PROJECT NAME:	**SECOND EXPORT FINANCE INTERMEDIARY LOAN (EFIL II)**

LOAN AMOUNT: **US$ 303.1 Million**
LOAN DURATION: **2004-2009 (Five years)**

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BACKGROUND: A combination of natural disasters and macroeconomic volatility in Turkey during the 1999-2002 period created an unfavorable and uncertain environment for exporting companies. In 1999, the massive destruction resulting from earthquakes impeded domestic production and led to a contraction in domestic demand. In 2000, the Government's IMF-backed stabilization program initially led to an expansion in imports and a contraction in exports. The current account worsened quickly, in part due to the anchoring of the exchange rate which eroded Turkey's competitiveness, but also as a result of an increase in oil prices and US$/Euro exchange rate developments which favored importers. The worsening fiscal and current account performance generated pressures on the fixed exchange rate system, and in combination with longstanding underlying structural banking sector problems, triggered banking crises in November 2000 and February 2001. In February 2001, the fixed exchange rate regime collapsed. The Turkish Lira was allowed to float and depreciated sharply, improving the competitiveness of Turkish exports. Many banks and local businesses were caught up in foreign exchange short positions and suffered significant losses. The magnitude and frequency of exchange rate fluctuations in the period immediately following the start of the floating exchange rate regime added to business uncertainty. Domestic demand dried up and the economy shrank significantly during 2001.

For a large number of companies, especially for those with limited export sales, 2001 was a period where they had to overcome difficulties in meeting working capital financing requirements and generating sufficient funds to maintain profitability and a sustainable financial structure in a shrinking economy, and uncertain macroeconomic and political environment. However, the depreciation of the currency in 2001 did create incentives for exporting activities, and some businesses could benefit from the price advantage. Firms, which could continue to produce, and which faced a rather price-elastic international demand, increased their export performance substantially.

In early 2002, economic recovery started and continued throughout that year and during the first half of 2003. GNP growth reached 7.8 percent in 2002, due among other factors to the strong growth in exports and tourism revenues following the 2001 exchange rate adjustment. Export growth continued steadily throughout 2002-03, despite a subsequent appreciation of the real effective exchange rate reflecting increased confidence in the TL, due to a sharp fall in real private sector wages after the crisis.

However, even though economic performance, mostly led by the export revival, continued to improve during the latter half of 2002 and the first half of 2003, the pick up in market sentiment did not readily lead to any significant increase in the overall level of bank credits to the productive sectors. Although the banking sector was significantly restructured and strengthened in the aftermath of the crises, banks were still risk averse, with real interest rates continuing to hover around 20-30%, and the high level of government debt continuing to crowd out private sector financing needs. While short term foreign currency bank financing was available to the best exporters at affordable US$-based interest rates, medium and long-term working capital and investment finance was still very scarce in Turkey. Lease finance – which often is an important source of longer-term investment finance for exporters in other countries - also has remained underdeveloped in Turkey, with the growth in lease receivables highly volatile and dependent on macroeconomic performance. Both the banking and leasing sectors lacked access to medium and long term funds, which provided the principal rationale for the Bank's involvement and the EFIL II.

PROJECT OBJECTIVE: The main objective of EFIL II project is to follow through on the achievement of the predecessor EFIL I project that has been successfully implemented during FY 99-04, and continue to serve as a catalyst to support export and real sector growth in Turkey. To this end, the project provides medium and long-term working capital and investment finance to Turkish exporting enterprises. One other main benefit of the project is fast private sector recovery and job creation, supported by a healthier and more developed financial system.

The project's **main objective** is to follow through on the achievement of the predecessor EFIL project and continue to serve as a catalyst to support export and real sector growth in Turkey during the EFIL II implementation period (2004-2009) and beyond, using the EFIL II reflows. To this end, the project provides medium and long-term working capital and investment finance to Turkish private exporting enterprises, at the time when export performance and demand for longer term credit is on the rise, while the financial sector is still unable to support these trends with much needed longer term funds.

The **secondary objective** of the loan is further improvement in the ability of the Turkish financial sector to provide financial resources to the enterprise sector, through further development of intermediation by private financial institutions, including banks and leasing companies. The project, through inclusion of leasing companies in addition to banks as PFIs, enables the Bank to start a dialogue with the leasing sector in Turkey, provides an opportunity to gain more insight into the sector, and enables the Bank to support its development. It needs to be noted that the inclusion of leasing companies as financial intermediaries is an innovative aspect of the project, not previously used in World Bank credit line operations in the ECA Region.

PROJECT DESCRIPTION: EFIL II project has a single component- a credit line for exporters that provides medium and long-term funds to exporters through two distinct channels (i) through commercial banks in the form of investment or working capital loans and (ii) through leasing companies in the form of lease finance for acquisition of productive assets. The credit line is provided to Turkish Industrial Development Bank- Turkiye Sinai ve Kalkinma Bankasi (TSKB), with a government guarantee.

The proposed EFIL II project substantially maintains the design of its predecessor EFIL project that was successfully implemented during FY99-04. The credit line is provided to TSKB, with a government guarantee, while TSKB passes it on in the form of subsidiary finance to participating financial intermediaries for further on-lending to eligible private exporters. The credit line for exporters is the only component of the EFIL II, and provides medium and long-term funds to exporters through two distinct channels, or sub-components: (i) US$215 million through commercial banks in the form of investment or working capital loans, and (ii) US$85 million through leasing companies in the form of lease finance for acquisition of productive assets (equipment and machinery).

IMPLEMENTING AND MONITORING: TSKB, a non-deposit taking private investment & development bank owned by local commercial banks and business groups, is the borrower and the implementation agency for the project. A separate project implementation unit (PIU) has been established by TSKB under the supervision of one of its executive vice presidents to oversee the implementation of EFIL II. The PIU is staffed with experienced management and staff, and, as the primary project counterpart for the Bank team, provides the overall administration of all aspects of the credit line and reports to the Bank.

BENEFITS:

- EFIL II provides continued support to broad based Enterprise development and Job creation and protection across the Country by aggressively financing growth of exports as the engine of growth;
- Contributes to meeting some of rising investment demand by providing Long term investment loans (up to 7 years) in addition to working capital, especially when the economy needs higher levels of investment;
- Helps deepen and broaden financial intermediation—bringing NBFIs along with Banks; by working with 4 second-tier banks and 6 leasing companies and therefore scaling up horizontally;
- Emphasizes lending to SME exporters by using leasing companies as a financial intermediaries bypassing collateral hurdles;
- Creates a significant funding velocity impact of several billions through recycling of Bank fund reflows over more than 10-15 years in the system.

PROJECT STATUS: As of June 30, 2007, the loan has been fully disbursed except for a small residual amount, which has been cancelled. Thus, the project has been completed.

RESULTS ON THE GROUND: 249 exporting firms have received US$300 million worth of loans and leases. The long term financing helps them grow their business and increase their exports. The sub-borrowers in the project have grown their employment by 9 percent (or 5,000 employees) and their exports by 117 percent (or by US$ 2.5 billion) between 2003 and 2006.