Project Information Document (PID)

Appraisal Stage | Date Prepared/Updated: 16-Oct-2020 | Report No: PIDA29626

BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Turkey	P174144	Turkey Rapid Support for Micro and Small Enterprises during the COVID-19 crisis	
Region	**Estimated Appraisal Date**	**Estimated Board Date**	**Practice Area (Lead)**
EUROPE AND CENTRAL ASIA	19-Oct-2020	10-Dec-2020	Finance, Competitiveness and Innovation
Financing Instrument	**Borrower(s)**	**Implementing Agency**	
Investment Project Financing	KOSGEB (Small and Medium Enterprises Development Organization of Turkey /Küçük Ve Orta Ölçekli Sanay	KOSGEB (Small and Medium Enterprises Development Organization of Turkey /Küçük Ve Orta Ölçekli Sanay	

Proposed Development Objective(s)

The Project Development Objective (PDO) is to avert the closure of viable micro and small enterprises (MSEs) affected by the COVID-19 crisis and maintain their employment levels during the crisis.

Components

Component 1: Performance-based reimbursable support for eligible MSEs in the manufacturing sector
Component 2: Performance-based reimbursable support for eligible innovative young firms
Component 3: Technical support to the PIU under KOSGEB

The processing of this project is applying the policy requirements exceptions for situations of urgent need of assistance or capacity constraints that are outlined in OP 10.00, paragraph 12.
Yes

PROJECT FINANCING DATA (US$, Millions)

SUMMARY

Total Project Cost	300.00
Total Financing	300.00
of which IBRD/IDA	300.00

Financing Gap	0.00

DETAILS

World Bank Group Financing

International Bank for Reconstruction and Development (IBRD)	300.00

Environmental and Social Risk Classification

Moderate

Decision

The review did authorize the team to appraise and negotiate

B. Introduction and Context

Country Context

Turkey is a large, upper-middle-income country with a strong record of inclusive growth, but recent shocks are risking the economic gains made since the early 2000s. Turkey achieved rapid economic and social development in the 2000s, with poverty incidence more than halving[1] and real Gross Domestic Product (GDP) increasing by 50 percent by 2008. Since the Global Financial Crisis (GFC), rapid growth continued but was increasingly associated with stagnant productivity, a rising current account deficit and growing foreign exchange-denominated debt stock. Turkey then experienced a sharp external adjustment in mid-2018 as the Turkish Lira (TL) depreciated more than 60 percent against the US dollar between January and September that year. This triggered a downturn in the Turkish economy as spending fell, inflation spiked, and the corporate sector struggled under an elevated debt burden. Turkey experienced three quarters of negative growth from late 2018 to mid-2019, close to one million jobs were lost, and unemployment rose from 10 percent in January 2018 to 13.8 percent by January 2020. Since 2008, GDP per capita has fallen to US$9,400, while poverty reduction progress stalled in 2018.

Turkey has been severely impacted by COVID-19, both in terms of the health impact and economic losses. Turkey recorded its first confirmed COVID-19 case on March 11, and over the following 20 days, the number of cases increased to 38,000, one of the fastest growth rates of the epidemic seen so far. The authorities responded rapidly, scaled up testing, implementing targeted curfews, closures of education facilities and other service providers that entail close contact, and imposing restrictions on the activity of other in-person and transportation services. The economy contracted by 9.9 percent in the second quarter (year-on-year) with large swathes of firms severely affected as they face the combined shocks of lower demand, activity restrictions, and supply chain disruption. The impact on firms comes immediately following a recession that has already hit many firms hard. Small and medium-sized enterprises (SMEs) are less likely to be able to

[1] The poverty headcount ratio at US$5.50 a day fell from 35 percent in 2002 to 16.9 percent in 2008.

access finance for much-needed liquidity, raising the risk of widespread layoffs and bankruptcies. While most restrictions were lifted by mid-2020, there remains a risk that a second wave of community transmission may then necessitate re-imposition of restrictive measures and further impacts on business.

The potential loss of employment and earnings could be devastating and may disproportionately hit women in work and marginal workers. Although little data on impact is available yet in this emerging crisis, if unmitigated, the shock to firms is expected to force them to lay off employees in huge numbers. Early data on the US shows an unprecedentedly large rise in the unemployment rate. The leisure and hospitality sectors have been, by far, the hardest hit, with employment declining by almost 3 percent in a single month, while many other industrial and service sectors saw employment declines. Globally, the International Labor Organization (ILO) estimates that working hours will decline by around 7 percent in the second quarter of 2020. World Bank (WB) estimates of the household impact of an unmitigated COVID-19 shock in Turkey suggest that the incidence of poverty could increase from around 10 percent at present by four percentage points nationwide, and a further three percent of the population would become vulnerable to falling into poverty.

Sectoral and Institutional Context

The onset of COVID-19 globally and in Turkey is a combination of multiple shocks to the economy on a scale which has not been seen in recent history. The incidence of the virus, the behavioral changes it calls for, and required policy responses to slow its spread have disrupted supply and reduced demand for most parts of the economy. In this difficult context of high need that is likely to far exceed the ability of the authorities to fully cushion the impact, it is important to try to ensure that interventions have the greatest possible positive impact.

Micro and small firms in Turkey account for more than half of formal employment and 40 percent of employment in the manufacturing sector, yet their access to finance is constrained, making them particularly vulnerable to a tightening of financing conditions. Micro and small enterprises account for 57 percent of total employment, 42 percent of total revenues, 38 percent of total exports, and represent 99 percent of all firms in Turkey[2]. Micro and small enterprises account for 36 and 21 percent of employment respectively. At a sectorial level, micro and small firms account for 64 percent of employment in the services sector and 61 percent in construction. Access to finance is a frequently cited constraint for micro and small firms—they rely more on internal sources of funding and state-owned banks for loans[3], and are more likely to have their loan applications rejected compared with medium-sized and large firms. Moreover, micro and small firms in Turkey rely more on internal funds for financing investment and working capital than their peers in other countries in the ECA region.[4]

Nearly all micro and small enterprises are facing difficulties with cashflow and are ill-prepared to withstand

[2] All figures based on 2018 data.
[3] The share of banks in total MSE cash-loans are 19 percent for state banks, 14 percent for domestic private banks and 14 percent for foreign banks as of April 2020.
[4] World Bank Group Enterprise Survey (2019) and Survey on Access to European Central Bank, Finance of Enterprises (2018).

the current crisis. A survey of 17,447 Turkish MSEs[5] conducted by KOSGEB between March 31 and April 7, 2020 found that 95 percent of all interviewed firms are currently experiencing cashflow difficulties and 82 percent do not have an emergency-response strategy that would have allowed them to deal better with a situation such as COVID-19. In addition, firms report having already laid off workers, and nearly two-thirds (63 percent) expect to close operation fully within the following three months, if the outbreak continues. The main measures to mitigate the negative effects of the crisis that firms expect from the government are direct grants and deferral of tax and social security obligations and other duties and fees. At the same time, only a quarter of surveyed firms (26 percent) feel that the measures adopted by the government thus far are sufficient.

The KOSGEB survey revealed the relative sensitivity of employment to be high in manufacturing firms, in terms of planned layoffs, compared to construction, trade and services. In services and construction, around 15 percent of all surveyed firms fired at least one employee since the beginning of the crisis. In manufacturing, the percentage of firms who fired workers is relatively lower (8 percent), but the percentage of firms that plan to fire in the future is higher in manufacturing (22 percent) than in services (20 percent). In the trade sector, which is the largest sector in terms of employment in Turkey, the share of firms who plan to fire employees is 20 percent and the ones who actually fired before the survey date is 9 percent. In manufacturing, the share of employees who are on temporary leave is the highest (26 percent) among all other sectors. The survey, however, does not ask if the temporary leave is paid or not, which is a critical aspect of the temporary leave for employees' welfare and for the continuation of the firm. Home-based work (HBW) adjustments are also more common in services, while HBW is less common in manufacturing (only 6 percent) mainly due to the nature of the manufacturing production, which generally necessitates on-site work of employees.

The manufacturing sector plays a vital role in Turkey's economy and domestic value chains while one of the key development objectives of the government is to boost manufacturing high value-added production and exports by improving the productivity and competitiveness of the manufacturing firms. According to the Annual Industry and Service Statistics (AISS) of the Turkish Statistical Agency (TURKSTAT), in 2018, out of the 3,160,396 enterprises operating in Turkey, 395,816 (12.5 percent) were manufacturing firms, and they accounted for 25.5 percent of total employment, 28.2 percent of total turnover, 27 percent of total purchases of goods and services, 44.2 percent of total production value, and 37.7 percent of total value added at factor costs. In addition, while the average amount of turnover and number of employees per enterprise in Turkey are approximately TRY 2.5 million and five people, respectively, these figures are more than TRY 5.5 million and 10 people for a manufacturing sector enterprise. Manufacturing accounts for 84 percent of Turkey's exports, compared to 16 percent for services.

The manufacturing sector is also a key pillar for Turkey's technology innovation and high-tech exports. According to AISS, manufacturing production grew by 5.3 percent annually on average over the period 2014-2018, and the sector ranked 13th in the world and 5th in Europe in terms of total value added in 2018. In addition, the share of high-technology sectors in manufacturing exports rose to 3.2 percent in 2018 from 3.1 percent in 2013, while the share of medium-high technology sectors rose to 34.6 percent from 31.5 percent, and the share of these sectors is around 60 percent of Turkey's total international trade. The Industrial

[5] The KOSGEB survey relies on a sample of firms registered in KOSGEB's database. The distribution of respondent firms is as follows: 21 percent self-employed, 58 percent – micro, 17% - small and 4% - medium firms.

Development Bank of Turkey (TSKB) has recently undertaken a study to identify high-priority sectors that require support in order to alleviate the negative impact of COVID-19: manufacturing was found to be a very high priority sector for minimizing job losses and maintaining employment. In its analyses, TSKB took into account three fundamentals: (i) protection of the value chain from the negative impacts of the global shock, (ii) protection and support of the labor market, and (iii) structuring the transformation of industry and service sectors. Although all sectors will need support in these three fields in order to eliminate the impacts of COVID-19, a prioritization methodology was introduced to identify the most vulnerable sectors that need urgent intervention. A data-based approach was adopted for the first two parameters: for the protection of the value chain, cash conversion cycles and for protection of the labor market, the share of each sector in overall employment was taken into account. In order to prioritize along the structural transformation parameter, the expected changes in the way of doing business during the pandemic were considered. The sectors were prioritized gradually at each fundamental point.

Prior economic and financial crises have also shown that young firms, which are typically small, have been particularly hit during recessions. Based on the KOSGEB survey, young firms[6] suffered both serious revenue and employment losses. Among all the firms who reported some revenue losses due to COVID-19, 34 percent are young firms. More than half of the firms who reported a loss of less than TRY 25,000 are young firms that are at most two years old. The share of young firms within the groups that make larger losses are smaller, but this is mostly because young firms tend to be small in terms of revenues and employment. Accordingly, 15,337 out of 17,447 firms reported that they did not fire any workers during the crisis (until the first week of April). Among those who reported at least one labor dismissal, the share of young firms is relatively large (39 percent) and larger than these firms' share in the total survey sample (34 percent). Most of the young firms reported that they fired between one and five employees, while the share of young firms in the group of firms who fired 11 to 15 employees is the largest and above 60 percent, demonstrating that young firms can be particularly vulnerable to the economic crisis caused by COVID-19 and this is especially visible in their labor dismissals since the crisis began.

Relationship to CPF

The operation is in line with the policy objectives set in the current WBG Country Partnership Framework (CPF) for Turkey, approved in July 2017, and recently extended through the Program and Learning Review (PLR). Improving competitiveness and employment in selected industries are listed among the CPF/PLR objectives under, respectively, Focus Areas I and II. The continued progress towards these policy objectives is currently at risk from the adverse economic impact of COVID-19. As described in the above section, Turkish firms are struggling to maintain production and employment in the face of a dual supply and demand shock, with micro and small firms being particularly vulnerable, as revealed in the recent KOSGEB survey. The proposed operation aims to alleviate the economic difficulties by providing emergency financial assistance in the form of performance-based reimbursable support to viable private manufacturing and young firms to help them survive the adverse effects of COVID-19 and resulting economic downturn, adapt to the new operating environment, and, eventually, contribute to the recovery stage. The main objective is to avert the closure of otherwise viable micro and small enterprises (MSEs) and keep workers in MSEs employed. This project is part of a larger COVID-19 support package mobilized by the WBG at the request of the Turkish

[6] For the purposes of this study, young firms are defined as those that are at most two years old in this case, accounting for 34 percent of the total sample; however, if firms that are at most five years old are also considered as young firms, their ratio increases to 55 percent of the sample.

authorities, including other operations in health, education, and access to finance for SMEs.

C. Proposed Development Objective

Development Objective(s) (From PAD)

The Project Development Objective (PDO) is to avert the closure of viable micro and small enterprises (MSEs) affected by the COVID-19 crisis and maintain their employment levels during the crisis.

Key Results

(i) Share of beneficiary MSEs that survive for at least six months after receiving performance-based reimbursable support (Baseline: 0, Target: 65 percent.)

(ii) Share of beneficiary surviving MSEs that maintain employment at 100 percent of the one in the month before the grant application, for at least six months after receiving performance-based reimbursable support (Baseline: 0, Target: 70 percent.)

(iii) Share of beneficiary innovative young firms that survive for at least six months after receiving performance-based reimbursable support (Baseline 0, Target: 50 percent.)

D. Project Description

Component 1. Performance-based reimbursable support for eligible MSEs in the manufacturing sector (US$259 million)

The component would finance performance-based reimbursable support to eligible manufacturing MSEs to prevent the reduction of employment and closures, thereby minimizing the disruption of firms' relations with employees, suppliers and creditors. Reimbursable support of different amounts proportional to the firm size would be made available to eligible MSEs. Eligibility will be restricted to formally registered private manufacturing MSEs (excluding individual entrepreneurs) that were viable prior to the COVID-19 crisis as demonstrated by meeting a minimum revenue threshold in 2019. While the Component would be scaled to ensure coverage of all eligible beneficiaries, in case of higher than expected uptake, reimbursable support would be awarded as per earmarked amounts for groups of firms (such as micro, small, and women-owned MSEs). The exact earmarked allocations would be determined during appraisal, but similar operations target at least 10 percent of reimbursable support to be earmarked for women-owned MSEs.

Reimbursable support would be "performance-based" since firms who receive the reimbursable support would commit to maintain employment levels as they were at the time of applying for the grant. KOSGEB would not verify how the reimbursable support is being utilized, as long as the enterprise is active and maintaining employment at the level of the base month (the month preceding the month of first application). If conditions are met and KOSGEB confirms from Social Security Institution (SGK) records that the firm has maintained employment at the level of the base month, the firm would receive a disbursement. The final details of the reimbursable support scheme would be specified in the project's reimbursable support Manual.

The reimbursable support would be disbursed electronically nationwide through KOSGEB's network. Global experience in the implementation of firm grant programs has shown that they have very high uptake and require significant resources to administer. For this reason, the reimbursable support would be deployed using KOSGEB as an agent responsible for confirming eligibility and verifying the use of funds.

Reimbursable support amounts are to be determined during project appraisal, but with scaled ceilings for micro and small firms per month, with precise amounts dependent on the firm's fixed and variables costs. These amounts would be estimated to cover payroll for an average firm for three months in each size category. They would be further fine-tuned to reflect the actual number of firm employees and size of payroll per month during appraisal. Given the estimated number of firms that would likely to be eligible for support in each category and assuming 100 percent grant take-up, this three-month payroll maintenance program would cost approximately US$940 million (see Table 1 below). If medium-sized firms are also considered (estimated at around US$111 million), the whole program cost would exceed US$1 billion. The Project will finance US$300 million of the total funding requirement, with other development partners and IFIs potentially providing the remainder (so far, the Japanese International Cooperation Agency (JICA) has expressed interest in providing parallel financing and matching the Project amount).

Table 1: Total Reimbursable Support Funding Needs (Estimate)

	Number of Eligible Firms	Reimbursable Support Size (Average for 3 months), US$	Total Cost of Reimbursable Support Funding (Assuming 100% Uptake), US$
Micro	153,326	4,347	666,506,383
Small	24,992	10,870	271,664,127
Total	**178,318**		**938,170,510**

Source: KOSGEB and Bank estimates

Component 2: Performance-based reimbursable support for eligible innovative young firms (US$40 million).

Innovative young firms are defined as firms established in 2017 or later and operating in the computer programming or scientific R&D sectors (NACE Rev 2 - Divisions 62 and 72, respectively). Since these technology-intensive young firms belong to a strategic sector for the country and are especially vulnerable during the crisis as mentioned above, they would be exempted from 2019 minimum revenue criterion and 25 percent sales loss criterion. Since 2017, there have been approximately 14,000 R&D and Innovation Projects which have been funded by public resources and the approximate number of registered patents and received technological product certificates are 7,500. As of 2020, the number of MSEs in Technology Development Regions and Centers are approximately 5500. These numbers are for all sectors and sizes of SMEs. There are approximately 10,000 young MSEs in the computer programming and scientific R&D sectors.

Reimbursable support for innovative young firms will be "performance-based" since firms would be required to maintain employment at the level of the time of grant application. Beyond the regular operating expenses such as payroll, suppliers, rent, and utilities, start-up firms would also be eligible for R&D related expenses, such as patent/royalty fees, technology licensing fees, and testing and certification fees. Given the emergency nature of the Project, beneficiary innovative young firms would not be required to provide proof of the use of the reimbursable support funds, as long as they remain operational and maintain employment.

Reimbursable support amounts are to be determined during project appraisal but would likely have ceilings similar to the reimbursable support in Component 1. Most innovative young firms are expected to fall into the micro category. Most R&D-related expenses do not occur on a monthly basis, so in the funding application to be filed with the KOSGEB, young firms in the sectors defined here can also request additional funding for specific R&D-related expenses, such as patent fees or technology licensing fees. The application would explain the purpose of the funding and the justification for such support, as well as the timeframe to use the funding. The final details of the reimbursable support scheme for innovative young firms will be specified in the Reimbursable Support Manual.

Component 3: Technical support to the PIU under KOSGEB (US$1 million). This component would be used to support the project implementation unit under KOSGEB. The eligible expenses would include staff costs, training, and project implementation related costs, such as monitoring and evaluation, auditing, financial management, as well as office equipment. If there is interest by KOSGEB, this component could also cover technical assistance (TA) for MSEs on adaptation to the post-COVID business model, including testing of workers, maintaining health and safety in the workplace and adjusting business operations, such as inventory management and maintaining client relations. Some limited TA could also be provided on topics of interest and where demand might be high, such as insolvency, out-of-court debt restructuring and workouts. It is important to note that, should JICA provide parallel funding, using the same project design, their Project will use the same PIU. This would require additional human resources within the PIU as the number of reimbursable support funds to administer will double (assuming JICA also provides reimbursable support of US$300 million).

Table 6: Project Cost and Financing

Project Components financed by IBRD Loan ($)	Project Cost	IBRD Loan	% Financing
1. **Component 1: Performance-based reimbursable support for eligible MSEs in the manufacturing sector**	$259,000,000	$259,000,000	**100%**
2. **Component 2: Performance-based reimbursable support for eligible innovative young firms**	$40,000,000	$40,000,000	100%
3. **Component 3. Technical Support for PIU**	$1,000,000	$1,000,000	100%
Total Cost of the Project Total IBRD Financing Required	**$300,000,000** **$300,000,000**	**$300,000,000** **$300,000,000**	**100%** **100%**

.

Legal Operational Policies

	Triggered?
Projects on International Waterways OP 7.50	No
Projects in Disputed Areas OP 7.60	No

Summary of Assessment of Environmental and Social Risks and Impacts

E. Implementation

Institutional and Implementation Arrangements

KOSGEB was established as an affiliated organization of the Ministry of Science, Industry and Technology in 1990 with the objectives of increasing MSEs' effectiveness and competitiveness, and ensuring industrial integration in conformity with economic development, to contribute to the social and economic needs of Turkey. Its support is organized along five different pillars: Entrepreneurship support; R&D and innovation support; Business development; and Finance and Incubation, with offices in all 81 provinces of the country. Overall, KOSGEB runs 14 different programs, and in 2019 delivered services for a total of US$420 million. KOSGEB will be the implementing agency as well as Borrower for this project and will establish a dedicated Project Implementation Unit (PIU) for the purpose of project implementation, financial management and monitoring and evaluation.

CONTACT POINT

World Bank

Stefka Slavova
Lead Economist

Pablo Facundo Cuevas
Senior Economist

Borrower/Client/Recipient

KOSGEB (Small and Medium Enterprises Development Organization of Turkey /Küçük Ve Orta Ölçekli Sanay
Necati GÜNAYDIN
Head of EU and Foreign Relations Department
necati.gunaydin@kosgeb.gov.tr

Implementing Agencies

KOSGEB (Small and Medium Enterprises Development Organization of Turkey /Küçük Ve Orta Ölçekli Sanay
Necati GÜNAYDIN
Head of EU and Foreign Relations Department
necati.gunaydin@kosgeb.gov.tr

FOR MORE INFORMATION CONTACT

The World Bank
1818 H Street, NW
Washington, D.C. 20433
Telephone: (202) 473-1000
Web: http://www.worldbank.org/projects

APPROVAL

Task Team Leader(s):	Stefka Slavova Pablo Facundo Cuevas

Approved By

Practice Manager/Manager:		
Country Director:	Auguste Tano Kouame	16-Oct-2020