FITCH AFFIRMS 4 LARGE PRIVATELY-OWNED TURKISH BANKS

Fitch Ratings-London-10 June 2016: Fitch Ratings has affirmed the IDRs, Viability Ratings (VRs) and Support Ratings of Turkiye Is Bankasi (Isbank), Akbank T.A.S. (Akbank), Yapi ve Kredi Bankasi (YKB) and Turkiye Garanti Bankasi (Garanti). The Outlook on YKB's Long-Term IDRs is Negative. The Outlooks on Akbank's, Isbank's and Garanti's Long-Term IDRs are Stable. A full list of rating actions is at the end of this rating action commentary.

Isbank and Akbank's 'BBB-' Long-term IDRs are driven by their standalone creditworthiness, as reflected by their 'bbb-' VRs. Garanti's and YKB's 'BBB' Long-term IDRs are driven by potential support from their controlling shareholders, Banco Bilbao Vizcaya Argentaria (A-/Stable) and Unicredit (BBB+/Negative), respectively. YKB's ratings are sensitive not just to Unicredit's ratings, but also to any decision by Unicredit to reduce or sell its stake in the bank.

The ratings of all four banks' subsidiaries are equalised with those of their parent institutions. Consequently, the Long-term IDRs of the subsidiaries of Isbank, Akbank and Garanti have been affirmed with Stable Outlooks, while the Outlooks on YKB's subsidiaries are Negative.

KEY RATING DRIVERS: IDRS, NATIONAL RATINGS AND DEBT RATINGS OF ISBANK AND AKBANK; VRS OF ALL FOUR BANKS
The 'bbb-' VRs of all four banks continue to reflect their still reasonable financial metrics in terms of performance and capitalisation, notwithstanding some weakening in 2015. They also consider the banks' strong franchises, which mean that any moderate deterioration in the operating environment should be manageable, in Fitch's view. We expect the domestic macroeconomic situation to be broadly supportive for sector loan growth and asset quality, and forecasts GDP growth at 3.5% in 2016 and 2017, but political tensions and security risks remain.

The banks' performance ratios remain adequate, despite having weakened in recent years. Reported returns on equity ranged from 8.8% to 12.8% in 2015, notwithstanding the difficult operating environment, higher loan impairment charges, margin pressure from competition, and the cumulative impact of regulation on profitability. Performance ratios have been supported by loan repricing, good cost efficiency and in 1Q16, a rise in business volumes. ROE rose strongly at Garanti (13.5%), YKB (12.1%) and Akbank (15.1%) in 1Q16 but fell at Isbank (10.7%) due to a one-off item.

Overall, Fitch considers the banks' loss absorption buffers to be sound and capital is of good quality. The banks' Fitch Core Capital (FCC) ratios fell by 50bp at Akbank (to 13.2%) and YKB (10.0%) and remained stable at Isbank (11.5%) and Garanti (12.5%) in 2015. FCC then rose slightly at all four banks at end-1Q16 post-Basel III implementation. There was uplift (by 65bp-85bp) to capital ratios in 2015 from the revaluation of fixed assets at YKB, Garanti and Isbank but this has not yet been implemented by Akbank.

Capitalisation is supported by the banks' still adequate internal capital generation and low levels of net non-performing loans (NPLs) to FCC. Pre-impairment profit is sound (ranging from 21% to 26% of the banks' equity bases in 2015) indicating significant capacity to absorb unexpected losses through income statements. Loan growth targets are also less aggressive than in preceding years, although internal capital generation could fall slightly short of banks' loan growth targets in the short term leading to moderate erosion of capital ratios. Capital ratios also remain sensitive to further depreciation of the Turkish lira.

Downside risks to the banks' asset quality, and therefore also performance, remain, notwithstanding their still reasonable headline asset quality ratios. NPLs (defined as loans overdue by 90 days) ranged from 2.0% to 3.9% of the banks' gross loans at end-1Q16, with Akbank, Isbank and Garanti outperforming the sector average (of 3.3%) in this respect. Regulatory group 2 watch list loans were generally manageable at between 2% and 3% of gross loans at end-1Q16. The exception was Garanti whose watch list loans rose to 4.4% from 2.8% at end-2014, but this partly reflected a single large loan. Regulatory group 1 but restructured loans ranged from 1.3% to 2.2% of gross loans at the four banks at end-1Q16, which Fitch also considers reasonable.

Specific reserve coverage of NPLs was an acceptable 75% at Isbank, Garanti and YKB at end-1Q16, and significantly above the sector average at Akbank (95%). However, total reserve coverage of NPLs and group 2 watch list loans (including specific and general reserves) was weaker at all banks at end-1Q16, ranging from a moderate 53% (Garanti) to 70% (Akbank, Isbank).

Fitch expects some weakening of asset quality ratios at all four banks given recent rapid loan growth, their high level of foreign currency (FC) loans (end-1Q16: between 36% and 42% of total portfolios at the four banks, including FC-indexed loans) and the sharp depreciation of the local currency in 2015. FC loans consist mainly of long-term exposures, often to weakly hedged borrowers, including some companies in vulnerable sectors such as energy-related project finance and tourism. As many are among the banks' largest exposures, they also bring concentration risk. However, these risks are mitigated by the fact that such loans are frequently to prime corporates in Turkey with diversified businesses and revenues. In addition, the long-term amortising repayment structures of these loans mean that any asset quality problems would feed through only slowly.

FC denominated wholesale funding, attracted mainly on international markets, is significant at all four banks (equal to between 21% and 29% of non-equity funding at end-2015), having risen significantly since 2011. This heightens FC liquidity risks, particularly given the sizable short-term component of this funding. However, the banks generally have sufficient FC liquidity (primarily placements with the Turkish Central Bank under the reserve option mechanism and maturing currency swaps) to cover liabilities falling due within one year, although a prolonged loss of market access could significantly strain their FC liquidity positions. Of the four banks, Fitch views liquidity risk as more moderate at YKB and Garanti as they would likely retain access to FC liquidity support from foreign shareholders in case of need. Akbank's FC liquidity coverage was weaker at end-2015 although it has since successfully rolled over a USD1.2bn syndicated loan. Fitch's base case is that the Turkish banks should continue to enjoy good market access.

YKB's and Isbank's subordinated notes ratings of 'BBB-' and 'BB+', respectively, are notched down once from the bank's IDR, in the case of YKB, and from the bank's VR in the case of Isbank, to include one notch for loss severity and zero notches for non-performance risk.

KEY RATING DRIVERS: YKB AND GARANTI's IDRS, NATIONAL RATING, SUPPORT RATING AND DEBT RATINGS
YKB and Garanti's IDRs and National Ratings are driven by potential support from Unicredit, via Unicredit Bank Austria (BBB+/Negative), and BBVA (A-/Stable), respectively. Unicredit Austria owns a 50% stake in YKB's holding company (which in turn holds an 82% stake in YKB). BBVA holds only a 39.9% stake in Garanti but has full management control via a majority of seats on the board of directors. Garanti is fully consolidated into BBVA's financial statements. Fitch considers Garanti and YKB to be strategically important subsidiaries for their parent banks, hence their Support Ratings of '2', which reflect a high probability of support in Fitch's view.

YKB is notched down once from its parent due to its high level of integration with Unicredit and longstanding status as a strategically important subsidiary of the group. Garanti is notched down twice from BBVA reflecting its recent acquisition and greater operational and management independence. The two notch difference for Garanti also reflects potential constraints on BBVA's ability to provide support to Garanti given the latter's size relative to BBVA (end-2015: equal to about 12% of group assets).

KEY RATING DRIVERS: AKBANK'S AND ISBANK'S SUPPORT RATINGS AND SUPPORT RATING FLOORS

Akbank and Isbank's '3' Support Ratings and 'BB-' Support Rating Floors (SRFs) are based on potential support from the Turkish sovereign (BBB-/Stable), reflecting their high systemic importance. The three-notch difference between Turkey's sovereign ratings and the SRFs reflects potential limitations on the authorities' ability to provide FC support, given the banks' sizable FC wholesale funding and the sovereign's moderate FC reserves.

KEY RATING DRIVERS: SUBSIDIARIES

The Long- and Short-term IDRs assigned to Akbank AG, Ak Finansal Kiralama A.S. Ak Yatirim Menkul Degerler A.S., Is Finansal Kiralama A.S., Is Faktoring A.S., Garanti Faktoring A.S., Garanti Finansal Kiralama A.S., Yapi Kredi Finansal Kiralama A.S., YapiKredi Yatirim Menkul Degerler A.S. and Yapi Kredi Faktoring A.S. and the Long-term National Rating of Is Yatirim Menkul Degerler A.S., are equalised with those of their respective parents, reflecting Fitch's view that they represent core, highly integrated, subsidiaries.

RATING SENSITIVITIES

VRS OF ALL FOUR BANKS; IDRS, NATIONAL RATINGS AND DEBT RATINGS OF ISBANK AND AKBANK

The VRs of all four banks remain sensitive to a marked deterioration in Turkey's economic performance, resulting in heightened pressure on the banks' asset quality, capital and/or liquidity positions. Likewise, if Turkish banks' access to wholesale funding markets became restricted (not Fitch's base case), resulting in a deterioration of FX liquidity position, this would also be a negative rating factor. Upside potential for the four banks' VRs is limited, given that they are already at the level of the sovereign rating. Isbank and Akbank's IDRs, National ratings and debt ratings are primarily sensitive to a change in the banks' VRs.

IDRS, NATIONAL RATING, SUPPORT RATING AND DEBT RATING OF YKB AND GARANTI

The Outlooks on YKB and Garanti's IDRs reflect those on their respective parents. A downgrade of Unicredit, which has a Negative Outlook, would result in a downgrade of YKB. Likewise a downgrade of BBVA would result in a downgrade of Garanti. A downgrade of Turkey's sovereign rating and revision of the Country Ceiling (BBB) would also result in a downgrade of the banks' Long-term FC IDRs. An upgrade of Garanti would require both positive rating action on BBVA and the raising of Turkey's Country Ceiling.

Unicredit has recently stated that it is considering different options to strengthen group capitalisation. While no plans have been announced, sale of stakes in listed subsidiaries, like YKB , is one possible option. If Unicredit decides to sell or reduce its stake in YKB, it would increase the likelihood of YKB's Long-term IDRs being downgraded by one notch to 'BBB-', the level of the bank's VR. However, if the stake in YKB was sold to a higher-rated shareholder, it could also be moderately positive for YKB's credit profile and result in the Outlook on YKB's Long-term foreign currency IDR being revised to Stable.

SUBORDINATED NOTES RATING OF ISBANK AND YKB

The notes' ratings are primarily sensitive to a change in the Isbank's VR and YKB's IDR. The ratings are also sensitive to a change in respective notching due to a revision in Fitch's assessment of the probability of the notes' non-performance risk or in its assessment of loss severity in case of non-performance.

SUPPORT RATINGS AND SUPPORT RATING FLOORS OF ISBANK AND AKBANK
The SRFs of Isbank and Akbank could be revised down if either (i) the Turkish sovereign is downgraded; (ii) the FC positions of the banks, or more generally Turkey's external finances, deteriorate considerably, or (iii) Fitch believes the sovereign's propensity to support the banks has reduced. The introduction of bank resolution legislation in Turkey aimed at limiting sovereign support for failed banks could negatively impact Fitch's view of support propensity, and hence the banks' SRs and SRFs, but Fitch does not expect this in the short term.

Upward revisions of the banks' SRFs are unlikely unless there is a marked strengthening of the sovereign's ability to support the banks in FC.

SUBSIDIARIES
The subsidiaries' ratings are sensitive to any changes in (i) the parents' ratings; and (ii) Fitch's view of the ability and propensity of the parents to provide support in case of need.
AAG's support-driven IDRs are also sensitive to a change in its strategic importance to Akbank.

The rating actions are as follows:

Turkiye Is Bankasi A.S. and Akbank T.A.S.
Long-term FC and local currency (LC) IDRs affirmed at 'BBB-'; Outlook Stable
Short-term FC and local currency IDRs affirmed at 'F3'
Viability Rating affirmed at 'bbb-'
Support Rating affirmed at '3'
Support Rating Floor affirmed at 'BB-'
National Long-term Rating affirmed at 'AA+(tur)'; Outlook Stable
Senior unsecured notes affirmed at 'BBB-'/'F3'
Subordinated notes (Isbank only) affirmed at 'BB+'

Turkiye Garanti Bankasi A.S.
Long-term FC and LC IDRs affirmed at 'BBB'; Outlook Stable
Short-term FC and LC IDRs affirmed at 'F2'
Viability Rating affirmed at 'bbb-'
Support Rating affirmed at '2'
National Long-term Rating affirmed at 'AAA(tur)' ; Outlook Stable
Senior unsecured notes affirmed at 'BBB'/'F2'

Yapi ve Kredi Bankasi A.S.
Long-term FC and LC IDRs affirmed at 'BBB'; Outlook Negative
Short-term FC and LC IDRs affirmed at 'F2'
Viability Rating affirmed at 'bbb-'
Support Rating affirmed at '2'
National Long-term Rating affirmed at 'AAA(tur)'; Outlook Negative
Senior unsecured debt affirmed at 'BBB'/'F2'
Subordinated notes affirmed at 'BBB-'

Akbank AG
Long-term FC IDR affirmed at 'BBB-'; Outlook Stable
Short-term FC IDR affirmed at 'F3'
Support Rating affirmed at '2'

Ak Finansal Kiralama A.S. and Ak Yatirim Menkul Degerler A.S.
Long-term FC and LC IDRs affirmed at 'BBB-'; Outlook Stable
Short-term FC and LC IDRs affirmed at 'F3'

Support Rating affirmed at '2'
National Long-term Rating affirmed at 'AA+(tur)'; Outlook Stable
Senior unsecured debt Long-term ratings affirmed at 'BBB-' (Ak Finansal only)
Senior unsecured debt Short-term ratings affirmed at 'F3' (Ak Finansal only)

Is Finansal Kiralama A.S. and Is Faktoring A.S.
Long-term FC and LC IDRs affirmed at 'BBB-'; Outlook Stable
Short-term FC and LC IDRs affirmed at 'F3'
Support Rating affirmed at '2'
National Long-term Rating affirmed at 'AA+(tur)'; Outlook Stable

Is Yatirim Menkul Degerler A.S.
National Long-term Rating affirmed at 'AA+(tur)'; Outlook Stable

Yapi Kredi Finansal Kiralama A.O., YapiKredi Yatirim Menkul Degerler A.S. and Yapi Kredi Faktoring A.S.
Long-term FC and LC IDRs affirmed at'BBB'; Outlooks Negative
Short-term FC and LC IDRs affirmed at 'F2'
Support Rating affirmed at '2'
National Long-term Rating affirmed at 'AAA(tur)'; Outlook Negative

Garanti Faktoring A.S. and Garanti Finansal Kiralama A.S.
Long-term FC and LC IDRs affirmed at 'BBB'; Outlook Stable
Short-term FC and LC IDRs affirmed at 'F2'
Support Rating affirmed at '2'
National Long-term Rating affirmed at 'AAA(tur)'; Outlook Stable

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Applicable Criteria
Global Bank Rating Criteria (pub. 20 Mar 2015)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=863501
Global Non-Bank Financial Institutions Rating Criteria (pub. 28 Apr 2015)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=865351