



**ASIAN INFRASTRUCTURE
INVESTMENT BANK**

P000698
Nov. 22, 2023

Sovereign-Backed Financing

Project Document

Republic of Türkiye

Turk Eximbank Green Infrastructure Support and Earthquake Response Project

Currency Equivalents

(As of Aug. 31, 2023)

Currency Unit – TRY
 TRY 1.00 = USD 0.04
 USD 1.00 = TRY 26.65

Borrower's Fiscal year

Jan. 1–Dec. 31

Abbreviations

AIIB	Asian Infrastructure Investment Bank
BRSA	Banking Regulation and Supervision Agency
CAPEX	capital expenditure
CAR	capital adequacy ratio
CBAM	Carbon Border Adjustment Mechanism
CBRT	Central Bank of the Republic of Türkiye
CDS	credit default swap
CPI	Consumer Price Index
CRF	Crisis Recovery Facility
DFI	development finance institution
DG	distributed generation
ECM	External Communications Mechanism
E&S	environmental and social
ESDD	Environmental and Social Due Diligence
ESF	Environmental and Social Framework
ESMS	Environmental and Social Management System
ESEL	Environmental and Social Exclusion List
ESP	Environmental and Social Policy
ESS	Environmental and Social Standards
EU	European Union
EUR	euro
FCIDD	Financial Crime and Integrity Due Diligence
FI	financial intermediary
FM	financial management
FX	foreign exchange
GDP	gross domestic product
GRI	Global Reporting Initiative
GRM	Grievance Redress Mechanism
IAS	International Accounting Standards
IBRD / WB	World Bank
ICIEC	Islamic Corporation for the Insurance of Investment and Export Credit
IFI	international financial institutions
IFRS	International Financial Reporting Standards
IMF	The International Monetary Fund

ISAs	International Standards on Auditing
KYC	Know Your Counterparty
MDB	multilateral development bank
MIGA	Multilateral Investment Guarantee Agency
MoTF	Ministry of Treasury and Finance in Türkiye
NPLs	nonperforming loans
OPIR	Operational Policy on International Relations
PDG	partial debt guarantee
PIR	Procurement Instructions for Recipients
PIU	Project Implementation Unit
POM	Project Operational Manual
Project P000447	AIIB P000447 Türkiye: Turk Eximbank COVID-19 Credit Line Project
PPM	Project-affected People's Mechanism
SBF	sovereign-backed financing
SMEs	small to medium-sized enterprises
SOE	state-owned enterprises
TOR	terms of reference
TRY	Turkish lira
Turk Eximbank	Türkiye İhracat Kredi Bankası A.Ş. / Export Credit Bank of Türkiye, or the Borrower
World Bank Guarantee Project	World Bank P171448 Turkey – Long-Term Export Finance Guarantee Project
USD	United States dollar

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1. Summary Sheet

Project No.	P000698 ¹
Project Name	Turk Eximbank Green Infrastructure Support and Earthquake Response Project
AIIB Member	Republic of Türkiye
Borrower and Project Implementation Entity	Türkiye İhracat Kredi Bankası A.Ş. (Export Credit Bank of Türkiye, or Turk Eximbank, or the Borrower)
Counter-Guarantor (Component A) Guarantor (Component B)	Republic of Türkiye
Sector Subsector	Multi-sector Multi-subsector
Alignment with AIIB's thematic priorities	Private Capital Mobilization Green infrastructure
Project Objective	To support green infrastructure as well as restore and develop infrastructure and related facilities in the earthquake-affected provinces of Türkiye
Project Description	<p>The Project has two components:</p> <p>Component A encompasses a sovereign-backed partial debt guarantee (PDG) of up to USD200 million or equivalent in euros (EUR) from AIIB to help Turk Eximbank raise long-term private sector funding to support green infrastructure in Türkiye (Component A). With support from AIIB's PDG, Turk Eximbank intends to raise a green loan² of up to USD285.7 million or equivalent in EUR (the Guaranteed Loan) from international banks (the Guaranteed Lenders). It is expected that 100 percent of Component A will qualify as climate mitigation finance.</p> <p>Component B encompasses a sovereign-backed loan of USD100 million from AIIB to Turk Eximbank as an emergency response to the earthquakes in 2023, to help restore and develop infrastructure and related facilities in the earthquake-affected provinces of Türkiye (Component B).</p>

¹ At present, AIIB's internal system does not support a project having two different instrument-types for the two components as in this Project (i.e., a partial debt guarantee and a direct loan) during project implementation and monitoring stage. Hence, after financing approval, the Project will be split into two projects with two different Project IDs during implementation and monitoring stage: P000698 is for the partial debt guarantee (Component A), and P000834 is for the direct loan (Component B).

² A green loan is a form of financing that enables borrowers to use the proceeds to exclusively fund projects that make a substantial contribution to an environmental objective. AIIB will work with Turk Eximbank and the Guaranteed Lenders on structuring Component A as a green loan (i.e., in line with Loan Market Association's green loan principles).

Implementation Period	<p>Component A: Start Date: Q4 2023 End Date: Q4 2027</p> <p>Component B: Start Date: Q4 2023 End Date: Q4 2027</p>
Expected Project Closing Date	Q4 2027
Financing Plan	<p>Component A: Sovereign-backed PDG of up to USD200 million or equivalent in EUR from AIIB to support a green loan from international banks of up to USD285.7 million or equivalent in EUR; and the funds will be disbursed by the Guaranteed Lenders.</p> <p>Component B: Sovereign-backed loan of USD100 million from AIIB.</p> <p>The proceeds of both Component A and Component B will be on-lent to eligible sub-borrowers.</p>
E&S Category	Financial Intermediary (FI)
Key Covenants	<p>a) The Borrower to undertake the Project in accordance with the Project Operational Manual (POM)</p> <p>b) Sub-loan cap per sub-borrower:</p> <ol style="list-style-type: none"> a. Small and medium-sized enterprises (SMEs)³: USD10 million or equivalent in other currencies b. Non-SMEs: USD30 million or equivalent in other currencies <p>c) Sub-loan tenor: Up to 10 years</p> <p>d) Prohibited uses: Items on AIIB Exclusion List, higher risk sub-project defined per AIIB's Environmental and Social Policy (ESP), and any sub-project that would involve any of the matters covered in the Operational Policy on International Relations (OPIR)</p>
Key Conditions for Effectiveness	<p><i>For the PDG (Component A)</i></p> <ol style="list-style-type: none"> a) Fully executed Indemnity Agreement and Project Agreement b) Provision of relevant legal opinions satisfactory to AIIB relating to the financing documents and Indemnity Agreement c) Adoption of POM

³ SMEs are defined as enterprises with less than 250 employees and not having annual revenues or assets exceeding TRY500 million. SMEs within the scope of this Project are defined according to regulation of the Republic of Türkiye's Ministry of Industry and Technology and the definition of SME shall be updated as such regulation is amended from time to time.

	<p>d) Project-level External Communication Mechanism is adopted in the form and substance in a manner satisfactory to AIIB</p> <p>e) Cashflow schedule of loan disbursements and repayments</p> <p>f) Payment of the Front-end Fee, the Guarantee Fee, and the Processing Charge</p> <p>g) Indicative pipeline of eligible sub-loans of at least the underlying loan amount raised under Component A</p> <p><i>For the SBF Loan (Component B)</i></p> <p>a) Adoption of POM</p> <p>b) Project-level External Communication Mechanism is adopted in the form and substance in a manner satisfactory to AIIB</p> <p>c) Fully executed Borrower Representation Letter</p> <p>d) Provision of relevant legal opinions relating to the Loan and Guarantee Agreements</p> <p>e) Indicative pipeline of eligible sub-loans of at least USD100 million or equivalent</p>
Claim by Guaranteed Lenders (and payment by AIIB) in Component A	In the event of a scheduled payment default of the Guaranteed Loan, the Guaranteed Lenders may deliver a payment request to AIIB and, following the requisite waiting period, AIIB will pay the principal and interest amount ⁴ of the defaulted scheduled payment that remains unpaid on the claim payment date.
Retroactive Financing (Loan % and dates)	None
Policy Waivers Requested	None
Policy Assurance	The Vice President, Policy and Strategy, confirms an overall assurance that AIIB is in compliance with the policies applicable to the Project.

⁴ While AIIB is supportive of both principal and interest being covered, total coverage under the AIIB guarantee will be capped at a maximum guarantee amount.

President	Jin Liqun
Vice President	Konstantin Limitovskiy
Director General	Najeeb Haider
Manager	Stefen Shin
Team Leader	Huaixue Fu (Sherry), Senior Investment Officer – Financial Institutions and Syndications
Co-PTL	Changyu Sun (Cassie), Investment Officer
Team Members	Jinwen Ye, Investment Analyst Bhavit Sharma, Guarantee Specialist Rong Zhou, Environment Specialist Ting Wang, Counsel Goktug Ersoy, Associate Counsel Guoping Yu, Senior Procurement Specialist Shonell Robinson, Financial Management Specialist Marcin Sasin, Senior Economist

2. Project Description

A. Project Overview

1. **Project Objective.** The Project aims to support green infrastructure as well as restore and develop infrastructure and related facilities in the earthquake-affected provinces of Türkiye.
2. **Project Description.** The Project has two components:
 - (i) Component A encompasses a sovereign-backed partial debt guarantee (PDG) with a maximum guaranteed amount of USD200 million or equivalent in EUR from AIIB to help Turk Eximbank raise long-term private sector funding to support green infrastructure in Türkiye. With support from AIIB's PDG, Turk Eximbank intends to raise a green loan of up to USD285.7 million or equivalent in EUR from international banks. It is expected that 100 percent of Component A will qualify as climate mitigation finance. This will be the first green loan for Turk Eximbank. Ministry of Treasury and Finance (MoTF) will provide the sovereign counter-guarantee to AIIB in the Indemnity Agreement.
 - (ii) Component B encompasses a sovereign-backed loan of USD100 million from AIIB to Turk Eximbank. Component B serves as an emergency response to the earthquakes in 2023, to help restore and develop infrastructure and related facilities in the earthquake-affected provinces of Türkiye.
3. **Project Context.** Türkiye has a large, diversified, dynamic, and business-oriented economy. In 2022, Türkiye's sovereign credit rating has been downgraded by each of the three major rating agencies to B (S&P and Fitch) and B3 (Moody's), due to macroeconomic stress, which the authorities have recently started to address. Türkiye is also vulnerable to surging prices of energy (as a net energy importer) and food (with a high share of food in the consumption basket). As a result, the energy import bill has almost doubled, and the current account deficit increased sharply to 5.4 percent of GDP in 2022, despite a record high tourism season and solid export performance. External borrowing costs have spiked, limiting the ability of Turkish banks to support companies that are vulnerable to fluctuations in the business cycle and susceptible to credit rationing. Financial and insurance / reinsurance markets have become less accessible and more expensive.
4. The export sector has been a critical driver of growth in Türkiye over the past two decades, representing 28 percent of the current GDP. The export sector is also deeply integrated into the wider Turkish economy, with supply chains throughout the country providing inputs for key export-oriented industries such as textiles, automobiles, apparel, and machinery. Supporting exporters is critical for the long-term sustainability of the Turkish economy. Component A of the Project serves an important need of the economy in this regard, as it will support exporters preparing for the ongoing Carbon

Border Adjustment Mechanism (CBAM)⁵, a critical endeavor as Europe is the main exporting market for Türkiye. The CBAM, recently launched on Oct. 1, 2023 by the European Union (EU), will require reporting on carbon emission for products imported into the EU and will impose charges that correspond to emissions relating to these imports. The CBAM, also referred to as a “carbon tariff,” is expected to have a significant impact on global trade patterns as well as relevant industries and supply chains. Many Turkish exporters are making efforts to comply with the CBAM regulation, including the installation of solar power generational capacity on their own premises to produce electricity for self-consumption and upgrading to / investing in energy efficient solutions.

5. The majority of solar generation capacity being installed by Turkish exporting companies is in the solar DG space (e.g., mini- and micro-grids and rooftop solar programs, distributed electricity generation for commercial and industrial use). This will not only reduce their carbon footprint, thereby decreasing the “carbon tariff” imposed on their products exported to the EU but also reduce their overall electricity bills, making solar-empowered manufacturing more attractive and cost-effective. This is in line with the AIIB Project team’s observations during the on-site due diligence where the team met a wide range of export companies in Türkiye. These Turkish exporters need funding support for their purchase and installation of solar panels which require longer-term financing to match the asset life of up to 25 years. Although commercial banks are generally interested in supporting renewable energy, they are not able to offer tenor beyond one to three years to Turkish borrowers under current economic conditions. AIIB will bridge the gap in the market by utilizing the PDG to help Turk Eximbank (which serves Turkish exporters) obtain longer-term financing from commercial banks at a reasonable cost and unlock capacity from international lenders that are otherwise reluctant to enter the Turkish market at this time.

6. Supporting solar generation development will help increase the penetration of renewable energy power generation in Türkiye and is aligned with Türkiye’s National Energy Plan for 2035. In addition, supporting energy efficient solutions is aligned with National Energy Efficiency Action Plan of Türkiye. These national plans emphasize the importance of increasing renewable energy capacity and decreasing energy intensity to achieve its net-zero emission target by 2053. Türkiye targets to achieve 74 percent of new electricity capacity to be produced by renewable energy by 2035 and expects solar energy capacity to increase by more than five times from the current level to 53 GW. This target is supported by Türkiye’s high energy potential (especially solar energy) due to its geographic situation. The yearly average solar radiation of Türkiye is 3.6kWh / (m²

⁵ The CBAM is EU’s landmark tool to put a fair price on the carbon emitted during the production of carbon intensive goods that are entering the EU, and to encourage cleaner industrial production in non-EU countries. The gradual introduction of the CBAM is aligned with the phase-out of the allocation of free allowances under the EU Emissions Trading System to support the decarbonization of EU industry. By confirming that a price has been paid for the embedded carbon emissions generated in the production of certain goods imported into the EU, the CBAM will ensure the carbon price of imports is equivalent to the carbon price of domestic production, and that the EU’s climate objectives are not undermined. The CBAM is designed to be compatible with WTO-rules. The CBAM regulation officially entered into force the day following its publication in the Official Journal of the EU on May 16, 2023. The CBAM itself will enter into application in its transitional phase on Oct. 1, 2023, with the first reporting period for importers ending Carbon Border Adjustment Mechanism in January 2024 (European Commission, https://taxation-customs.ec.europa.eu/carbon-border-adjustment-mechanism_en). For more information on CBAM, see [Annex 7](#).

day) and the total yearly insulation period is approximately 2640 hours, which is sufficient to provide adequate energy for solar thermal applications. Given this strong potential, solar demand in Türkiye has risen rapidly in recent years (**Annex 7**).

7. Southern Türkiye was hit by three devastating earthquakes (with magnitudes of 7.8, 7.5, and 6.0) within 24 hours on Feb. 6, 2023, followed by many aftershocks. Beyond human losses and suffering, the earthquakes have caused severe disruption and damage to essential infrastructure—energy, water, and transport—in affected provinces. Companies operating in or having supply chains from those affected provinces are struggling which necessitates financing support for a greener, more resilient recovery. The earthquakes have also exacerbated the country’s economic pressure and elevated risk premia. Component B of the Project will help restore and develop infrastructure and related facilities in the earthquake-affected provinces. Due to the emergency nature of the response to the earthquakes, it is proposed that AIIB will provide a direct sovereign-backed loan as the financing instrument for Component B to simplify the implementation process, building on the successful experience from the existing AIIB project (P000447 Türkiye: Turk Eximbank COVID-19 Credit Line Project or Project P000447) which is also a sovereign-backed loan to Turk Eximbank.

8. During on-site due diligence in Türkiye, the AIIB Project team learned that the government, with limited resources and capacity, has prioritized building housing for people who lost their homes in the earthquakes, leaving many private sector corporates in the earthquake-affected provinces still grappling with infrastructure damage, operational disruptions, and financial losses. They need funding to restore infrastructure and rebuild production facilities so that they can resume business operations and rehire employees. Infrastructure and production facilities normally have long asset life and hence require longer-term financing. Unlike the humanitarian response led by the government or large-scale infrastructure development (such as the reconstruction of railroads) managed by the public sector, the proposed AIIB Project targets to bridge the long-term financing gap required by the private sector corporates including small-to-medium-sized enterprises (SMEs) in the earthquake-affected provinces. As the private sector corporates, especially SMEs, are key to job creation and sustainable development of the local economy, the proposed AIIB Project is expected to complement the efforts of the government and the public sector to jointly support a greener, more resilient recovery of the earthquake-affected provinces.

9. **Expected Results.** Based on the assessment of the indicative pipeline, the expected results will be monitored via the following indicators:

Project Objective Indicators

- (i) For Component A, number of green infrastructure financed
- (ii) For Component B, number of infrastructure, machinery and related facilities financed for post-earthquake recovery
- (iii) For Component A, renewable energy capacity installed
- (iv) For Component A, greenhouse gas emission avoidance

Intermediate Indicators

- (v) For Component A and B, medium to long-term financing⁶ amount provided to eligible sub-borrowers
- (vi) For Component A, amount of private capital mobilization⁷
- (vii) For Component A, amount of financing for climate mitigation or climate adaptation purposes
- (viii) For Component A, number of energy efficiency / water efficiency sub-loans
- (ix) For Component A and B, non-performing loans (NPL) ratio of the sub-loan portfolio
- (x) For Component A and B, number of eligible sub-borrowers financed under the Project
- (xi) For Component A and B, percentage of sub-loans provided to women-inclusive enterprises⁸

10. **Expected Beneficiaries.** This Project's financing will be used to fund the capital expenditure of Turk Eximbank's sub-borrower clients for green infrastructure development (Component A) and post-earthquake recovery (Component B). As such, eligible sub-borrower companies in need of long-term funding will be among the major beneficiaries of the Project. The employees of the sub-borrowers will also be benefited, as the companies continue to operate, and business continues to grow.

11. In the case of Component B, the eligible sub-borrowers are predominantly export-oriented firms whose operations have been shut down or severely disrupted by earthquake damage. Many of these firms, such as textile producers in the southern and central parts of the country, are the economic engines of their local communities as they are large employers and source raw materials from their surrounding regions. The resumption of production at these firms, including SMEs, will help restore the livelihoods of their employees and revive local economies. The impact of these firms also extends beyond Türkiye as the recovery of exporters also supports global trade and economic growth.

12. Turk Eximbank itself is also considered to be a beneficiary of the Project, as this Project will help this Borrower access a wider funding pool and strengthen its capacity to raise long-term funding in the international market. The Guaranteed Lenders (who would not have been able to extend a long-term loan without the PDG) would also stand to benefit from the PDG. Their participation in this transaction can help revive the credit market and encourage the return of other lenders watching from the sidelines.

⁶ Financing of longer than one year is considered as medium to long-term financing.

⁷ Under the joint MDB methodology, the total amount of the loan being guaranteed by the MDB is counted as direct private capital mobilization (PCM). Therefore, the PCM target is set to be USD285.7 million.

⁸ Enterprises that are (i) owned by women (i.e., with at least one female shareholder with a properly documented representative and managing powers); or (ii) managed by women (i.e., with at least one female C-level manager or with at least 25 percent female representation in mid-level management); or (iii) employing a ratio of women that is higher than the average ratio observed in the respective sector; or (iv) has increased the share of women employment by at least five percent in the previous year.

B. Rationale

13. **Strategic Fit for AIIB.** The Project is aligned with AIIB's Private Capital Mobilization and Green Infrastructure Thematic Priorities.

14. **Thematic Priority–Private Capital Mobilization.** AIIB will provide the much-needed credit enhancement through its PDG product that would allow Turk Eximbank to secure longer-term, counter-cyclical financing from private sector international banks to support green infrastructure in Türkiye when private sector appetite for the country is limited. The AIIB guarantee will effectively improve the risk profile of the Borrower and allow its access to a wider pool of commercial lenders and longer-term private sector funding that otherwise won't be possible under the current challenging market conditions. The innovative design enables AIIB's product offering to transition from traditional credit lines to more market-based, leveraged instruments to support financial intermediation needed at times of stress in economies such as Türkiye. This Project exemplifies AIIB's catalytic role in mobilizing private capital for its clients.

15. The AIIB guarantee will have short-term and potential long-term beneficial impacts on Turk Eximbank and Turkish exporters. In the short term and under the current challenging market conditions, AIIB's guarantee will improve confidence in the transaction sought by Turk Eximbank from the market and help unlock the capacity of commercial lenders and potential insurers who would otherwise be unlikely to participate in the financing. The AIIB guarantee will significantly crowd in financing from commercial institutions with the target of 70 percent cover⁹, which reflects the current market reality and is believed to be the lowest guarantee level needed to mobilize the private capital to achieve the proposed transactional financing amid current market conditions in Türkiye. AIIB's PDG, by providing a maximum guaranteed amount of up to 70 percent of loan principal, is providing capital relief to international lenders under the Basel III framework and helping Turk Eximbank to mobilize private capital well above the notional amount of the AIIB guarantee and achieve significantly longer maturity and lower all-in cost than what is currently available on a standalone loan basis (without any guarantee).

16. In the longer term, the transaction is expected to generate a demonstration effect, with the completion of an AIIB guarantee transaction leading, over time, lenders to stretch uncovered loans (i.e., not backed by a guarantee) to maturities previously not considered—benefiting the banking sector and exporters overall. The success of this Project as the first-ever AIIB guarantee on a loan could be replicated globally with other banks and state-owned enterprises who wish to pursue commercial financing as an alternative to relying on public resources and traditional loans from AIIB and other multilateral development banks (MDBs).

17. **Thematic Priority–Green Infrastructure.** The Project is aligned with AIIB's Thematic Priority of Green Infrastructure. AIIB's Corporate Strategy states that “AIIB will prioritize green infrastructure and support its members meet their environmental and

⁹ While AIIB is supportive of both principal and interest being covered, total coverage under the AIIB guarantee will be capped at USD200 million or 70 percent of the principal amount. For example, for a USD285.7 million loan, the maximum guaranteed amount of AIIB's PDG is up to USD200 million, including interest and principal.

related development goals by financing projects that deliver local environmental improvements and investments dedicated to climate action.” This Project supports renewable energy as well as energy efficiency and potential water efficiency initiatives of export companies in Türkiye.

18. **Energy Sector Strategy.** The Project will contribute to the development of green infrastructure by supporting activities that promote renewable energy and energy efficiency. These enabling activities are expected to be instrumental in promoting renewable energy access and security, integrating cleaner solutions to energy access, supporting the transition into a more efficient energy system, and thereby realizing greater energy efficiency potential, all of which strongly align with the Guiding Principles of AIIB’s Energy Sector Strategy.

19. **Paris Agreement Alignment and Climate Finance.** AIIB targets to align its operations with the goals of the Paris Agreement by July 1, 2023, reinforcing AIIB’s long-standing pledge to support climate action. This Project represents the first instance where Turk Eximbank strategically considers Paris Agreement alignment after Türkiye officially ratified its Paris Agreement target in October 2021. The implementation of the Paris Agreement alignment still represents a relatively new topic in Türkiye’s banking sector.

20. According to the joint MDB methodologies, all of the sub-loans in Component A will automatically be Paris Agreement-aligned under BB1¹⁰ (mitigation), as they will contribute to the development of green infrastructure or support decarbonization pathways, thereby delivering climate mitigation impacts. Sub-loans in Component B are also expected to be Paris Agreement-aligned (mitigation), given the proceeds will support activities such as construction / reconstruction / repair / maintenance of buildings and related facilities and thus are considered Paris Aligned under BB1. Equipment purchase, if included, shall also be Paris Agreement-aligned under BB1, meeting AIIB’s requirement.

21. The Project is considered to be Paris Agreement-aligned under BB2¹¹ (adaptation). A counterparty approach using AIIB Paris alignment methodology was applied for BB2 assessment, analyzing the overall sector and country climate risk exposure of Turk Eximbank’s current lending portfolio. The analysis focused on the level of exposure of Turk Eximbank’s lending portfolio in terms of sectors and countries. Turk Eximbank has a diversified portfolio with no single sector dominating more than 25 percent of its portfolio. Hence, Turk Eximbank has a low climate risk exposure and is considered BB2 aligned.

22. Furthermore, Turk Eximbank is actively progressing toward a more adequate climate risk management and reporting system to comply with the Fifth Strategic Plan and Sustainable Banking Strategic Plan published by the Banking Regulation and Supervision Agency (BRSA) in Türkiye, to examine the impact of Carbon Adjustment Mechanisms over capital adequacy.

¹⁰ Building Block 1.

¹¹ Building Block 2.

23. In this context, the Project is considered 100 percent climate mitigation finance for Component A, implying a total climate mitigation of more than 66 percent¹².

24. **Value Additions by AIIB.**

- (i) AIIB will support an existing client through this repeat deal, expanding AIIB's product offering from a loan for AIIB's own account to a guarantee that helps the client mobilize capital from international banks under the current difficult financial environment.
- (ii) AIIB's Triple-A credit will enable Turk Eximbank to achieve a longer maturity and lower all-in cost than is possible without AIIB's PDG. Currently, it is very difficult for Turkish banks to secure financing longer than three years from international commercial banks and the bond market. AIIB's PDG will enable Turk Eximbank to obtain financing of up to 10 years from international banks.
- (iii) AIIB's PDG will unlock capacity for international lenders that may otherwise be reluctant to provide long-term financing and support Turkish green infrastructure development in a challenging market.
- (iv) In this Project, AIIB is introducing new potential lender(s) to Turk Eximbank and hoping to build new relationships that would diversify Turk Eximbank's funding sources and expand its existing lender pool.
- (v) Through this Project, Turk Eximbank will take Paris Alignment into comprehensive consideration for the first time. AIIB will adopt a supportive, enabling approach and help the Borrower build its capacity for upgrading its on-lending operations that will be consistent with national low-emissions development pathways and compatible with the objectives of the Paris Agreement. Turk Eximbank, as the on-lending agent, will also play the catalytic role in helping to enhance its sub-borrowers' ability to adapt to climate change and meet related requirements of the Paris Alignment. Furthermore, this Project will have a demonstration effect, serving as an example for other Turkish banks to follow and adopt Paris Alignment-related requirements in their lending operations.
- (vi) One hundred percent of Component A of the Project is expected to be climate finance. AIIB, together with the Guarantee Lenders, will help Turk Eximbank complete its first green loan. The Project will also contribute to global efforts to combat climate change and Türkiye's efforts to achieve its net-zero emission target by 2053.
- (vii) Component B of the Project will provide urgently needed capital to support the recovery from earthquake damage, amidst very constrained credit conditions in the country. The sub-loans will help restore and

¹² Component A amount (USD200 million)/Total Project amount (USD300 million) = 66 percent.

develop infrastructure and related facilities in the earthquake-affected provinces and potentially build more climate-resilient facilities against future disasters.

25. **Value Additions to AIIB.**

- (i) The Project represents the first-ever AIIB guarantee on a loan. With top-tier international banks joining under AIIB's PDG, it offers a great opportunity to test / market AIIB's recently approved PDG product and gain insights into how AIIB's guarantee is perceived in the market, possibly bringing many more opportunities with these international banks in AIIB's other member countries.
- (ii) AIIB will be able to obtain valuable experience in the design and implementation of PDG projects. The Project can serve as a tested reference to similar kinds of projects in other AIIB members. Turk Eximbank, as an experienced partner who has implemented a similar product in the World Bank Guarantee Project¹³, is a suitable counterparty to work with on this new type of product for AIIB.
- (iii) The Project represents an opportunity to strengthen relationships with Turk Eximbank and the MoTF, demonstrating an extended, multi-faceted partnership with existing clients.

26. **Lessons Learned.** The Project will build on the experience from AIIB's prior direct sovereign-backed loan transaction with Turk Eximbank to support the working capital needs of exporters that were adversely affected by the pandemic (Project P000447). AIIB has learned valuable lessons from this prior transaction (i.e., how to swiftly resolve due diligence questions and effectively implement the on-lending operation through Turk Eximbank). For instance, the implementation period required to achieve full Borrower disbursements of AIIB loans to sub-borrowers in the previous transaction was 1.5 years. The 2021 facility mainly supports working capital loans with more flexibility on the use of proceeds, and hence relatively straightforward for implementation. The Bank took this into account when structuring the proposed Project.

27. Overall, the implementation of Project P000447 has been relatively smooth with no material issues. Turk Eximbank has also followed the implementation requirements in the Project Operational Manual. Turk Eximbank's Project Implementation Unit for Project P000447 has been responsive to information requests and queries.

28. The structuring and design for Component A of the Project has benefited from the experiences of the World Bank Guarantee Project and Turk Eximbank's other earlier guarantee projects with Multilateral Investment Guarantee Agency (MIGA) and insurance projects with the Islamic Corporation for the Insurance of Investment and Export Credit (ICIEC). The AIIB Project team has had conference calls and in-person meeting with the relevant World Bank team to understand the transaction structure of

¹³ World Bank P171448 Turkey - Long Term Export Finance Guarantee Project. April 2020. [Development Projects : Long Term Export Finance Guarantee - P171448 \(worldbank.org\)](https://www.worldbank.org/development/projects/long-term-export-finance-guarantee-p171448).

the previous World Bank Guarantee Project and its implementation arrangement (including the project implementation period), which has been taken into consideration for this Project.

29. Building on the lessons learned from other MDBs in previous guarantee transactions, AIIB has also tried to incorporate new features in the design of this Project in response to the fast-changing market conditions and shifting global priorities. For example, climate change impact is a key consideration when AIIB structured this Project. As a result, the guaranteed component of this Project is considered to be 100 percent climate mitigation finance. AIIB also plans to work with commercial lenders to help Turk Eximbank structure its first green loan in the market which will have significant climate benefits. In addition, this Project is 100 percent Paris Agreement aligned, and it marks the first time for Turk Eximbank to incorporate Paris Agreement considerations in its operations. As compared to the market environment where the World Bank Guarantee Project was executed from 2020 to 2021, this Project is being executed in much more challenging market conditions resulting from multiple sovereign rating downgrades and extremely scarce insurers' appetite for Türkiye.

C. Components

30. **Component A.** The Guaranteed Loan will be on-lent to eligible sub-borrowers for green infrastructure development in Türkiye. The Guaranteed Loan has a tenor of up to 10 years with a grace period of up to 3 years.

31. **Component B.** The direct loan will be on-lent to eligible sub-borrowers for post-earthquake recovery in the affected provinces in Türkiye. The direct loan has a tenor of up to 10 years including a grace period of up to 3 years.

D. Cost and Financing Plan

32. **Facility Amount.** For Component A, supported by AIIB's PDG of up to USD200 million or equivalent in EUR with the guarantee level of 70 percent of loan principal, Turk Eximbank aims to raise a green loan of up to USD285.7 million¹⁴ or equivalent in EUR from international commercial banks. For Component B, AIIB will provide a sovereign-backed loan of USD100 million to be on-lent to eligible sub-borrowers in the earthquake-affected provinces.

33. **Guarantee Pricing.** The guarantee pricing follows the standard pricing guidelines¹⁵ applicable to sovereign-backed guarantees. Fees and charges applicable to sovereign-backed guarantees include front-end fees, processing charges, standby fees, and guarantee fees, all of which will be borne by the Guaranteed Lenders (or by the Guaranteed Borrower on behalf of the Guaranteed Lenders). For the indicative legal structure and key terms of the Partial Debt Guarantee of this Project, please refer to **Annex 4** and **Annex 5**.

¹⁴ USD200 million/70 percent = USD285.7 million

¹⁵ AIIB. Sovereign backed Loan and Guarantee Pricing. June 2021. <https://www.aiib.org/en/policies-strategies/operational-policies/sovereign-loan-pricing.html>.

34. **Sub-loan Pricing.** The sub-loans' pricing and maturity will be determined by Turk Eximbank based on the commercial assessment of the sub-borrowers and in line with market practice. It is expected that the interest rate will be equal to the sum of the cost of funds to Turk Eximbank (either through the Guaranteed Loan or AIIB direct loan) and a risk-adjusted spread.

35. **Use of Proceeds.**

36. For Component A, the Guaranteed Loan proceeds will be on-lent by Turk Eximbank to eligible sub-borrowers to support green infrastructure development in Türkiye.

37. The Guaranteed Loan can be used for the following purposes:

- (i) Financing solar power generation facilities, mostly rooftop / DG solar facilities and potentially utility scale solar power generation facilities.
- (ii) Financing energy efficiency investments, with a minimum efficiency ratio threshold of 15 percent; and
- (iii) Potentially financing other types of green infrastructure such as wind power generation facilities and the purchases of water-efficient equipment.

38. For Component B, the direct loan provided by AIIB will be used to finance post-earthquake recovery activities, including:

- (i) Construction, reconstruction, repair, recalibration, replacement, and maintenance of facilities, storehouses, infrastructure, installations, pipework and fixed assets;
- (ii) Strengthening of current facilities against future earthquakes (and potentially other natural disasters);
- (iii) Re-reclamation and improvement of soil; construction and reconstruction of a greenhouse;
- (iv) Construction, reconstruction, repair, and maintenance of tourist facilities; strengthening of such facilities against future earthquakes (and potentially other natural disasters); and
- (v) Purchase of equipment related to Paris Agreement automatically-aligned activities; considered energy-efficient equipment; or for SME sub-borrowers.

39. Component B will be used to support eligible sub-borrowers whose operations have been disrupted by earthquake damage in the earthquake-affected provinces, including Kahramanmaras, Adana, Malatya, Elazig, Adiyaman, Diyarbakir, Sanliurfa, Hatay, Osmaniye, Kilis, and Gaziantep.

40. For more details on the eligibility criteria, please refer to **Annex 2**.

41. **Pipeline.** For Component A, approximately 65 percent of the proposed sub-loans in the indicative pipeline are to finance solar power generation facilities (which are mostly rooftop / DG solar facilities), while the remaining 35 percent of the sub-loans are to support energy efficiency (such as acquiring / replacing more energy efficient equipment for business operation). The sub-borrowers mostly engage in manufacturing activities in textile, machinery, and food products. The breakdown of Component A pipeline by sub-borrower sector is presented in **Figure 1** below.

Figure 1: Indicative Pipeline for Component A – Breakdown by Sub-Borrower Sector

Sub-Borrower Sector	Loan Amount (in USD million)	% of Total Pipeline (Component A)
Manufacturing	274.0	87.0%
Sales and trade	31.0	9.8%
Others	10.0	3.2%
Total	315.0	100.0%

42. For Component B, a summary of the indicative pipeline across different earthquake affected provinces is presented in Figure 2 below. Sub-borrowers under the indicative pipeline are mostly manufacturers with a focus on export in the earthquake affected provinces, including manufacturers of textile, wearing apparel, etc. The indicative pipeline for both Component A and Component B are subject to change as other eligible sub-projects may be identified.

Figure 2: Indicative Pipeline for Component B – Breakdown by Affected Provinces

Province	Loan Amount (in USD million)	% of Total Pipeline (Component B)
Adana	192.0	53.9%
Kahramanmaraş	84.0	23.6%
Gaziantep	77.0	21.6%
Malatya	3.0	0.8%
Adıyaman	0.5	0.1%
Total	356.5	100.0%

E. Implementation Arrangements.

43. **Implementation Period.** The Project implementation period is expected to be from Q4 2023 (estimated Effectiveness Date) to Q4 2027 (estimated Project Closing Date). The implementation period is expected to be approximately four years to deploy sub-loans to eligible sub-borrowers.

44. For this Project, there is an actual need for a relatively long allocation period during which Turk Eximbank sources suitable sub-projects / sub-borrowers that will meet the high international standards required by AIIB from E&S, Procurement, Financial Management, and Paris Alignment perspectives and deploy the funds to the eligible sub-borrowers. The four-year implementation period for both Component A and Component B is to accommodate the time required for Turk Eximbank to fully disburse the loan proceeds in accordance with AIIB standards. The previous World Bank Guarantee Project also has an implementation period of four years.

45. **Implementation Entity.** Turk Eximbank will be responsible for the implementation of the Project. A Project Implementation Unit (PIU) has been set up and operationalized within Turk Eximbank, which will serve as the main implementing team of the Project and will oversee all the sub-loans. The eligibility criteria and requirements are expected to be set out in the legal agreements among Turk Eximbank, Guaranteed Lenders, and AIIB.

46. Owing to the previous facilities / projects with AIIB and other MDBs, Turk Eximbank has an existing operationalized PIU with adequate budgetary and human resources, ready to oversee the on-lending to sub-borrowers, including the selection, appraisal, monitoring, record keeping, information management and reporting to AIIB. The PIU will ensure Turk Eximbank and the sub-borrowers to comply with the applicable law, as well as AIIB's requirements set forth in the legal agreements and the POMs.

47. **AIIB's Implementation Support.** A Project Operations Manual (POM) for each Project Component will be generated to help streamline and support the PIU in conducting the necessary analysis and oversight on the sub-borrowers. The Bank plans to conduct annual supervision missions, the execution of which will depend on implementation progress and complexity, and travel constraints.

48. **Eligibility Criteria.** Proceeds from the loans will be available to each sub-borrower in accordance with selection criteria and parameters (**Annex 2**) and the POM. Sub-borrowers will be Turk Eximbank's existing and new customers which are generally companies in Türkiye's export sector. It is expected that the sub-borrowers will be private entities that are registered and operated in Türkiye.

49. **Procurement.** AIIB will provide a sovereign-backed PDG to help Turk Eximbank raise financing from international commercial banks and a direct loan to Turk Eximbank for post-earthquake recovery. As the FI borrower, Turk Eximbank will on-lend the loan proceeds to eligible sub-borrowers in accordance with the POMs which are expected to follow the version from Project P000447 being implemented by Turk Eximbank. The loan proceeds will be on-lent for investment / CAPEX purposes. Under such circumstances, the private entities' provisions for financial intermediaries in AIIB's Procurement Policy

and Section III Procurement by Private Entities under the associated Interim Operational Directive on Procurement Instructions for Recipients (PIR) shall apply to the Project.

50. Potential sub-borrowers will be local private entities including entities with more than 50 percent of its shares owned privately, and that are financially and managerially autonomous from the government as well as operate as private entities¹⁶. A PIU with a designated experienced and professional staff has been established by Turk Eximbank to provide oversight on the packaging of procurement activities, procurement methods and procedures, screening of AIIB's debarment list for eligibility of suppliers, contract management, procurement reporting and record keeping etc., and will ensure that sub-borrowers carry out the procurement of works, goods or services following the normal procurement practices of the private entities, including established commercial practices or appropriate procurement methods that are specified in the POMs and acceptable to AIIB, which is aimed to ensure that the costs are in line with the fair market price. AIIB has reviewed the proposed procurement arrangements including the review procedures as specified in the procurement part of the POMs prepared by Turk Eximbank, and found they are acceptable to AIIB.

51. **Financial Management.** Turk Eximbank is staffed with financial and accounting professionals most of whom have experience managing the Financial Management (FM) function of Project P000447, and the previous World Bank Guarantee Project similar in nature and size of this current operation. Additionally, Turk Eximbank has vast experience in lending operations. Thereby, it is fully capable of managing the FM function of this Project.

52. Turk Eximbank's existing financial procedure manuals and financial systems will be applied to this Project. The core financial system "New Loan Project" will be used to capture Project transactions. This will enable the accurate and timely capturing of financial information on finances received under the Project, as well as capturing transactions for sub-loans by Project Components, from loan initiation through to the accounting and reporting. The Project's Financial Management and internal controls procedures will be guided by the POMs to ensure that the Project-specific FM requirements and eligibility criteria are met.

53. Turk Eximbank is required to provide to AIIB, both entity- and Project-level annual audit reports, which both will become due to AIIB within six months after the end of each financial year, except the final Project audit report will be due to AIIB within six months after the Project Closing Date. The audit reports will be executed by an independent external audit firm approved by BRSA and deemed acceptable by AIIB. The entity financial statements will be published on the website of Turk Eximbank, and in a similar manner, the Project audited financial statements will be made publicly available within 60 days of AIIB's approval. If funds raised under Component A are not fully used before the Project Closing Date, AIIB reserves the right to request an external audit any time after the Project Closing Date and before the expiry of the PDG.

¹⁶ Currently under negotiation and will be finalized in the Project Operational Manuals.

54. The Project audit report will include a review of a selected sample of sub-loans funded both directly with AIIB's financing and those financed through the Guaranteed Loan. Among others, the audit includes verification of sub-loan eligibility criteria as set forth in the Project documents and an audit of the terms of reference (TOR) approved by AIIB.

3. Project Assessment

A. Technical

55. AIIB has reviewed Turk Eximbank's capacity to implement the Project during due diligence. Turk Eximbank has a track record of managing MDB-funded / guaranteed facilities and on-lending to sub-borrowers and this format represented approximately 18 percent of its total funding in 2022. Turk Eximbank is an existing client of AIIB, and the Project shall benefit from the execution, implementation, and monitoring of Project P000447.

B. Economic and Financial Analysis

56. **Economic Benefits.** The economic benefits catalyzed by Component A include a reduction in carbon emissions, and cost-saving benefits arising from the transition to solar energy¹⁷.

57. Based on the current indicative pipeline, approximately 65 percent of the sub-loans are in the solar energy sector, indicating an approximately loan size of USD185 million out of the total Component A loan size of USD285.7 million. Based on this, the estimated total solar energy generation capacity is around 150MW, with an estimated carbon emission reduction of around 84,172 tons per year.

58. From a cost-effectiveness perspective, several manufacturers have indicated during the Project's due diligence that the adoption of solar energy will help reduce the cost of production in the long term. It is estimated that electricity from fossil fuels costs between 5 and 17 cents per kilowatt-hour, while solar energy typically costs between 3 to 6 cents per kilowatt-hour and is expected to further decrease in the future.

59. Aside from the sub-loans that support solar energy generation capacity, the remaining amount of Component A is expected to help promote the adoption of energy efficiency solutions in Türkiye, with a minimum improved efficiency ratio of 15 percent.

60. Furthermore, with the EU's CBAM starting to be implemented from October 2023, the transition into renewable energy helps Turkish exporters continue to remain competitive in the market, as manufacturers with non-renewable energy sources may incur carbon taxes as high as EUR100 per metric ton of carbon emission. Moreover, the energy efficiency and potential water efficiency sub-projects will contribute to GHG emission avoidance and benefit water conservation.

¹⁷ The economic benefit is estimated based on the current indicative pipeline.

61. The economic cost for Component A is USD285.7 million or equivalent (i.e., same as the size of the underlying loan in Component A), of which AIIB provides a PDG of up to USD200 million.

62. For Component B, the main economic benefits include restoring exporters' economic activities and rehabilitating damages caused by the earthquakes in 2023. The Project also creates economic value by reducing the degree of negative impact from future earthquakes on properties as a result of enhanced building protection and urban standards, improving resiliency to future disasters.

63. Furthermore, additional temporary employment and other multiplier effects in the form of associated economic activities will be generated. For Component B, it is anticipated that the economic benefits would outweigh the economic cost (which is USD100 million).

64. **Macroeconomic Overview.** Türkiye is an upper-middle-income country with an income per capita of around USD11,000 (or around USD39,000 in purchasing power parity) and a population of around 85 million. Türkiye has enjoyed robust growth since the early 2000s, with an average annual growth rate of around 5.5 percent. However, since 2016, Türkiye's sovereign credit rating has deteriorated, due to reliance on short-term stimulus to boost growth, unpredictable and unorthodox policies, declining fiscal and foreign exchange (FX) buffers, high dependence on external finance, perceived erosion of institutional checks and balances, as well as rising geopolitical risks—according to observers.

65. In particular, the past three years have been marked by financial volatility and increasing macroeconomic vulnerabilities, including currency depreciation and elevated inflation. A set of increasingly complex macro-prudential measures has been put in place to stem depreciation, promote de-dollarization, direct credit, and keep the growth going. While growth in 2022 was still high, at 5.5 percent, these policies are believed to have led to distortions in the economy.

66. The election in May 2023 cleared political uncertainty and opened the way for policy normalization. The new economic team is reputed to be supportive of more orthodox policies and has signaled intentions to lower inflation, reduce external imbalances, and maintain fiscal discipline. Since June 2023, the Central Bank of the Republic of Türkiye (CBRT or the Central Bank) has raised the interest rate by 26.5 percent to counter inflation. The market reacted positively, with the country's 5-year Sovereign Credit Default Spread (CDS) tightening to around 380 bps as of Aug. 30, 2023, down from a peak of around 900 bps, as of mid-July 2022. In September 2023, S&P and Moody's revised Türkiye's credit outlook upwards to stable.

67. The economy continues to perform relatively well on the back of post-earthquake reconstruction, strong tourism, and resilient consumption. According to the International Monetary Fund (IMF), growth is expected to reach 4.0 percent in 2023, and then converge to the medium-term potential of around 3.0-3.5 percent. Average inflation in 2023 is expected to decline to around 55 percent. In this context, the private sector has demonstrated resilience and has considerable experience in navigating through the volatile environment. Large firms report sufficient liquidity, positive short-term net open

FX positions and significant natural FX hedges. Public debt is also generally low and sustainable.

68. **Turkish Export Sector.** Export represents a critical and strategic area of Türkiye's development, accounting for approximately 28 percent of the country's GDP¹⁸. Türkiye's total export has continued to grow on the upward trajectory and expanded 12.9 percent in 2022, reaching USD254 billion¹⁹ at the end of 2022. The earthquakes that took place during February 2023 have negatively affected the export volume of Türkiye in February 2023, but the effect is gradually diminishing as the economy normalizes. For the month of August 2023, exports from Türkiye rose 1.6 percent year over year, while the year-to-date volume still represents a marginal decrease of 0.4 percent from 2022 year over year²⁰. At the same time, Türkiye is looking to increase exports to USD255 billion by the end of 2023²¹. The strong resiliency and growth in the export sector have further increased the demand for export loans.

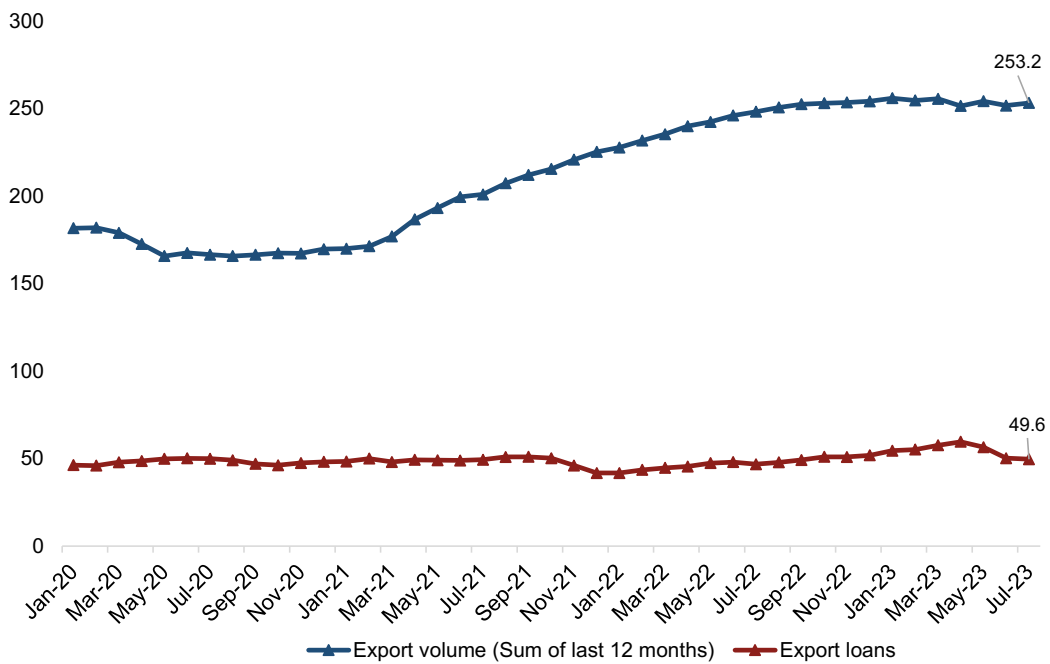
69. However, due to the instability and volatility experienced by the Turkish economy, international lenders have been reluctant to provide financing to Turkish exporters in support of their continued growth, resulting in relatively constant export loan levels despite the strong financing needs of exporters. **Figure 3** demonstrates the trends of export loans in comparison to Türkiye's export growth in recent years.

¹⁸ 2022 GDP: USD906 billion; 2022 export volume: USD254 billion.

¹⁹ Turkish Statistical Institute. Foreign Trade Statistics. December 2022. <https://data.tuik.gov.tr/Bulten/Index?p=Foreign-Trade-Statistics-December-2022-49633&dil=2>

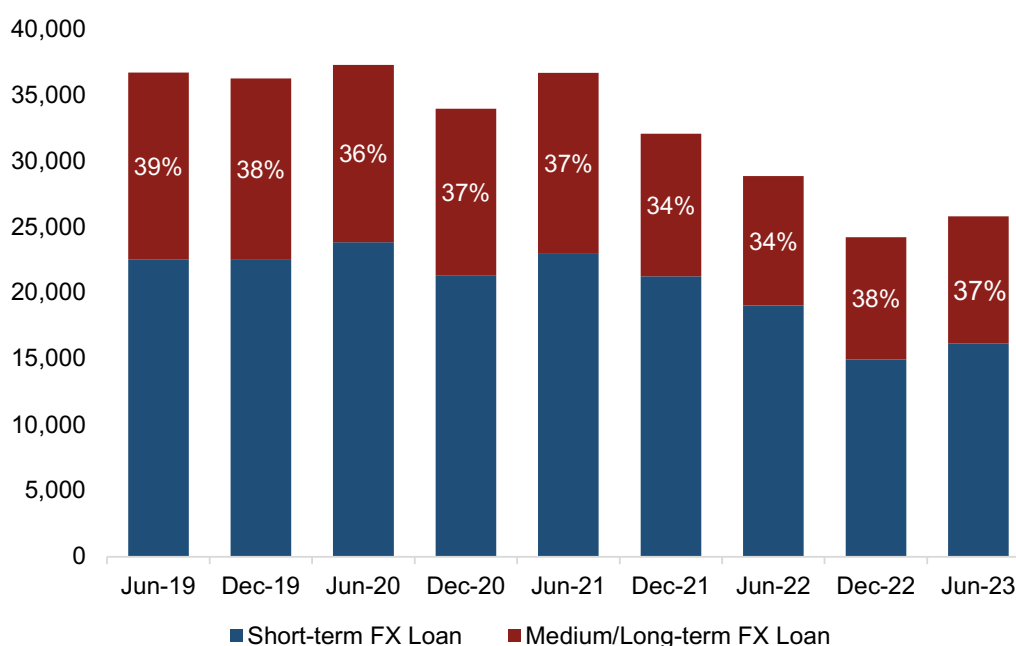
²⁰ Turkish Statistical Institute. Trading Economics. August 2023. <https://tradingeconomics.com/turkey/exports>

²¹Medium Term Program. "<https://www.sbb.gov.tr/wp-content/uploads/2023/09/Medium-Term-Program-2024-2026.pdf>").

Figure 3: Turkish Export Loan Trend (in USD billions)²²

70. In addition, Turkish exporters encounter greater challenges in accessing medium-to-long-term FX loans as compared to short-term FX loans. As shown in **Figure 4**, medium-to-long-term export loan amounts have consistently remained lower than short-term export loan amounts, further exacerbating the funding gap between the financing demand of the borrowers and the existing lending supply in FX. The overall FX export loans amount has also decreased.

²² Bankacılık Düzenleme Ve Denetleme Kurumu (BDDK). Monthly Banking Sector Data (Basic Analysis). 2023. <https://www.bddk.org.tr/BultenAylık/en>. Data based on rolling sum of the previous 12 months.

Figure 4: Export Loans Breakdown (in USD millions)²³

71. The Project will support Türkiye's development in green infrastructure, as the credit enhancement embedded in the Project will diversify and attract long-term funding sources that otherwise would not be accessible to the Borrower, allowing it to continue supporting the export sector. Such long-term funding is critical for Turkish exporters of both regular business expansion and post-earthquake recovery.

72. **Turkish Banking Sector.** The Turkish banking sector has experienced a challenging operating environment over the recent years. Policy easing, high inflation, rising global interest rates, and macroprudential policy in the run-up to the presidential elections create considerable risks to macroeconomic and financial stability.²⁴ However, the sector overall has demonstrated resilience with considerable experience in navigating through the volatile economic environment (**Annex 7**).

73. **Description of the Borrower.**

74. **Overview.** Turk Eximbank was established in 1987 as Türkiye's official export credit agency. Turk Eximbank is state-owned, and operates from a headquarter in Istanbul, with three regional directorates, 11 liaison offices, and 23 branches across the country as of Dec. 31, 2022. Its primary objectives comprise increasing export volumes, diversifying export goods and services, developing new export markets, increasing Turkish exporters' share of international trade, promoting and supporting the production and sale of investment goods for export, and gaining competitiveness. Turk Eximbank is the largest development and investment bank in Türkiye.

²³ Bankacilik Düzenleme Ve Denetleme Kurumu (BDDK). Monthly Banking Sector Data (Basic Analysis). 2023. <https://www.bddk.org.tr/BultenAylık/en>.

²⁴ Fitch Ratings. Turkish Banks Outlook 2023. December 2022. <https://www.fitchratings.com/research/banks/turkish-banks-outlook-2023-16-12-2022>

75. Turk Eximbank operates through two business segments: Investment Banking segment and Corporate Banking segment. The Investment Banking segment is mainly involved in fund management activities, including local and foreign currency capital markets activities, foreign exchange, and derivatives, accounting for approximately 30 percent of Turk Eximbank's revenues in 2022. The Corporate Banking segment accounted for the majority (~70 percent) of Turk Eximbank's total revenues in 2022, and comprises financing, insurance, and guarantee products. This segment supports exporters with financing and other activities for both pre- and post-shipment periods.

76. Turk Eximbank offers a variety of products. Its Pre-Export Credit Program provides short-term financing to exporters and manufacturers producing goods for export, thereby strengthening confidence to buyers that exporters have sufficient liquidity to get goods ready for shipment. Turk Eximbank also offers medium- to long-term products, such as its Export Oriented Investment Credit Program. The program finances machine and equipment which require longer-term financing because of their long-term usage properties. Turk Eximbank also provides confidence and assurance to exporters, overseas contractors and international investors through its insurance and guarantee products. Turk Eximbank's current portfolio is heavily weighted toward short-term loans, however, the bank aims to increase focus on medium- and long-term lending.

77. In aggregate, Turk Eximbank provided c. USD44.9 billion in support to the Turkish export sector in 2022, comprising USD19.6 billion in loans (benefiting around 12,000 firms) and USD25.3 billion in insurance and guarantee programs. For 2023, Turk Eximbank expects to reach a total support volume of USD50 billion, in line with the nation's growing exports.

78. **Sovereign Support and Ratings.** As the official export credit agency, Turk Eximbank benefits from a range of special provisions provided by the Turkish government to support its core objective. These include the full reimbursement of any losses realized resulting from political risk,²⁵ exemption from corporate and stamp duty tax, exemption from the reserve requirement ratio, exemption from loan loss provision and Liquidity Coverage Ratio requirement and guarantees from the MoTF for borrowings from IFIs and other supranational organizations. In 2022, Turk Eximbank was downgraded to a long-term issuer rating of B3 by Moody's and B- by Fitch in August and July 2022 (**Figure 5**). The rating actions reflected the downgrade of Türkiye's sovereign rating. In September 2023, Fitch revised its outlook on Türkiye from negative to stable.

Figure 5: Credit Rating Summary

Rating	Moody's	Fitch
Turk Eximbank Long-Term Foreign Currency	B3 (Stable)	B- (Stable)
Türkiye Sovereign Rating	B3 (Stable)	B (Stable)

²⁵ The definition of political risk includes transfer restrictions, foreign exchange restrictions, and war, and claims made in relation to this must be addressed to the MoTF.

79. **Financial and Commercial Due Diligence.** The AIIB Project team has completed its business and financial due diligence on Turk Eximbank through both virtual and on-site meetings.

Key Due Diligence Areas	Key Findings
Overall	Turk Eximbank is the sole official Export Credit Agency of Türkiye. Turk Eximbank is well-run operationally with strong financial metrics and risk controls and experienced in working with MDBs.
Financial performance and risk management	<p>While Turk Eximbank is exempt from multiple regulatory requirements, the bank follows commercial bank practices to manage its financial performance and risks.</p> <p>Turk Eximbank's recent financial performance is characterized by a stable ROAE on the back of resilient net interest margin and stable loan book size. This enabled Turk Eximbank to retain a solid capital adequacy ratio, well above regulatory floors. Turk Eximbank's NPL ratio remains at a minimal level, reflecting its benign asset quality.</p>
Policy and corporate governance	<p>Turk Eximbank has a sound corporate governance system in place with effective internal control systems. The Board of Directors is in charge of reviewing the bank's business target, compensation of employees and approving transactions of significant amounts. Senior management committees are responsible for providing strategic direction, supervising risk management, and ensuring compliance with relevant regulations and internal policies. Turk Eximbank has established a conservative underwriting policy and rigorous loan monitoring process.</p> <p>Turk Eximbank is undertaking a transition program to incorporate market practices in its operations, including performance-based merit, to increase productivity and retain employees. Turk Eximbank is regulated by BRSA.</p>
Implementation capacity	As the largest development and investment bank in the country, Turk Eximbank has worked with several IFIs through multiple transactions, and it has substantial experience with the implementation of partial debt guarantee facilities of this nature. The staff are experienced in managing the implementation of projects financed by MDBs.

C. Fiduciary and Governance

80. **Financial Management.** The Financial Management assessment concluded that Turk Eximbank has the necessary capacity to carry out the required financial management function of the Project. The financial management arrangements and systems are deemed to be adequate and should enable the timely and reliable financial reporting on financing raised under Component A as well as the eligible utilization of funds for Components A and B.

81. The key risk factors identified are that the funds may be disbursed to ineligible sub-borrowers, or that the funds may not be used by eligible sub-borrowers for the purposes intended. In addition, due to stringent changes by audit firms in Türkiye, the Project's audit report may not meet all of AIIB's requirements. These risks will be mitigated through Turk Eximbank having experienced staff who have managed operations of this size and nature. Secondly, the bank's screening and approval process for sub-loan applications and the review and approval process for expenditures incurred by sub-borrowers are well designed. An AIIB-approved Audit Terms of Reference (ToR) will be prepared detailing AIIB's requirements. As needed, AIIB will also provide early guidance to Turk Eximbank on its negotiation with the audit firm. In addition, the draft audit report will be reviewed by AIIB before finalization.

82. The internal control includes segregation of duties, proper review and authorization of transactions. The internal control environment is further enhanced through the Internal Audit Directorate and Internal Controls Directorate, which plan and execute risk-based audits and reports directly to the audit committee. The Project's internal control will be intertwined with that of Turk Eximbank's structure and internal control framework. The Project's pipeline of sub-loans will be reviewed by AIIB and the required planning and budgeting arrangements of Turk Eximbank will apply to the Project.

83. **Disbursement.** Under Component A, all proceeds raised under the PDG will be deposited into a pooled operating account with respect to the currency of receipt. Although these sub-loans will be financed using funds raised from commercial banks, they are required to meet eligibility criteria and AIIB's requirements as per the POM. Therefore, the indicative pipeline of sub-loans will be submitted to AIIB for review and clearance.

84. In respect to Component B, the disbursement will be made in advance (i.e., Advance Method). Turk Eximbank will submit to AIIB a request for advancing the total USD100 million, which will be made via either multiple disbursements or a single disbursement provided that the pipeline of sub-loans supports this amount. The advance request will be supported by a list of sub-borrowers and forecasted required amounts over a defined period based on eligibility criteria to be set out in the POM. Upon AIIB's approval, AIIB will transfer the funds to a pooled USD operating account of Turk Eximbank, maintained at Citibank, for dissemination to sub-borrowers. Turk Eximbank will be required to submit semi-annual Summary of Expenditures (SoEs) and withdrawal applications to record disbursements made against sub-loans.

85. For both Component A and Component B, Turk Eximbank will disseminate proceeds to eligible sub-borrowers in the form of sub-loans denominated in EUR, Turkish lira (TRY) or USD. The foreign currency exchange risks derived from cross-currency utilizations will be monitored and controlled by Turk Eximbank's Treasury Department.

86. **Accounting and Reporting.** Transactions will be accounted for on an accrual basis and in accordance with the International Financial Reporting Standards (IFRS). The Project's Interim Unaudited Financial Reports (IUFR) presented to AIIB will be prepared using a cash-basis of accounting. This report will cover funds received from all financing sources, and the eligible expenditures (i.e., disbursements made against sub-loans). To ensure the accuracy and reliability of these reports, a separate project profile will be designed in the New Loan Project system. This will capture finances raised per sources of finance and disbursement per sub-borrowers. The IUFR will cover semi-annual periods and shall be submitted to AIIB within 45 days after the reporting period ends. The format and content of the report will be agreed on with AIIB and included in the Project's POMs.

87. **Governance and Anti-corruption.** Turk Eximbank is subject to prudential regulatory oversight by BRSA, and its activities are overseen by the Turkish government via the Supreme Advisory and Credit Guidance Committee, which is chaired by government officials. Turk Eximbank is a state-owned entity, and all of its Board members are elected by the general assembly of Turk Eximbank (with the exception of the general manager, who is elected by the Board).

88. Turk Eximbank is also subject to the audit of the Turkish Court of Accounts, which is the supreme audit institution that performs audits on state-owned entities on behalf of the Parliament.

89. Turk Eximbank is committed to preventing fraud and corruption across its operations. It shall therefore ensure that its sub-loans and sub-projects are in strict compliance with AIIB's Policy on Prohibited Practices. The implementation of the sub-projects will be monitored regularly by Turk Eximbank, and AIIB will be notified of any suspected Prohibited Practices and investigations on Prohibited Practices involving Turk Eximbank, a sub-borrower, or a sub-project. AIIB reserves the right to investigate alleged Prohibited Practices under the Policy on Prohibited Practices.

90. **Financial Crime and Integrity Due Diligence (FCIDD) and Know Your Counterparty (KYC).** The AIIB Project team has conducted due diligence and risk assessment on financial crime, integrity, and Know Your Counterparty on the Borrower (i.e., Turk Eximbank), the Guarantor / Counter-Guarantor (i.e., Republic of Türkiye), the representative of the Guarantor / Counter-Guarantor (i.e., MoTF), and the expected Guaranteed Lenders (international banks). There have been no convictions or official investigations against Turk Eximbank, MoTF, the Republic of Türkiye or the expected Guaranteed Lenders. Findings show that no sanctions have been reported on Turk Eximbank, as a state-owned entity (SOE), its shareholders (i.e., MoTF), key personnel, as well as Türkiye as a state. Although associations with sanctioned countries have been reported for the Borrower in the past, no current association with any of the sanctioned countries has been identified.

91. Additional diligence on all the Guaranteed Lenders shall be conducted prior to the signing of legal agreements. Screening against the signatories who will sign the legal documents on behalf of Turk Eximbank shall also be performed before signing.

92. **Reporting and Monitoring.** During Project implementation, it is anticipated that AIIB will retain the right to review all sub-loans and conduct supervisory visits, including visits to the sub-borrowers, where it deems appropriate.

D. Environmental and Social.

93. **Environmental and Social Policy and Categorization.** AIIB's Environmental and Social Policy (ESP) including Environmental and Social Exclusion List (ESEL) and Environmental and Social Standards (ESSs) will apply to this Project. The Project has been placed in Category FI, because the financing structure involves AIIB providing direct funding to Turk Eximbank and PDG to international commercial banks who extend an on-lending loan facility to Turk Eximbank, whereby AIIB and the Guaranteed Lenders delegate to the Borrower the decision-making on the sub-projects / sub-borrowers supported by the direct loan and Guaranteed Loan. This will include the selection, appraisal, approval, and monitoring of sub-projects / sub-borrowers in accordance with AIIB's ESP requirements. The E&S instrument will be incorporated in the POMs. Activities included in AIIB's ESEL will not be eligible for financing. Coal mining, coal transportation and coal-fired power plants, as well as infrastructure services exclusively dedicated to support any of these activities, will also be excluded.

94. **Environmental and Social Management System (ESMS).** Turk Eximbank ESMS follows the Organization for Economic Co-operation and Development (OECD) common approaches, which refer to a common list of illustrative Category A and B projects, Environmental and Social Due Diligence (ESDD), IFC Performance Standards, and World Bank Group EHS guideline. It was enhanced to meet AIIB's Environmental and Social Framework (ESF) in the scope of Project P000447's Crisis Recovery Facility (CRF) financed by AIIB in 2021. Turk Eximbank implements its ESMS to (i) screen the proposed sub-loans against its E&S exclusion list; (ii) assign an E&S categorization at sub-borrower level and lending activity level; (iii) conduct an E&S assessment; (iv) monitor E&S risks and impacts and (v) disclose relevant E&S information to stakeholders and (vi) report to its management accordingly. The existing corporate-level ESMS is materially aligned with AIIB ESP.

95. **Environmental and Social Capacity.** The Borrower has had experience working with AIIB and other MDBs and demonstrated sufficient capacity. Turk Eximbank is taking a conservative approach on E&S categorization, which considers both client level and lending activity level E&S risk. Turk Eximbank has six in-house E&S experts to support ESMS implementation, supplemented with independent consultants for complicated sub-projects. Considering that the proposed Project will support longer-term finance for renewable energy sub-projects and post-earthquake reconstruction, which is of higher risk in nature as compared to the previous AIIB project (Project P000447) which focused primarily on working capital loans, the AIIB Project team has carefully reviewed Turk Eximbank's previous track records to implement utility scale renewable energy projects and manufacture sector projects and is convinced that Turk Eximbank has adequate internal capacity to implement the project.

96. **Environmental and Social Characteristics.** Component A encompasses a PDG for a loan that would finance green sub-projects including rooftop solar, on-land distributed solar, utility scale solar sub-projects, and may include wind energy, and energy efficient and water efficient sub-projects. Component B encompasses a direct loan to support earthquake recovery activities such as reconstruction, repair and maintenance of facilities, infrastructure, and equipment damaged by earthquakes. Category A sub-project and higher risk Category B activities will be excluded. As some of the renewable energy sub-projects might require additional land for installation, it is agreed with the Borrower that this Project will only support sub-project that purchase the land on a voluntary basis in a legally recorded market or use the land on a rental basis. All sub-projects will be carefully screened against potential risk of land acquisition and involuntary resettlement risk under the E&S assessment model, and any sub-project that triggers ESS2 will be excluded.

97. **Environmental and Social Instrument.** The Project presents a variety of E&S risks. Relying on Turk Eximbank's existing ESMS, a dedicated E&S procedure to manage the AIIB Project will be developed to align with AIIB ESP. The E&S procedure will update specific operational tools to reflect E&S assessment and mitigation plan reflected in **Annex 6**.

98. **Labor and Working Conditions.** The ESMS of Turk Eximbank includes requirements to identify and mitigate potential health, safety, social, and environmental hazards in all Project activities that pose a risk to employees and may also have the potential for disruption of site works. In addition, the Borrower will be advised of the importance of implementing an appropriate supply chain review to identify and address issues related to the solar sub-projects, including labor and working conditions as well as health and safety matters. Representations and warranties will be provided to the Borrower if required.

99. **Gender, Diversity and Inclusion.** Women suffered disproportionately in the aftermath of earthquake disaster. All Project-supported activities will follow protocol to prevent gender-based violence. Turk Eximbank will allocate a portion of the funding to support women-inclusive enterprises. Turk Eximbank will also track sub-project level on women economic empowerment performance.

100. **Information Disclosure and Grievance Redress Mechanism.** Turk Eximbank discloses on its website its sustainability policies²⁶ including Environmental and Social Impact Policy as well as the Climate Change Adaptation and Mitigation Policy. At the institution level, Turk Eximbank has published an annual sustainability report²⁷ which is prepared in accordance with the Global Reporting Initiative (GRI) Standards requirements. Turk Eximbank has disclosed its External Communication Mechanism ECM,²⁸ which is aligned with AIIB's ESP requirements.

²⁶ Turk Eximbank. [Sustainability Policies](https://www.eximbank.gov.tr/en/about-us/sustainability/sustainability-policies). <https://www.eximbank.gov.tr/en/about-us/sustainability/sustainability-policies>

²⁷ Turk Eximbank. [Sustainability Report. 2021](https://www.eximbank.gov.tr/content/files/bcd0e85b-8616-4150-9c52-37618964aa04/sustainability-report-2021). <https://www.eximbank.gov.tr/content/files/bcd0e85b-8616-4150-9c52-37618964aa04/sustainability-report-2021>

²⁸ Turk Eximbank. External Communication Mechanism. <https://www.eximbank.gov.tr/en/contact-us>.

101. Under E&S procedure to be agreed with AIIB, Turk Eximbank will require the sub-projects to establish a Grievance Redress Mechanism (GRM) scaled to the environmental and social risk, including GRMs for the affected community and construction workers. Provision will also be made to inform Project-affected people and Project workers of the availability of Turk Eximbank's ECM and AIIB's PPM.

102. **AIIB Independent Accountability Mechanism.** AIIB's Policy on the PPM applies to the Project. The PPM has been established by AIIB to provide an opportunity for an independent and impartial review of submissions from Project-affected people who believe they have been or are likely to be adversely affected by AIIB's failure to implement its ESP in situations when their concerns cannot be addressed satisfactorily through the Project-level ECM or the processes of Bank Management. Information on the PPM is available at AIIB's website²⁹.

103. **Monitoring and Supervision Arrangement.** Turk Eximbank will be required to maintain a comprehensive database comprising all relevant E&S information and report to AIIB a summary of the E&S aspects and overview of the E&S performance of the Project's portfolio annually. AIIB is allowed to conduct reviews of the selection and implementation of sub-loans as part of its regular supervision, comprising engagements, potential site visits and detailed review of the E&S documentation of selected sub-borrowers.

104. **Operational Policy on International Relations (OPIR).** Because the pipeline of sub-projects for this operation is still indicative, the possibility that the OPIR might be applicable in a given case cannot be completely ruled out. Consequently, Turk Eximbank will screen sub-projects against the OPIR and exclude any sub-project that would involve any of the matters covered in the OPIR. The AIIB Project team will work with Turk Eximbank on the POMs to apply this exclusion.

E. Risks and Mitigation Measures

Risk Description	Assessment (H / M / L)	Mitigation Measures
Implementation Risk <i>Risk that the Borrower is unable to implement the Project as approved.</i>	<i>Low</i>	a) The Borrower has extensive experience and institutional capacity to undertake the Project and has a solid track record of implementing on-lending facilities and guarantees from IFIs. b) The implementation and monitoring have been relatively smooth for Project P000447 with no material issues. c) The Borrower has worked with the World Bank on a similar guarantee

²⁹ AIIB. Policy on Project-affected People's Mechanism. <https://www.aiib.org/en/policies-strategies/operational-policies/policy-on-the-project-affected-mechanism.html>.

		<p>transaction. The AIIB Project team has discussed with the World Bank project team on lesson learned and understands that the World Bank Guarantee Project is performing well.</p> <p>d) The Borrower has also worked with other partners on guarantee transactions, including MIGA and ICIEC.</p> <p>e) The Borrower has set up a Project Implementation Unit (PIU) with experienced staff. The PIU will serve as the main implementing team of the Project.</p>
<p>Macroeconomic Risk</p> <p><i>The elevated inflation, depreciating currency and deterioration in the current account balance may create concerns on the ability of the Turkish authorities to support the bank in the event of a severe downturn.</i></p>	<p><i>High</i></p>	<p>a) The Turkish economy has shown remarkable resilience despite a volatile environment, with the dynamic private sector skillfully navigating the macro-financial challenges.</p> <p>b) Key strengths anchoring Türkiye's longer-term debt sustainability include moderate levels of public debt, as well as a sizable, diversified economy with a young population and entrepreneurial spirit which translate into substantial growth potential.</p> <p>c) The election in May 2023 reduced political uncertainty and opened the way for policy normalization. Since the election, the Central Bank has raised the interest rate to 25 percent, as of August 2023 to counter inflation, signaling a return to more traditional economic policies.</p> <p>d) Historically, Türkiye has never defaulted on any IFI loans.</p> <p>e) Turk Eximbank receives strong backing from the sovereign and is systematically important as it's the largest development bank in Türkiye in terms of assets.</p> <p>f) Yields for bonds issued by the Turkish banking sector have decreased, as have credit default swaps for Turkish government bonds since the last quarter of 2022.</p>

		<p>g) The export sector should remain resilient even in the event of deteriorating domestic economic circumstances.</p> <p>h) Turk Eximbank has a proven track record in the capital markets, having issued a number of debt securities in both the Eurobond and domestic Turkish market, with the most issuance done in October 2023. Turkish banks have continued to maintain access to the syndicated loan market.</p>
<p>FX Risk</p> <p><i>The risk that open unhedged FX exposures due to weaker TRY, leads to potential losses of Turk Eximbank.</i></p>	<p><i>Medium</i></p>	<p>a) Turk Eximbank's foreign exchange position is monitored on a daily basis. Turk Eximbank attempts to match its FX assets and FX liabilities through its on-balance sheet and off-balance sheet activities. Assets and liabilities, and currency swaps are used to manage its position, where appropriate. On a net basis, Turk Eximbank's FX Risk Ratio is much lower than the BRSA regulatory requirement. As a result, Turk Eximbank's historical financial statements show that volatility on FX is net off by the profits and loss generated by the corresponding derivatives position.</p> <p>b) As of 2022, approximately 30 percent to 35 percent of the loan book is denominated in TRY (most of which are for the Rediscount Program), while the remaining is primarily denominated USD and EUR. TRY loans are primarily funded by the funds from the government for the Rediscount Program and Turk Eximbank's own equity, hence no significant currency mismatch.</p> <p>c) Through the Project, Turk Eximbank will only support exporters with revenue in foreign currency, so FX risk is naturally hedged.</p>
<p>Asset Quality Risk</p> <p><i>Risk of deterioration of the quality of the portfolio as</i></p>	<p><i>Medium</i></p>	<p>a) Turk Eximbank presents a conservative lending profile and substantially lower-than-industry NPL ratios at 0.2 percent due to the</p>

<p><i>evidenced by NPL ratio and other metrics.</i></p>		<p>nature of its lending and risk management measures.</p> <p>b) Low-risk collateral is comprised fully of guarantees from any banks deemed acceptable by Turk Eximbank or government-funded Credit Guarantee Fund and similar institutions.</p> <p>c) 100 percent of political risk losses are indemnified by the MoTF.</p> <p>d) For its insurance products, a significant portion of its insurance risk is transferred to reinsurers.</p>
<p>E&S Risk</p>	<p><i>Medium</i></p>	<p>a) Turk Eximbank has experience with respect to E&S from the prior on-lending transaction between AIIB and is familiar with AIIB's requirements.</p> <p>b) Turk Eximbank has established ESMS, Turk Eximbank Sustainability Management System, and is familiar with MDB requirements.</p> <p>c) Turk Eximbank possesses adequate in-house E&S resources, with employees making conservative E&S categorizations.</p> <p>d) Turk Eximbank will maintain a database and records of its initial E&S assessment of sub-loans, and subsequent monitoring of E&S commitments and performance throughout sub-loan tenor for reporting to AIIB. AIIB will conduct reviews and supervision when required.</p> <p>e) All higher risk sub-projects defined per AIIB ESP will be excluded.</p>

Annex 1: Results Monitoring Framework

Project Objective		To support green infrastructure development as well as restore and develop infrastructure and related facilities in the earthquake-affected provinces of Türkiye.			
Indicator Name	Unit	Baseline	End Target ³⁰	Reporting Frequency	Responsibility
Project Objective Indicators:					
1. Number of green infrastructure financed	Number	0	33	Annually	Turk Eximbank
2. Number of infrastructure, machinery and related facility financed for post-earthquake recovery	Number	0	12	Annually	Turk Eximbank
3. Renewable energy capacity installed	MW	0	150	Annually	Turk Eximbank
4. Greenhouse gas emission avoidance	Tons of CO ₂ equivalent per year	0	84,172	Annually	Turk Eximbank

³⁰ End targets are cumulative values by the end of the implementation period, except for greenhouse gas emission avoidance (i.e. target #4) which is on a per year basis by the end of the implementation period.

Project Objective		To support green infrastructure development as well as restore and develop infrastructure and related facilities in the earthquake-affected provinces of Türkiye.			
Indicator Name	Unit	Baseline	End Target ³⁰	Reporting Frequency	Responsibility
Intermediate Results Indicators:					
5. Medium to long-term ³¹ financing amount provided to eligible sub-borrowers	USD million	0	385.7	Annually	Turk Eximbank
6. Amount of private capital mobilized	USD million	0	285.7	Annually	Turk Eximbank
7. Amount of financing for climate mitigation or climate adaptation purposes	USD million	0	285.7	Annually	Turk Eximbank
8. Number of energy efficiency / water efficiency sub-loans	#	0	15	Annually	Turk Eximbank

³¹ Financing of longer than one year is considered as medium to long-term financing.

Project Objective		To support green infrastructure development as well as restore and develop infrastructure and related facilities in the earthquake-affected provinces of Türkiye.			
Indicator Name	Unit	Baseline	End Target ³⁰	Reporting Frequency	Responsibility
9. Non-performing loans (NPL) ratio in the sub-loan portfolio	Percentage	0	<2%	Annually	Turk Eximbank
10. Number of eligible sub-borrowers financed under the Project	Number	0	45	Annually	Turk Eximbank
11. Percent value of sub-loans provided to women-inclusive enterprises ³²	Percentage	0	10%, of which 3% is on a best effort basis	Annually	Turk Eximbank

³² Enterprises that are (i) owned by women (i.e., with at least one female shareholder with a properly documented representative and managing powers); or (ii) managed by women (i.e., with at least one female C-level manager or with at least 25 percent female representation in mid-level management); or (iii) employing a ratio of women that is higher than the average ratio observed in the respective sector; or (iv) has increased the share of women employment by at least five percent in the previous year.

Annex 2: Eligibility Criteria

Component A

A sub-loan may be considered eligible under the Project if it meets the following requirements:

1. The sub-loan is used to finance:
 - a. roof-top and on-land distributed solar PV projects.
 - b. utility-scale solar PV project.
 - c. wind projects.
 - d. equipment considered energy efficient, i.e., at least 15 percent energy saving compared with (i) previous machinery (for replacement) or (ii) average consumption rate of its sector or similar machinery (for new purchase); alternatively, equipment listed on Green Technology Selector³³ can also be considered eligible.
 - e. equipment considered water efficient, i.e., at least 20 percent water efficiency saving compared with (i) previous machinery (for replacement) or (ii) average consumption rate of its sector or similar machinery (for new purchase).
2. All sub-loans with higher E&S risk defined in ESS1 shall be excluded, including:
 - a. All Category A activities.
 - b. Selected Category B activities, as determined by AIIB, that may potentially result in:
 - (i) Land Acquisition and Involuntary Resettlement;
 - (ii) Risk of adverse impacts on Indigenous Peoples and / or vulnerable groups;
 - (iii) Significant risks to or impacts on the environment, community health and safety, biodiversity, and cultural resources;
 - (iv) Significant retrenchment of more than 20 percent of direct employees and recurrent contractors; and / or
 - (v) Significant occupational health and safety risks.
3. All sub-loans in AIIB Exclusion List shall be excluded.
4. All sub-loans that would involve any of the matters covered in the OPIR shall be excluded.

³³ Green Technology Selector. Tech Selector. [Green Technology Selector \(techselector.com\)](http://techselector.com)

Component B

A sub-loan may be considered eligible to under the Project if it meets the following requirements:

1. The sub-loan is used to support sub-borrowers whose operations have been disrupted by earthquake damage in the earthquake affected region by financing:
 - a. costs of construction / reconstruction / repairs / recalibration / maintenance of facilities, storehouses, infrastructure, installations, pipework, and fixed assets.
 - b. strengthening costs of current facilities against future earthquakes (and potentially other natural disasters).
 - c. cost of re-reclamation and improvement of soil, construction / reconstruction of greenhouse.
 - d. costs of construction / reconstruction / repairs / maintenance of tourism facilities and strengthening of such facilities against future earthquakes (and potentially other natural disasters).
 - e. purchase of equipment that is:
 - i. related to Paris Agreement automatically-aligned activities; or
 - ii. considered energy efficient equipment;³⁴ or
 - iii. for SME³⁵ sub-borrowers.
2. All sub-loans with higher E&S risk defined in ESS1 shall be excluded, including:
 - a. All Category A activities.
 - b. Selected Category B activities, as determined by AIIB, that may potentially result in:
 - (i) Land Acquisition and Involuntary Resettlement;
 - (ii) Risk of adverse impacts on Indigenous Peoples and / or vulnerable groups;
 - (iii) Significant risks to or impacts on the environment, community health and safety, biodiversity, and cultural resources;
 - (iv) Significant retrenchment of more than 20 percent of direct employees and recurrent contractors; and / or
 - (v) Significant occupational health and safety risks.

³⁴ Same criteria as Component A.

³⁵ SMEs are defined as enterprises with less than 250 employees and not having annual revenues or assets exceeding TRY500 million. SMEs definition provided within the scope of the Facility is based on current Republic of Türkiye Ministry of Industry and Technology regulation and shall be amended upon an amendment in the related regulation.

3. All sub-loans in AIIB Exclusion List shall be excluded.
4. All sub-loans that would involve any of the matters covered in the OPIR shall be excluded.

I. Eligible Sub-borrowers (for both Components A and B):

An entity may be eligible to receive a sub-loan if it meets the following requirements, among others:

1. It does not engage directly or indirectly through its consolidated Sub-entities in any activities listed in the E&S Exclusion List of the AIIB ESP or any excluded activity list in the POMs and does not intend to use the proceeds from the AIIB Sub-loan for such activities.
2. It is a private entity: (i) which is carrying out or is established for a business purpose, and is operating on a commercial basis; (ii) which has more than 50 percent of its shares owned privately (i.e. not directly or indirectly by any Governments nor Government-owned entities); (iii) which is financially and managerially autonomous from the Government; and (iv) whose day-to-day management is not controlled by the Government.
3. It is registered, operates primarily or has a fixed place of business in the Republic of Türkiye.
4. Demonstrates not to be engaged directly or indirectly in activities purposed for supporting the expansion of production, transportation, and use of oil and natural gas.
5. It has obtained all the necessary approvals, certifications and permits to carry out its activities, and is in compliance with all applicable national environmental, social, health and safety legislations and employment regulations and standards in effect in the Republic of Türkiye;
6. Itself, its parents or subsidiaries are not included in the Bank's published Debarment List.³⁶

³⁶ Debarment List. AIIB. <https://www.aiib.org/en/about-aiib/who-we-are/debarment-list/index.html>

Annex 3: PDG Rationale

The Rationale of Utilizing PDG for Component A

1. Turk Eximbank and MoTF have requested an AIIB partial debt guarantee (PDG) to support Turk Eximbank's plan to raise long term financing from international banks to support green infrastructure in Türkiye when private sector appetite for the country is limited. The AIIB guarantee will effectively improve the risk profile of the Borrower and allow its access to a wider pool of commercial lenders and longer-term private sector funding that otherwise won't be possible under the current challenging market conditions.
2. While MoTF understands that AIIB extending a direct sovereign-backed loan may be cheaper and more straightforward than mobilizing private capital with a sovereign-backed PDG, MoTF does not differentiate sovereign-backed loan from sovereign-backed PDG in terms of budget allocation, as MoTF will need to provide the same corresponding guarantee to AIIB regardless of whether AIIB provides a sovereign-backed loan (as in Component B) or sovereign-backed PDG (as in Component A). Meanwhile, MoTF appreciates AIIB's efforts to: (i) expand its product offering to an existing client from a sovereign-backed loan to a sovereign-backed PDG, and (ii) help Turk Eximbank diversify its funding sources by using the PDG to attract potential new lender(s) that may continue to support Turk Eximbank in the future. MoTF views the PDG as an additional instrument that complements standard sovereign-backed loans, recognizing the fact that the PDG is a useful tool to mobilize private capital especially amid heightened economic difficulties that Türkiye is currently facing.

Market Sounding

3. The AIIB Project team conducted extensive market sounding and facilitated the process for collecting detailed loan offers from potential commercial lenders to allow AIIB to proceed with the minimum guarantee cover needed to mobilize financing, while keeping Turk Eximbank and MoTF comfortable with the market funding terms.
4. During three rounds of market sounding, the AIIB Project team held discussions with close to 15 international banks with rich experience working with MDBs such as the World Bank and MIGA on guarantee transactions, including top tier commercial banks from Europe, the U.S., and Asia. The market sounding feedback suggested that due to the challenging macro-economic situation in Türkiye and the pressure on its sovereign credit rating, the commercial lenders had limited interest to participate in a transaction supported by an AIIB PDG with guarantee level of less than 95 percent of principal amount. Only a few banks could consider a guarantee level of below 95 percent who submitted proposals on an individual basis to participate in the transaction mostly at around 70 percent guarantee level.
5. All these banks who can potentially accept a guarantee level below 95 percent would require additional cover from the private insurance market. The AIIB Project team has also

sounded the private insurance market to understand the potential appetite for credit insurance either individually or through an insurance broker. After multiple approaches to close to 40 private insurers, insurance capacity was found to be extremely constrained for Turkish banks. Nevertheless, some private insurers advised that their view will be more positive if a transaction involves guarantee from AIIB which will increase their chances of getting approval to provide coverage to the commercial lenders benefitting from AIIB's PDG. Even with limited credit insurer's appetite, some of these commercial lenders plan to seek additional credit insurance coverage when available to combine with the AIIB guarantee, to offer the full volume targeted at the most competitive price.

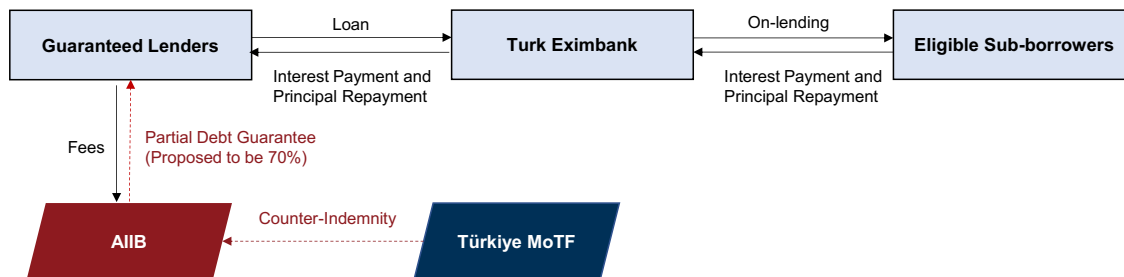
6. In summary, the 70 percent guarantee level proposed for this AIIB PDG reflects the current market reality and is believed to be the lowest guarantee level needed to mobilize the private capital to achieve the proposed transactional financing amid current market conditions in Türkiye. AIIB's PDG, by providing maximum guaranteed amount of up to 70 percent of loan principal³⁷, is providing capital relief to international lenders under the Basel III framework and helping Turk Eximbank to mobilize private capital well above the notional amount of the AIIB guarantee and achieve significantly longer maturity and lower all-in cost than what is currently available on a standalone loan basis (without any guarantee).

³⁷ While AIIB is supportive of both principal and interest being covered, total coverage under the AIIB guarantee will be capped at USD200 million, or 70 percent of the principal amount. For example, for a USD285.7 million loan, the maximum guaranteed amount of AIIB's PDG is up to USD200 million, including interest and principal.

Annex 4: PDG Transaction Structure

The proposed PDG will encompass a Loan between Turk Eximbank and the Guaranteed Lenders, with the PDG covering non-payment risk of principal and interest of up to USD200 million (equal to up to 70 percent of the original principal amount of the Guaranteed Loan), payable only if Turk Eximbank defaults on repayment of the Guaranteed Loan. Moreover, MoTF will provide a counter guarantee and indemnity to AIIB and be fully responsible for reimbursing AIIB for any payments AIIB makes under the PDG and to indemnify AIIB for all liabilities and expenses the Bank incurs in connection with the PDG. The proposed transaction structure is illustrated below.

Proposed PDG Transaction Structure



Turk Eximbank, as the Borrower, would have the primary obligation to ensure timely repayment to the Guaranteed Lenders. If Turk Eximbank fails to make a scheduled repayment, the Guaranteed Lenders could call on AIIB's PDG to pay the covered portion of the defaulted payment. Following such payment by AIIB, the Bank may, at its sole discretion and as provided in the Indemnity Agreement, demand immediate repayment from the MoTF or provide different repayment terms. Refer to **Annex 4** for further details on the terms and conditions of the proposed PDG and Indemnity Agreement.

Annex 5: SBF Partial Debt Guarantee–Key Terms

Below is a summary of the key terms and conditions from AIIB’s sovereign-backed PDG term sheet, which are subject to negotiations of the PDG Agreement and related agreements with the Borrower, Guaranteed Lenders and the AIIB Member providing the sovereign counter-guarantee and indemnity. This summary is for discussion purposes only. The provision of a Guarantee is subject, *inter alia*, to compliance with all applicable policies of AIIB, including those related to AIIB’s Environmental and Social Policy, review and acceptance of the ownership, management, financing structure (including in connection with shareholders, suppliers, equipment, and Project design), review and acceptance of project / transaction documentation by AIIB and the approval of the management and Board of Directors of AIIB in their sole discretion.

Guarantor	AIIB
Parties	AIIB and the Guaranteed Lenders and / or a Facility Agent acting on behalf of the Guaranteed Lenders.
Guarantee Face Value	USD200 million or EUR equivalent, up to 70 percent of the principal of the Guaranteed Loan.
Nature of Guarantee	AIIB’s PDG is a guarantee of payment (not collection) that is irrevocable and unconditional except as specifically provided in the Guarantee Agreement.
Partial Debt Guarantee	AIIB would guarantee payment of principal [and interest amounts] ³⁸ due on each defaulted scheduled payment that remains unpaid and outstanding after the requisite waiting period until the aggregate of AIIB’s guarantee payments reaches the Maximum Guaranteed Amount.
Maximum Guaranteed Amount	Up to USD200 million or EUR equivalent (not to exceed the Guarantee Face Value).
Guarantee Period	AIIB’s PDG is in force from the Effective Date until the final scheduled payment date (aligned with loan tenor) or when the balance of the guaranteed amount has been reduced to zero.
Guarantee Currency	USD and / or EUR
Sovereign Counter-Guarantee and Indemnity	The Indemnity Agreement sets forth the government’s obligations in respect of the PDG, including an obligation to reimburse AIIB for any payments AIIB makes under the PDG and indemnify AIIB for all liabilities and expenses AIIB incurs in connection with the PDG.
Fees	Processing Fee, Front-end Fee, Guarantee Fee and Standby Fee. For details, see the separate table below.

³⁸ While AIIB is supportive of both principal and interest being covered, total coverage under the AIIB guarantee will be capped at 70 percent of the principal amount. For example, for a USD285.7 million loan, the maximum guaranteed amount of AIIB’s PDG is up to USD200 million, including interest and principal.

<p>Conditions Precedent to the Effective Date</p>	<p>Conditions Precedent typically include that AIIB shall have received, <i>inter alia</i>, (a) relevant legal opinions, written notice from the Guaranteed Lender that all conditions precedent to the first disbursement under the Guaranteed Loan Agreement have been satisfied, (b) Payment of the Front-end Fee and, as applicable, the Processing Fee, and (c) a fully executed Indemnity Agreement and Project Agreement (as applicable).</p>
<p>Exclusions³⁹</p>	<p>Guaranteed Lender’s fraud, misrepresentation, or breach of its obligations under this Agreement; any act by the Guaranteed Lender in connection with the Project that constitutes a Prohibited Practice or breach of any Anti-Corruption Laws; failure to pay fees on time.</p>
<p>Representations and Warranties</p>	<p>Description of Applicable Representations and Warranties. These include (without limitation) that, as of the Execution Date, the Effective Date and on the date of each disbursement of the Guaranteed Loan, (a) the Guaranteed Loan and the project each have been fully and accurately described in the written information provided to AIIB and that all material facts have been disclosed to AIIB; (b) the Guaranteed Lender has not been convicted or subject to any investigation under any anti-bribery and corruption law and has not been suspended or barred by AIIB or by any multilateral development bank, and (c) the Guaranteed Lender has not committed or engaged in any “Prohibited Practice” as referred to in AIIB’s Policy on Prohibited Practices with respect to the Project or any transaction contemplated by the Finance Documents.</p>
<p>Duties of the Guaranteed Lenders</p>	<p>Description of the duties of the Guaranteed Lender, including but not limited to, (a) acting with the utmost good faith as would a reasonably prudent unguaranteed lender in similar circumstances; (b) exercising its rights under the Finance Documents in accordance with AIIB’s written directions; and (c) cooperating with AIIB in connection with AIIB’s exercise of any of its rights, after a claim payment. If the Guaranteed Lender fails in any material respect to perform any of its obligations to AIIB, AIIB has the right to reduce or cancel the amount of compensation for any loss to the extent that such loss occurred as a result of, or was increased by, such failure.</p>
<p>Amendment and waivers relating to the Guaranteed Loan</p>	<p>The Guaranteed Lenders shall not amend in any material respect or agree to any material amendment or waiver of any provision of a Finance Document, including any change in the nature or scope of the Project, or enter into</p>

³⁹ “Exclusions” in Annex 5 covers only events (misconduct by lenders) that trigger exclusions from AIIB PDG’s coverage, rather than exclusions from use of proceeds (which can be found in Annex 2).

	any additional Finance Document, except with AIIB's prior written approval or at its direction.
Project Agreement and Breach of Project Agreement	<p>The direct agreement between AIIB and the Borrower in respect of project-specific representations and undertakings to be given by the Borrower in favor of AIIB.</p> <p>Upon AIIB's determination in its sole discretion that the Borrower has breached its obligations under the Project Agreement, AIIB may notify the Guaranteed Lender of such breach and instruct the Guaranteed Lender to take one or more actions pursuant to the Guaranteed Loan Agreement, including but not limited to: (a) suspending further disbursements; (b) declaring an Event of Default; (c) accelerating repayment of the Guaranteed Loan; and (d) canceling any undisbursed amount of the Guaranteed Loan Commitment.</p>
Claims	The Guaranteed Lender may deliver a Payment Request to AIIB following a Scheduled Payment default but typically not later than 30 days after the expiration of the applicable waiting period.
Subrogation	Upon any payment made by AIIB pursuant to the Guarantee, AIIB shall be fully subrogated to the rights of the Guaranteed Lender relating to any such paid amount.
Acceleration of the Guaranteed Loan	<p>The Guaranteed Lender shall not accelerate the Guaranteed Loan, including upon the occurrence of an Event of Default, without AIIB's written consent.</p> <p>Acceleration or mandatory prepayment of a scheduled payment (which shall only occur with AIIB's prior consent) will not give rise to a corresponding acceleration of AIIB's obligation to pay a claim under this Guarantee.⁴⁰ AIIB will only be obligated to pay a claim for a defaulted payment following its scheduled payment date.</p>
Information Sharing	The Guaranteed Lender shall provide to AIIB all information that is material to AIIB's exposure under the Guarantee Agreement which the Guaranteed Lender receives or to which it has access, as well as such other information as AIIB may reasonably request.
Environmental and Social Undertakings and Prohibited Practices	The project will be subject to AIIB's environmental and social and integrity policies. The Guaranteed Lender shall consult with, and refer to, AIIB any and all decisions to be taken or discretion to be exercised under each Finance Document in respect of environmental and social requirements and allegations of Prohibited Practices

⁴⁰ [AIIB is considering the retention of an option, in its sole discretion, to accelerate its guarantee payments to the Guaranteed Lenders under the PDG but the Bank is unlikely to exercise such an option].

	concerning the Project, include determining Events of Default or Defaults.
Termination	AIIB shall be entitled to terminate the Guarantee Agreement if (a) any Guarantee Fee or Standby Fee payment is not made within thirty (30) days of notice that such fee was not paid when due. AIIB will not be liable for any loss arising while an overdue fee remains unpaid; (b) a representation made by the Guaranteed Lender to AIIB is false or materially misleading; (c) the Guaranteed Lender has failed in any material respect to perform any of its obligations to AIIB under the Guarantee Agreement beyond any applicable cure period; and (d) any employee, agent, or representative of the Guaranteed Lender has, in connection with the implementation of the Project, engaged in a Prohibited Practice.
Governing Law	English law

Annex 6: Key E&S Requirement for Implementation

1. All sub-project activity will be screened against AIIB Exclusion list and Turk Eximbank's project investment E&S assessment questionnaire.
2. All higher risk sub-project defined per AIIB ESP will be excluded. For Component B, geological hazards such as landslides will be screened to avoid any secondary hazard.
3. For any on-land solar sub-project and other greenfield sub-project that may need additional land resources, Turk Eximbank will review the land status against AIIB ESS2 criteria. Any sub-project that involves land acquisition and involuntary resettlement will be excluded. For project that will buy land on willing-buy-willing sell basis, Turk Eximbank will review if there is any legacy compensation issue and on-going grievances.
4. For any on-land solar sub-project and other green field sub-project, Turk Eximbank will consult local authorities and other stakeholders to avoid any potential risk to culture heritage.
5. For all solar sub-projects with loan application of USD5 million or above, Turk Eximbank will have an E&S specialist to site visit the sub-project to review the OHS management and collect the OHS data during the construction period, also identify any potential GBV risk on-site and require an action plan to mitigate risk, if needed.
6. For all utility solar sub-projects⁴¹ and distributed solar sub-projects with an installation capacity of more than 20MW, Turk Eximbank will review the sub-borrowers' supply chain information and screen for any potential adverse labor and working conditions, involving their SPV suppliers. To this end, Turk Exim Bank will:
 - (a) confirm the sub-borrowers' due diligence of the subproject.
 - (b) require, through representations, covenants, or conditions, that the sub-borrowers obtain confirmation that to the best knowledge of the sub-borrowers' SPV suppliers, the supplied SPV systems for the subproject were produced without adverse labor and working condition issues.
 - (c) require the sub-borrowers to have procedures and capacity to review and monitor their SPV supply chain requirements.

⁴¹ The local energy law defines and distinguishes "licensed solar project" from "un-licensed solar project."

"Un-licensed solar projects" are those that do not require any license and are considered to be distributed solar projects; such projects: a) have generation facility of less than 5 MW; b) have generation facility, regardless of size, that does not supply to the transmission/distribution system but is located in the same metering point as the consumption facility; or c) generation facility based on renewable energy resources, provided its capacity is limited to two times the contracted for power set out in the connection agreements with municipalities (or affiliated institutions thereof), industrial facilities and agricultural irrigation facilities or other persons.

"Licensed solar project" will be considered as utility solar projects.

Turk Eximbank will prepare the loan covenants to reflect the requirements (b) and (c) of this paragraph in the POMs.

7. All sub-projects will establish a Grievance Redress Mechanism (GRM) scaled to the risk and impact of the sub-project. The GRM will be accessible to both sub-project workers, including construction workers, and project-affected community. The GRM may utilize existing formal and informal compliant handling mechanisms if properly designed and implemented.
8. Turk Eximbank will sustain a GRM to handle any grievance related to this Project and disclose the availability of AIIB PPM⁴².

⁴² AIIB. Policy on the Project-affected People's Mechanism. <https://www.aiib.org/en/policies-strategies/operational-policies/policy-on-the-project-affected-mechanism.html>.

Annex 7: Borrower Key Financial Information

BRSA Financial Highlights⁴³

Balance Sheet (Data in USD' 000)	Year Ended 12/31/2020	Year Ended 12/31/2021	Year Ended 12/31/2022	Half Year Ended 6/30/2023
<i>Exchange Rate</i>	7.44	13.32	18.69	26.05
	<i>BRSA, Audited</i>	<i>BRSA, Audited</i>	<i>BRSA, Audited</i>	<i>BRSA, Limited Review</i>
Audited/Limited Review/Non-audited				
Cash & Cash Eq.	1,570,338	1,462,457	777,794	728,288
Investment Securities	1,559,101	865,365	786,146	773,533
Derivatives	66,185	115,542	76,683	65,227
Total Gross Loans	24,067,731	21,630,036	16,355,308	15,866,797
Expected Credit Losses	(105,007)	(48,904)	(41,375)	(31,141)
Total Net Loans	23,962,723	21,581,132	16,313,933	15,835,656
PPE & Intangibles	3,623	1,687	4,487	10,580
Other Assets	292,361	175,240	559,656	402,367
Total Assets	27,454,331	24,201,423	18,518,700	17,815,651
Liabilities				
Interbank Money Market Deposits	184,918	489,293	423,343	364,665
Securities Issued	3,085,613	2,798,996	2,232,826	2,743,762
Funds Borrowed and Other Funds	21,593,632	18,813,880	13,912,372	13,018,070
Subordinated Debt	600,040	414,684	348,244	309,863
Other Liabilities	455,814	592,254	330,861	295,635
Total Liabilities	25,920,016	23,109,107	17,247,647	16,731,996
Equity				
Share Capital & Premium	1,246,169	810,774	738,529	529,708
Reserves	84,969	48,331	198,983	141,266
Retained Earnings	203,176	233,211	333,541	412,681
Total Equity	1,534,314	1,092,316	1,271,053	1,083,654
Total Equity and Liabilities	27,454,331	24,201,423	18,518,700	17,815,651

⁴³ Financial highlights table is prepared based on BRSA financial statements. BRSA financial statements, on the other hand, do not apply inflation accounting and therefore shows purely underlying business performance. Ratios are calculated based on reporting currency (i.e., TRY) denominated figures to avoid misrepresentation as a result of the USD/TRY volatility. Where applicable, key ratios are annualized for interim results.

Income Statement (Data in USD' 000)	Year Ended 12/31/2020	Year Ended 12/31/2021	Year Ended 12/31/2022	Half Year Ended 6/30/2023
<i>Exchange Rate</i>	7.02	8.89	16.58	19.90
	<i>BRSA, Audited</i>	<i>BRSA, Audited</i>	<i>BRSA, Audited</i>	<i>BRSA, Limited Review</i>
<i>Audited/Limited Review/Non-audited</i>				
Total interest income	713,950	808,657	1,039,627	917,674
Interest Expense	(539,726)	(493,515)	(692,141)	(709,624)
Net interest income	174,224	315,142	347,487	208,050
Fee & Commission Income	81,769	103,970	101,344	48,650
Fee & Commission Expense	(49,798)	(55,539)	(49,627)	(23,351)
Net Fee & Commission Income	31,971	48,430	51,718	25,298
Net gain on investment securities (loss)	(219,353)	227,553	216,716	(865)
Net FX gain (loss)	339,724	(155,212)	(172,882)	36,884
Other Operating Income	2,104	14,178	12,573	5,703
Operating Income	328,669	450,092	455,611	275,071
Provision for Loan Losses	(52,635)	(26,043)	(16,754)	(9,716)
Other Provision Expense	(2,035)	(16,989)	(10,048)	(3,552)
Operating Income after Impairment	273,999	407,059	428,809	261,803
Personnel Expenses	(37,164)	(33,812)	(35,114)	(29,119)
Other Admin. Expenses	(21,520)	(23,895)	(17,688)	(11,571)
Operating Expenses	(58,683)	(57,706)	(52,802)	(40,690)
Profit / (Loss) before Tax	215,316	349,353	376,008	221,112
Taxes	-	-	-	-
Profit / (Loss) after Tax	215,316	349,353	376,008	221,112

Key Financial Ratios	Year Ended 12/31/2020	Year Ended 12/31/2021	Year Ended 12/31/2022	Half Year Ended 6/30/2023
<i>Audited/Limited Review/Non-audited</i>	<i>BRSA, Audited</i>	<i>BRSA, Audited</i>	<i>BRSA, Audited</i>	<i>BRSA, Limited Review</i>
I- Profitability				
Return on Average Assets	0.8%	1.2%	1.9%	2.2%
Return on Average Equity	14.7%	23.9%	32.5%	33.9%
Net interest Margin	0.7%	1.1%	1.9%	2.2%
Net Interest Spread	0.7%	1.1%	1.8%	2.1%
Average Cost of Funding	2.2%	1.8%	3.7%	7.6%
Average Yield of Earning Assets	2.9%	2.9%	5.6%	9.7%
II. Efficiency				
Operating expenses/Operating income	17.9%	12.8%	11.6%	14.8%
Operating expenses/Avg assets	0.2%	0.2%	0.3%	0.4%
III- Capital Adequacy				
Tier I Regulatory Ratio	15.8%	14.9%	18.5%	14.7%
Regulatory CAR	20.0%	18.0%	20.9%	16.4%
Equity /Assets	5.6%	4.5%	6.9%	6.1%
IV- Liquidity				
Net Loans / Borrowings	0.9	1.0	1.0	1.0
Liquid Assets (Cash + Cash Eq.)/ Total Assets	5.7%	6.0%	4.2%	4.1%
Cash + ST Investments/ Borrowings	0.12	0.10	0.09	0.09
V- Portfolio Data				
Net Loans/Assets	0.87	0.89	0.88	0.89
NPLs (90+days past due)/Gross Loans	0.27%	0.19%	0.21%	0.17%
Write-Offs/Average Gross Loans	0.00%	0.01%	0.01%	0.00%
Total Provisions/NPLs	1.59	1.16	1.19	1.16
OLER ((NPLs-Provisions)/Total Capital)	-1.8%	-0.5%	-0.4%	-0.3%
VI- Growth Rates				
Assets	25.4%	57.9%	7.3%	34.1%
Gross Loans	24.9%	60.9%	6.1%	35.3%
Borrowings	25.9%	58.3%	5.4%	35.5%
Equity	25.7%	27.5%	63.2%	18.9%

Annex 7: Sector Background Information

Türkiye Banking Sector

According to Banking Regulation and Supervision Agency (i.e., BRSA or BDDK) data, the overall Turkish banking sector has achieved strong earnings growth in 2022, as a result of strong loan growth momentum, higher lending rates compounded with moderate increase in funding cost, and healthy growth in fees and commissions. In effect, in 2022, the Turkish banking sector has benefited from the more contained funding costs relative to the loan rates and securities income, especially from CPI linkers⁴⁴.

Over the last 12 months, the Central Bank imposed strict macroprudential measures on banks, including penalties on banks that hold large amounts of foreign-currency deposits, lending rate caps and mandatory reserves in the form of government securities. The interest rate margin has narrowed during the first half of 2023 due to higher funding costs and caps on lending rates. CPI-linked security will also record lower gains, although it should still contribute significantly to banks profitability as inflation will remain elevated in 2023.

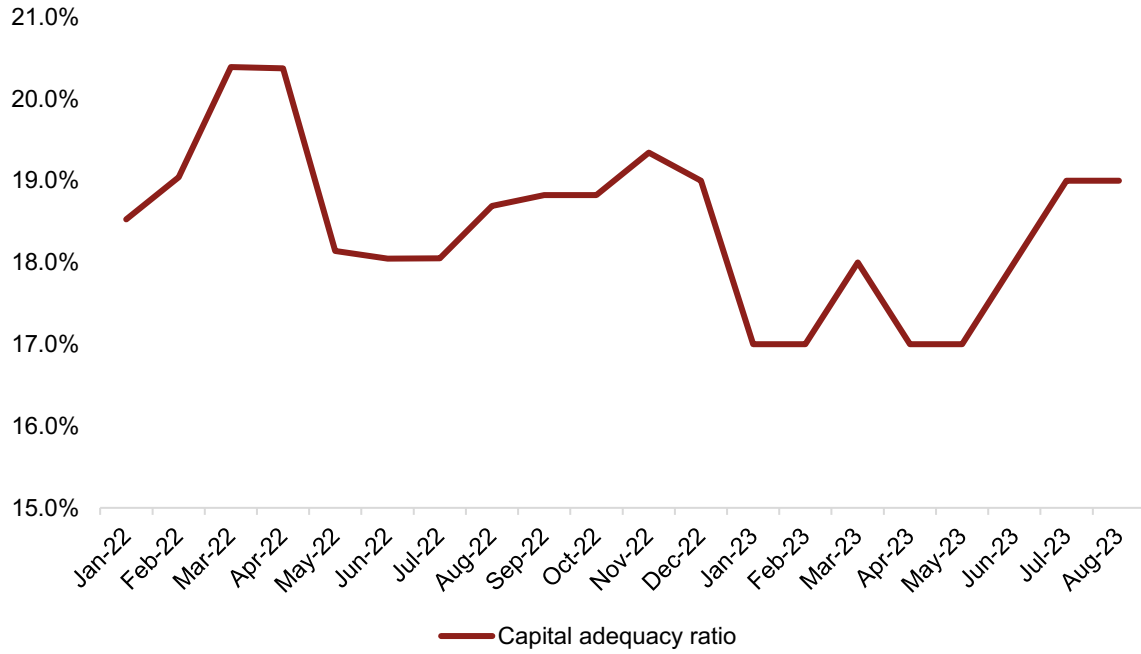
Following the election at the end of May 2023, a new finance minister has been appointed as well as a new Central Bank governor. The Central Bank has raised interest rates 5 times to 35 percent⁴⁵ as of October 26, 2023. Interest rate hikes effectively increased the interest rate cap imposed on the banking sector's lending rates. Moreover, the Central Bank has also lifted some of the macroprudential measures, such as lowering requirements against holding foreign-currency deposits and the requirements of holding reserves against loans in the form of government securities. These moves should help ease profitability pressure on the banks and aid the recovery of the banking sector.

Although TRY has experienced accelerating depreciation, the strong growth in earnings in 2022 allowed the Turkish banking sector to preserve its capital adequacy ratio (CAR) at a high level, above the regulatory requirements. Specifically, the Turkish banking sector CAR was 19 percent according to the BDDK as of the end of August 2023. The monthly CAR of Turkish Banking sector is shown below.

⁴⁴ ING. Bank Outlook 2023. November 2022. <https://think.ing.com/articles/strong-earnings-growth-for-turkish-banks-in-2022>

⁴⁵ Bloomberg. Turkey's Mega Hike Has Most Analysts Cheering, Asking for More. August 2023. <https://www.bloomberg.com/news/articles/2023-08-25/turkey-s-mega-hike-has-most-analysts-cheering-asking-for-more>

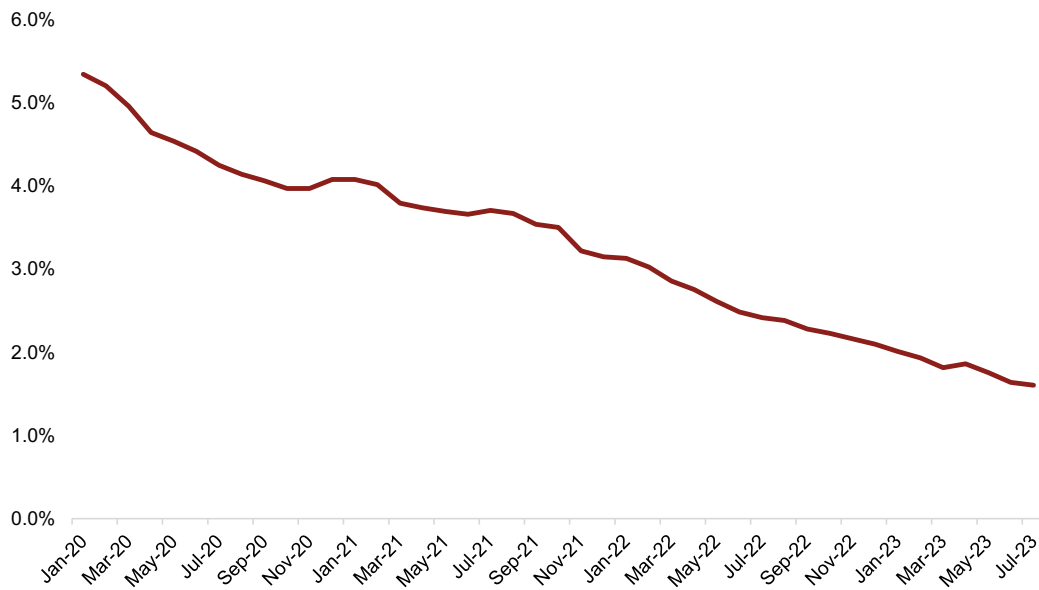
Capital Adequacy Ratio of Turkish Banking Sector⁴⁶



Turkish banking sector NPL has remained stable. BRSA has lifted the forbearance on NPL recognition, yet the banking sector NPL has been trending down steadily since 2020, reflecting limited NPL generation against the deterioration in the operating environment. It is understood that companies are conservative in managing their liquidity hence NPL is not going up, although asset quality would come under pressure in case of a sharp economic contraction. The low banking sector NPL ratio is also driven by the high nominal loan growth in the inflationary environment.

⁴⁶ Bankacılık Düzenleme Ve Denetleme Kurumu (BDDK). Monthly Banking Sector Data (Basic Analysis). <https://www.bddk.org.tr/BultenAylik/en>.

Turkish Banking Sector NPL



Although Turkish banks' FX maturities is not expected to pose any material near-term risks, foreign borrowing is shrinking.⁴⁷ The situation has started to improve in 2023, especially with some alleviation after the election in May.

Renewable Energy in Türkiye

Rapid growth. In Türkiye, renewable energy production has more than doubled since 2009, with strong growth in geothermal, hydro, wind and solar. Despite the rapid growth in domestic renewable energy production, Türkiye relies mostly on energy imports for its supply. Hence, Türkiye continues to promote the further development of renewable energy resources.

Türkiye's overall energy policy stems from its rapid economic growth as well as efforts to reduce the country's dependence on imported energy sources. The Ministry of Energy and Natural Resources (MENR) is responsible for formulating and implementing energy policies and regulating the energy sector. The policy prepared by the MENR focuses primarily on reducing Türkiye's reliance on imported energy resources and is based on three main pillars: (i) improving energy supply security; (ii) localization, including increasing the use of domestic energy resources; and (iii) improving predictability in energy markets.

In 2021, Türkiye ratified the Paris Agreement and set a target of achieving net-zero emissions by 2053. In its recently published 2035 Türkiye National Energy Plan, Türkiye targets to achieve 74 percent of the new electricity capacity to be produced by renewable energy by 2035 and expects solar energy capacity to increase by more than five times from the current level to 53 GW.

⁴⁷ ING. Bank Outlook 2023. November 2022. <https://think.ing.com/articles/strong-earnings-growth-for-turkish-banks-in-2022>.

Government incentives. Türkiye's unlicensed electricity generation regime, introduced in 2013, led to a major growth of rooftop and ground-mounted solar PV projects from 1 MW to 5 MW capacity. To help address the huge growth of unlicensed solar PV projects, the government introduced new incentives in May 2019, for residential, commercial, and industrial sectors. This includes a net metering scheme where homeowners can receive a monthly energy credit for solar exports to the grid, which can be used to offset electricity bills.⁴⁸ It covers both self-consumption and supply of excess generation to the grid, where the eligible projects are mainly solar rooftop applications.

Reduction in cost. Various manufacturers have also indicated that the adoption of solar energy will help reduce the cost of production in the long term. It is estimated that electricity from fossil fuels costs between 5 and 17 cents per kilowatt-hour, while solar energy typically costs between 3 to 6 cents per kilowatt-hour and is expected to further decrease in the future.⁴⁹

Carbon border tax. To reduce global carbon emissions, the European Union's Carbon Border Adjustment Mechanism (CBAM) is an attempt to price carbon dioxide emissions associated with a range of imports to promote cuts in industrial emissions.⁵⁰ As of September 2023, 18 European countries have implemented carbon taxes to various degrees. These carbon tax ranges from less than EUR1 to EUR100 per metric ton of carbon emissions, including countries such as Sweden, Switzerland, Finland, and many more.⁵¹ The implementation of carbon tax has further encouraged Turkish exporters to adopt and invest in solar energy, as more than 40 percent⁵² of Türkiye's total export trade in 2022 was with the European Union countries.

⁴⁸ Institute for Energy Economics and Financial Analysis. New Incentives Brighten Türkiye 's Rooftop Solar Sector. December 2019.

⁴⁹ Consumer Affairs. Solar Energy vs. Fossil Fuels. June 2023. <https://www.consumeraffairs.com/solar-energy/solar-vs-fossil-fuels.html>.

⁵⁰ Bloomberg. The EU Wants to Make Global Trade Greener. August 2023.

⁵¹ Tax Foundation. Carbon Taxes in Europe. September 2023. <https://taxfoundation.org/data/all/eu/carbon-taxes-in-europe-2023/>.

⁵² Statista. Share of exports from Türkiye to the EU. August 2023. <https://www.statista.com/statistics/1045891/share-of-exports-to-the-eu-in-total-export-trade-of-turkey/>.

Annex 8: Sovereign Credit Fact Sheet

Background. Türkiye is an upper-middle-income country with an income per capita of around USD11,000 (or around USD39,000 in purchasing power parity) and a population of around 85 million. Türkiye is a large, diversified, dynamic and business-oriented economy. Since the early 2000s, it enjoyed robust growth, around 5.5 percent per year on average, underpinned initially by a strong focus on development, macroeconomic stability, strong fiscal frameworks, trade openness and institutional reform. During this time, income per capita has tripled, while poverty fell from 42 percent to 13 percent (as of 2019).

However, since 2016, Türkiye's sovereign credit rating has deteriorated, due to reliance on short-term stimulus to boost growth, unpredictable and unorthodox policies, declining fiscal and FX buffers, high dependence on external finance, perceived erosion of institutional checks and balances, as well as rising geopolitical risks—according to observers.

In particular, the past three years have been marked by financial volatility, increasing macro-financial vulnerabilities and macroeconomic stress. In a typical cycle, expansionary policies (e.g., large credit expansion) or an external shock, or both, would lead to a higher current account deficit, higher inflation, and negative real interest rates. This would in turn put pressure on the currency (with occasional sharp depreciations), drain international reserves and lead to market anxiety and potential credit downgrades. This could be followed by further policy changes to restore confidence.

Selected economic indicators 1/	2019	2020	2021	2022	2023*	2024*	2025*
GDP growth 2/	0.8	1.9	11.4	5.5	4.0	3.2	3.2
Inflation 2/	15.2	12.3	19.6	72.3	54.6	60.9	52.5
Fiscal balance 3/	-4.7	-5.1	-4.0	-2.1	-6.0	-5.5	-3.3
Gross public debt	32.6	39.6	41.7	29.4	34.0	34.5	32.2
Gross public financing needs	8.4	10.5	12.1	12.9	13.3	13.5	13.8
Current account balance	1.4	-4.4	-0.9	-5.4	-4.1	-3.1	-2.8
Gross external debt 4/	54.4	59.8	54.1	52.0	47.2	47.4	..
Gross external financing needs	22.3	29.4	27.6	23.2	22.3	23.4	..
Gross FX reserves (USD billion) 4/	106.3	93.2	111.1	128.8	126.1
Exchange rate (TRY/USD) 4/	5.9	7.3	13.0	18.7	28.0

Sources: IMF Press Release 23/343; IMF World Economic Outlook Oct 2023; IMF Country Report 23/303, CBRT, MoTF

Notes: 1/ In percent of GDP, except where noted; figures for 2023-25 are projections; 2/ Percent change, year-on-year; average; 3/ Nonfinancial public sector, IMF definition (excluding one-off items); 4/ most recent data from the CBRT, TRY=Turkish lira, end-of-period, for 2023: as of October 20.

Recent Developments. Since September 2021, the central bank has cut its policy rate several times despite high and accelerating inflation and against the ongoing global monetary tightening, which has led to capital outflows and a sharp depreciation. The currency has lost two-thirds of its value, while average annual inflation has risen sharply to over 80 percent at the peak in 2022. Over that period, a host of increasingly complex and nontransparent macro-prudential measures has been put in place to stem depreciation, promote de-dollarization, direct credit and keep the growth going. While growth in 2022 was still high, at 5.5 percent, these policies are believed to have led to distortions in the economy.

Additionally, Türkiye has been hit by several shocks. Notably, the geopolitical conflict in Europe has had significant negative spillovers via higher energy and food prices, and higher risk premia. The energy import bill has almost doubled, and the current account deficit has increased sharply 5.4 percent of GDP in 2022. Furthermore, the earthquakes in early February 2023, even if not causing lasting damage to productive potential, have been a major humanitarian disaster.

In parallel to these developments, all three major rating agencies downgraded Türkiye's sovereign credit, to B negative (S&P), B negative (Fitch) and B3 stable (Moody's), as of August 2023.

The electoral victory in May 2023 of the incumbent, President Erdogan, cleared political uncertainty and raised hopes for policy normalization. The new economic team is reputed to be supportive of more orthodox policies and has signaled intentions to lower inflation, reduce external imbalances and maintain fiscal discipline. The Central Bank has started increasing interest rates, with a cumulative 2,650bps hike delivered so far, and gradually dismantling the many distorting macroprudential regulations. On account of these developments, in September 2023, S&P and Moody's revised Türkiye's credit outlook to stable.

Outlook and Risks. The economy continues to perform relatively well on the back of post-earthquake reconstruction, strong tourism, and resilient consumption. According to IMF, growth is expected to reach 4.0 percent in 2023, and then converge to the medium-term potential of around 3.0-3.5 percent. Inflation in 2023 is expected to decline to around 55 percent. The outlook is characterized by high uncertainty. Key unknowns relate to tight external liquidity, the volatile market sentiment, and the durability of the recent improvements macroeconomic policies.

As for the latter, the shift toward more orthodox and predictable policies is a welcome development, that would improve economic resilience and boost credit ratings in the medium term. However, Türkiye is yet to build a track record for that, as such normalizations are prone to reversals, should the economy slow, or electoral calendar interfere. Also, the needed decisive and sustained policy tightening is likely to come at the cost of a growth slowdown, while the unwinding of the complex web of macroprudential regulation will be challenging and carry financial stability risks. Disinflation and restoring external balances may thus take some time.

That said, the private sector has demonstrated resilience and has considerable experience in navigating through the volatile environment. Large firms report sufficient liquidity, positive short-term net open FX positions and significant natural FX hedges. Regarding the banking sector, despite recent shocks and large depreciations, reported capitalization remains adequate, non-performing loans are low, while reported liquidity and profitability metrics are adequate. Despite the sector's dependence on wholesale FX funding and short-term FX deposits, domestic banks have been able to roll over obligations even amid high market uncertainty. Ultimately, the system hinges on residents' confidence and willingness to keep their sizeable dollar deposits in domestic banks, which so far has been sustained.

According to the IMF, public debt is generally low and sustainable, even if vulnerabilities have been rising. After dipping in 2022 on account of high inflation, debt is expected to increase over the medium term to around 37 percent of GDP. Rating agencies expect debt to stabilize at somewhat lower levels, around 30-35 percent of GDP. Overall, the government's relatively strong balance sheet and uninterrupted access to financial markets allay sustainability concerns. Key strengths anchoring Türkiye's longer-term debt sustainability include a track record of economic resilience, as well as a large, diversified economy with a young population and entrepreneurial spirit which translate into substantial growth potential. Likewise, Türkiye's external debt is expected to remain sustainable over the medium term.