

Financial Services
Turkey
Credit Analysis

Is Yatirim Menkul Degerler A.S.

Ratings

	Current Ratings
National	
Long-Term	AAA(tur)
Sovereign Risk	
Foreign Long-Term IDR	BB-
Local Long-Term IDR	BB

Outlook

National Long-Term	Stable
Sovereign Foreign Long-Term IDR	Stable
Sovereign Local Long-Term IDR	Stable

Financial Data

Is Yatirim Menkul Degerler A.S.

	30 Sep 08	31 Dec 07
Total assets (USDm)	1,172.5	1,070.4
Total assets (TRYm)	1,444	1,241
Total equity (TRYm)	266.2	243.8
Operating profit (TRYm)	9.2	42.1
Published net income (after minorities, TRYm)	36.8	33.7
ROAA (%)	3.7	3.8
ROAE (%)	19.2	17.0
Op. profit margin (%)	12.3	39.7
Adjusted leverage (x)	3.50	3.04
Equity/assets (%)	27.9	32.8

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Rating Rationale

- The National Long-Term Rating of Is Yatirim Menkul Degerler A.S. (Is Investment) reflects support it could expect to receive from its parent, Turkiye Is Bankasi A.S. (Isbank; 'BB'/Stable Outlook, Individual 'C') if needed.
- Is Investment's core revenues include customer driven service revenues and net trading revenues from equities, fixed income and derivatives. Trading volumes and revenues are mainly driven by proprietary trading and they tend to be volatile. In 9M08, Is Investment's operating earnings were hit by losses from proprietary trading operations, due to large falls in the volatile equities market, although they were partly mitigated by bonds and mutual funds trading operations. Service revenues include all commission revenues from the clients as well as investment banking operations and tend to be more stable. The company is focusing on diversifying its revenues into the futures market for the purpose of hedging and arbitrage positions (FX and ISE-index futures), which became the most profitable segment in 9M08, although it is not a very stable source of income. Is Investment also engages in short-term money market transactions.
- Is Investment is the first local securities firm to have a dedicated risk management department in Turkey, although this is not a regulatory requirement. All trading and margin limits are set by the regulator, although Is Investment operates within more prudent internal limits.
- The company has no long-term debt, and short-term debt is covered by short-term liquid assets. The short-term liquid assets to short-term liabilities ratio was a satisfactory 104% in Q308.

Support

- Its majority ownership by Isbank, its common brand name and its strategic importance to the parent means that Isbank would have high propensity to provide support to Is Investment if needed. However, Isbank's ability to do so is moderate given its 'BB' Foreign Currency Long-Term IDR.

Key Rating Drivers

- Although small, Is Investment is an integral part of Isbank. As a result, Is Investment's National Rating would mirror any changes at Isbank.

Profile

Is Investment, which is 72.1% owned by Isbank Group, is the investment banking arm of the parent. Is Investment makes use of Isbank's branch network, liquidity facilities and infrastructure in the course of its activities, whereas Isbank utilises the asset management and custody services provided by Is Investment. It shares its parent's brand name, logo and senior management. Is Investment's main business lines include providing brokerage and trading services for its clients, investment advisory, asset management, private equity and corporate finance services for public offerings, M&As and strategic consultancy. Is Investment is the largest securities house in Turkey in terms of asset size and it is a market leader in many sub-segments.

- Investment banking arm of Isbank and very close integration with the parent
- The largest securities house in Turkey in terms market share in many segments
- Subject to regulation by the Capital Markets Board

Profile

Is Investment was established by Isbank in 1996, as the investment banking arm of the bank, and is an integral part of the parent as it completes the range of financial services offered. The main shareholder is Isbank with 65.7%. Together with other group companies, Isbank Group holds 72.1% of the total shares. In 2007, Is Investment carried out an IPO and listed its shares on the Istanbul Stock Exchange, making it the only listed securities house in Turkey. The IPO generated about TRY100m in cash proceeds, to be used for future organic growth. Is Investment used TRY30.5m of these proceeds to acquire a 50% share of Is Asset Management from Isbank in June 2007, thereby increasing its stake in this company to 70%.

Isbank was established in 1924 as the first private commercial bank in Turkey to support the country's economic development. It has the second-largest asset-size and branch network in the sector. It had an unconsolidated asset size of TRY92.0bn at end-Q308. Is Investment shares its parent's brand name, logo and senior management.

At Is Investment, members of the board are drawn from the ranks of Isbank. The client base is composed of about 4,100 high-net-worth individuals, 565 corporate clients, 340 foreign institutional clients and the retail brokerage clientele of Isbank. It holds the market leader position in many of the segments that it operates in, including a 6.6% market share in equity trading volumes, a 14.1% share in the bills and bonds market (among the brokerage houses) and a 13.7% share in the derivatives market at end-2008. The company has about TRY7.2bn of assets under management, mainly through its asset management subsidiary. It generates around 24% of its equity trading volume from Isbank's retail brokerage clients.

Is Investment has nine subsidiaries including Is Asset Management, Is Private Equity and Is Investment Trust and a fully owned company, Maxis Securities, established in London with the aim of expanding its international business. The distribution network consists of six branches in major Turkish cities, two representative offices (one located in Kazakhstan) and more than 1,000 Isbank branches acting as agents spread around the country. Being one of the founding members of Turkish Derivatives Exchange (TurkDEX), it holds 6% of the capital.

Is Investment is Organised Around the Following Main Divisions

The Brokerage Group

Brokerage is the core operating segment of Is Investment and runs the trading activities both for the clients and its own proprietary trading operations. The company is active in trading securities, including domestic and international equities, fixed-income, derivatives and commodities. It also has access to the international capital markets and actively trades Turkish eurobonds, corporate bonds, foreign equities, commodity futures and credit-linked notes. In a partnership with Danish Saxo Bank, Is Investment has offered its clients a trading platform facility called TMI (Trade Master International) since end-2007 that provides them with an online-trading service in the international equity and futures markets. Owing to this facility, the number of derivative contracts increased by more than 4x in 9M08, while trading volumes in international markets grew by 33% in the same period. The company also has in place a dedicated risk management system that copes with counterparty and credit risks specifically embedded in this trading platform.

Table 1: Is Investment Shareholder Structure

(Q308)	(%)
Isbank	65.65
Is factoring	2.43
Is leasing	2.43
Sisecam	1.45
Camis investment hol.	0.17
Free float	27.87
Total	100

Source: Is Investment

Investment Banking and Corporate Finance Group

This division deals with public offerings of equities and corporate bonds, privatisations, strategic consultancy and M&A advisory. Is Investment benefits from the widespread distribution network that many of its competitors lack. This position enables Is Investment as a strong competitor in public offerings. Although the market is small in absolute terms, Is Investment maintains the number one position in terms of public offerings – it has been involved in 59 M&A deals with a total of USD4.9bn since 2000. In 9M08, the company participated in total M&A deals worth USD2.1bn. However, given the sharp global slowdown in investment banking transactions, this segment is likely to lose growth momentum, especially in the short term.

Portfolio Management Group

This division manages its own mutual funds, pension funds and discretionary portfolio management activities. The company seeks to develop new products to meet investors' needs; a new hedge fund and a bond ETF (exchange-traded fund) was added to the product range in late 2008. The group has a 21% market share in mutual funds and a 19% share in pension funds with total funds under management of close to TRY7.2bn at end-Q308.

Regulation

The Capital Markets Board (CMB) has oversight of Is Investment's activities and the latter is subject to all CMB's requirements on capital, liquidity, investment limits and margin trading limits. The UK subsidiary (Maxis Securities) is supervised by the FSA in the UK. Maxis Securities holds a "Category B" licence, and this may be upgraded to a "Category A" licence in the future.

Strategy

Is Investment aims to retain its leading position in the domestic market while further diversifying its business and product ranges. Turkish derivatives exchange and access to international markets are relatively new segments and management plans to develop these areas to diversify and enhance its revenue base. Is Investment is still aiming to add new branches and grow its human resources as stated in its IPO prospects within frame of the long-term plans, despite the challenging and volatile operating environment.

Presentation of Accounts

Unless otherwise stated, all references in this report are to the bank's consolidated financial statements in accordance with CMB regulations, which are mainly in line with IFRS regulations. Consolidated interim figures are also in accordance with CMB regulations. In 2008, Is Investment changed its consolidation practices slightly in line with regulatory changes, which resulted in some restatements in FY07 accounts. The impact on the balance sheet was negligible (less than 1% change in total assets) whereas 9M07 earnings increased by TRY3.0m (14.2% higher) as a result of restatements. In this report, Fitch refers to the audited restated FY07 assets and liabilities figures. At the time of this report, the audited "restated" profit and loss (P&L) statement was not yet available for FY07.

Performance

Is Investment's revenues are driven by customer-driven service revenues and net trading revenues.

Service revenues are more stable and include commission revenues from clients, income from investment banking activities and portfolio management fees. Increased competition and the weaker operating environment in 9M08 (compared with 2007) has been reflected in the performance of this segment, where net revenues contracted by an annualised 17% in 9M08. However, this segment continued to be one of the largest contributors to operating revenues (see Table 2 below). Net trading revenues are generated from equities, bonds, mutual funds and

- Operational earnings hit by volatile market conditions
- Growing contribution from trading in futures markets compensate loss-making equity segment

derivative instruments. Volumes are mainly driven by proprietary trading; however, profitability tends to be volatile (see Table 1). Despite 5% annualised growth in trading volumes in 9M08, Is Investment recorded a net TRY13.0m loss from its sales and trading operations, compared with a net profit of TRY9.4m in 2007.

In 2006, and increasingly from 2007, the company started to make use of alternative revenue sources to enhance earnings diversification. For this purpose, it focused more on trading of FX futures and ISE-Index futures through hedging and arbitrage transactions. Although not a very stable source of income, this segment proved to be the most profitable, generating a pre-tax income of TRY33.7m in 9M08.

Another line that is increasingly being utilised for short-term borrowing is the ISE money market. Almost all the financial borrowings of Is Investment are composed of such short-term facilities. These funds are then deposited in various banks to benefit from the arbitrage and earn a spread. This practice helped to generate about TRY3.4m of net pre-tax income in 9M08 (2007: TRY18.8m). The fast asset growth in 2007 was driven mainly by these money-market borrowings. Receivables and payables from/to customers are a result of outstanding transactions that are to be realised, which have no impact on operations, as the receivables and payables have the same maturity.

Costs

Costs are mainly salaries and administrative expenses. In 9M08, costs increased by an annualised 36%, especially due to the rapid increase in marketing expenses, which is mainly driven by the transaction fees related to the growing volumes of foreign marketable securities. Efficiency ratios (as well as profitability ratios) are volatile due to the unstable nature of earnings.

Table 2: Is Investment Profit and Loss and Performance Ratios

(TRYm)	30 Sep 08	31 Dec 07	31 Dec 06	31 Dec 05
Gross revenues	74.7	106.2	71.6	85.5
- Of which sales of equities ^a	-47.2	3.2	-6.9	15.1
- Of which sales of private and public bonds ^a	24.4	15.6	5.1	16.7
- Of which sales of treasury bills ^a	0.5	2.9	3.8	0.8
- Of which sales of mutual funds ^a	9.5	-12.3	-0.1	0.0
- Of which other revenues (including futures trading)	44.7	26.6	25.9	3.1
- Of which service revenues	43.1	69.6	43.9	49.7
Operating Expenses (-)	65.5	64.1	44.3	42.4
Operating profit	9.2	42.1	27.4	43.1
Op. EBITDA	9.6	43.0	28.3	44.7
Ratios (%)				
Operating profit margin	12.3	39.7	38.2	50.4
EBITDA margin	12.9	40.5	39.5	52.3
ROAE ^b	19.2	17.0	10.8	21.6
Personnel expenses/net revs	26.3	19.2	28.5	17.5
Prop. income/net revs	-17.1	8.9	2.7	38.1

^a Net of costs, excludes financial income, ^b Annualised for 9M08
Source: Is investment financial statements, adapted by Fitch

Prospects

Is Investment is the leading securities and brokerage house in Turkey, having the strongest domestic franchise, backed by Isbank's widespread branch network. The company's aim is to maintain its market leader position while diversifying its revenues. However, due to the volatile nature of the business and challenging market conditions, profitability is likely to be negatively affected, despite the relative stability of service revenues.

Risk Management

Is Investment has an independent risk management department that reports to the board of directors through an audit committee; it simultaneously provides

- First to have dedicated risk management in Turkey, among all local brokerage houses
- Trading and margin limits set by the regulator. Internal limits are even more prudent
- A speculative short-FX position opened in 9M08

information to senior management. The company is the first among all Turkey's brokerage houses to have a dedicated risk management department. Risk management practices are constantly being strengthened in certain areas. The company has modified and integrated external risk management software for its own needs, which enabled it to integrate its entire trading book into the market risk module. Monte Carlo simulations, parametric value-at-risk (VAR) and historical simulations are regularly being produced with this module. A comprehensive ALM application is at the data testing stage and will be implemented in 2009. It will enable extensive duration-gap analysis, cash flow forecasts and economic value of equity calculations.

Exposure to credit, operational and compliance risk arises through brokerage activities, while market risk arises through the bank's proprietary positions. Liquidity risk arises from the cash flow management of the trading activities.

Credit risk arises from counterparty risk or client default risk on settlements. Transaction and position limits for each counterparty are determined by the board of directors. A total limit of USD13.9bn was approved for 109 international and 17 domestic corporate counterparties at end-December 2008. Rules like trading limits and margin maintenance, which regulate the credits extended for brokerage business are set by the CMB. However, Is Investment operates within far more prudent internal limits. Credit limits are subject to evaluation by credit committee for amounts up to TRY5m and to board approval for amounts above TRY5m. The total credit limit assigned was TRY256m at end-2008, of which TRY34.5m was utilised by clients. The liquidity and concentration of securities subject to credit risk can be volatile, and these are monitored by the risk management department and board of auditors on a daily basis.

Is Investment monitors intra-day, overnight and stop-loss limits to control market risk in its trading portfolios. These limits are reported daily to senior management and monthly to the board of directors. With the integration of the risk management software into the trading portfolio, Is Investment has become the first in Turkey to implement risk-based limits to daily operations, thereby minimizing possible trader risks. Separate VaR and stress limits on the portfolio were introduced in 2008. A scenario analysis of a 10% decline in equity prices and a 5pp increase in term-loan (TL) interest rates implied a 3.3% and 1.8% respective reduction in the trading portfolio, at end-Q308. The proprietary trading limits set by the board on the TRY fixed-income portfolio and TRY equity shares are equivalent to 30% and 20% of equity, respectively. However, the actual positions were much lower, at around 2% of capital at end-Q308. The company has some short-FX positions, especially due to off-balance-sheet FX commitments (due from derivative FX contracts), resulting in a net TRY44.3m short-FX position at 9M08, equal to 16.7% of equity.

Operational Risk

Is Investment's operational risk practices are carried out by its risk management department and are overseen by the audit committee. Key risk indicators that are monitored cover an array of operational risks (regulatory, IT, legal and personnel). An independent IT audit was performed on the company's systems in 2008. New products are all subject to a rigorous review process. The bank has a disaster recovery centre and system backup storage in Ankara.

Funding and Capital

Is Investment acquires letters of guarantee from various parties including Isbank (Q308: TRY1,104m) and borrows from the ISE money market using these letters of guarantee as collateral. The company then pledges these funds to various banks, usually at a small margin above the funding cost. All the short-term financial debt is composed of such funding. It had a TRY1.2bn available line from the ISE money market and TRY798m of this limit was used at end-Q308. Is Investment has no long-term debt, and short-term debt is covered by short-term liquid assets. The short-

- Leverage is driven by short-term ISE money-market borrowings
- Capital adequacy figures comfortably exceed minimum requirements

term liquid assets to short-term liabilities ratio was a satisfactory 104% in Q308. Funding also comes from balances such as short-term customer payables arising in the course of its business; however payables and receivables usually balance each other out. Is Investment also applies to its parent bank for daily liquidity facilities, and an intraday liquidity window of TRY50m from Isbank is available, although this is not widely used.

Is Investment's balance sheet is linked to its trading activity levels and this brings an element of volatility to capital/leverage ratios. The company's minimum equity, paid-in capital and capital adequacy basis requirements are determined by the CMB; Is Investment's figures comfortably exceeded the minimum requirements at end-Q308 (see Table 3). The equity/total assets ratio stood at 28% at end-Q308 (2007: 33%). This indicates a low leverage, although partly warranted by the intrinsic volatility of the markets.

Table 3: Capital Adequacy Requirements

(TRYm)	Minimum	Q308 actual
Equity requirement	1.95	237.2
Paid-in capital requirement	0.5	119.4
Capital adequacy basis requirement	118.5	174.2

Source: Is investment

As a result of the strong capitalisation driven by large proceeds from the IPO in 2007, the company distributed a generous TRY21.8m cash dividend from 2007 earnings (57% of net earnings). In future, the company aims to maintain a 30% dividend pay-out ratio.

Table 4: Leverage/Debt Service

Absolute values (TRYm)	9M08	FY07	FY06	FY05
Assets	1,444	1,241	542	368
Equity (including minorities)	403	406	280	264
Gross LT debt (A)	0	0	0	0
Cash (B)	829	681	172	57
Net LT debt/(cash) (A-B)	-829	-681	-172	-57
Op. EBITDA	10	43	28	45
EBITDA-capex	9	41	26	44
Ratios				
Equity/assets (%)	27.9	32.8	51.7	71.5
Adjusted leverage ^a (x)	3.50	3.04	1.92	1.38

^a Assets less reverse repo/equity
Source: Financial statements

Appendix A

Is Investment

(TRYm)	30 Sept 08	31 Dec 07	31 Dec 06	31 Dec 05
Assets				
Cash and cash equivalents	829	681	172	57
Securities owned, at market or fair value	244	303	206	218
Receivables from brokers and customers	304	224	128	70
Receivables from related parties	0	0	1	1
Long-term financial assets	35	22	22	19
Land, furniture, equipment, building and intangible assets	5	5	3	3
Goodwill	0	0	-6	-6
Other assets	27	6	17	7
Total assets	1,444	1,241	542	368
Liabilities				
Financial borrowings	798	636	15	24
Money market borrowings	3	2	189	36
Payables to brokers and customers	226	183	49	38
Other liabilities	14	14	9	7
Total liabilities	1,041	834	262	105
Share capital	119	119	97	97
Reserves and past profits	81	86	40	16
Profit and loss account	37	38	16	27
Total equity	266	244	153	139
Minorities	136	163	128	125
Total liabilities and net worth	1,444	1,241	542	368

Source: Is investment financial statements

Is Investment (Continued)

	30 Sep 08	31 Dec 07	31 Dec 06	31 Dec 05
Revenues				
Equity, securities and mutual funds trading	-13.0	9.4	1.9	32.6
Service revenues	43.1	69.6	43.9	49.7
Financial and other income/(expenses) (net)	77.4	57.7	24.9	28.5
Total revenues	107.7	136.7	70.6	110.8
Expenses				
Service expenses	0.3	0.7	1.9	11.3
Employee compensation	25.7	31.0	20.4	15.0
Marketing	16.0	7.5	3.2	2.5
General and administrative	22.5	23.7	17.8	12.0
Amortisation and depreciation	1.1	1.2	0.9	1.6
Total expenses	65.5	64.1	44.3	42.4
Net income before income taxes and minorities	41.9	73.3	26.3	68.5
Minorities	-3.7	31.2	8.4	34.4
Income taxes	8.8	8.3	2.2	7.6
Net income	36.8	33.7	15.7	26.5
Ratios summary				
Average assets	1,342	892	455	307
Average equity	255	198	146	123
Short term borrowings (mainly money market and Bank loans)	801	638	203	60
Long term debt	0	0	0	0
Net financial and other income	77	58	25	29
Dividends paid	n.a.	21.8	1.4	0
Profitability (%)				
Return on average assets (ROAA)	3.7	3.8	3.5	8.6
Return on average equity (ROAE)	19.2	17.0	10.8	21.6
Compensation/total revenues	26	19	29	17
Total revenues/average assets	7.4	11.9	15.7	27.8
Financial condition (%)				
Long term debt/equity	0.0	0.0	0.0	0.0
Gross debt/equity	199	157	73	23
Equity/assets	27.9	32.8	51.7	71.5

Source: Is investment financial statements; ratios calculated by Fitch

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