



1. Project Data

Project ID

P130864

Project Name

TR SME III

Country

Turkey

Practice Area(Lead)

Finance, Competitiveness and Innovation

L/C/TF Number(s)

IBRD-82750

Closing Date (Original)

29-Dec-2017

Total Project Cost (USD)

300,000,000.00

Bank Approval Date

26-Jun-2013

Closing Date (Actual)

29-Dec-2018

IBRD/IDA (USD)
Grants (USD)

Original Commitment

300,000,000.00

0.00

Revised Commitment

300,000,000.00

0.00

Actual

300,000,000.00

0.00

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2. Project Objectives and Components

a. Objectives

According to the Loan Agreement (page 5), the project development objective of the Turkey Third Access to Finance for SMEs Project (SME III) was "to improve access to medium- and long-term finance for small and medium enterprises through lease financing."

b. Were the project objectives/key associated outcome targets revised during implementation?



No

c. Will a split evaluation be undertaken?

No

d. Components

The project had a single component.

The Line of Credit provided a financial intermediary loan (FIL) to the state-owned Türkiye Cumhuriyeti Ziraat Bankası A.Ş. (Ziraat Bank), as the apex bank, to fund a line of credit to small and medium enterprises (SMEs) through banks and leasing companies, as participating financial institutions (PFIs). Subsidiary loans from the apex bank to PFIs would: (a) carry a minimum maturity of 5 years; (b) charge loan rates that covered the cost of funds plus an administrative overhead plus a risk premium; and, (c) be capped at a maximum US\$60 million for each PFI (dropped during the second restructuring). Sub-loans from PFIs to SMEs for sub-projects would: (a) carry a minimum maturity of 3 years; (b) apply the same risk-based interest rate formula; and, (c) be capped at US\$5 million for each SME sub-borrower and US\$3.5 million for each SME sub-loan. The apex bank would assume the credit risk of the PFIs, and the PFIs would assume the credit risk of the SME borrowers.

e. Comments on Project Cost, Financing, Borrower Contribution, and Dates

Project Cost: The cost of the project was estimated at appraisal at US\$375 million.

Project Financing: The project was financed by a US\$300 million loan from the IBRD to Ziraat Bank, the borrower. In a guarantee agreement, the Republic of Turkey unconditionally guaranteed all loan payments due to the IBRD. Moreover, under the loan agreement, Ziraat Bank was to reflow the principal repayment for the IBRD loan for another lending cycle to SMEs once the principal repayments collected by Ziraat Bank from the PFIs have reached US\$50 million. The IBRD loan was fully disbursed. Ziraat Bank started the reflow in June 2019, after accumulating repayments of US\$90 million, according to the ICR (page 37).

Borrower Contribution: Ziraat Bank and/or the PFIs were to provide co-financing for the project in the amount of 25 percent of the project loan, US\$75 million. According to the ICR (page 13), the PFIs provided US\$83 million of their own funds to co-finance sub-loans under the project, or US\$8 million more than planned at appraisal.

Dates: The project was approved on June 26, 2013 and became effective on December 13, 2013. The project was restructured twice, the first on October 5, 2015, and the second on April 12, 2017. The project closed on December 29, 2018, one year after the original closing date of December 29, 2017.

Restructuring: The first restructuring, with US\$41.8 million (13.9 percent) of the US\$300 million IBRD loan disbursed, loosened financial covenants that were deemed too restrictive. The Amendment to the Loan Agreement of October 5, 2015: (a) raised the debt-to-equity ratio required of SMEs from 80:20 to 85:15; (b) lowered the debt-service-coverage ratio required of SMEs from 1.2:1 to 1.1:1; (c) scrapped the application of these two covenants for sub-loans that were equal to or lower than US\$1 million and for SMEs in the “priority regions” of the country; and, (d) redefined SMEs as having assets less than Turkish Lira (TL) 40 million, sales of less than TL 40 million, and employees fewer than 250, following the new government



definition of SMEs of November 2012. The second restructuring, with US\$133 (44.3 percent) of the US\$300 million IBRD loan disbursed, made further changes to financial covenants. The Amendment to the Loan Agreement of April 12, 2017: (a) removed the limit on the maximum aggregate amount of subsidiary loans allowed for each PFI (US\$60 million); (b) lifted the requirement that at least 15 percent of the project loan be used for sub-projects in the “priority regions”; (c) updated the project procurement guidelines to make them consistent with the new Bank Procurement Framework of 2016; (d) narrowed the definition of SMEs to a single benchmark – number of employees fewer than 250; and, (e) extended the project closing date by a year.

3. Relevance of Objectives

Rationale

The project objective was highly relevant to the problems of, and development strategies for, the SME sector, both at project appraisal and closing.

- Ninety-nine percent of all enterprises in Turkey were SMEs, and they were vital to the national economy, accounting for 55 percent of total value-added, 50 percent of investments, 59 percent of exports, 65 percent of sales, and 78 percent of employment.
- Yet, SMEs faced disproportionately severe constraints with access to finance, according to the Investment Climate Assessment of 2010, which cited the lack of cash-flow-based financing and the high collateral requirements for loans as significant problems for SMEs. Overall, SMEs, which contributed more than half of value-added in the economy, obtained only 25 percent of all loans.
- SMEs were also at considerable risk during credit crunch episodes. In 2009, their share of total credit dropped to 20 percent following the global financial crisis of 2008. And, in 2012, they were severely affected by the deceleration in credit growth in Turkey (from 30 percent in 2011 to 16 percent in 2012), as the authorities tightened monetary policy and prudential regulations in response to uncertainties in global and Euro area growth.
- The government had drafted successive SME Strategy and Action Plans (SSAPs) to support the SME sector, the first in 2003 as Turkey considered applying for accession to the European Union. At the time of project appraisal, the SSAP for 2011-13 and the Ninth Development Plan for 2007-13 focused on access to finance as one of five strategic national development priorities. Both plans advanced actions to improve SME access to bank loans, venture capital investment, and capital market finance.
- In 2012, and with Bank support, Parliament enacted the Leasing, Factoring, and Financing Companies Law that aimed to promote the growth of the leasing industry, address operational barriers to lease transactions, establish a registry of leasing contracts and leased movable assets, and equalize treatment between foreign and local leasing companies. SMEs were the largest users of leasing in Turkey and the development of the leasing industry was expected to improve access to finance by SMEs.
- At project closing, the SSAP for 2016-20 and the Tenth Development Plan for 2014-18 continued to advocate state support for SMEs and for entrepreneurship, emphasizing that access to finance for SMEs would be facilitated, including by improving angel investments, venture capital, credit guarantees, and capital markets.



The project objective was aligned with the Bank Group strategy in Turkey at the time of project appraisal and project closing.

- The “Country Partnership Strategy for the Republic of Turkey for the Period 2012-2015” (CPS) focused on three strategic objectives --- to enhance competitiveness and employment, to improve equity and public services, and to deepen sustainable development. The project objective was aligned with one of several outcomes targeted by the first CPS strategic objective --- a “deepened and broadened access to finance.”
- At the time of project appraisal, Bank support for SMEs in Turkey had begun more than a decade earlier and delivered some US\$4 billion of commitments in over 11 credit line operations that also targeted exporters and energy sector enterprises. According to the PAD (page 4), a Bank study in 2011 had concluded that the credit-line projects were successful at addressing the working capital and the investment financing needs of SMEs and exporters. Three credit line operations were ongoing at the time of appraisal --- the Fourth Export Finance Intermediation Loan Project, the Second Access to Finance for SMEs Project, and the SME Energy Efficiency Project, all of which aimed to provide medium- and long-term finance to SMEs and exporters. Ziraat Bank was itself a PFI under two of these --- the Second Access to Finance for SMEs Project and the SME Energy Efficiency Project --- and had gained knowledge and experience with Bank operations, including with safeguards requirements and fiduciary guidelines.
- The project objective remained aligned with the Bank Group strategy in Turkey at the time of project closing. The “Country Partnership Framework for the Republic of Turkey for the Period FY18-FY21” (CPF) focused on three areas of engagement --- growth, inclusion, and sustainability. The project objective was aligned with the first focus area, which aimed to: (a) increase fiscal space; (b) “increase access to finance for under-served markets”; and, (c) enhance competitiveness and employment. The CPF objective to “increase access to finance for under-served areas” would be evidenced by the number of persons, SMEs, and exporters provided with financial services.

Rating

High

4. Achievement of Objectives (Efficacy)

OBJECTIVE 1

Objective

To improve access to medium- and long-term finance for small and medium enterprises through lease financing.

Rationale

Theory of Change: Providing long-term funds to financial institutions through an apex bank would enable the financial institutions to increase long-term lease financing and to offer new leasing products to SMEs. Lease



financing would convey to SMEs the benefits of fixed rates, longer maturities, and no additional collateral requirements, which were important for small firms and new entrepreneurs. Lease financing would also bring small firms into the formal financial system, allowing them to build a history of financial transactions, which was important in economies where the business environment, in terms of creditor rights, collateral laws, and asset registries, were not robust for small firms. The provision by financial institutions of leases to SMEs would improve access by SMEs to medium- and long-term finance.

Outputs: The project achieved all four of the intermediate results targets set at appraisal.

- The number of PFIs participating in the project was nine by end-2018, exceeding the target of 6 PFIs. The PFIs were all leasing companies, all of which were subsidiaries of banks.
- The percent of the project loans disbursed that financed sub-projects in “priority regions” of the country was 15.24 percent by end-2018, meeting the target of 15 percent. The “priority regions” were previously defined by the Council of Ministers under Decree No. 2012/3839. This target --- either that sub-project capital investment were located in the “priority regions” or that sub-project working capital were used in the “priority regions” was set in the Loan Agreement, but scrapped in the second restructuring. The 15 percent target was met by the project nonetheless.
- The volume of bank support for SMEs (i.e., the dollar value of lines of credit for MSEs) was US\$383 million by end-June 2018, exceeding the target of US\$300 million.
- Ziraat Bank and the PFIs complied with prudential regulations (i.e., regulations that require financial firms to control risks and hold adequate capital as defined by capital requirements, liquidity requirements, concentration risk or large exposure limits, reporting and public disclosure requirements, and supervisory controls and processes), meeting the target.

Outcomes: The project achieved four of the five outcome indicator targets defined at appraisal.

- The number of SME beneficiaries financed by PFIs under the project was 925, exceeding the target of 500 SME beneficiaries. The SMEs were enterprises in the industrial (food processing, garment and textile, household appliance, etc.) and service (consulting, informatics, and tourism, etc.) sectors.
- The number of new SME beneficiaries financed by PFIs under the project (SMEs that had not received financing from the PFI in the past) as a percentage of the total number of SME beneficiaries financed by PFIs was 41 percent (i.e., 41 percent of SMEs financed by PFIs under the project were new), exceeding the target of 10 percent.
- The ratio of the average maturity of sub-loans financed under the project to the maturity of the SME leasing portfolio of the PFIs was 1.8 (i.e., the average maturity of sub-loans financed under the project was 80 percent longer than that the maturity of leases financed by the PFIs using their own financial resources), meeting the target that the ratio exceed 1. The average maturity of sub-loans under the project was around four and a half years, according to data reported by Ziraat Bank in May 2019.
- The number of new PFIs under the project (PFIs that had not received funding from IFIs in the past) was two, meeting the target of two PFIs. Of the nine PFIs participating in the project, two had not received any financing from an IFI before this project.
- The number of PFIs introducing new leasing products was one, failing to meet the target of three PFIs. Of the nine PFIs participating in the project, only one offered a non-finance lease --- a sale-and-leaseback contract (a hybrid debt product wherein an enterprise sells a procured asset to a leasing firm and leases the asset back, allowing the enterprise to gain access to the asset without increasing its debt). The ICR (page 14) offers some reasons for the limited progress with this target: (a) the PFIs



had low institutional capacity to innovate; (b) the sale-and-leaseback (in which an enterprise leases back a procured asset that it had sold to a leasing firm) could not easily comply with Bank procurement rules and financial management guidelines; and, (c) there were market constraints to the introduction of the operating lease (in which a leasing firm assumes ownership of the leased asset at the end of leasing term) --- the product required an active second-hand market for the leased asset, but these markets remained thin in Turkey.

Core Sector Indicators: The ICR (pages 28-31) also reported the results for five “core indicators”, which were drawn from the Bank’s “Results Platform – Core Sector Indicators” (the list of July 2013). For the MSME Finance sector, the Bank’s “core indicators” cover: the volume of Bank funding for SME finance (6 indicators); outreach (9); portfolio quality (4); and, financial sustainability (3). The PAD (pages 12-15) listed, but did not define any targets, for five “core indicators” for this project. The ICR reported the following:

- The outstanding SME loan portfolio of the PFIs (i.e., their total SME loan portfolio, including that financed by the IBRD project loan) was US\$2.385 billion by end-2017.
- The number of active SME loan accounts of the PFIs (i.e., the total number of SME loan accounts, including that financed by the IBRD project loan) was 19,400 by end-2017.
- The percent of the SME loan portfolio at risk (following the definition for non-performing loans set by the Banking Supervision and Regulation Authority) at Ziraat Bank and at the PFIs, including that of the portfolios financed by the IBRD project loan was 1.6 percent by end-June 2018. The baseline value was 2.9 percent in end-2012.
- The return on equity of the project was 14.7 percent by end-June 2018. The baseline value was 17.6 percent in end-2012.
- The return on assets of the project was 1.7 percent by end-June 2018. The baseline value was also 1.7 percent in end-2012.

Rating

Substantial

OVERALL EFFICACY

Rationale

The degree of achievement of the project development objective is assessed as substantial. The project achieved all four output targets and four of five outcome targets.

Overall Efficacy Rating

Substantial



5. Efficiency

Economic Efficiency: The PAD did not conduct an economic or financial efficiency analysis of the project. The PAD (page 9) argued that SME sub-projects could not be identified ex-ante and, therefore, a traditional economic and financial analysis of the project could not be conducted.

The ICR (page 15) did not conduct an economic analysis of the project either, arguing that an economic analysis would require considerable resources and the participation of many parties including Ziraat Bank, the PFIs, and SME project beneficiaries, but would have lacked baseline data anyway. The ICR instead posits that the project yielded positive economic benefits: (a) the project was cost-effective because Ziraat Bank re-flowed principal payments collected from the PIFs into at least another round of lending to SMEs; and, (b) the project advanced equity objectives because more than 15 percent of the IBRD loan was directed at SME sub-projects in priority regions of the country.

Operational Efficiency: The project was restructured twice, triggered by lower-than-expected Bank loan disbursement rates. Moreover, the project closed one year later than originally scheduled.

Efficiency Rating

Modest

a. If available, enter the Economic Rate of Return (ERR) and/or Financial Rate of Return (FRR) at appraisal and the re-estimated value at evaluation:

	Rate Available?	Point value (%)	*Coverage/Scope (%)
Appraisal		0	0 <input type="checkbox"/> Not Applicable
ICR Estimate		0	0 <input type="checkbox"/> Not Applicable

* Refers to percent of total project cost for which ERR/FRR was calculated.

6. Outcome

The project development objective was highly relevant to development priorities in Turkey and to the Bank Group country strategy for Turkey. The project's efficacy in achieving the project development objective was substantial, with the project achieving all four output targets and four of five outcome targets set at appraisal. The efficiency of the of the project, however, was modest, with little basis for judging economic efficiency. Delays with the IBRD loan disbursements preceding two restructurings and with project closing reflected operational inefficiencies.

a. Outcome Rating

Moderately Satisfactory



7. Risk to Development Outcome

Macroeconomic risk: Although economic growth resumed in the first half of 2019 following a sharp depreciation of the currency and an associated recession in the second half of 2018, the Turkish economy remains susceptible to external and domestic risks, according to the IMF (the 2019 Article IV Consultation). Expansionary fiscal policy and rapid credit expansion by state banks aided the turnaround, but the recovery remains fragile --- nonfinancial corporate balance sheets are stressed, private sector foreign exchange debt is high, international reserves are low, bank loan restructuring has increased, and the quality of bank assets is strained. The probability of weak near- to medium-term growth poses risks to both the business prospects for SMEs and the financial capacity of PFIs to expand lending to SMEs, with the risks likely to be substantial if, as the IMF warns, Turkey were to stall with structural reforms.

Institutional capacity risk: The PFIs need continuous capacity building with various aspects of SME project and portfolio management, including with Bank guidelines for procurement, environmental safeguards, and monitoring and evaluation. Institutional and staff knowledge of these topics are important as the apex bank reflows principal payments from subsidiary loans to PFIs for another round of lending to SMEs. The ICR (page 23) cites the need for the maintenance of "core teams" at the PFIs as well as the continuous training of the staff for these functions, although the operational experience of the PFIs with the project in 2014-2018 would appear to make this risk modest.

8. Assessment of Bank Performance

a. Quality-at-Entry

The theory of change was sound. Drawn by the ICR (pages 6-7) from the results framework detailed in the PAD (pages 12-17), the underlying results chain was: providing long-term funds to financial institutions through an apex bank would encourage the financial institutions to increase long-term loans and to offer new leasing products to SMEs.

The institutional capacity of Ziraat Bank to act as the apex bank in financial intermediary lending was well-vetted by the Bank. An SOE, Ziraat Bank was the largest bank by branches in Turkey and the second largest by assets, with a loan portfolio of US\$40 billion and extensive experience in direct lending to SMEs. Ziraat Bank had completed a financial and operational restructuring in 2001 and in 2011, which, according to the PAD (pages 35-38), strengthened its financial position and improved its corporate governance. According to the ICR (page 9), the Bank concluded, after a due diligence review at appraisal, that Ziraat Bank had the financial and operational capacity to fulfill the functions of an apex bank.

Apart from clearly setting the terms and conditions of subsidiary loans from the apex bank to PFIs and of sub-loans from the PFIs to SMEs, the Bank established quantitative criteria for the eligibility of PFIs and SMEs, following lessons learned from previous line of credit operations that quantitative criteria for PFI and SME eligibility represented "good operational practice". Set in the Loan Agreement (pages 6-16) as loan covenants, the eligibility criteria for PFIs covered the PFI's: legal status, size of total assets or total lease receivables, regulatory compliance, and profitability. Eligibility criteria for SMEs pertained



to their: private ownership, debt ratios, availability of cash flow statements, and compliance with government laws and regulations. Criteria for SME loans were also clearly established: technical feasibility and commercial viability, compliance with environmental laws and regulations, and a negative list.

The Bank designed mitigation measures to address risks that it identified as threats to the efficient implementation of the project. The PAD (pages 30-33) listed "implementing agency capacity risk" as a substantial risk --- it would be the first time that Ziraat Bank would act as an apex bank to PFIs, and "project design risk" as a moderate risk --- co-financing requirements and the reflow of principal payments were new elements in the Bank's line of credit operations in Turkey. To address the foregoing risks, the Bank required that Ziraat Bank and PFIs submit all subsidiary loan agreements for Bank clearance and drafted an action plan (PAD, pages 22-29) to enhance the project implementation arrangements, including by requiring Ziraat Bank to: (a) issue project implementation guidelines to PIFs; (b) have a ready information technology (IT) infrastructure for project management; (c) develop an information tool on procurement consistent with Bank guidelines; and, (d) liaise closely with their internal auditors.

There were moderate deficiencies in the quality of entry, however.

The project lacked an economic efficiency analysis at appraisal. The PAD (page 7) had stated that poor monitoring of overall project impacts had been a problem in previous Bank line of credit operations in other countries. The ICR (page 21) suggests that the PAD could have constructed a sample loan portfolio to conduct the economic analysis, obviating the need to identify projects ex-ante.

The ICR (page 21) also contends that a review of the market, institutional, and regulatory constraints to the development of new leasing products would have led to a better project design. Considering that only one PFI introduced only one new leasing product --- the sale and leaseback contract, this would be a deficiency at project entry.

The Bank could have chosen a more robust set of indicators to measure the evidence supporting the achievement of the project objective. The ICR (pages 12-14) defines four that would have measured the incremental impact of the project over the SME lending operations of the PFIs without the project.

Quality-at-Entry Rating

Moderately Satisfactory

b. Quality of supervision

A co-task team leader (co-TTL) based in the Bank country office in Istanbul maintained direct communication with the Government and provided support to Ziraat Bank. Bank staff at the country office also interacted regularly with the Government and Ziraat Bank, with these in-country consultations leading to actions in response to emerging issues. In addition, implementation support missions were fielded regularly. Bank specialists in financial management, procurement, environmental safeguards, and social safeguards helped supervise the project. Altogether, the Bank devoted some 108 staff weeks for project supervision.



Nine Implementation Status and Results Reports (ISRs) were filed, the last of which rated the project's implementation progress (IP) be moderately satisfactory and the progress toward development objectives (DO) to be satisfactory. Three Aide Memoires (one each in 2015, 2016, and 2017) were prepared, which reported on progress with the project, updated information on the country's SME sector, and always outlined the "next steps" in the implementation plan.

Two restructuring events helped address lower-than-expected Bank loan disbursement rates in 2015 and 2017. In response to market feedback, the Bank adjusted some loan covenants that were considered too restrictive --- for example, the requirement that smaller SMEs operating in the informal sector in the "priority regions" also file quality financial statements.

Overall, according to the ICR (pages 22-23), the Bank: (a) periodically verified compliance with the project legal covenants; (b) verified the eligibility of the PFIs using independent audit reports; (c) consulted regularly with the PFIs on the progress of the project; (d) visited SMEs in the field; and, (e) collected SME data, including through statistical sampling methods.

Quality of Supervision Rating

Satisfactory

Overall Bank Performance Rating

Moderately Satisfactory

9. M&E Design, Implementation, & Utilization

a. M&E Design

The results framework for the project defined: (a) 9 intermediate results, 5 of which were listed as "core indicators" without any targets, and (b) 5 PDO-level outcome indicators. The "core indicators" were drawn from the Bank's "Results Platform – Core Sector Indicators" (see Section 4).

According to the ICR (page 19), there were deficiencies with the choice of results indicators for the project. At least one of the intermediate results indicator --- the number of PFIs in the project --- was an input, rather than output, indicator. Moreover, three of the outcome indicators --- the number of SME beneficiaries, the number of new SME beneficiaries, and the number of new PFIs --- were output, rather than outcome, indicators.

The M&E plan called for Ziraat Bank, through its Project Implementation Unit, to monitor the intermediate results and PDO-level outcome indicators as well as additional indicators, both defined in the project results framework and in the project operations manual, on a quarterly, semiannual, and annual basis. Ziraat Bank would obtain M&E data from reports provided by the PFIs and from Ziraat Bank's own internal records. Ziraat Bank would use reporting templates designed jointly with the Bank and included in the project operations manual.



b. M&E Implementation

M&E was conducted regularly, as reflected in the ISRs.

However, there were cases of deficiency with M&E implementation, according to the ICR (page 20): (a) there was only one ISR filed between October 2017 and October 2018, and it reported M&E data as of June 2018, probably reflecting the lack of data at that time; (b) the ISRs did not report on “additional indicators”, principally for analytic purposes, that were required by the PAD (page 19 and 28) and defined in the project operations manual; and, (c) Ziraat Bank reported difficulty collecting data from PFIs, in part because the data were confidential to the PFIs and Ziraat Bank was a market competitor to the PFIs.

c. M&E Utilization

According to the ICR (page 20), it was not clear that M&E data were used to improve the project’s performance. For instance, the monitoring reports lacked information why the project made little progress with the results target that at least 3 PFIs introduce new leasing products --- by the project closing date, only one PFI had introduced a new leasing product.

M&E Quality Rating

Modest

10. Other Issues

a. Safeguards

Environmental Safeguards: The operation was listed as an Environmental Assessment category “FI” project and triggered safeguard policy OP/BP 4.01 (Environmental Assessment). Ziraat Bank, the borrower and project implementing agency, prepared an Environmental Assessment Framework and published the document on its website in September 2013. Made part of the project operations manual, the framework described the environmental assessment and environmental due diligence procedures to be used in sub-project evaluation and defined the responsibilities of Ziraat Bank, the PFIs, and the Bank with sub-project environmental review and clearance. According to the PAD (page 11), the framework was also consistent with the Government’s environmental assessment requirements. The project’s compliance with safeguard policy OP/BP 4.01 was rated satisfactory in October 2018, before project closing in end-2018. The ICR (page 20) quoted the apex bank stating that “the Turkish environmental legislation is already in line with EU standards and environmental risk management is a requirement for the companies when they engage in risky projects”; and “the SME investments mostly fell under category “C” which had minimal or zero environmental impact requiring no further environmental screening.”

b. Fiduciary Compliance

Procurement: The PAD (page 20) stated that PFIs were to be responsible for ensuring that SMEs complied with Bank procedures for the procurement of goods, works, and services under sub-projects



financed by the project, specifically with the Bank's "Guidelines - Procurement of Goods, Works and Non-Consulting Services under IBRD Loans and IDA Credits and Grants by World Bank Borrowers" (January 2011), "Guidelines - Selection and Employment of Consultants under IBRD Loans and IDA Credits and Grants by World Bank Borrowers" (January 2011), and "Guidelines on Preventing and Combating Fraud and Corruption in Projects Financed by IBRD Loans and IDA Credits and Grants" (October 2006 and revised in January 2011). According to the ICR (page 21), the PFIs had varying capacities to ensure compliance by SMEs with Bank procurement guidelines, however the deficiencies were addressed early by Ziraat Bank which had the capacity to perform the function. Procurement was rated satisfactory during project implementation and in the last ISR for the project.

Financial Management: The PAD (page 34) stated that the Bank would supervise the financial management of the project by reviewing: the project disbursement and financial management arrangements and performance during implementation support missions, the project's semi-annual Interim Financial Reports (IFRs), and the project's and Ziraat Bank's annual audited financial statements. The ICR (pages 20-21) reports that there had been an issue in early 2016 with the collection of financial management information from the PFIs; however, the missing information was subsequently obtained from the PFIs. The ICR also reports that Ziraat Bank and the PFIs submitted audited financial reports on time and that the audit reports were unqualified.

c. Unintended impacts (Positive or Negative)

d. Other

11. Ratings

Ratings	ICR	IEG	Reason for Disagreements/Comment
Outcome	Moderately Satisfactory	Moderately Satisfactory	
Bank Performance	Moderately Satisfactory	Moderately Satisfactory	
Quality of M&E	Modest	Modest	
Quality of ICR	---	High	

12. Lessons

Three lessons are drawn from the ICR (pages 23-24), with some adaptation.

The use of quantitative PFI and SME eligibility criteria and their inclusion, together with SME loan terms and conditions, in legal covenants of FIL operations help ensure that lending to SMEs observe commercial and financial viability standards. In this project, quantitative criteria



were drawn for the eligibility of PFIs to act as lenders and SMEs as borrowers. The quantitative criteria, covering among others the asset size and profitability of PFIs, coupled with the inclusion of these criteria as covenants in the Loan Agreement, were designed to screen out troubled financial institutions from the project. Similarly, the project also established quantitative criteria for the eligibility of SMEs and quantitative conditions for SME sub-projects, setting them as legal covenants, to reduce the risk that the loan funds would be wasted on non-performing SME loans.

Potential market competition (between an apex bank and PFIs) should be considered carefully in the choice of an apex bank in a financial intermediary lending operation. The Bank had carefully considered the financial condition and record of financial performance of the candidate institution, its credit and risk management practices, and the overall quality of its corporate governance. But, the Bank should be careful about selecting an apex bank that competes with PFIs in the same target market of the FIL operation. In this project, Ziraat Bank encountered problems collecting information from PFIs; according to the ICR, it was difficult for PFIs to share data about its customers and its portfolio with the apex bank because the PFIs and the apex bank were competitors in the same leasing market.

Mandates to introduce new financial products should be supported by technical assistance to the sponsoring financial institutions. This project required the PFIs to introduce new leasing products, but only one PFI managed to offer one new product to the market over the five-year life of the project. The ICR explains that there were institutional, market, and project design constraints to the introduction of new leasing products (see Section 4). Technical assistance to the government, the apex bank, and the PFIs would have helped uncover and address these issues, including with changes to the project design or with proposals for additional financial sector development measures.

13. Assessment Recommended?

No

14. Comments on Quality of ICR

The ICR articulated a theory of change for the project, which, it drew from the results framework table, included as Annex 1 of the PAD. The ICR statement of the underlying results chain for the project was sound and logical (see Section 8.A).

After candidly arguing that the one of the intermediate results indicator was an input, and three of the outcome indicators were outputs, the ICR (pages 12-14) offers an alternative assessment of the efficacy of achievement of the project objective. Setting "improved leasing services to SME beneficiaries" as the project outcome, and defining "improved PFI balance sheet structure with regard to leasing operations", "longer average maturity of sub-loans compared to the average maturity of PFIs' SME loan portfolio funded using their own resources", "expanded SME customer base for PFIs", and "introduction of new leasing products" as the outcome indicators, the ICR concludes that the project "largely met the project outcome."



- The project helped the PFIs to improve their balance sheet structure with the longer-term funding. Before the project, the leasing companies were largely funded by their parent banks, which relied on short-term deposits. Under the project, the apex bank's subsidiary loans to the PFIs had a minimum maturity of five years. The apex bank gave the PFIs one-year grace period for principal repayment.
- The sub-loans had an average maturity of four and half years while the average maturity of the leasing products financed by PFIs own funding was less than three years.
- The nine PFIs extended their customer base by over 41 percent under the project (these were new customers for the PFIs). The PFIs' sub-loans to eligible SME borrowers had a maturity of at least three years and the rates were reasonable. The SMEs reported that some sub-loans had a maturity of five years with a 2-year grace period, with the favorable terms allowing the PFIs to be more competitive compared to leasing companies that did not participate in the project.
- Little progress was achieved with the introduction of new leasing products. Only one PFI offered once a sale-and-leaseback product to an SME.

The ICR was also candid with its assessment of other aspects of project design. The apex bank was a competitor of the PFIs in the leasing market, which created problems with operational and financial data-sharing and reporting. There were market and project design constraints to the introduction of new leasing products (see Section 4).

a. Quality of ICR Rating
High