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PRESS RELEASE

A. CENTRAL BANK'S INVOLVEMENT IN THE PRIMARY DEALERSHIP PROGRAM

1. The Primary Dealership (PD) System was initiated by the Undersecretariat of Treasury in May 2000 with the aim of achieving effectiveness in public debt management, attaining stability in public borrowing, deepening the secondary markets for government securities and improving the financial system. However, this program had to be abandoned de facto due to the crisis that broke out in November 2000, and de jure with the expiration of contracts made with the primary dealer banks in May 2001. In 2001, the Treasury launched another study in order to reactivate the PD system and determined its principles. Finally, the PD System was reintroduced on September 2, 2002.

2. Thanks to the progress in structural reforms in the last one and a half year period, fundamental institutional arrangements have been realized. Banking sector reforms carried out by the Banking Regulation and Supervision Agency, enactment of the Public Borrowing Law that is crucial for the borrowing discipline and securing clearly of the Central Bank's independence under the amended Central Bank Law are among the most important structural arrangements. In particular, as the Central Bank no longer grants advance to the Treasury and does not purchase debt instruments issued by the Treasury and public institutions from the primary market, the transparency of the Central Bank policies has increased, which in turn enabled the Central Bank to better express the purposes of its operations to the public.

3. Actually, the Central Bank policies for the past one and a half year have been carried out within the framework of the price stability goal as stated in its law. As explained in almost every press release, the primary objective of the Central Bank's monetary policy will continue to be attaining price stability and the Central Bank will avoid all operations and transactions that might be in contradiction with that objective. While financial stability is the required supportive goal for the effective conduct of policies to attain price stability, efficient and sound functioning of the foreign exchange, bond and money markets is another prerequisite.

4. Regulations adopted by the Banking Regulation and Supervision Agency, and particularly the banking sector recapitalization scheme, contribute to the establishment of a sound banking system. Within this framework, the Central Bank is gradually abandoning its intermediation function in the interbank money and foreign exchange markets in order to promote development and deepening in the financial markets and improve the risk assessment capabilities of the banks.

5. Supporting the establishment of sound and well functioning money and foreign exchange markets, in which the Central Bank is no longer a counterparty, is necessary for the stability in financial markets and is concord with the price stability goal. In fact, in line with its primary objective of price stability, the Central Bank attaches great importance to the following arrangements that has contributed or will contribute to the improvement and stability of the financial markets:

- Undertaking the necessary work for the establishment of a forward foreign exchange market,
- Giving support for the removal of the tax on foreign exchange sales and forward transactions,
- Taking part in TRLIBOR arrangements, and supporting thereof,

- Conducting four-week maturity TL deposit buying auctions,
- Conducting quick repo tenders when needed,
- Providing a late liquidity window facility,
- Providing liquidity facility to the banks under recapitalization process through repurchase transactions in case they face a liquidity shortage.

6. Deepening of the financial markets is vital in improving the effectiveness of the monetary policy and it is expected that the PD System will also contribute to the deepening of financial markets. In the same way, TRLIBOR initiated on August 1, 2002 by the Banks Association of Turkey has resulted in the formation of benchmark interest rates that the economic agents have been looking for. The formation of benchmark interest rates is an important development as they will increase transparency of the markets, form a sound yield curve in money markets and improve forward transactions by pricing financial assets more effectively. The primary dealer banks are expected to be active and to play an important role in TRLIBOR.

7. Therefore, in line with the price stability goal, the Central Bank has decided to support the PD System and provide a TL liquidity facility for the primary dealer banks through open market operations. This liquidity facility, which is actually in contrast with the past quasi-currency board monetary policy, is consistent with the current monetary policy under the floating exchange rate regime, whose aim is to adopt inflation targeting. These arrangements are organized within the framework of open market operations and the Central Bank is not a counterparty to the contracts to be made between the Undersecretariat of Treasury and the primary dealer banks.

B. GENERAL FRAMEWORK OF THE LIQUIDITY FACILITY TO BE PROVIDED BY THE CENTRAL BANK FOR THE PRIMARY DEALER BANKS

8. The general framework of the liquidity facility to be provided by the Central Bank for the primary dealer banks are as follows:

- a) The maximum amount of liquidity to be provided for the primary dealer banks will be 10 percent of the TL denominated and not redeemed Treasury securities purchased from the primary market starting from July 22, 2002 (the net amount of the TL securities purchased from auctions, public offerings, TAP sales, noncompetitive sales, second round sales and switching auctions will be included. FX indexed securities are excluded).
- b) Banks under the PD program are allowed to conduct repurchase transactions within this 10 percent limit via quotation method or they can use at most half of this limit by selling to the Central Bank these purchased TL denominated securities which are accepted as the benchmark by the Treasury.
- c) In the said repurchase transactions, the Central Bank will prefer the quotation method and will determine the interest rates. It is expected that the current excess liquidity in the markets may last for a long period of time. Therefore, the short-term money market interest rates are expected to be around the Central Bank's borrowing rates. The Central Bank will determine the interest rates of repurchase transactions made with the primary dealer banks taking into consideration the market rates and by adding a premium to the Central Bank's borrowing rate, but will

not allow this rate to exceed the average of the Central Bank's TL borrowing / selling quotations. The primary dealer banks will conduct the repurchase transactions between 10:00 – 16:00 hours.

- d) For the outright purchase of benchmark securities from the primary dealer banks, the Central Bank will prefer to hold auctions that would better reflect the market conditions. The primary dealer banks in need of liquidity will give their security selling offers to the Central Bank. The Central Bank, after negotiating with the other primary dealer banks, will determine the relevant benchmark securities to be purchased through auctions. However, by taking into consideration the market conditions, the Central Bank can also use the quotation method in purchasing securities from the primary dealer banks. The maximum amount of securities to be purchased per day cannot exceed 20 percent of the total limit for selling securities given to the primary dealer banks.
- e) Thus, as the liquidity facility provided for the primary dealer banks is limited, and due to the methods used in these transactions, the liquidity provided for the primary dealer banks is not expected to be a continuous funding source and the interest rates will reflect the market conditions.
- f) The maturities of the repurchase transactions via quotation method to be conducted with primary dealer banks under the liquidity facility limits are overnight and one-week. The interest rates for both of these maturities will be 49 percent, starting from September 3, 2002.