

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

**Report No.:** PIDISDSC15528

**Date Prepared/Updated:** 19-Oct-2015

**I. BASIC INFORMATION**

**A. Basic Project Data**

<b>Country:</b>	Turkey	<b>Project ID:</b>	P157691
		<b>Parent Project ID (if any):</b>	
<b>Project Name:</b>	Micro Small and Medium Enterprise Project (P157691)		
<b>Region:</b>	EUROPE AND CENTRAL ASIA		
<b>Estimated Appraisal Date:</b>	19-Oct-2015	<b>Estimated Board Date:</b>	21-Dec-2015
<b>Practice Area (Lead):</b>	Finance & Markets	<b>Lending Instrument:</b>	Investment Project Financing
<b>Sector(s):</b>	SME Finance (75%), Banking (25%)		
<b>Theme(s):</b>	Micro, Small and Medium Enterprise support (75%), Other Financial Sector Development (25%)		
<b>Borrower(s):</b>	Türkiye Halk Bankası A.Ş. (Halkbank)		
<b>Implementing Agency:</b>	Türkiye Halk Bankası A.Ş. (Halkbank)		
<b>Financing (in USD Million)</b>			
	<b>Financing Source</b>	<b>Amount</b>	
	Borrower	0.00	
	International Bank for Reconstruction and Development	200.00	
	Total Project Cost	200.00	
<b>Environmental Category:</b>	F - Financial Intermediary Assessment		
<b>Concept Review Decision:</b>	Track I - The review did authorize the preparation to continue		
<b>Is this a Repeater project?</b>	No		
<b>Other Decision (as needed):</b>			

## **B. Introduction and Context**

### **Country Context**

Turkey's achievements have recently been challenged by an uncertain 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. Despite strong exports and supportive government spending, real GDP growth dropped to 2.9 percent in 2014. Exchange rate pass-through and higher food prices pushed inflation to 8.2 percent by end 2014, much higher than the Central Bank's target rate. Moderate growth and exchange rate depreciation reduced external imbalances, and the current account deficit (CAD) narrowed to below 6 percent of GDP in 2014, from close to 10 percent in 2011. Nevertheless, the CAD remains large, while financing becomes difficult. The hoped-for external adjustment fueled by a weaker lira and significantly lower oil prices has not materialized. Despite a significantly lower energy deficit, Turkey's CAD widened to USD45 billion in the 12 months through July 2015 (gold adjusted). The deterioration is mainly due to weaknesses in trading partners, particularly slow growth in the EU, difficulties in MENA and Russia, and a fall in tourism revenues over the summer of 2015. On the financing side, domestic political concerns and global financial market jitters dried up short-term inflows.

Growth outlook remains subdued, despite stronger than expected growth in the first half of 2015. Economic growth surprised positively with 3.4 percent in the first half of 2015, up from 2.9 percent in 2014, despite political uncertainty in the run-up to the June parliamentary election. The election resulted in a hung parliament. With another election scheduled for November 1, 2015, uncertainties continue. Against this backdrop, economic activity is expected to slow sharply in the second half of 2015. Consumer confidence hit the lowest level since January 2009, and business confidence dropped notably in August and September. Moreover, credit growth momentum fell below the Central Bank's target of 15 percent by mid-September. In addition, businesses are likely to cut investment spending from the second quarter and postpone investment decisions until a new stable political equilibrium is reached. On the external side, considering the deterioration in the gold and energy adjusted current account balance, the positive impact of lower oil prices on the current account will be very limited. Against this backdrop, we see growth slightly rising to 3.2 percent, from 2.9 percent in 2014, CAD easing to 5.5 percent of GDP, and inflation remaining well above Central Bank's target in 2015. Over the medium-term, Turkey's growth prospects depend on the recovery of private investment, structural reforms and stronger economic institutions.

### **Sectoral and Institutional Context**

Micro, Small and Medium Enterprises (MSMEs) are the most affected by access to finance constraints, despite playing a critical role in employment and growth. MSMEs are estimated to account for 99.9 percent of all enterprises, 76 percent of employment, 54 percent of investments, and 60 percent of exports. The last Investment Climate Assessment -From Crisis to Private Sector Led Growth (May 2010)- found strong evidence that MSMEs face disproportionately severe constraints in accessing finance. Overall, they receive only 27 percent of total loans and grow slower relative to both large enterprises in Turkey and MSMEs in peer comparison countries. Micro enterprises are particularly affected, receiving only 25 percent of MSME loans in volume, while accounting for over 75 percent of MSME borrowers. The IFC Enterprise Finance Gap Database estimates a significant SME credit gap of over USD72 billion.

The banking sector is increasingly experiencing performance headwinds, impacting credit growth

and MSMEs that are the first casualties of financing pressures during a slowdown. The banking sector's profitability has decreased in recent years (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). As the sector's loan to deposit ratio has increased to 121 percent, and in the face of external funding volatility due to global market uncertainty, credit growth has slowed down, dropping to 24 percent as of end 2014, about nine percentage points slower than the average of past years. Notably, the MSME 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 MSMEs are among the first and most affected casualties of a financing crunch. During economic downturns, working capital becomes a priority for MSMEs as they typically experience delays in the payments for goods sold and services provided.

The banking sector is also suffering from limited access to long-term finance. The banking system is funded mostly by 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. 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.

Medium and large enterprises are particularly constrained by the lack of long-term finance, indirectly impacting MSMEs integrated into their local supplier value chains. Long term finance reduces firms' exposure to rollover and interest rate risks, enabling them to undertake longer term fixed investments. Medium and large enterprises, many times exporting firms, 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 suffering 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. Ultimately, MSMEs participating into value chains, whereby smaller enterprises are integrated as local suppliers of larger enterprises, are further impacted by the effect of the economic uncertainty on the buyers of their goods and services.

Halkbank's strategy is to increase the share of MSMEs in its loan portfolio, by ramping up recently launched programs focused on smaller enterprises and the value chain. Halkbank has traditionally focused on the MSME segment as a core business line. It had about 1.2 million MSME clients in 2014, accounting for over half of its total non-retail client base, with significant penetration in rural areas. It has the largest share of MSME loans in its loan portfolio among state-owned banks, at 39 percent, above the sector average of 27 percent.

Halkbank, similar to the overall banking sector, faces limited access to long term funding. Overall, almost 82 percent of the bank's liabilities had remaining maturities of one year or less, while over 47 percent of the bank's assets had remaining maturities of over a year. As a result, Halkbank had a negative liquidity gap spiking at the one to five year maturity.

### **Relationship to CAS/CPS/CPF**

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 MSMEs. The project is also complementary to other private and financial sector initiatives, including: (i) the Financial Sector Development technical assistance that aims to support the development of the capital markets, the non-bank financial sector, and financial infrastructure, for example in the area of secured transactions; (ii) ongoing World Bank line of credit operations (Innovative Access to Finance – P147183, SME III – P130864, and SME Energy Efficiency – P122178) that aim to provide medium to long-term finance to MSMEs and exporters; (iii) ongoing IFC projects targeting MSMEs, through bonds purchases and loans. In particular the proposed operation is a natural continuation of the SME series of projects (SME I-III, P107173, P118308, P130864) that focused on MSMEs.

### **C. Proposed Development Objective(s)**

#### **Proposed Development Objective(s) (From PCN)**

The Project Development Objective (PDO) is to improve access to finance for micro, small and medium enterprises, and longer term finance to large enterprises involved in domestic value chains.

#### **Key Results (From PCN)**

Key PDO indicators include the following:

- (a) Ratio of the average portfolio maturity of MSME and LE sub-loans under the project, over the average portfolio maturity of Halkbank's MSME and LE portfolio not financed under the project.
- (b) Number of MSME and LE beneficiaries financed under the project.
- (c) Volume of Bank support.

### **D. Concept Description**

A single component will provide USD200 million to Halkbank for extending sub-loans to MSMEs and Large Enterprises (LEs) involved in domestic value chains. For the purpose of this project, MSMEs will be defined as firms employing fewer than 250 people, and LEs as firms employing fewer than 1,000 people. The definition of a LE involved in domestic value chains will be LEs with payables against MSMEs of at least USDX. At least 60 percent of the Guaranteed Loan will be used to fund MSMEs. Although micro enterprises will be supported by the project, it is expected that the majority of the sub-loans will be to small and medium enterprises. At least 15 percent of the Loan amount allocated for MSME sub-loans, shall be utilized for MSME sub-projects in underserved Priority Regions. There will be no sectoral restrictions, and financing will be extended on market terms to avoid any distortion.

## **II. SAFEGUARDS**

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

Halkbank will provide sub-loans to MSMEs and LEs throughout Turkey, so the project locations are unclear at this moment.

### **B. Borrower's Institutional Capacity for Safeguard Policies**

Halkbank has worked with World Bank projects as a FI bank for several years and has developed a good capacity regarding safeguards. Halkbank is experienced in screening and evaluating the sub-projects regarding environmental safeguards and ensuring that mitigation measures are fully monitored and documented. Halkbank is also experienced in screening for sub-projects that could generate land acquisition or associated involuntary resettlement, and is knowledgeable that they would not be eligible for financing.

### C. Environmental and Social Safeguards Specialists on the Team

Arzu Uraz (GSURR)

Esra Arikan (GENDR)

### D. POLICIES THAT MIGHT APPLY

Safeguard Policies	Triggered?	Explanation (Optional)
Environmental Assessment OP/BP 4.01	Yes	Sub-project env. assessments carried out by Halkbank will be in accord with the Turkish Environment Law and the WB EA requirements (OP 4.01). Applications are expected for working capital or inv. loans, incl. machinery purchase/replacement or small scale constr. works. No large scale significant and/or irreversible impact is expected. Category A sub-projects will not be eligible. The EMF, which will explain the env. review procedures, will be prepared by Halkbank, and will be approved by WB.
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	Land acquisition is not eligible under the proposed project so OP 4.12 is not triggered. Halkbank will screen the sub-projects to identify those that could generate land acquisition or associated involuntary resettlement, and that would trigger the OP 4.12, and these sub-projects will not be eligible for financing. Halkbank should not fund projects that have also recently acquired land involuntarily (through expropriation) in anticipation of use for the project to be funded by Halkbank.
Safety of Dams OP/BP 4.37	No	
Projects on International Waterways OP/BP 7.50	No	Halkbank 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

20-Oct-2015

#### 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.

Halkbank will prepare an OM that will include the env. review procedures and implementation arrangements under this project. The Env. Review section (in the form of env. management framework –EMF) will be shared with the WB and, after consent, the plan will be translated to Turkish and will be disclosed in Halkbank's web site. The WB will provide training to Halkbank staff to ensure that they understand the requirements and screening of OP 4.12, and continuous support and guidance as necessary.

### III. Contact point

#### World Bank

Contact: Ilias Skamnelos

Title: Lead Financial Sector Speciali

Contact: Alper Ahmet Oguz

Title: Sr Financial Sector Spec.

#### Borrower/Client/Recipient

Name: Türkiye Halk Bankası A.Ş. (Halkbank)

Contact: Ali Fuat Taşkesenlioğlu

Title: General Manager

Email: halkbank.ir@halkbank.com.tr

#### Implementing Agencies

Name: Türkiye Halk Bankası A.Ş. (Halkbank)

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### IV. For more information contact:

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### V. Approval

Task Team Leader(s):	Name: Ilias Skamnelos, Alper Ahmet Oguz	
<b><i>Approved By</i></b>		
Safeguards Advisor:	Name: Agnes I. Kiss (SA)	Date: 19-Oct-2015
Practice Manager/ Manager:	Name: Aurora Ferrari (PMGR)	Date: 19-Oct-2015
Country Director:	Name: Eavan O'Halloran (CD)	Date: 19-Oct-2015

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.