

Turkey  
Credit Analysis

# Is Yatirim Menkul Degerler AS

## Ratings

	Current Ratings
<b>National Long-Term</b>	AAA(tur)
<b>Sovereign Risk</b>	
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.	31 Dec 06	31 Dec 05
Total Assets (USDm)	385	274
Total Assets (TRYm)	542	368
Total Equity (TRYm)	153	139
Operating Profit (TRYm)	8	43
Published Net Income (TRYm)	16	26
ROAA (%)	3.5	8.6
ROAE (%)	10.8	21.6
Op Profit Margin (%)	15.4	50.4
Adjusted leverage (x)	1.9	1.4
Equity/assets (%)	51.7	71.5

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## Rating Rationale

- The National Long-Term Rating of Is Yatirim Menkul Degerler AS (Is Investment) reflects support it could expect to receive from its parent, Turkiye Is Bankasi AS (Isbank; National Rating 'AAA(tur)' /Stable Outlook) in case of need.
- Is Investment's core revenues include customer driven 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. Service revenues, which include all commission revenues from the clients as well as investment banking operations, are relatively more stable.
- In 2006 and 9M07, Is Investment focused more on new revenue sources for diversification, including futures market (FX and ISE-Index futures) and arbitrage through short-term ISE money market borrowings. Assets grew by a fast 115% in 9M07, driven mainly by these money market borrowings. The company listed its 29.7% shares on the ISE in 2007, through a capital increase. The IPO generated about TRY100m in cash proceeds, to be used for future organic growth.
- 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; yet Is Investment operates with more prudent internal limits.
- The company has no long-term debt, and short-term debt is met by short-term liquid assets. The short-term assets/short-term liabilities ratio on a standalone basis is a comfortable 118% as at 3Q07.

## Support

- In Fitch Ratings' opinion the strategic importance of Is Investment to its parent means that Isbank would provide support if needed. However, its ability to do so is moderate given its 'BB' Foreign Currency Long-Term IDR.

## Key Rating Drivers

- Is Investment's National Rating has a Stable Outlook, reflecting that on Isbank.

## Profile

Is Investment, 70% 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. 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. It is the market leader, with a 6.3% share in equity trading volumes and a 17.5% share in the derivatives market. It consistently holds one of the top three positions among brokerage houses in the fixed-income securities market, with 11.8% market share at end-2007.

- Investment banking arm of Isbank, closely integrated with the parent
- Market leader in equity and derivative trading and portfolio management
- Subject to regulation by the Capital Markets Board

## Profile

Is Investment was established by Isbank in 1996, as the investment 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 its 63.8% share. Together with other group companies, Isbank Group holds 70.3% of total shares. In 2007, Is Investment carried out an IPO and listed its 29.7% 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, increasing its stake in this company to 70%.

Is Investment shares its parent's brand name, logo and senior management. Isbank was established in 1924 as the first private commercial bank in Turkey to support the country's economic development. It had the second-largest asset-size and branch network in the sector at end-Q307. Its main business lines include retail, corporate, commercial and private banking and capital markets operations, whereas its financial participations provide services in insurance, private pension, asset management, venture capital, investment banking, real-estate investment trusts, leasing, factoring, brokerage and custody services.

At Is Investment, members of the board are drawn from the ranks of Isbank. The client base is composed of about 3,500 high-net-worth individuals, 300 corporate clients, 200 foreign institutional clients and the retail brokerage clientele of Isbank. It holds the market leader position, with a 6.3% market share in equity trading volumes and 17.2% in the derivatives market while holding consistently one of the top three positions in the bills and bonds market, with 11.8% at end-2007. The company has about TRY6.7bn assets under management, mainly through its asset management subsidiary. The company generates approximately 20% 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 also a fully-owned company, Maxis Securities, established in London with the aim of expanding its international business. The distribution network consists of five branches in major Turkish cities, two representative offices (one located in Kazakhstan) and over 900 Isbank branches acting as agents spread around the country. Being one of the founding members of Turkish Derivatives Exchange (Turdex), it holds 6% of the capital.

## Is Investment is organised around the following main divisions:

### *The Brokerage Group*

Active in trading securities including domestic and international equities, fixed-income and derivatives. In the international capital markets it trades Turkish eurobonds, corporate bonds, US and European equities ADRs, GDRs, bond and equity options, commodity futures and credit-linked notes. It also trades in the local derivatives market "Turdex futures" including equity, FX, interest rate and commodity futures along with OTC options.

**Table 1: Is Investment Shareholder Structure (as at Q307)**

Is Investment Shareholder Structure (as at Q307)	
(%)	
Isbank	63.78
Is Factoring	2.43
Is leasing	2.43
Cam Marketing	1.45
Camis Investment Hol.	0.17
Free Float	29.73
<b>Total</b>	<b>100</b>

Source: Is Investment

### *Investment Banking and Corporate Finance Group*

This division benefits from domestic knowledge and experience, as well as the distribution network that many competitors lack. This position has enabled it to win several mandates in 2007 where it was the sole or primary adviser. 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 46 M&A deals with a total amount of USD4.0bn since 2000. In 2007, with the completion of IPOs such as Tekfen Holding and Halkbank (the largest IPO of the year) the total amount executed reached USD1.9bn – well above the USD700m of 2006. However with the arrival of global investment banks into the market, competition has been intensifying.

### *Portfolio Management Group*

This division manages mutual funds and discretionary portfolio management activities. The group has 22% market share in the asset management market with funds under management of TRY6.7bn (USD5.4bn) at end-Q307.

### *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 there's an intention that this may be upgraded to "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. Its increasing volume of business in the derivatives market and access to international markets through its UK subsidiary should help towards that end. Furthermore it is making a significant investment in human resources and also plans to open new branches domestically to increase its ability to cater to its expanding client base's needs.

### **Presentation of Accounts**

Unless otherwise stated, all references in this report are to the bank's consolidated financial statements in accordance with CMB regulations. Consolidated interim figures are also in accordance with CMB regulations.

### **Performance**

Is Investment's core earnings include customer-driven revenues and net trading revenues generated from equities, bonds, mutual funds derivative instruments. Volumes are mainly driven by proprietary trading; however these operations tend to be volatile and this affects margins (see Table 1). Indeed, despite the 42% annualised growth rate in trading volumes in 9M07, the company recorded net losses from proprietary trading in the same period, compared with a breakeven in 2006; whereas these operations had generated TRY33m net revenue in 2005. Service revenues, which include all commission revenues from the clients as well as investment banking operations tend to be more stable. The adjusted annualised growth (adjusted for the acquisition of Is Portfolio) of net service revenues in 9M07 was 13.4%, partly compensating for the loss-making trading operations<sup>1</sup>.

- Volatile operational earnings
- Fast asset growth is driven by ISE money market borrowings

<sup>1</sup> The company acquired 50% of Is Portfolio in June 2007, increasing its stake to 70% from 20%. As a result, it also started full consolidation as of that date. Although not very significant, this transaction synthetically boosts the revenues and income in 9M07, ie making up 4.8% of earnings.

Starting in 2006, and increasingly in 2007, the company started to make use of alternative revenue sources to enhance earnings diversification. Accordingly, the company focused more on trading of FX futures and ISE-Index futures. In this segment, Is Investment generated a net pre-tax income of about TRY16.5m in 9M07 and about TRY10m in 2006.

Another line that is increasingly being utilised is the ISE money market for short-term borrowing. These funds are then deposited in various banks so as to benefit from the arbitrage and earn a spread. This practice helped to generate about TRY3.9m net pre-tax income in 9M07 and about TRY5.8m in FY06. Is Investment's assets grew by a fast 115% in 9M07, driven mainly by these money market borrowings. Receivables and payables from/to customers are a result of outstanding transactions to be realised, which has no impact on operations, as the receivables meet the payables at the same maturity.

### Costs

The costs are mainly salaries and administrative expenses. In 9M07, costs increased by an annualised 28%, in line with the revenues. Due to the one-off expenses during the IPO, marketing expenses were hiked by 80% in 9M07. Despite the fact that costs are relatively stable in absolute terms, efficiency ratios (as well as profitability ratios) are volatile due to the volatile nature of earnings.

**Table 2: Is Investment P&L & Performance Ratios**

(TRYm)	30 Sep 07	31 Dec 06	31 Dec 05	31 Dec 04
Gross Revenues	51.5	52.3	85.5	82.2
- of Which sales of Equities <sup>a</sup>	-17.8	-6.9	15.1	12.8
- of Which sales of Private and Public bonds <sup>a</sup>	10.1	5.1	16.7	19.3
- of Which sales of Treasury Bills <sup>a</sup>	1.5	3.8	0.8	7.8
- of Which sales of Mutual Funds <sup>a</sup>	4.3	-0.1	0.0	0.0
- of Which service revenues	53.2	50.5	52.9	42.4
Operating Profit	9.0	8.1	43.1	42.9
Op. EBITDA	9.5	9.0	44.7	44.9
<b>Ratios</b>				
Op Profit Margin	17.5%	15.4%	50.4%	52.1%
EBITDA Margin	18.4%	17.2%	52.3%	54.6%
ROAE	14.7%	10.8%	21.6%	5.1%
Compensation/Net Revs	38.2%	39.0%	17.5%	15.1%
Prop. Income/Net Revs	-3.7%	3.6%	38.1%	48.5%

<sup>a</sup> Net of costs, excludes financial income  
Source: Financial Statements, adapted by Fitch

### Prospects

Is Investment is the leading securities and brokerage house in Turkey, offering a wide range of financial services to meet the needs of individuals and corporates. The domestic franchise is one of the strongest, backed by Isbank's widespread branch network. However, due to the volatile nature of the business, the profitability will be volatile at times, despite the relative stability of service revenues.

### Risk Management

Is Investment has an independent risk management department reporting to the board of directors through an audit committee; it simultaneously provides information to senior management. The company is the first among all brokerage houses in Turkey to have a dedicated risk management department. 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. Risk management practices are constantly being strengthened in areas such as asset-liability management.

- First to have a dedicated risk management in Turkey, among all local brokerage houses
- Trading and margin limits set by the regulator. Internal limits are even more prudent
- Risk management practices under development still

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 position limit of USD3.6bn was approved for 85 international and 17 domestic corporate counterparties as at end-2007. According to CMB regulations, credits extended for brokerage business are to be used by customers to purchase capital market instruments traded on the ISE. Trading limits are set by the CMB; however, Is Investment operates with 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 TRY234.2m as of end-2007, of which TRY44.8m was utilised. The liquidity and concentration of securities subject to credit risk can be volatile, and these are monitored by 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 on a daily basis to senior management. A stop-loss limit of the lower of TRY2.5m total trading position or a 10% reduction in value is in place. Intra-day limits for both bonds and equities are calculated as a multiple of projected liquidity and are based on detailed cash flow forecasts. Trading limits for the portfolios are determined by the fund management department as a position amount with duration sensitivity. Separate VaR and stress limits on the portfolio will also be introduced by the end of Q108. The proprietary trading limit on the TRY fixed-income portfolio and TRY equity shares are equivalent to 30% and 20% of equity, respectively. The actual positions were standing at around 1% of capital, well below these limits, at end-Q307. The company does not speculate on the FX market and had a fairly well matched FX position at end-Q307. Total assets VaR is calculated by historical simulation method using a 99% confidence level and a one-day holding period, which has fluctuated between TRY3m and TRY0.95m over the past 12 months, including correlation adjustments.

### 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 are monitored, covering an array of operational risks (regulatory, IT, legal, personnel, etc). New products are all subject to a rigorous review process. The bank has a disaster recovery centre and system backup storages in Ankara.

### Funding and Capital

Is Investment has no long-term debt, and short-term debt is covered by short-term liquid assets. The short-term assets to short-term liabilities ratio was a comfortable 118% at Q307. Is Investment borrows from the ISE money market and ISE clearing bank and has letters of guarantee from Isbank (Q307: TRY284.7m). Funding also comes from resources such as short-term customer payables and customers prepayments arising in the course of its business. Cash-flow forecasting and liquid asset cover of short-term liabilities is used for liquidity management purposes. Is Investment also relies on its parent bank for daily liquidity facilities, and an intraday liquidity window of TRY50m from Isbank is often used. A new system of asset-liability management is being developed to enable the head of trading to monitor cash flow requirements in different maturity brackets.

Is Investment's balance sheet is linked to its trading activity levels and is liable to rapid increases or decreases. This brings an element of volatility to capital/leverage ratios. The company maintains a high level of free capital, equal to 50% of total equity at end-Q307. Despite the capital increase during the IPO, the equity/total assets ratio stood at a moderate 33.8% at end-Q307 (2006: 51.7%).

- Leverage is volatile, dependent on trading activity
- Liquidity facility used from parent bank
- Capital increase with the IPO

**Table 3: Leverage/Debt Service (Consolidated)**

Absolute values (TRYm)	9M07	FY06	FY05	FY04
Assets	1,165	542	368	247
Equity & tangible equity	394	280	264	211
Gross LT debt (A)	0	0	0	0
Cash (B)	467	172	57	8
Net LT debt/(cash) (A-B)	-467	-172	-57	-8
Op. EBITDA	9	9	45	45
EBITDA-capex	8	7	44	45
<b>Ratios</b>				
Equity/assets (%)	33.8%	51.7%	71.5%	85.7%
Adjusted leverage <sup>a</sup> (x)	2.87	1.92	1.38	1.16
LT debt/tang. equity (%)	0.0%	0.0%	0.0%	0.0%
LT debt/cash (%)	0.0%	0.0%	0.0%	0.0%
LT debt/op. EBITDA (%)	0.0%	0.0%	0.0%	0.0%

<sup>a</sup> Assets less reverse repo/equity  
Source: Financial statements

## Appendix A

### Is Investment (Consolidated)

(TRYm)	30 Sep 07	31 Dec 06	31 Dec 05	31 Dec 04
<b>Assets</b>				
Cash and Cash Equivalents	467	172	57	8
Securities Owned, at Market or Fair Value	238	206	218	204
Receivables From Brokers & Customers	426	128	70	13
Receivables From Related Parties	1	1	1	0
Long-term financial assets	14	22	19	18
Land, Furniture, Equipment, Building and Intangible assets	4	3	3	4
Goodwill	11	-6	-6	-3
Other assets	3	17	7	1
<b>Total Assets</b>	<b>1,165</b>	<b>542</b>	<b>368</b>	<b>247</b>
<b>Liabilities</b>				
Financial Borrowings	13	15	24	0
Money market borrowings	400	189	36	0
Payables to Brokers and Customers	349	49	38	30
Other Liabilities	10	9	7	6
<b>Total Liabilities</b>	<b>771</b>	<b>262</b>	<b>105</b>	<b>35</b>
Share Capital	119	97	97	45
Reserves and past profits	95	40	16	56
Profit & Loss Account	21	16	27	5
<b>Total Equity</b>	<b>236</b>	<b>153</b>	<b>139</b>	<b>107</b>
Minorities	158	128	125	105
<b>Total Liabilities and Net Worth</b>	<b>1,165</b>	<b>542</b>	<b>368</b>	<b>247</b>

Source: Is Investment financial statements

**Is Investment (Continued)**

	30 Sep 07	31 Dec 06	31 Dec 05	31 Dec 04
<b>Revenues</b>				
Equity, securities and mutual funds trading	-1.9	1.9	32.6	39.9
Service revenues	42.8	43.9	49.7	39.7
Financial and other income/(expenses) (net)	54.8	24.9	28.5	5.2
<b>Total Revenues</b>	<b>95.7</b>	<b>70.6</b>	<b>110.8</b>	<b>84.8</b>
<b>Expenses</b>				
Service Expenses	0.6	1.9	11.3	10.1
Employee Compensation	19.6	20.4	15.0	12.4
Marketing	4.3	3.2	2.5	3.6
General and Administrative	17.5	17.8	12.0	11.1
Amortisation and Depreciation	0.5	0.9	1.6	2.0
<b>Total Expenses</b>	<b>42.5</b>	<b>44.3</b>	<b>42.4</b>	<b>39.4</b>
<b>Net Income Before Income Taxes and Minorities</b>	<b>53.3</b>	<b>26.4</b>	<b>68.4</b>	<b>45.4</b>
Minorities	26.8	8.4	34.4	13.3
Income Taxes	5.3	2.2	7.6	5.3
<b>Net Income</b>	<b>21.2</b>	<b>15.8</b>	<b>26.5</b>	<b>26.8</b>
<b>Ratios Summary</b>				
Average Assets	854	455	307	123
Average Equity	194	146	123	107
Short Term Borrowings (Mainly money market and Bank Loans)	412	203	60	0
Long Term Debt	0	0	0	0
Net financial and other income	55	25	29	5
Proposed Dividends	0	1	2	3
<b>Profitability (%)</b>				
Return on Average Assets (ROAA)	3.3%	3.5%	8.6%	4.5%
Return on Average Equity (ROAE)	14.7%	10.8%	21.6%	5.1%
Compensation/Total Revenues	38%	39%	17%	15%
Total Revenues/Average Assets	8.0%	11.5%	27.8%	66.7%
<b>Financial Condition (%)</b>				
Long Term Debt/Equity	0.0%	0.0%	0.0%	0.0%
Gross Debt/Equity	104%	73%	23%	0%
Equity/Assets	33.8%	51.7%	71.5%	0.6%

Source: Is Securities Financial statements; ratios calculated by Fitch

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