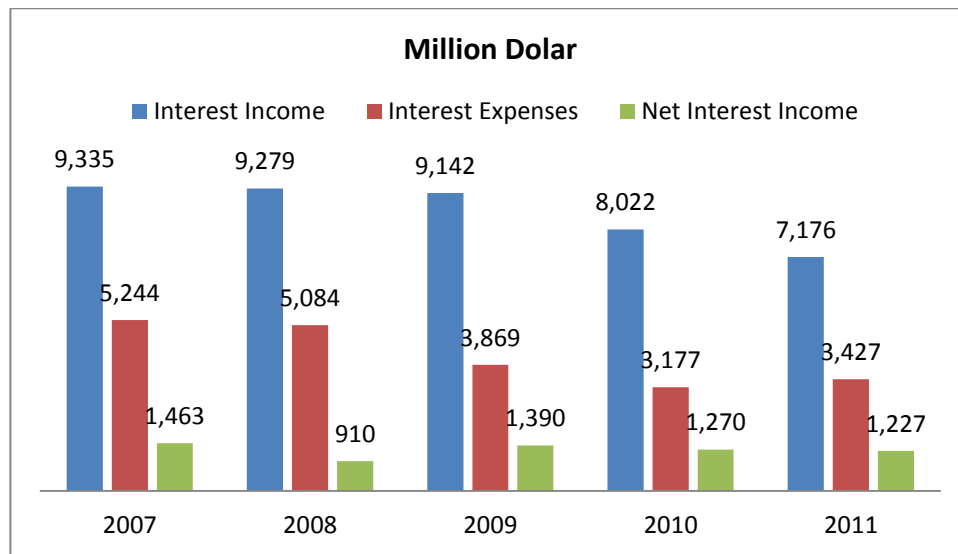


Figure 4: Interest Income, Interest Expenses, and Net Interest Income  
 Source: BRSA

In parallel with the growth in the national economy during this period credit demand continued to increase. Falling interest rates and inflation has led banks to make more loans.

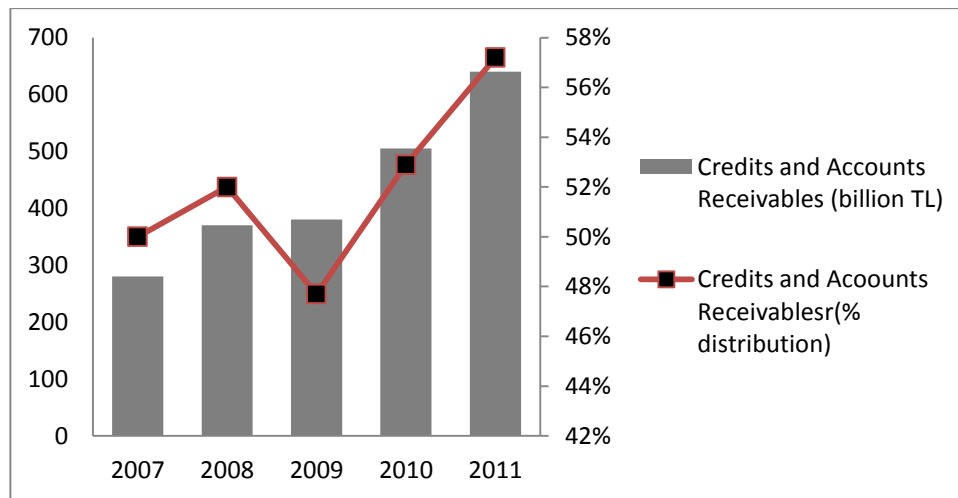


Figure 5: Credits, Accounts Receivables (billion TL), and the Balance Sheet Distribution (%)  
 Source: BRSA

Credits and account in the balance were 50 percent in 2007, they fell to 48 percent in 2009 and then reached to about 58 percent in 2011 as it can be seen from the distribution of the balance sheet by years. These data indicate that there is a growth in total assets of the bank due to the increase of credits in that period.



During this period the number of active customers using internet and mobile banking services has increased by 235%. At the end of 2007 the number of active customers reached almost 4.5 million and it became around 14.5 million at the end of 2011. These developments brought about a decline in the number of employees per branch in 2011 as 18 in 2011 and it was 21 in 2007.

This period, shareholders' equity has reached 138 billion TL from 73 billion TL. However, total assets of the bank stood at 1.2 trillion TL level in 2011 compared to 2007, an increase of \$ 600 billion. The share of loans in total assets rose to 57 percent from 50 percent in the four-year period level and has maintained its high share in total assets. It observed an increase in banks' branches and each year the number of staff and especially the internet and mobile banking has experienced significant developments in the industry. The non-performing loans in the year 2011, -1.1 billion TL in 2007- reached the 234 billion TL by an increase of 3.5%. When viewed proportionally as the ratio of non-performing loans in total loans and receivables 0.43 percent in 2007, while it is observed that this ratio increased to 0.53 percent in 2011.

### **5. The Period after 2011**

The deposits collected by banks, non-deposit sources, and shareholders' equity were 700 billion TL, 252 billion TL, and around 138 billion TL respectively. Thus, the deposit has continued to be the most important source of funding in liability and it has maintained a steady share in this period. Total assets were declared as TL 1.2 trillion levels by banks. Banks, as in previous years, the increase in assets are performed with substantially due to the increase in credit. In fact, when the balance sheet of the banking sector after 2002 is dealt with, it is observed that the total assets of the sector to GDP ratio shows a continuously increasing trend-except in 2003 and 2004- that is also a fast and stable growth record (CBRT, 2015).

The number of banks was 43 in 2011 and 45 by the year March 2015. The changes were due to the number of banks that were taken over in 2014, one bank reduced-funds in the last bank- and the increase in the number of foreign banks which was 16 in 2011 and 19 in March 2015. Considering the number of branches and employees it is seen that the increase in the previous period continued during this period. After 2013, the situation is striking here is that this upward trend has slowed and followed as a nearly stable number of staff especially.

When the total share of interest income, interest expenses, and net interest income in the total assets are compared between 2011 and March 2015, it is seen that the ratio of net interest income has fallen and then it follows a horizontal way that seems to continue after 2013. It entered again into some increased tendency to fall in subsequent years in 2012. The ratio of banks' net operating income in total assets was 2.1 percent in 2011 and it decreased a percentage of 1.55 in 2014. The following year-March 2015- it remained at this level with a very small increase. During this period, the annual growth trend seen in US dollar deposits showed a different situation due to the increase in dollar exchange rate. Deposits in terms of dollar increased from 2011 to 2012 however in the later periods there was decline year by year based on the previous year. The equity in terms of dollar increased in year 2012 based on the previous year however it also decreased year by year in this period like deposits in terms of dollar and it became lower than the level of 2012. On the other hand non-deposit sources increased each year based on the previous year between 2011 and March 2015 in terms of both TL and US dollar. Internet and mobile banking

continued to evolve in the world as well as all in Turkey in the same period. The number of active customers was 8.6 million in 2011 and it was about 15.3 million in March 2015 which means a 78% increase.

## 6. Conclusion

The Turkish banking sector restructuring process launched in February 2001 following the economic crisis. "Strong Program for Transition Economies" and "Banking Sector Restructuring Program" had tried to establish the stability. Prior to 2002, the economy had to deal with both high interest and exchange rate risks. Furthermore there was a fund management performing with in the open position of banks. Due to these obstacles the desirable stability in this period had resulted in failure to achieve the economic programs' outcomes. The regulations applied in the banking sector before 2002 started to fructify after 2002. Political stability was one of the most important key points of the success in this period. Moreover the money of which source was known flowed the country after 2002 and it also contributed to achieve the target of the economic programs designed before 2002 according to Central Bank's report. Central bank reserves rose by more than expected in that period with this funding. The positive developments seen in years 2002-2007 and 2007-2011 increased the expectations. Istanbul Finance Center was introduced in 2011 and these expectations were announced as the future plans. However these expectations were not realized based on the US dollar. Deposits and equities were declined and again after 2012 interest income and net income of the banks decreased in March 2015 based on the year 2012. From 2002 to 2014 credits and account receivables increased 18 times, total deposits increased 11 times, total assets increased 12 times. Considering the annual growths in the sectors balance sheet it is seen that assets, credits and account receivables made strong progress over the all other items. The number of banks fell in 2014. However the number of personnel increased from 123,271 to 200,886 in the same period. There is a significant increase in the number of borrowers in 12 years. That number is 8.8 times more than the number in 2002. The dramatic increases are also observed in credit card loans and non-performing consumer credits. Credit card loans and non-performing consumer credits increased by 137 times and 27 times more than the year 2002. These data show that besides the positive developments in financial sectors there are negative events in terms of sociological facts.

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