COMBINED PROJECT INFORMATION DOCUMENTS / INTEGRATED SAFEGUARDS DATA SHEET (PID/ISDS)
CONCEPT STAGE

Report No.: PIDISDSC15470

Date Prepared/Updated: 03-Mar-2016

I. BASIC INFORMATION

A. Basic Project Data

Country:	Turkey	**Project ID:**	P156252
		Parent Project ID (if any):	
Project Name:	Long Term Export Finance (P156252)		
Region:	EUROPE AND CENTRAL ASIA		
Estimated Appraisal Date:	14-Apr-2016	**Estimated Board Date:**	01-Jul-2016
Practice Area (Lead):	Finance & Markets	**Lending Instrument:**	Investment Project Financing
Sector(s):	Banking (50%), SME Finance (50%)		
Theme(s):	Micro, Small and Medium Enterprise support (50%), Other Financial Sector Development (50%)		
Borrower(s):	Turkiye Ihracat Kredi Bankasi (Turk Eximbank)		
Implementing Agency:	Turkiye Ihracat Kredi Bankasi (Turk Eximbank)		
Financing (in USD Million)			
Financing Source			**Amount**
Borrower			0.00
International Bank for Reconstruction and Development			300.00
Total Project Cost			300.00
Environmental Category:	F - Financial Intermediary Assessment		
Concept Review Decision:	Track I - The review did authorize the preparation to continue		
Is this a Repeater project?	No		
Other Decision (as needed):			

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B. Introduction and Context

Country Context

1. Turkey's post-2001 economic development has resulted in impressive economic achievements. After a banking crisis in 2001, the country embarked on a concerted path of structural reforms supported by strong fiscal consolidation, strengthened banking supervision, and a shift to a flexible exchange rate regime with an independent central bank responsible for inflation targeting. Per-capita income and the incomes for the bottom 40 percent tripled since the start of the century, but, in several dimensions of well-being, Turkey continues to face numerous structural challenges.
2. Turkey's achievements have recently been challenged by a less favorable economic and political outlook, and a large current account deficit in deteriorating financing conditions. After a swift rebound from the recession of the global crisis of 2008-09, economic growth slowed significantly since 2012. Real GDP growth dropped to 2.9 percent and inflation reached 8.2 percent by end 2014, above the Central Bank's target rate. Moderate growth and exchange rate depreciation reduced external imbalances, and the current account deficit (CAD) narrowed to below six percent of GDP in 2014, in large thanks to favorable global oil prices. Nevertheless, the CAD remains large in a period of challenging financing. Important factors include weaknesses in trading partners, particularly in the European Union (EU), the Middle East and North Africa (MENA) and Russia (including sanctions over the border incident in late 2015). Exports coverage of imports in 2015 was about 73 percent. On the financing side, domestic political concerns and global financial market jitters dried up short-term inflows in 2015, with global financial conditions remaining fragile in early 2016.
3. The growth outlook remains cautious, despite a stronger than expected third quarter in 2015. Economic growth surprised positively despite political uncertainty in the run-up to the June parliamentary election. Seasonally adjusted GDP grew at an annualized rate of 5.2 percent q-o-q. The election results of November 1, 2015, have provided clarity over political uncertainties, yet economic uncertainty persists. Consumer confidence hit the lowest level since January 2009, and business confidence dropped notably in August and September, 2015. Private investment dropped sharply in Q3, suggesting that the private sector cut back capital spending. Inventory de-stocking continued for the third consecutive quarter and contributed negatively to growth. Against this backdrop, real GDP growth is projected to drop to 3.5 percent in 2016. Over the medium-term, Turkey s growth prospects depend on the recovery of private investment, structural reforms and stronger economic institutions.

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Sectoral and Institutional Context

4. The authorities have set an ambitious development vision for 2023 that will require significant efforts to catalyze export growth. Merchandise exports increased from USD36 billion in 2002 to over USD158 billion in 2014, mostly represented by large enterprises at 44 percent of the exports. Turkey now aims to become one of the ten largest economies in the world by 2023, with exports rising to USD500 billion under the "Turkish Exports Strategy for 2023" initiated by the Ministry of Economy and Turkish Exporters Assembly in 2009. Yet, with the recent slowdown of the global economy both in advanced and emerging economies, Turkey may not benefit simply from the 'pull' of growing global demand to the extent that it did over the past decade. Achieving sustained rapid export growth and reaching the government's export targets will require a significant increase in Turkey's global market share. This, in turn, will require that exporters become more competitive by producing goods at more attractive prices, expanding their product range to the faster growing products sphere, and improving quality and technological sophistication to command higher prices in export markets.
5. A shift to diversify market reach and provide more capital intensive and sophisticated products

presents unique challenges, placing the emphasis on the provision of longer term finance. Since the global financial crisis, amid a sluggish expansion in demand in traditional markets, the share of Turkey's exports to the European Union (EU) and the European Free Trade Association (EFTA) declined, while that of Middle East and North Africa (MENA) and other markets rose. The composition of Turkey's export basket has also been changing over the past decade, as the economy moves increasingly to capital-intensive products from those predominantly intensive in inexpensive labor. Mid-tech exports have replaced garments and textiles, playing an important evolution in export sophistication. Meanwhile, by 2010, the majority of Turkish exports switched to the mid to high-end of the quality range, in particular in the machinery sector. However, expanding into new markets, where importers require deferred payment terms, and increasing the supply of more capital intensive and sophisticated goods require access to longer term finance. Foreign direct investment has been low, constraining export growth, mostly held back from business environment impediments, with Turkey comparing unfavorably with many competitors in the Doing Business indicators.

6. The bank-dominated financial sector has limited ability to provide the maturity required to support recent export trends. Banks represent 90 percent of the financial sector and about 114 percent of GDP. Despite significant progress to deepen the capital market, the diversity of corporate debt instruments is limited, banks dominate issuances, and bonds are almost exclusively floating rate securities with an average maturity of one year and overall less than three years to maturity. The banking sector has limited access to long-term finance, and foreign borrowing barely breaches three years in maturity. The banking system is funded mostly by relatively stable customer deposits, backing 53 percent of total assets. However, about 87 percent of the sector's deposits had maturity below three months, while 77 percent of the lending was concentrated above three months. Characteristically, only 4.1 percent of deposits had maturity of over one year, dropping to only 1.6 percent for Turkish Lira (TL) deposits. The result is a negative liquidity gap (i.e. more liquid liabilities than assets, also known as the liquidity mismatch risk) that peaks in the one to five year maturity. With the system's loan to deposit ratio increasing to 121 percent, banks have drawn on balance sheet liquidity and wholesale funding from abroad (with foreign liabilities to total assets standing at 22 percent). However, the maturity of the sector's foreign liabilities barely breaches three years. Longer term sources of foreign debt, through for instance securitizations and subordinated debt, remain limited and constitute just above 15 percent of the total. In addition, following the Banking Regulation and Supervision Agency's (BRSA) authorization in 2010, banks begun to issue domestic bank bonds, with tenor ranging between six to 18 months. Nevertheless, only 1.5 percent of total assets are funded by Turkish lira bonds, while the weighted average of the maturity remains under one year.

7. Medium and large exporting enterprises are particularly constrained by the lack of long-term finance, indirectly impacting SMEs integrated into their local supplier chains. Large and medium enterprises account for 43 and 18 percent of exports, respectively. Long term finance reduces firms' exposure to rollover and interest rate risks, enabling them to undertake longer term fixed investments. Medium and large exporting enterprises frequently undertake lumpy purchases of physical investment to remain competitive or explore new markets. The banking sector is the largest provider of long term finance in Turkey, and is characteristically facing maturity mismatches from limited access to long-term finance. In addition, banks and large enterprises (that are typically able to tap financial markets directly) have been negatively affected from the recent volatility on international markets through worsening loan availability and terms. Ultimately, SMEs participating in supply chains, whereby smaller enterprises are integrated as local suppliers of larger enterprises, are strongly impacted by the effect of the economic uncertainty on the buyers of their goods and services.

8. In addition, the sector has been increasingly experiencing performance headwinds, impacting credit growth and Small and Medium Enterprises (SMEs) in particular, which are the most affected by financing pressures during a deceleration. The banking sector’s profitability has decreased in recent years (Return on Assets –ROA– and Return on Equity –ROE– of 1.3 percent and 12.3 percent respectively, compared to ROA and ROE of 1.6 and 14.2 percent, respectively, in 2013, and even higher rates prior to the global financial crisis). With the sector’s loan to deposit ratio increasing to 121 percent, in the face of external funding volatility due to global market uncertainty, and in part due to macro-prudential measures to curb household borrowing, credit growth has slowed down, dropping to 18.5 percent as of end 2014, about nine percentage points slower than the average of past years. Notably, the SME share in total credit declined in the aftermath of the global crisis by about five percentage points to just over 20 percent in 2009, the sharp fall demonstrating how SMEs are among the first and most affected during financial distress. During economic downturns, working capital becomes a priority for SMEs as they typically experience delays in the payments for goods sold and services provided. Overall, they receive only 27 percent of total loans and grow slower relative to both large enterprises in Turkey and SMEs in peer comparison countries.

9. Non-bank financial intermediaries can play an increasingly important role to support exporters and SMEs. Beyond larger exporters and SMEs in their value chain, Turkey’s firm distribution reveals a surprising lack of dynamism among Turkey’s mid-sized firms in terms of exports (as well as productivity growth) - a phenomenon called missing middle. Leasing allows SMEs access to income-producing assets without a significant base for collateral, and can play a critical role in their inclusion in the formal financial system. Leasing remains underdeveloped, with Turkey ranking below most European countries with respect to leasing penetration, with a rate of about 0.7 percent of annual leasing volume to GDP. Although the leasing sector is the largest financial segment after banking (capturing about 40 percent of the non-bank financial sector), its assets correspond to about one percent of total financial sector assets. The largest users of leasing are SMEs and the average term stands at three years.

10. The World Bank has been working through various channels to support long term finance, SMEs and exporters. Over the past fifteen years, the World Bank has provided lines of credit for SMEs and exporters as a bridge until financial infrastructure constraints are lifted and alternative sources of long-term finance are developed, which can be a long-term process. The government has been taking significant steps to lift these constraints, in many instances with the support of the World Bank – for example through DPF supporting reform on capital markets, leasing and factoring, and technical assistance to strengthen Turkey’s capital markets, non-bank financial sector, and financial infrastructure.

Relationship to CAS/CPS/CPF

11. The project is consistent with and supports the IBRD/IFC/MIGA Country Partnership Strategy (CPS) for the FY12-16 period, including the updated Progress Report. The CPS has three main strategic objectives and pillars: (i) enhanced competitiveness and employment; (ii) improved equity and public services; and (iii) deepened sustainable development. The project supports the strategic objectives of enhancing competitiveness and employment that includes the provision of medium and long-term funding to SMEs and exporters. The project is also consistent with the government’s latest MSME Strategy and Action Plan, the Turkish Exports Strategy for 2023, as well as the 10th National Development Plan (NDP) and the NDP priority transformation action plans.

C. Proposed Development Objective(s)

Proposed Development Objective(s) (From PCN)

The Project Development Objective (PDO) is to improve access to longer term finance for export oriented small, medium and large enterprises.

Key Results (From PCN)

13. Key PDO indicators include the following: (i) Ratio of the average maturity of sub-finance under the project, over the average maturity of Participating Financial Intermediaries' (PFIs) portfolio (for Large Enterprises –LEs- or SMEs and by PFI segment); and (ii) Number of LEs or SME beneficiaries financed under the project.
14. Key intermediate indicators and additional indicators, monitored for analytical purposes and aimed to help improve exports and SME related policies and projects will also be developed. Key intermediate indicators (e.g. increase in exports by LEs and SMEs, volume of support, financial performance indicators, compliance with prudential indicators) and additional indicators (e.g. profile –including gender- and performance of LEs, SMEs, and their financing) will be monitored for analytical purposes and aimed to help improve LE or SME related policies and projects.

D. Concept Description

15. Two project components will provide a total of US$300 million to be intermediated by Eximbank through on-lending to banks and leasing companies and by direct lending targeting export oriented LEs and SMEs. The credit line, guaranteed by the Turkish government, will be intermediated by Eximbank, which will be the Borrower and implementing agency for this project. Export oriented enterprises include existing and potential exporters, with enterprises making an initial export commitment. Ultimately, the exporter submits to the PFI the customs declaration form at an amount at least equal to the allocated credit and not later than the maturity date of the credit plus one month. The customs declaration from is annexed by the PFI with its export credit, ensuring that the exporter cannot benefit from multiple loans for the same goods.
Under Component 1, Eximbank will on-lend funds through PFIs, which can be banks (including participation banks, i.e. Islamic finance) and leasing companies. Eximbank will select PFIs pursuant to criteria agreed with the World Bank, and subject to no objection by the World Bank. The selected PFIs will, in turn, provide sub-finance to private export oriented LEs and SMEs, the final beneficiaries of the credit line. The PFIs will assume the credit risk of the sub-borrowers that will be selected based on agreed upon eligibility criteria. Eximbank will have exposure only to the selected PFIs and will assume the credit risk for on-lending funds to PFIs. Sub-finance will be for longer term investment financing and short term working capital financing (to accommodate the nature of export finance, potential delays in the payments for goods sold and services provided in an uncertain macro-financial environment, as well as, more generally, to provide flexibility to smaller size enterprises).
Under Component 2, Eximbank will act as a PFI (and will be bound by the same upper exposure limit as other PFIs at USD60 million), lending directly to export oriented LEs and SMEs, assuming the credit risk of sub-finance to the sub-borrowers. The eligibility criteria of sub-finance and for sub-borrowers will be different under Component 1 and 2 to reflect the differences in financing models. Eximbank direct lending will be more targeted (e.g. in terms of targeting new exporters, smaller beneficiary size, longer maturity length, etc.).
16. On-lending will take place on an 'open doors' and 'first come first serve' model for interested and qualifying financial intermediaries. Financial intermediaries that satisfy the PFI eligibility criteria will sign Subsidiary Finance Agreements (SFAs) with Eximbank and be assigned PFI status (at any stage during project implementation). The PFI status will not impose any cost, or oblige the financial intermediaries to access funding. There will be a maximum utilization of the funding per PFI (including Eximbank as a direct lending PFI under Component 2). PFIs will

make a request to Eximbank to refinance eligible sub-finance extended to eligible final borrowers for eligible sub-projects. PFIs will be served on a ‘first-come first-serve’ basis until the funding is fully utilized. The PFI subsidiary-finance amount will be equivalent to the aggregate amount of principals of all sub-finance made by the respective PFI. The PFIs will be required to repay interest and principal on the PFI subsidiary-finance.

17. This will be the first time an ‘open doors’ and ‘first-come first-serve’ approach will be used in Turkey. The advantage of ‘open doors’ is that a wider base of financial intermediaries will be tapped – among banks, participation banks, and leasing companies. A ‘first-come first-serve’ model will promote competition among financial intermediaries, although upper limits will ensure that capture is avoided.

18. Project preparation will include detailed definition of eligibility criteria, and terms and conditions: (i) the Loan terms and conditions between IBRD and Eximbank; (ii) the eligibility criteria for the PFIs that will be financed by Eximbank, and the terms and conditions of subsidiary finance between Eximbank and PFIs; and (iii) the eligibility criteria for the LEs and SMEs that will be financed by PFIs (and separately Eximbank under direct financing), and terms and conditions of sub-finance between PFIs (and separately Eximbank under direct financing) and LEs/ SMEs.

II. SAFEGUARDS

A. Project location and salient physical characteristics relevant to the safeguard analysis (if known)

Eximbank and PFIs will provide sub-loans to SMEs and Large Enterprises (LEs) throughout Turkey, so the project locations are unclear at this moment. The client will need to prepare an umbrella framework (environmental management framework-EMF) to discuss the process of sub-project screening, impact assessment and due-diligence analysis as per national environmental requirements and safeguard policies of the Bank. There is no sector specific limitation regarding the type of SMEs or LEs to be financed.

B. Borrower’s Institutional Capacity for Safeguard Policies

Eximbank will be responsible for the implementation of the project and was selected based on its experience with exporters, SMEs and with World Bank projects. Eximbank was selected for its experience with exporters and the World Bank. Eximbank, Turkey’s sole official export financing institution with a lending portfolio of over US$20 billion, has extensive experience in the export sector, and in direct lending and on-lending through PFIs. Additional criteria for selecting Eximbank include the Bank’s financial soundness, and its good performance as one of the Borrowers in the completed EFIL IV (P096858) and EFIL I (P065188) projects financed by the World Bank. During EFIL project implementation, Eximbank dedicated staff for the implementation of environmental management framework. Dedicated staff participated in Bank's safeguards trainings and improved their capacity on OPs. For this new loan Eximbank is establishing a PIU which includes staff who were experienced in the safeguards implementation of the previous WB projects and other IFI projects (i.e. MIGA project in 2015).

The Project Implementation Unit (PIU) at Eximbank is staffed with qualified personnel, capable of satisfactorily implementing all aspects of the project, already performed under past World Bank projects. Its responsibilities will include: (i) selection of and on-lending to PFIs; (ii) monitoring of PFIs to ensure compliance with project criteria; (iii) coordination of Eximbank’s direct lending; (iv) responsibility for adherence to all fiduciary and safeguard requirements of the World Bank for final borrowers; and (v) monitoring and evaluation based on key project development indicators.

It should be noted that in this new loan Eximbank will also be responsible for coordinating the PFIs for the successful implementation of the EMF and therefore may need more training related to safeguards concepts. Training arrangements will be discussed during project preparation and will be reflected in the PAD and Appraisal stage ISDS.

Eximbank will screen out sub-projects that could trigger OP 4.12. The Bank will conduct relevant training and capacity building for the FI to screen sub-projects and to monitor the PFIs to successfully screen sub-projects.

C. Environmental and Social Safeguards Specialists on the Team

Arzu Uraz (GSU03)

Esra Arikan (GEN03)

D. POLICIES THAT MIGHT APPLY

Safeguard Policies	Triggered?	Explanation (Optional)
Environmental Assessment OP/BP 4.01	Yes	The Environmental Category of the project is FI, since it'll be conducted via a Financial Intermediary Bank. And since it'll be an on-lending project to SMEs and LEs, the investments (sub-projects) will not be identified until project implementation. Environmental issues of the sub-projects will be addressed through the sub-loan environmental eligibility assessments. Environmental review process will be carried out in accordance with both Government of Turkey's environmental legislation and World Bank OP 4.01 requirements. Due to the nature of the project, working capital or investment loan applications are expected. Working capital loans are generally targeted to purchase of raw material. Investment loans are expected to mainly focus on equipment purchase/replacement. To be on the safe side the Environmental Management FW (EMF) will also address small scale construction works and its review and assessment process although it is not expected that Eximbank will focus on construction involved sub-loan agreements. It is expected that there will be no large scale significant and/or irreversible impacts. Sub-projects in environmental Category A will not be eligible for funding. The environmental assessment (including environmental due diligence) procedures will be conducted according to the environmental review/

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		management framework (EMF) that will be prepared by Eximbank and approved by WB. The EMF will also include evaluation forms for assessing the environmental due-diligence of the existing facilities which will be applying for working capital or investment loans. While on-lending the PFIs, Eximbank will include the EMF as part of the sub-loan agreement and will be responsible for monitoring and ensuring the satisfactory performance of PFIs to comply with the EMF. None of the safeguards policies other than OP 4.01 is being triggered, with the understanding that 1) any sub-projects that could trigger the other safeguards policies will not be eligible for financing, 2) the EMF will include a checklist to ensure that sub-projects are screened according to this criteria, 3) the Bank will conduct relevant training and capacity building for the FI to screen sub-projects and to monitor the PFIs to successfully screen sub-projects, and 4) the Bank will conduct prior review for an initial set of sub-projects and from then after conduct supervision spot checks for a number of sub-projects.
Natural Habitats OP/BP 4.04	No	Most of the sub-loans will not involve construction works. For the cases where small scale construction works are involved, projects in natural habitats will not be eligible for financing.
Forests OP/BP 4.36	No	
Pest Management OP 4.09	No	
Physical Cultural Resources OP/BP 4.11	No	
Indigenous Peoples OP/BP 4.10	No	
Involuntary Resettlement OP/BP 4.12	No	Any sub-project that involves involuntary land acquisition that will trigger OP 4.12 will not be eligible for financing. The EMF will include a checklist to ensure that sub-projects are screened according to this criteria. The Bank will conduct relevant training and capacity building for the FI (Exim) to screen sub-projects. The Bank will monitor the PFIs to successfully screen sub-projects, and the Bank will conduct prior review for an initial set of

		sub-projects and from then after conduct supervision spot checks for a number of sub-projects. Eximbank should not fund projects that have also recently acquired land involuntarily in anticipation of use for the project to be funded by Eximbank.
Safety of Dams OP/BP 4.37	No	
Projects on International Waterways OP/BP 7.50	No	Eximbank will screen sub-projects to ensure that the investments (if related to water sources) are located in the basins listed as national waterways (positive list of basins of Turkey). The full list of national waterways will be provided in the EMF document.
Projects in Disputed Areas OP/ BP 7.60	No	

E. Safeguard Preparation Plan

1. Tentative target date for preparing the PAD Stage ISDS

01-Mar-2016

2. Time frame for launching and completing the safeguard-related studies that may be needed. The specific studies and their timing should be specified in the PAD-stage ISDS.

Eximbank will prepare an Operations Manual that will include the environmental review procedures and implementation arrangements under this project. The Environmental Review section will be shared with the WB and, after consent, the plan will be translated to Turkish and will be disclosed in Eximbank's web site. The Environmental Review will also be included in the subsidiary loan agreements between Eximbank and selected PFIs. The World Bank will provide training to Eximbank and PFI staff to ensure that they understand the requirements and screening of the WB OPs, and continuous support and guidance will be provided as necessary.

III. Contact point

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Contact: Alper Ahmet Oguz
Title: Sr Financial Sector Spec.

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V. Approval

Task Team Leader(s):	Name: Ilias Skamnelos,Alper Ahmet Oguz	
Approved By		
Safeguards Advisor:	Name: Agnes I. Kiss (SA)	Date: 07-Mar-2016
Practice Manager/ Manager:	Name: Aurora Ferrari (PMGR)	Date: 07-Mar-2016
Country Director:	Name: Johannes C.M. Zutt (CD)	Date: 09-Mar-2016

1 Reminder: The Bank's Disclosure Policy requires that safeguard-related documents be disclosed before appraisal (i) at the InfoShop and (ii) in country, at publicly accessible locations and in a form and language that are accessible to potentially affected persons.