

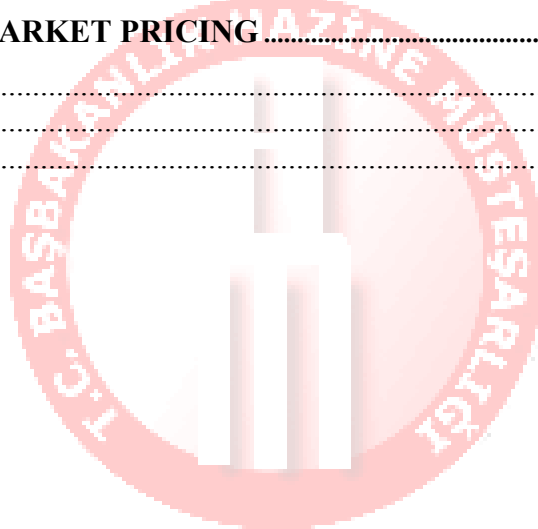
**REPUBLIC OF TURKEY
PRIME MINISTRY
UNDERSECRETARIAT OF TREASURY**

**CONSUMER PRICE INDEX (CPI) INDEXED
GOVERNMENT BONDS**

INVESTORS GUIDE

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I. GENERAL ISSUES

In line with its objectives of diversifying the instruments issued, broadening the investor base and lengthening the borrowing maturities; the Undersecretariat of Treasury will issue Inflation (Consumer Price Index-CPI) Indexed Government Bonds. The first CPI Indexed Government Bond will be auctioned on February 19, 2007.

By guaranteeing a real return, CPI Indexed Government Bonds serve as an alternative asset class to the investors. These securities are preferred by investors because they provide a reduced exposure to changes in inflation due to their stable real returns. By eliminating the risk of inflation uncertainty over the total return, CPI Indexed Government Bonds allow investors to lengthen their investment horizon. Consequently, in most issuing countries, such securities are generally sold with maturities longer than 40 years.

The principal payment of the securities is not eroded by inflation. The interest revenue is also protected in the same way. The real return of the bond is fixed, no matter what the inflation rate will be over the life of the bond.

II. TERMS OF THE BONDS

1. Maturity

The bonds will have a maturity of five years with semi annual coupon payments.

2. Issuance Technique

CPI Indexed Government Bonds will be issued through uniform price auctions. Bidders will submit their price bids for the securities with YTL 100 par value for which the real coupon has been fixed by the Treasury. Within this context, the lowest price (highest return) at the cut off point will be applied to all bids.

The Treasury auctions are open to all local and international investors, institutional or individual, with a minimum bid requirement of YTL 100. The monthly auction calendar is announced on the last business day of the preceding month on

Treasury web site www.hazine.gov.tr, together with a press release. Similarly, the details of auctions are also announced on the last business day of the previous week.

3. Real Coupon Rate

The real 6 month coupon rate will be announced prior to 19.02.2007 via weekly auction announcement and this rate will be fixed over the life of the bond.

4. Index to Be Used and Indexation Method

CPI, as announced by the Turkish Statistical Institute (TurkStat) will be used for all payments of the bond. The detailed information on CPI can be found on the web page of Turkstat (www.tuik.gov.tr).

i) Principal Payment

The inflation valuation of the principal will be paid to investors at maturity. So the bond with YTL 100 par value will not be affected by the inflation difference over the maturity in real terms.

The principal per YTL 100 to be paid at maturity will be calculated according to the formula provided below:

$$Principal\ Payment = \frac{Reference\ Index_{Maturity}}{Reference\ Index_{Issue\ Date}} \times 100$$

(Reference Index calculations are explained in section 5.)

ii) Coupon Payments

Semiannual coupon payments will also be protected from inflation. Accordingly, the coupon payments for YTL 100 par value will be calculated according to the formula below:

$$Coupon\ Payment = \left(\frac{Reference\ Index_{Coupon\ Date}}{Reference\ Index_{Issue\ Date}} \times 100 \right) \times Real\ Coupon\ Rate$$

iii) Guaranteed Return

It is guaranteed that the principal payment would not be less than the par value. In other words, in cases where the reference index at maturity would be below the reference index at issuance, the YTL 100 par value is paid. Therefore, should deflation occur over the lifetime of the bond, the principal to be paid would be equal to the par value.

There is also a guarantee for the coupon payments in case of the reference index at coupon payment date to be below the reference index at issuance. In such cases, coupon payments would be calculated over the YTL 100 par value and the 6 month real coupon rate determined by the Treasury.

5. The Computation of Daily Reference Indices

The Consumer Price Index announced by the Turkish Statistical Institute (TurkStat) will be used for all the principal and coupon payments and the secondary market pricing of the bonds.

Reference index for g^{th} day of a^{th} month is calculated as follows.

$$\text{Daily Reference Index} = CPI_{a-3} + \frac{g-1}{AG} \times (CPI_{a-2} - CPI_{a-3})$$

CPI_{a-2} : CPI of $(a - 2)$ month g : number of past days in (a) month

CPI_{a-3} : CPI of $(a - 3)$ month AG : number of total days in (a) month

As shown in the above formula, the reference index for the first day of any calendar month is the CPI for the calendar month falling three months earlier. The reference index for the other days of the month will be calculated by interpolation using CPI_{a-2} and CPI_{a-3} . The method used in the calculation of the reference index has also been used in other countries which issued Inflation Indexed Bonds and it generates the efficiency in the secondary markets by allowing forward value transactions and the calculation of the settlement price.

The daily reference indices will be calculated based on the above formula and the indices will be rounded to six digits. The calculated indices will be announced on the Treasury web page www.hazine.gov.tr.

In case of a change in the base year of the index, the index before the change will be used. However, the index will be revalued according to the inflation realization based on the new index.

III. SECONDARY MARKET PRICING

The pricing of the inflation indexed bonds, which includes “clean price”, “accrued interest” and “settlement price” calculations are given below.

Clean Price

Clean price formula for these bonds, which excludes the inflation valuation is given below:

$$F_t = \sum_{j=1}^n \frac{r \times 100}{(1+i)^j} + \frac{100}{(1+i)^n}$$

Where F_t is the clean price, n = remaining number of coupons, r = real coupon rate and i = real return demanded by the investor

As can be seen from the formula, the only difference from the fixed coupon bond pricing is that; instead of nominal coupon and discount rate; the real coupon rate and real return demanded by the investors are used respectively.

Accrued Interest

The accrued interest (BF_t), excluding the inflation valuation, for the CPI indexed bond will be calculated just like other coupon paying securities, as follows:

$$BF_t = r \times 100 \times \frac{\text{Number of days accrued in the coupon period}}{\text{Total number of days in the coupon period}}$$

Settlement Price

Settlement price covering the accrued interest and inflation valuation will be calculated by using the formula as shown below.

$$\text{Settlement Price} = (F_t + BF_t) \times \frac{\text{Reference Index}_{\text{Settlement Date}}}{\text{Reference Index}_{\text{Issue Date}}}$$

The price quotations will be given over the Settlement Price formula as given above; until the technical studies concerning the CPI Indexed Bond are finalized by the Istanbul Stock Exchange (ISE).

Following the conclusion of the preparations by the ISE, prices will be quoted over the dirty price ($F_t + BF_t$) comprising the accrued interest and excluding the inflation valuation. The related information will also be given by the ISE.