




FROM BEIJING TO BUDAPEST

Winning Brands, Winning Formats*

2005/2006

4th Edition

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PRICEWATERHOUSECOOPERS 



Turkey

Turkey

ECONOMIC OVERVIEW

Turkey is one of the largest economies in the region, with a population of 70 million and a GDP of around EUR240billion. Turkey's geographical proximity to Europe, dynamic business environment, liberalised markets, young and productive population, increasing urbanisation and unsaturated market structure, all make the country attractive for international investors.

Turkey's vibrant economy is a complex mix of modern industry and commerce along with a traditional agriculture sector that in 2004 accounted for 11% of GDP. It has a strong and rapidly growing private sector. While the state still plays a significant role in basic industry, banking, transport and communication, serious steps have been taken towards the liberalisation and privatisation of these sectors. The most important industry – and largest exporter – is textiles and clothing, followed by white goods, brown goods and automotive, which are almost entirely in private hands.

The disinflation trend and interest rate cuts have fuelled consumption during recent years. The economy has been marked by erratic economic growth, booming foreign trade and increasing foreign interest. Real GNP growth

reached its highest level in almost four decades, while the Productivity Index increased from 100 to 150 in 2004. Meanwhile, the public sector fiscal deficit has stabilised due to increasing tax revenue.

Located at the crossroads of Europe and Asia, Turkey has historically played a critical role as a bridge between the East and the West. Turkey is a member of major international organisations, including NATO, OECD, UN, IMF and WTO, and is now seeking to integrate with the EU.

In December 2004, Turkey's long wait for EU membership reached a satisfactory point with the EU formally approving the opening of membership talks.

GDP and CPI

Turkey's economic growth soared in 2004 at the fastest pace in nearly four decades. The real GDP grew by 7.5%. With some help from the strong lira, Turkey's per capita GDP surged to EUR3,360 (EUR6,220 in PPP terms).



Area ('000 sq km)¹: 774.8
(US 9,600 – EU25 3,981 – World 133,700)

Capital²: Ankara
(Number of inhabitants: 4 million)

Population (million)³: 72.3
(US 293 – EU25 456 – World 6,376)

GDP (USD billion)³: 302
(US 11,735 – EU25 12,723 – World 39,503.5)

GNI per capita (USD)¹: 2,800
(US 37,870 – EU25 22,810 – World 5,110)

Currency: Turkish New Lira (TRY)

Languages: Turkish (official), Kurdish, Arabic, Armenian, Greek

Main religions: Muslim

Government type: Republican parliamentary democracy

Sources: CIA Factbook; (1) World Bank 2005; (2) City Population; (3) Economist Intelligence Unit 2004 data

The strong growth was supported by a 45% increase in private sector investments and a 10% increase in consumer spending. Improved business sentiment and positive expectations were responsible for the dramatic increase in private sector investment, while consumer spending soared due to a realisation of postponed demand, especially in consumer durables and motor vehicles. A strong increase in inventory accumulation suggests the production sector is confident about the sustainability of strong demand. Impressive foreign trade figures, which rose 25% in imports and 13% in exports, were another factor in the strong growth experienced in 2004.

Turkey's economic outlook has been positive with declining inflation, which is at its lowest in more than 30 years, a strong economy and productivity growth. While economic growth is expected to slow down and consumer demands reduce to more reasonable levels, forecasted growth is still strong at 5% in 2005.

Inflation fell below the government's target rate in 2004, despite strong consumption demand and rising petroleum prices, with CPI hitting its lowest level in more than three decades and stimulating expectations for interest rate cuts.

GDP and CPI

	2001	2002	2003	2004
GDP growth (%)	-7.5	7.9	5.8	8.9
CPI (%)	54.4	45.0	25.3	8.6

Source: EIU, August 2005

Unemployment

No improvement was observed in the unemployment rate, which was a drawback of the increase in productivity, despite strong economic growth since 2002. On the other hand, the job market is expected to recover in 2005 with companies likely to begin the employment process having almost filled up idle capacity. As of end-2004, the working population was 21.8 million and the unemployment rate was 10.3%. In order to meet employment demands of a workable population, the Turkish economy needs to grow by at least 5% per year.

Unemployment

	2001	2002	2003	2004
Unemployment rate (%)	8.5	10.4	10.5	10.3

Source: EIU, August 2005

Economic forecasts

The Turkish economy is expected to continue to enjoy strong growth and low inflation rates. The main assumption is that the implementation of current prudent policies and reforms will continue together with Turkey's EU integration process. Declining indebtedness and borrowing requirement of the government, and a reduction of real interest rates will stimulate investment in the real economy.

Key economic forecasts

	2005	2006	2007
GDP (%)	4.9	3.9	5.7
CPI (%)	8.4	9.6	8.1
Unemployment rate (%)	10.0	10.4	9.9

Source: EIU, August 2005

REGULATORY ENVIRONMENT

Foreign direct investment

Despite its strong potential, Turkey has not benefited much from increased foreign direct investment (FDI) flows brought on by globalisation. Until 2004, annual inflows of FDI amounted to less than 0.5% of GDP. In order to improve Turkey's attractiveness, a new FDI Law

was adopted in 2003, and other efforts have been made by the Turkish authorities to increase the transparency and effectiveness of business. These efforts, together with Turkey's improved outlook and approval of EU membership negotiations, have contributed to a significant increase in FDI in 2004. FDI almost doubled in 2004, reaching EUR2.1 billion. There is strong ongoing interest

in Turkish assets, which is expected to result in significant inflows in the following years.

The Turkish lira is transferable and convertible, exchange controls are liberal and capital earnings after taxes can be freely repatriated. Almost all industries are open to foreign investment and 100% foreign ownership is permitted both in the formation of new businesses and in the acquisition of existing businesses.

While a new FDI Law, approved in June 2003, was designed to simplify procedures, other legislation still needs to be harmonised in the fields of public procurement, taxation, IP rights, anti-trust policy, monitoring of state aid and the adjustment of state monopolies. Under the government-initiated “Reform Programme for the Improvement of the Investment Environment in Turkey”, ten inter-ministerial technical committees comprising public and private sector representatives have proposed a substantial number of amendments in a number of legislative instruments affecting the investment environment.

According to the new FDI Law, entry conditions for foreign investors establishing a company in Turkey are the same as for comparable local companies. Key aspects of the Law include:

- Elimination of bureaucratic details with regard to screening, approval, share transfer and minimum capital requirements
- Reassurance of existing guarantees to foreign investors of their rights
- Redefinition of “foreign investor” and “foreign direct investor” in line with international standards
- A policy shift from “control” to a “promotion and facilitation” approach
- Guarantees for investor rights
- Equal rights and treatment between Turkish companies and foreign companies established in Turkey

FDI

	2001	2002	2003	2004
FDI (TRY bn)	4.4	1.4	2.1	3.4
FDI (USD bn)	3.3	1.04	1.6	2.6

Source: EIU, August 2005 (Exchange rate: December 31, 2004)

Expected impact following EU entry

Turkey has demonstrated considerable progress since the European Council approved the country’s candidacy for accession in December 1999. Political reforms have been introduced by means of a series of constitutional and legislative changes adopted since then. There have been two major constitutional reforms in 2001 and 2004, and eight legislative packages were adopted by Parliament between February 2002 and July 2004. New codes have been adopted, including a Civil Code and a Penal Code. Numerous other laws, regulations, decree and circulars were issued, and the government has taken major steps to achieve better implementation of the reforms.

At the same time, Turkey has made considerable progress towards being a functioning market economy – in particular by reducing its macroeconomic imbalances – while the resilience of the Turkish economy has significantly increased.

Continuation of the ongoing reform process is vital to transform the current positive dynamics into sustained growth and stability.

Property/Real estate regulations

Real estate acquisition of foreign real and legal persons has been regulated in Article 35 of the Land Registry Law numbered 2644, which was modified by Article 19 of the new Law numbered 4916 approved in July 2003.

The new Article 35 reads: “With the reservation of being reciprocal and complying with legal restrictions, real persons of foreign nationalities and trade companies having with a legal personality established in foreign countries according to the laws of these countries, can acquire real estate within the boundaries of the Republic of Turkey. In the implementation of the reciprocity principle, it is essential that real estate acquisition rights given by a foreign country to its own citizens and to trade companies established in foreign countries according to the laws of those countries are also given to the citizens and trade companies of the Republic of Turkey.”

This amendment eased requirements for foreigners buying property in the country. The number of foreign citizens owning real estate has increased by some 7,000 since then. According to a report of the Turkish General Directorate of the Land Registry, a total 44,740 foreigners from 68 countries own real estate property in 70 Turkish provinces as of August 2004. Individuals who have already received the title deed of the property will not be affected.

The Constitution Court annulled Article 19 of the new Law numbered 4916 in April 2005. The annulment decision of the Constitution Court shall become effective after three months of its announcement date in the Official Gazette.

Other regulations

Competition Law

Turkish law prohibits unfair competition in a very general manner. It provides for injunctions and compensation of damages to a person who suffers as a result of its competitor's actions, which includes misrepresentation and other sanctions that are contrary to good faith principles. The Turkish Commercial Code defines unfair competition as the misuse of competition in a financial sense, through misleading actions, untrue statements or any other type of action that is not in accordance with good faith principles.

The Anti-Dumping Law is designed to protect the competitive nature of the market economy against foreign-sourced dumping activities, or foreign-sourced trade incentives.

Regarding competition, the Protection of Competition Law provides that any agreement between persons engaged in any industry in Turkey that restricts the competitive nature of the market or misuse of power can be subject to preventive action by the authorities.

One of the most common applications of the competition rules is during M&A transactions. It is unlawful and prohibited for one or more enterprises to merge in a manner that impedes market competition within the goods or services sector, in whole or in certain parts of the country, in order to create and strengthen a dominant position.

Tax and VAT

Direct and indirect taxes are applicable in Turkey. Direct taxes are corporate tax and individual income tax, while indirect taxes consist of taxes on wealth and expenditure. Taxes on wealth range from inheritance and gift taxes to motor vehicle and property tax. Taxes on expenditure include value added tax (VAT), special consumption tax, banking and insurance transaction taxes, and minor municipality taxes.

Companies whose legal or business headquarters are located in Turkey, or whose operations are centrally managed from Turkey, are subject to corporation tax on

worldwide income. The corporate tax rate applicable on corporate tax base connected with the taxable income is 30%. A 10% withholding tax applies to dividends distributed by resident corporations to real and legal persons.

The implementation of VAT is similar to practices in EU countries. As a rule, all deliveries of goods and services that take place in Turkey are subject to VAT. Goods and services imported to the country are also subject to VAT, while exports are exempted. The Council of Ministers has the authority to raise VAT rates to a maximum rate of 40% or to reduce them to 1%.

Store openings

The regulation of supermarket establishments is conducted through city planning and development law, and overseen by the government. There are no limitations on opening hypermarkets in city centres; the only problem is finding a convenient location.

The draft Retail Law, which has made it onto the government's agenda from time to time over the past three years, would bring certain restrictions on store openings. However, the organised retailing sector is still underdeveloped in Turkey. Therefore, the draft Law is expected to remain shelved for the time being, especially with global retailers pressuring the government. According to the new draft Retail Law, existing stores will be allowed to remain at their current locations, but the establishment of new stores in metropolitan areas will require the approval of the governor's office for stores smaller than 2,500sq m and the Minister of Industry and Commerce for stores larger than 2,500sq m.

Imports

The party liable for the payment of VAT is the importing party in the case of imports. VAT paid can be offset against output VAT if the import transaction is directly related to their business activities. In addition, a Special Consumption Tax is levied on the delivery, first acquisition or imports of different kinds of goods. Incentive measures exist to ensure that imported machinery and equipment within the scope of an incentive certificate are imported to Turkey with full exemption from custom duties and fund levies. Since most machinery and equipment imported from the EU has been exempt from customs duties due to the customs union, this exemption applies mainly to imports from outside the EU. Imported raw materials, intermediary goods and packaging materials used in the production of goods to be exported are also exempt from customs duties, VAT and other charges.

DEMOGRAPHICS AND CONSUMER BEHAVIOUR

Population

Population evolution

According to the latest data, Turkey's population is more than 70 million. The population is concentrated in the coastal and agricultural areas.

Population

	2001	2002	2003	2004
Population (m)	69.3	70.3	71.3	72.3

Source: EIU, August 2005

Population by age group

Turkey's population is relatively young, with 15-64 year olds accounting for 69% of the population.

Age profile

% of total population	1998	2003	2008 (f)
0 – 14 years	30.4	27.2	24.4
15 – 64 years	63.9	66.4	68.6
Over 65 years	5.7	6.4	7.0

Source: EIU, September 2004

Urbanisation of the population

Turkey's urbanisation rate gained momentum in the 1990s, rising to 78% in 2003 from 73% in 1998, and it is expected to reach 83% in 2008.

Urban/Rural split

% of total population	1998	2003	2008 (f)
Urban	72.9	77.9	82.5
Rural	27.1	22.1	17.5

Source: EIU, September 2004

Income/Buying power

Annual average income increased steadily YoY, as did expenditure and savings.

Annual average income, expenditure and savings rate per capita

	2002	2003	2004	2003–2004 (%)
Income (TRY)	4,059	5,179	6,054	17
Expenditure (TRY)	3,385	4,378	4,966	13
Savings* (TRY)	673	801	1,087	36

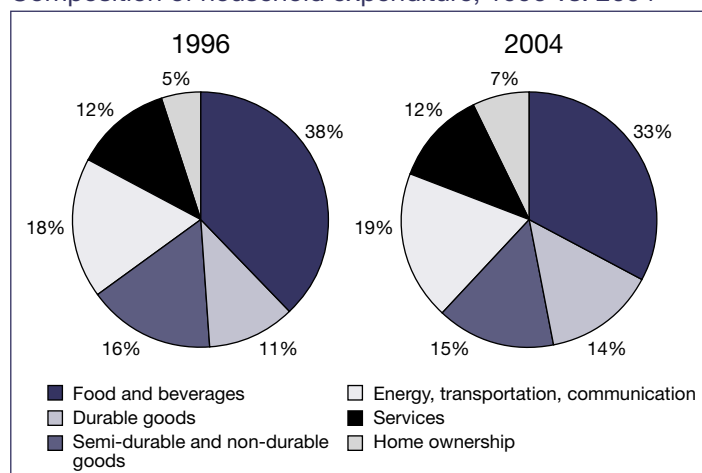
Source: State Institute of Statistics; *Defined as fixed capital formation

Consumer behaviour

Average household spending patterns

According to research conducted in 1996 by the State Institute of Statistics, an average consumer spends 38% of his/her income on food and beverages, 11% on durable goods, 16% on semi-durable and non-durable goods, 18% on energy, transportation and communication, 12% on services and 5% on home ownership. According to 2004 results, spending on food and beverages declined while spending on durable goods and home ownership increased during the eight-year period.

Composition of household expenditure, 1996 vs. 2004



Source: State Institute of Statistics

Lifestyles/Shopping habits

Consumer behaviour shows the increasing popularity of shopping malls. In Turkey, half the population is under the age of 25 and the younger population prefers more leisure-focused, one-stop shopping malls to traditional high street shopping. Istanbul has many sizeable shopping malls, with many others presently under construction.

Though Turkey has traditionally eschewed imports, its food consumption patterns are changing as per capita income grows, urbanisation rates increase and the rise in the number of women in the workplace influences food trends. Urban consumers, who are receptive to imports, are more aware of international trends, have higher incomes and transportation to the larger stores. In this respect, locally-owned retail chains tend to be concentrated in smaller towns where imports do not fare as well.

Another important trend has been the increase in consumption fuelled by declining inflation and increased purchasing power. Demand for durable goods, especially cars and white goods, has surged due to decreasing interest rates on consumer loans and credit cards.

Brand/Price sensitivity

Consumer behaviour has been changing rapidly, partly as a reflection of strong international trends for consumer rights and the entrance of international companies into the Turkish market, and partly due to increasing competition. The saying “the customer is king” has been gaining ground in Turkish markets. Companies, brands and salespeople who do not act accordingly are challenged strongly in the media and other public domains.

RETAIL & CONSUMER SECTOR PERFORMANCE

Major consumer goods players

In Turkey, expenditure on food and beverages accounted for 33% of total consumer expenditure in 2004, compared to 36% in 2003. Turkish white goods and consumer electronics industries are well developed and mainly export-oriented, with many domestic companies producing a wide range of white goods and electronic goods under licences from various large international companies.

During the past ten years, local producers have faced strong competition among themselves and from big international companies such as Unilever, Coca Cola, Nestlé, Philip Morris, BAT, JTI, Bosch, Siemens, Procter & Gamble and Gillette. This competitive phase has seen the weaker local companies eliminated. The survivors have continued to be market leaders against international competitors, and have built up good reputations in Central European and Middle Eastern markets.

Major consumer goods players

Ranking	Top local players	Category of products	2004 net sales (EUR m)
1	Koç Holding (Arçelik, Beko, Aygaz and Türk Demirdöküm brands)	White goods	3,485
2	Tekel (Turkish state monopoly in tobacco)	Cigarettes, cigars	2,425 (2003)
3	Zorlu Holding (Vestel brand)	White goods	2,411
4	Ulker	Food and beverages	912
5	Efes Pilsen	Beer	752
6	Yaşar Group (Pınar brand)	Dairy products, meat and mineral water	397
7	Gidasa (Piyale brand)	Food and beverages	212
8	Koç Holding (Maret, Pastavilla and Tat brands)	Food and beverages	208
9	Eczacıbaşı	Home and personal care products	145 (2003)
10	Sütaş	Dairy products	114

Source: Company data and derived from AMPD

Major retail players

The classification of food retail outlets in this report is based on outlet size in square metres (sq m):

Hypermarkets – more than 2,500sq m

Large supermarkets – between 1,000 and 2,500sq m

Supermarkets – 400 to 1,000sq m

Small supermarkets – less than 400sq m

Medium markets – 100 to 50sq m

Bakkals – 50sq m or less

Market share evolution by retail format

With a per capita income of USD2,248 in 2004 (EUR1,932 in 2003), the average Turkish consumer usually shops in small, traditional, specialised, neighbourhood retail food outlets called “bakkals”, which sell fresh and prepared foods, and other products; and bazaars, where food prices are relatively low. A consumer’s food budget is mainly allocated to bread, rice, potatoes, vegetables and pasta products. For the entire population, processed foods make up only 15-20% of total consumption.

The longstanding popularity of bazaars is enhanced by convenient locations and lower prices for a variety of consumer products, such as fresh fruits and vegetables. Though few products at these outlets are imported – prices for imported processed goods are extremely high

– some fruit is generally not available domestically, such as bananas, kiwis, pineapples, mangos, papayas and, more recently, apples. Imported dried beans and rice are also available since domestic supplies fall short of demand.

The Turkish retail market is still in the hands of traditional retailers, despite the strong growth achieved by organised retailers over the past five years. Only a small segment of the population can afford to shop in modern retail outlets. Industry sources estimate that only five to seven million people do the majority of their shopping in modern retail outlets.

Traditional retailers accounted for 63.5% of the market in 2004, while organised retailers captured 36.5% of the market (28% in 2003). Forecasts show that by 2010, traditional retailers will have 45% of the market and organised retailers 55%. Turkey’s top-five retailers’ combined market share was only 22.5% in 2004 (Table 13), compared to an average of 40% in EU countries for the same period.

Total retail sales growth

	2002	2003	2004
Total sales (EUR m)	73,250	76,700	95,900
Growth rate (%)	21.0	4.7	25.0

Source: Company data and derived from AMPD

Breakdown by number of stores

	Hypermarkets	Large supermarkets	Supermarkets	Small supermarkets	Medium markets	Bakkals
2004	152	396	1,082	3,179	15,197	122,781
2003	143	367	968	2,764	14,537	124,283

Source: Company data and derived from AMPD

Market share by retail channels

%	Hypermarkets	Large supermarkets	Supermarkets	Small supermarkets	Medium markets	Bakkals
2004	10.0	11.5	13.4	13.8	7.7	32.1
2003	10.4	11.4	12.1	12.7	8.3	33.1

Source: Derived from AMPD

Trends in products and services provided by the major chains include private-label food items, phone and internet purchases, delivery and membership cards. Since bakkals have traditionally provided a delivery service, and the minimum purchase level is relatively low, supermarkets hope this service will increase their customer base. In order to increase their sales, large supermarkets have increased their advertising spend and have started various promotional campaigns. Although the combined market share of bakkals and medium markets decreased from 41.4% to 39.8% in 2004, this segment continues to boast more than EUR8bn in annual sales. However, the growth in larger outlets is negatively affecting bakkals and an increasing number of them are closing.

After the recovery period from 2001 to 2003, food sales grew by almost 25% in 2004 (4.7% in 2003) in real terms. Such growth is partly attributable to the real appreciation of the TRL (the previous currency).

Despite the slower growth since the crisis in 2001, hypermarkets and supermarkets continue to be among the most dynamic sub-sectors. While existing food retail chains started to consolidate or continued opening new stores, new international chains acquired local chains or established their own stores. For example, very recently Migros acquired 70% equity stakes of Tansas and Carrefour bought 60% equity stakes of Gima, both local retail chain operating in the hyper and supermarket segment with total of 335 stores.

Hard discount stores have also started to grow rapidly since 2001. These formats have benefited from a shift in consumer preferences towards lower-priced goods.

Scope of organised retailing by retail format

Throughout 2003 and 2004, organised retailers were able to develop organically. The consensus is that further organic growth can be maintained in the following years, despite the Turkish food retailer market being overcrowded and ready for consolidation.

The organised retail market in Turkey is shared chiefly by four domestic chains and three multinational firms, as well as a number of other medium-scaled retailers that constitute some 22.5% of the market. The significant domestic players are Migros, which operates in hypermarket, supermarket and discount formats under the Migros, Sok, Tansas and Makro brands, Yimpaş and BIM, the hard-discount markets operator. One of the multinational players is the Carrefour Group, a JV of Sabanci Holding and Carrefour of France. CarrefourSA operates ChampionSA hypermarkets, Gima supermarkets, and the DiaSA and Endi discount stores. Metro Group operates Cash&Carry stores as well as the Real hypermarkets and the Praktiker DIY stores. Tesco also entered the market in the last quarter of 2003, acquiring majority stakes in Kipa – the Aegean region’s hypermarket operator.

Key food retailers

Store brands	Retail formats	Group name	2004 sales (EUR million excl. VAT)	Number of stores
Migros SOK Tansas Makro	Hyper, super & discount stores, e-trade	Koç Holding	1,629 (1,041 + 588)	283 Sok 180 Migros 206
CarrefourSA ChampionSA DiaSA Gima Endi	Hypermarkets Supermarkets Discount stores Supermarkets Discount stores	Carrefour & Sabancı Holding	1,087 (702 + 385)	11 CarrefourSA 7 ChampionSA 239 DiaSA 79 Gima 50 Endi
BIM	Hard discount stores	N/A	N/A	1,097
Metro Real	Cash & Carry Hypermarkets	Metro Group	669 (486 + 183)	9 Cash & Carry 7 Real
Yimpaş	Hyper & supermarkets	Yimpaş Holding	N/A	65
Tesco-Kipa	Hypermarkets	Tesco Plc	220	5
Kiler	Supermarkets	Kiler	183	53
Afra	Hypermarkets	Kombassan	N/A	46

Source: Company data and derived from AMPD

Key specialty stores

Store brands	Group name	Retail formats	2004 Sales (EUR million excl. VAT)	Number of stores
Carsi	Boyner	Department Stores	200	30
Marks & Spencer	Marks & Spencer	Department Stores	78	22
Praktiker	Metro Group	DIY	63	8
Koçtas	KOÇ and B&Q	DIY	N/A	5
YKM	N/A	Department Stores	N/A	39
Tekzen	Tekfen Holding	DIY	N/A	16
Bauhaus	Bauhaus	DIY	N/A	3

Source: Company data and derived from AMPD

The majority of the leading retailers have ambitious expansion plans, which should see them capture an increasing share of the market through alliances with small local players. However, local players are also formulating strategies to strengthen themselves through alternative alliances.

Food retail channels

As Turkey's food retailing structure moves from small to large outlets, often as part of chains, distribution companies are also adapting. Hypermarkets, major supermarkets and discount chains do import a small portion of items directly, however, along with smaller outlets, they depend on importers, distributors and agents for most of their imported products. E-commerce is available, where many outlets order domestic and imported products via the internet for home or business delivery.

Typically, an importer or agent may also be a wholesaler or distributor, or both. Nearly half of the country's distributors have a nationwide network, with 30% of major manufacturers operating their own distribution companies nationwide.

Hypermarkets, supermarkets and discount stores

Hypermarkets have recently become fashionable investments within the retailing sector in Turkey. Sabanci and Koç— two major Turkish conglomerates – are heavily involved in this sector. There are more than 50 different chains operating in Turkey's retail business. Foreign investors present in the Turkish food retail markets include Metro (Germany), Carrefour (France) and Tesco (UK).

Large western style retail outlets have flourished in Istanbul, Ankara, Izmir and other large cities such as Adana, Gaziantep, Bursa, Kocaeli, Konya and Mersin. Locally owned retail chains tend to concentrate on middle to small cities and towns of Turkey, where consumers are also aware of international trends, have higher disposable incomes, and have automobiles to travel to and from the stores. However, it is not easy for the sector to expand at high speeds; in many cases, the search for, as well as the administrative hurdles in buying, large sites cause substantial difficulties.

Turkey today has a portfolio of, at least in most cases, very modern hypermarkets, in part due to the influence of foreign operators. Hygiene standards meet international standards and store equipment often satisfies the highest expectations. However, the product range is often very limited; although trading from identical store sizes, they sometimes sell three to four times less items than their French, German or British counterparts.

Hypermarkets are also under increasing pressure from the rising popularity of discount stores, with their low prices and convenient locations. Many operators are now focusing on expanding their discount store chains, rather than the hypermarket format.

German-style hard-discount retailing has only been present in Turkey since 1995, with the launch of BIM and Şok. Nonetheless, the two leading companies in the sector have been able to build up large store networks, and discount stores are now the major growth format in Turkey. The stores gained their popularity during the economic downturns of 1999 and 2001, when many consumers switched from hypermarkets and supermarkets in search of more price-competitive goods.

Although the economic situation is now picking up, discount stores remain extremely popular and the rapid proliferation of the format is undoubtedly affecting the other grocery formats. In response, most of the leading domestic and foreign grocers in Turkey have launched their own discount store chains on the market and all are pursuing ambitious expansion policies. The undisputed market leader in Turkish discount retailing is BIM, a hard-discount store very much in the mould of Aldi, which is not surprising since the chain was set up by a former Aldi manager, and some of the management was trained in Germany. As with the efficiency oriented model of Aldi, BIM only sells limited product ranges, offering them in torn-open cardboard boxes.

The second largest chain is Migros Türk's discount banner, Şok. Şok has been the fastest growing chain within Migros Türk over the past few years. The group has focused its expansion on the chain in an attempt to benefit from the growing popularity of discount stores in Turkey. Its stores are located in Western Turkey and the company as yet has no presence in the east of the country.

Following the success of BIM and Şok, many of the other major grocery retailers have launched their own discount store chains. Carrefour, for example, has introduced its Dia format, which is now the third largest discount store chain, while Gima (acquired by Carrefour in 2005) has taken over control of the Endi chain.

Convenience stores

Convenience stores are relatively unimportant and there are only a few major chains to note. Opet, one of the leading petrol retailers and suppliers in Turkey, acquired the licence to expand the 7-Eleven convenience store chain in Turkey in late 2001. The licence had previously been held by Marso Gıda, which only managed to open 12 7-Eleven outlets when it was established in the country in the mid- 1980s. All of these stores are located in Istanbul. Due to its low level of investment, 7-Eleven Inc. sought another license to develop the chain further. Opet was chosen for its petrol forecourt sites, which are ideal operating environments for 7-Eleven stores. Opet has more than 650 petrol stations in Turkey, all of which have a convenience store concept operating within them. According to its agreement with 7-Eleven Inc, Opet must open 180 7-Eleven stores over the next five years, although Opet plans to exceed this number.

Traditional markets

Bakkals, certain types of convenience stores and open-air bazaars are forms of traditional outlets in Turkey. Bakkals are small outlets, which sell anything from food (fresh and prepared) to personal care products. Convenience stores mostly sell dry nuts, confection items, tobacco products and soft drinks. Open-air bazaars mainly concentrate on fresh vegetables and fruit. All three are still preferred by the majority of Turkish consumers, due to the accessibility and delivery service of bakkals and convenience stores, and the wide variety of low-priced products, fresh fruits and vegetables, clothing, over-the-counter products and personal care products offered at corner bazaars.

Non-food retail channels

None of the major grocery players operate major drugstore formats. AS Watson's drugstore chain entered in 2005 through the acquisition of a small local chain, and is now looking to open 100 stores in the long term.

Gas station mini-marts are also new in Turkey, with seven or eight major brands. Marketim, a market chain, formed an agreement with Elf Gas Stations to open 24-hour service gas station mini-marts. Other gas stations and gas mini-marts do not operate as part of a chain.

E-commerce

Less than 4% of the population has access to the internet – although the number is increasing at an accelerating rate. Those with internet access are generally the wealthiest members of society and many of the leading grocery retailers have developed transactional websites in anticipation of a demand growth in the future.

E-commerce has become a sell-side channel as a result of the increasing competitiveness between major retailers. Although the current internet penetration rate is considered to be very low compared with European averages, it is likely to increase in the future. Furthermore, initiation of shopping via catalogues, digital TV, home telephones and cellular phones is in progress.

The pioneer of online shopping in Turkey was Migros Türk, which launched its virtual market service in late 1997, initially under the name of Migros Cyber Shopping. Today, the service area covers all the regions of Istanbul and all of Izmir, as well as Ankara, Marmaris, Bodrum, Bursa, Antalya and Adana. Migros has since launched the Kangurum (Kangaroo) site. Gima's online store has been active since June 2001.

M&A activity

M&A activity since 2003

Year	Acquiring company	Acquiree/JV company	Nature of business	Equity stake
2003	Kipa	Tesco Plc	Food retail	82%
2005	Gima	Carrefour/ Sabanci Holding	Food retail	60%
2005	Tansas	Migros	Food retail	70%

RETAIL & CONSUMER CHALLENGES, OPPORTUNITIES AND EMERGING TRENDS

Challenges

Strong growth potential during the EU accession negotiations

Considering that Turkey has undergone much economic, political and social change in the past five years, and will do more so during the period leading up to EU accession negotiations, there is great potential in the Turkish retail sector. In addition to strong demand growth potential, it is expected that substantial structural changes will occur over the next 10 years.

Consolidation in the local retail sector

Consolidation in the Turkish retail sector will most definitely bring several positive outcomes. First, there will be an increase in bargaining power with suppliers. Second, a more rational pricing strategy will be adopted. A higher market share for organised retailers should lead to higher prices, as they increase their competitive strength over traditional retailers.

Favourable demographic factors, strong growth potential with EU accession and a strong rebound in macroeconomic indicators make Turkey a potential target for international retailers who seek growth opportunities on a global basis. Considering the fragmented market structure where the top-five retailers account for only 22.5% of the market, consolidation in the sector will accelerate quickly through nationwide mergers (like the recent acquisition of Gima by Carrefour) or international acquisitions.

The most important segment of the market is food retailing, which accounts for 60% of total sales. Organised retailers have a 36.5% market share in the food-retailing segment and are increasing their shares at the expense of traditional stores. The purchasing power of organised stores enables them to offer lower prices while achieving higher margins, which could cause an accelerated shift in organised retailers in 2006.

Changes in demographic characteristics – transformation phase

The main factor attracting retailers to invest in the sector and to develop modern structures has been growth potential due to a large and growing population, and unsaturated market conditions. Factors such as the growth of disposable income, along with changes in the composition of the country's production factors, demographic characteristics, lifestyles and consumption patterns, have all fostered positive expectations.

Retailers have been building up a wider network of store chains with the emphasis on ergonomics and parking lots, improving service quality and attempts to attract new customers while retaining existing ones. In order to increase their market share, large supermarkets have conducted various promotional campaigns, initiating phone and internet purchases, deliveries and issuing membership cards. The transformation to modern-format food retailing has mainly occurred in large cities where shopping habits are changing rapidly and the market size justifies large-scale investment.

Improving operational efficiency

Operational efficiency, better use of information technology in inventory management, purchase planning, customer data warehousing, customer relationship management and category management are the main areas in which Turkish retailers need to improve.

Opportunities

Positive medium-term outlook

The retail industry is highly susceptible to the developments on the main economic front. Changes in inflation figures and interest rates affect consumers' disposable income and, in turn, have an effect on consumer confidence. Turkish food retailers last experienced this susceptibility in 2001, where the industry recessed in parallel to the contraction of GDP. However, since 2002, demand, consumer confidence and revenues have started to ameliorate. Consumer confidence has been boosted by last year's political stability attained by the single-party government, accompanied by the commitment to fiscal prudence and the improved expectations through EU accession.

Conversely, small, independent neighbourhood stores face intense pressure from newcomers – large, modern operators offer their customers a wide range of products at attractive prices in new facilities. Without modern methods, traditional operators can only respond by offering a narrow and incomplete product line-up at prices 30% higher. Plus, they can only stay in business without modernising by operating informally – that is by evading taxes and other financial obligations to the state.

The progress of traditional operators will be central to the development of the sector, since they account for almost 90% of employment. Today, their inefficiencies hobble the industry and help pull total sector productivity down. If traditional operators can be encouraged to modernise and guided along the path (i.e., franchises, buying groups, specialisation), they could participate fully in the continued rapid growth. They will also lift themselves and their employees out of today's marginal livelihoods. The upside is enormous; the Turkish retail sector could more than double its productivity by 2015 and become a primary job creation engine in a rapidly growing economy.

Despite periodic setbacks, the medium-term economic outlook is positive and a number of trends and events will positively influence the retail sector. Income growth, high urbanisation rates and the increasing number of women in the workforce all influence changes in tastes and preferences that support the development of the retail sector.

Chain retailing

Despite the progress, chain retailing remains a largely unexplored market in Turkey, with organised retail representing only a 36.5% share of the total turnover in 2004. There are approximately three hypermarkets and 17 supermarkets per one million of the population in Turkey, compared to an average of 15 hypermarkets and 150 supermarkets in EU countries. These figures show that the Turkish market still has lots of potential.

The Turkish retail sector is also relatively fragmented. At present, the top-five players hold a combined market share of under 25% of the modern grocery distribution.

Branded imported items

A change in the retailing structure has opened new areas for branded import items. Industry sources estimate that only the top 5-10% of the Turkish population can afford imported food items.

Emerging trends

CRM activities

Organised retailers have started to concentrate on CRM activities and to observe consumer behaviour in order to retain their customers and create brand loyalty. Therefore, they have initiated store cards, which bring extra benefits (mostly discounts) to consumers holding the card of that store. Strategic partnerships with banks to increase the use of credit cards and, in return, to gain extra benefits or discounts for consumers, have been widely implemented by retailers.

Increasing interest in own-label products

Retailers have been putting more emphasis on private label products in order to provide cost efficiency for the benefit of their customers. After the economic crisis in 2001, consumers have been more inclined toward private-label or non-label products as these products have a price advantage. The share of purchased private-label products comprised almost 55% of total consumers in 2004,

compared to 39% in 1999. Not only are own-branded products sold at higher margins, they also allow retailers to stand out from the competition.

Other own labels, meanwhile, have built a reputation similar to those of manufacturers' brands. Given Turkey's overall economic situation, well-managed own brands have a good chance of swiftly increasing their market shares. The growing number of hard-discount stores has also led to an increased acceptance of own-label goods among Turkish consumers. Turkey's own labels are often comparable to corresponding manufacturers' labels in terms of quality, but are sold at prices between 30% and 50% lower.

On the other hand, the majority of small supermarket chains carry no own labels. It is therefore conceivable that they will lose some of their customers to the modern retail companies. The more natural it becomes for retailers to sell own-branded lines, the less likely price will be the only relevant distinctive feature in the competition.

Implementation of foreign retailers

Most Turkish conglomerates entered the retail market in the past decade with increased expectations of financial income and with the aim of achieving synergies, such as creating a customer database and higher prestige. Seeing this through the cold light of operational performance, most foreign retailers may have avoided penetrating Turkey so far. Among the leading international retailers, only Carrefour, Metro, Tesco and, more recently, IKEA are present in Turkey. However, there are strong signs indicating that more foreign retailers are eyeing Turkey for possible acquisitions.