“Turkish Banking Crisis 2001”

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LONDON
The Crisis

Shocks

- Sharp increase in interest rates
- Sharp depreciation of the Turkish Lira
- Contraction in economic activity
- Political Instability

Impact on the Banking Sector

- Maturity mismatches $\rightarrow$ funding losses.
- Short FX positions $\rightarrow$ FX losses
- Asset Quality $\downarrow$ $\rightarrow$ NPLs $\uparrow$
- Credit Risk $\uparrow$ $\rightarrow$ Lending Appetite $\downarrow$
- Funding From Abroad $\downarrow$ $\rightarrow$ liquidity shortages
- Ineffective Interbank Market $\rightarrow$ crippled settlements

LEADING TO
Eroding....................... CAPITAL BASE
Drying up.................... LIQUIDITY
Loss of Confidence..... RUN ON BANKS
Signalling.................... MORE BANK FAILURES
Further Shaking.......... POLITICAL PLATFORM
Collapse of............... ECONOMY

CRISIS is SYSTEMIC and EXPENSIVE
Banks owed 16 bio USD to Foreign Creditors. Threats of activating cross-default and force-major clauses in loan agreements.

BRSA: Banking Regulation and Supervision Agency
SDIF : Savings Deposit Insurance Fund
State owned banks will be restructured.

Problem Banks will be floated within SDIF.

Banks will be Recapitalized.

Regulatory and Supervisory Framework will be strengthened.
A. RESTRUCTURING OF STATE OWNED BANKS

1. FINANCIAL CONDITION

- Accumulated Duty Losses : 26 billion $
- O/N Borrowings : 14 billion $
- Deposit Interest Rates > Market Rates.
- Capital Increase : 4 billion $
- Proper asset classification. (NPLs: 1 billion $ ➤ 3.5 billion $; LLPs: 250 million $ ➤ 2.7 billion $)
- Back to Profitability. (-896 million $ ➤ ▲ -37 million $ in 8 months and ➤ ▲ +1.172 billion $ in 20 months)
A. RESTRUCTURING OF STATE OWNED BANKS

2. OPERATIONAL AND LEGAL

- Joint Board for synergy and cost cutting.

- Reorganization (Distribution Channels, Operations, Marketing/Sales, Internal Control and Risk Management).

- Advisors-Experts appointed for operations re-engineering.

- Intensive Public relations.

- Laws Amended: State Personnel, Bankruptcy, Early Retirement, Authorization to Restructure Loans etc.
B. PROBLEM PRIVATE BANKS TO BE TAKEN OVER BY THE SDIF, OTHERWISE...

- SDIF would need 14 bio USD cash instead of GBonds.
- Treasury would need to borrow more.
- More pressure on interest rates.
- Unsustainable domestic debt dynamics.
- Run from banks. Domino effect.
- Deposits getting out of the banking system.
- No more foreign credits for a considerable period of time. (Cooled off external pressures.)
- No more active payment system.

WHAT COSTS MORE THAN “A LOSS OF CONFIDENCE IN BANKS”?
Therefore:

✓ Selling the banks individually or after merging them to optimum sizes as soon as possible, or

✓ Subjecting them to immediate P&As, and

✓ Liquidating the rest

Were the options preferred.
<table>
<thead>
<tr>
<th>Name of Bank</th>
<th>Strategy</th>
<th>Resolution (Months)</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td></td>
<td>13</td>
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<tr>
<td>B</td>
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<td>13</td>
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<tr>
<td>C</td>
<td>Merger with Good Bank Q.</td>
<td>13</td>
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<td>D</td>
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<td>H</td>
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<td>9</td>
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<tr>
<td>I</td>
<td>Merger with Bad Bank N.</td>
<td>6</td>
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<tr>
<td>J</td>
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<td>14</td>
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<td>K</td>
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<td>L</td>
<td></td>
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<tr>
<td>M</td>
<td>Merger with a State Owned Bank</td>
<td>29</td>
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<tr>
<td>N</td>
<td>Bad Bank</td>
<td>-</td>
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<tr>
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<td>30</td>
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<td>P</td>
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<td>10</td>
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<tr>
<td>Q</td>
<td>Direct Sale</td>
<td>20</td>
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<tr>
<td>R</td>
<td></td>
<td>6</td>
</tr>
<tr>
<td>S</td>
<td></td>
<td>16</td>
</tr>
<tr>
<td>T</td>
<td>Liquidation through bankruptcy</td>
<td>-</td>
</tr>
<tr>
<td>U</td>
<td>Voluntary liquidation</td>
<td>-</td>
</tr>
</tbody>
</table>

Source: SDIF, BRSA. Compiled from BSRP reports

*: Do not have “misuse” of Bank resources.
C. RESTRUCTURING OF PRIVATE BANKS

- Debt swap operation ($7.5 billion against LCY GBonds)
- Recapitalization Program
  - Three Stage Audit (CAR ≥ 8 %)
  - Government to capitalize systemic bank (TA ≥ 1% of market) up to 5 % CAR (Tier 1), if owner pays in at least 50 % of what is required.
  - Government to provide sub-loan for the rest up to CAR = 9%.
  - Ensured transparency and confidence in banking system.
  - Restored market discipline.
Moving towards international standards, introduced new and revised regulations on;

- Capital Adequacy.
- Risk management.
- Lending limits and loan loss provisioning.
- Related party exposure.
- Accounting standards and independent auditing.
- Facilitating mergers and acquisitions.

Aiming at introducing risk based supervision and tighter prudential supervision.

- And signed MoUs with other countries’ supervisory authorities to improve cross-border supervision.
Results of Restructuring Efforts

- Consolidation in the banking sector
- Decline in the share of the State and the SDIF banks
- Reduction of financial risks to manageable levels
- Improved transparency
- Improved profitability
- Strengthened capital structure
- Increased credit extension
- Increased foreign funding
## Improvements in capital structure

<table>
<thead>
<tr>
<th>Year</th>
<th>Capital Base (Billion USD)</th>
<th>Of Total Assets (%)</th>
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<tbody>
<tr>
<td>2001</td>
<td>1.4</td>
<td>1.2</td>
</tr>
<tr>
<td>2002</td>
<td>5.7</td>
<td>4.4</td>
</tr>
<tr>
<td>2003</td>
<td>13.0</td>
<td>7.2</td>
</tr>
<tr>
<td>2004</td>
<td>19.2</td>
<td>8.4</td>
</tr>
<tr>
<td>2005</td>
<td>20.0</td>
<td>13.3</td>
</tr>
<tr>
<td>2006</td>
<td>41.2</td>
<td>12.0</td>
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<tr>
<td>2007</td>
<td>63.0</td>
<td>13.1</td>
</tr>
<tr>
<td>2008</td>
<td>54.4</td>
<td>11.8</td>
</tr>
<tr>
<td>2011</td>
<td>80.6</td>
<td>11.8</td>
</tr>
</tbody>
</table>

Source: BRSA, [www.bddk.org.tr](http://www.bddk.org.tr)

BAT, (Banks Association of Turkey) [www.tbb.org.tr](http://www.tbb.org.tr)
Funding From Foreign Banks (billion USD)
Loans
(billion USD)

- 2000: 51 billion USD
- 2001: 35 billion USD
- 2002: 34 billion USD
- 2003: 50 billion USD
- 2004: 77 billion USD
- 2005: 114 billion USD
- 2006: 155 billion USD
- 2007: 242 billion USD
- 2008: 241 billion USD
- 2011: 379 billion USD
HOW ABOUT
UKRAINES’s CRISIS OF 2008......
In addition to similarities with the Turkish Crisis...

Effects of the Global Financial Turmoil.

Resulted in...

FX liquidity shortage; Devaluation; Increasing NPLs and Solvency problems in banks.

But wait ...
Credit Growth from 2004 to 2008

%

- Hungary
- Turkey
- Poland
- Russia
- Bulgaria
- Belarus
- Kazakhstan
- Romania
- Ukraine

Source: EBRD
Loans / Deposits (%)
And inevitably ...... And inevitably ......

**Exchange Rate**

**Outstanding Consumer Loans**

Source: Reuters

and

Source: NBU
And...

Private Sector Credit to GDP

Source: NBU
So...

Ukrainian Banks Capital 2006-2011

Source: NBU
Although...

Since October 2008, the NBU has intervened in problem banks, resulting in appointing provisional administrators for 27 banks, liquidation of 19 banks, change in private ownership in 4 banks (including one of the largest banks), and nationalization of 3 systemic banks...
Ukraine could not consolidate the system
Today’s Most Important Problem... Total Loans (in billion LCY)

only 6% increase!
Micro steps to be taken...

- Development of an efficient UAH market.
- Only healthy banks to be permitted to exist.
- Improve legislation and practices related to;
  - protection of creditors’ rights,
  - enforcement of collateral,
  - simplifying and shortening the judicial and enforcement procedures.
Recommendations based on Lessons Learned

I. **Preventive Measures:**

- Make sure you have clear, strong, healthy rules for licencing.

- Make sure your on-site inspections include financial investigative techniques.

“Take out the Bad Apples from the Basket”
Recommendations based on Lessons Learned

II. Crisis Management Lessons:

- You may have to introduce blanket guarantee. Announce the rules and conditions.
- Provide information to public.

“Keep Your Settlement System Intact”
Recommendations based on Lessons Learned

III. Resolution of intervened banks:

- “Merge and then resolve” strategy.
  Immediately start cost cutting.

- Do P&As.
  If the bank cannot be sold in a short period of time, then start selling the B/S in pieces.

- Closing branches and laying – off personnel.
  Do it on time.

“ If there is a need to act fast…then act fast”
Recommendations based on Lessons Learned

IV. Consolidate Further:

- **Develop legislative framework for mergers and acquisitions.**
  - Encourage M&As by giving incentives.

- **Corporate debt restructuring.**
  - Develop principles / guidelines and the legislative framework.
  - Have stand-still rules for justified cases.
  
  "Reward the Effort Without Forbearance"
IN SHORT

- Prompt exit of non-viable banks from the system is a must.

- Design a recap strategy for the rest.
  - Make sure owners are written down for the losses.

- Make sure assets are disposed of a.s.a.p.
  Wealth will be changing hands. Protect yourselves.

- There may not be an environment for proper asset evaluation.
  Be flexible; use more than one evaluator.

- For the banks which will need Public Funds; decide on eligibility & exit criteria.