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LIMITATIONS ON FOREIGN CURRENCY DERIVATIVE TRANSACTIONS

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Noting increased volatility and risk in the global markets triggered by the ongoing COVID-19 pandemic, the Turkish Banking Regulatory and Supervision Agency ("**BRSA**") and the Capital Markets Board of Turkey ("**CMB**") announced new measures limiting foreign currency swap, forward, option and other derivatives transactions (where the parties swap Turkish Lira and foreign currency) ("**FX Derivatives Transactions**") as of 12 April 2020 and 13 April 2020, respectively.

The BRSA's latest controls expand upon its previous actions[1] concerning local banks ("**Banks**"), which it began implementing in 2018 as a response to heavy fluctuation in the value of the Turkish Lira (cumulatively, "**BRSA Imposed FX Derivatives Limitations**"). The CMB had not previously imposed similar restrictions and with its announcement, institutions which are regulated by the CMB[2] ("**Capital Markets Institutions**") have also become subject to restrictions on their FX Derivatives Transactions ("**CMB Imposed FX Derivatives Limitations**" and together with BRSA Imposed FX Derivatives Limitations, "**FX Derivatives Limitations**").

The most recent changes to the BRSA Imposed FX Derivatives Limitations specify that, for FX Derivatives Transactions between Banks and non-resident counterparties:

- if at settlement a Bank receives Turkish Lira; (1) the previously imposed volumetric threshold of 10% of the Bank's regulatory capital, has now been revised as 1% and (2) variable weighting based on maturity shall no longer be applicable;
- if at settlement a Bank provides Turkish Lira; whereas previously a volumetric threshold of 10% of the Bank's regulatory capital had been imposed on transactions with seven days or less remaining until settlement, new thresholds shall be 1% for transactions with seven days remaining until settlement, 2% for transactions with thirty days remaining until settlement and 10% for transactions with one year remaining until settlement; and
- any early settlement or extension of the original settlement date (for whatever reason) of any transaction falling within the scope of the BRSA Imposed FX Derivatives Limitations shall be subject to the prior written consent of the BRSA.

The CMB Imposed FX Derivatives Limitations apply to Capital Markets Institutions rather than Banks and track the BRSA Imposed FX Derivatives Limitations.

Following these developments, the FX Derivatives Limitations can be summarized as follows:

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[1] BRSA Press Releases dated 13 August 2018, 15 August 2018, 17 August 2018, 8 September 2018, 17 September 2018, 18 December 2019, and 9 February 2020; and BRSA Letter to the Banks Association of Turkey dated 19 September 2018.

[2] The Capital Markets Law No. 6362 specifies capital markets institutions as: (i) investment firms, (ii) collective investment schemes, (iii) independent audit firms, appraisal firms and credit rating agencies that are active in the capital markets, (iv) portfolio management companies, (v) mortgage finance institutions, (vi) housing finance and asset finance funds, (vii) asset leasing companies, (viii) central clearing institutions, (ix) central depository institutions, (x) trade repositories and (xi) other capital market institutions falling under the regulation of the CMB.

- Pursuant to the BRSA Imposed Derivatives Limitations, FX Derivatives Transactions between Banks and non-resident counterparties shall be subject to the following restrictions:
  1) Where at settlement a Bank receives Turkish Lira; the total notional amount of FX Derivatives Transactions may not exceed %1 of the Bank's most recently calculated regulatory capital (delta values may be taken into consideration for options transactions), and if any excess exists, further such FX Derivatives Transactions may not be executed and any such FX Derivatives transactions may not be renewed;
  2) Where at settlement a Bank provides Turkish Lira; depending on the settlement date of the FX Derivatives Transactions, their total notional amount may not exceed certain ratios based on the Bank's most recently calculated regulatory capital (delta values must be taken into consideration for options transactions) as follows: (i) 1% for transactions with seven days remaining until settlement, (ii) 2% for transactions with thirty days remaining until settlement and (iii) 10% for transactions with one year remaining until settlement. Furthermore, for purposes of the calculation above, the effective date shall be taken into consideration for FX Derivatives Transactions where the effective date is after the transaction date. If any excess exists, further such FX Derivatives Transactions may not be executed within the maturity ranges with limit breaches;
  3) Banks' transactions with their consolidated non-resident credit and financial institution affiliates are exempt from the FX Derivatives Limitations;
  4) The above ratios must be calculated daily, on a solo and consolidated basis; and
  5) Any early settlement or extension of the original maturity date (for whatever reason) of any transaction falling within the scope of the BRSA Imposed FX Derivatives Limitations shall be subject to the prior written consent of the BRSA.
- Pursuant to the CMB Imposed FX Derivatives Limitations, FX Derivatives Transactions between Capital Markets Institutions and non-resident counterparties shall be subject to the following restrictions:
  6) Where at settlement a Capital Markets Institution receives Turkish Lira; the total notional amount of FX Derivatives Transactions may not exceed %1 of the Capital Markets Institution's capital calculated at the end of the preceding month pursuant to applicable capital adequacy calculation laws, and if any excess exists, further such FX Derivatives Transactions may not be executed and any such FX Derivatives transactions may not be renewed;
  7) Where at settlement a Capital Markets Institution provides Turkish Lira; depending on the settlement date of the FX Derivatives Transactions, their total notional amount may not exceed (on any day) certain ratios based on the Capital Markets Institution's capital (as calculated in (6) above): (i) 1% for transactions with seven days remaining until settlement, (ii) 2% for transactions with thirty days remaining until settlement and (iii) 10% for transactions with one year remaining until settlement;
  8) The above ratios must be calculated on a daily basis; and
  9) Any early settlement or extension of the original maturity date (for whatever reason) of any transaction falling within the scope of the CMB Imposed FX Derivatives Limitations shall be subject to the prior written consent of the CMB.

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