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CREDIT GUARANTEE SCHEME AND SMALL AND MEDIUM-SIZED ENTERPRISE FINANCE: THE CASE OF TURKEY

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Abstract

This study examines the recently revived credit guarantee fund (KGF) mechanism in Turkey from a comparative historical perspective and identifies the structural features of the Turkish economy that complicate access to finance for SMEs. The banking-based financial system in Turkey, state banks and the public sector, was unable to resolve the access to finance problem of SMEs in the near past. Consequently, the public authorities revived the KGF in early 2017. The KGF was established in 1993 but stayed idle until recently. Despite these efforts, structural impediments to easing SMEs' access to finance persist in the Turkish economy. This paper identifies the chronic current account deficit, high inflation, large size of the informal economy, and bank-based financial system as the major structural obstacles to easing SMEs' access to finance. Moreover, the global financial crisis has exacerbated the access to finance problem of Turkish SMEs. This paper posits that, for Turkey to resolve the financing problem of SMEs, it is necessary to identify clearly the sustainability of the recently revived KGF and its impact on public and private debt. In addition, the KGF mechanism needs to prioritize SME financing in value-added tradeable goods so that it can contribute to long-term, sustainable economic growth in Turkey.

Keywords: credit guarantee fund, SMEs, Turkey, access to finance

JEL Classification: E44, G10, G18, P16

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1. INTRODUCTION

In Turkey, small and medium-sized enterprises (SMEs) constitute the largest business segments in terms of their share of the economy and their contribution to employment and economic growth. According to the data released by the Turkish Statistical Institute (Turkstat), as of 2014, SMEs in Turkey account for 99.8% of the total number of enterprises, 73.5% of the total employment, 54.1% of wages and salaries, 62% of turnover, 53.5% of value added at factor cost, and 55% of gross investment in tangible goods (Turkstat 2016). Despite the significance and dominance of SMEs in the Turkish economy, it has not been possible to resolve their access to finance problems over the years. This led the Turkish government to revive the idle credit guarantee scheme (CGS) in 2017 with special emphasis on assisting SME financing. This chapter examines the Turkish CGS from a historical perspective and aims to bring a comparative perspective to the Turkish case. Furthermore, this study identifies the structural features of the Turkish economy that aggravate SMEs' access to finance.

The Turkish Credit Guarantee Fund Commercial Management and Research Incorporated Company (Kredi Garanti Fonu İşletme ve Araştırma Ticaret Anonim Şirketi) was first incorporated in 1991. The Turkish–German Technical Cooperation Agreement of the Council of Ministers and Cabinet Decree 93/4496 led to the formal foundation of the Turkish Credit Guarantee Fund in 1993 and the amendment of its name to the Credit Guarantee Fund Incorporated Company (Kredi Garanti Fonu Anonim Şirketi—in short KGF) in 2007. The KGF became effective by granting its first guarantee in 1994. Although it became operational in 1994, until recently its activities were very limited in assisting the financing needs of micro, small, and medium-sized enterprises (MSMEs). Along with the KGF, the Small and Medium Business Development and Support Administration (KOSGEB) functions as the key public entity to support SMEs and start-ups in Turkey. The KGF's main function is to ease access to finance for SMEs and to offer guarantees to SMEs via the banking system for this purpose. On the other hand, the KOSGEB's support for SMEs and start-ups includes not only financial aid and grants but also training, research and development support, and an overall knowledge base for SMEs and start-ups. Thus, the KOSGEB is involved in all the stages of building a business from scratch or developing an existing one.

Until recently, several factors in the Turkish economy contributed to the financing problems of SMEs. The historically high inflation and interest rates, the banking-based financial system in Turkey, the large size of the informal economy in Turkey, SMEs' inability to offer adequate financial statements to the banks, and banks' unwillingness to offer loans to SMEs because of the high risk perception have all contributed to the financing problems of SMEs. Levitsky and Prasad (1987) assert that the main reasons behind the SMEs' limited access to finance are that banks consider lending to SMEs to be risky, banks are biased in favor of lending to large corporations, the administrative costs of lending to SMEs are high, and SMEs lack proper accounting records and financial documents. These obstacles are all relevant to Turkish SMEs. In early 2017, the Turkish government took several measures to enhance the functioning of the KGF. These measures not only improved the financing activities of SMEs but also boosted the economic growth rates in the short run. Due to the very short period during which these new measures have been in effect, this chapter's main goal is to provide a comparative historical perspective to the credit guarantee scheme (CGS) in Turkey with other country groups while underlining the structural features of the Turkish economy that exacerbate the financing problems of SMEs, especially after the global financial crisis. Thus, this chapter presents a case study of the KGF in Turkey, examines its revival with new measures since early 2017, evaluates the pros and

cons of the new perspective, and posits policy recommendations for an effective, sustainable CGS in operation. In addition to empirical evidence that illustrates SMEs' financing problems, this chapter presents expert interviews with financial and real sector representatives. This approach helps to acquire a deeper understanding of the financing problem in the Turkish economy and to determine how the interviewees from divergent realms of the Turkish economy view the financing problems of SMEs.

This chapter proceeds as follows. The second section examines the status of SMEs in the Turkish economy, and the third section outlines the KGF, its recent revival since early 2017, and its impact on the financing activities of MSMEs and the general economy. The fourth section explains the structural features of the Turkish economy that challenge the KGF and posits that the aftermath of the global financial crisis exacerbated SMEs' financing problem because of the extra-low interest rates in the international markets. The fifth section locates Turkish SMEs in relation to other country groups, presents empirical evidence in several respects, and cites expert interviews from real and financial sector representatives. The sixth section concludes with policy recommendations.

2. STATUS OF SMES IN THE TURKISH ECONOMY

In Turkey, decision 2018/11828 of the *Official Gazette* (2018) revised the classification of SMEs in 2018. According to the new classification, an SME is "an enterprise that employs less than 250 persons per year and either its annual net sales revenue or balance sheet value does not exceed 125 million Turkish Liras." This definition includes micro, small, and medium-sized enterprises in Turkey with the acronym KOBİ (meaning SME). Table 1 and Table 2 below present the distinction between micro, small, and medium-sized enterprises in the Turkish context and the equivalent European Union criteria, respectively.

Table 1: SME Criteria in Turkey

Turkish Criteria	Micro SME	Small SME	Medium SME
Staff Headcount	< 10	< 50	< 250
Annual Sales Revenue	≤ 3 million TRY	≤ 25 million TRY	≤ 125 million TRY
Annual Balance Sheet Total	≤ 3 million TRY	≤ 25 million TRY	≤ 125 million TRY

Source: Official Gazette (2018).

Table 2: SME Criteria in the European Union

European Union Criteria	Micro SMEs	Small SMEs	Medium SMEs
Staff Headcount	< 10	< 50	< 250
Annual Sales Revenue	≤ 2 million euro	≤ 10 million euro	≤ 50 million euro
Annual Balance Sheet Total	≤ 2 million euro	≤ 10 million euro	≤ 43 million euro

Source: European Commission (2017).

According to the sectoral groups, 39.2% of SMEs are active in wholesale and retail trade and the repair of motor vehicles and motorcycles, 15.4% in transportation and storage, and 12.4% in manufacturing as of 2014 (Turkstat 2016). According to an older statistic dated 2012, 44% of Turkish SMEs are in wholesale and retail trade, 17% in transportation and storage, 14% in manufacturing, 10% in accommodation and food

services, 6% in professional, scientific, and technical activities, 6% in construction, and 1% in the information and communication sectors. The 2012 figures are more detailed than the latest available data about SME sectors. This shows that the knowledge gap about SMEs is a critical factor in designing a more effective CGS in Turkey. When classifying the SMEs in the manufacturing sector in terms of their technology level, 59.7% of them are in low technology, 31% in medium-low technology, 9.1% in medium-high technology, and only 0.3% in high technology as of 2014 (Turkstat 2016). The technology level of SMEs in the manufacturing sector is critical to grasp their different needs and to design appropriate guarantee mechanisms to address their financing difficulties. Table 3 provides the classification of Turkish companies (micro, small, medium, and large) with respect to their manufacturing technology level. These figures also include start-up businesses in Turkey. As the introduction articulated, the KOSGEB is involved in different aspects of building and developing SMEs and start-ups and is responsible for start-up financial interventions and grants, whereas the KGF is the main entity facilitating SMEs' access to finance via guarantees.

Table 3: Proportion of SMEs in the Manufacturing Industry by Size Class and Technology Level, 2014

	Technology Level (Share in %)			
Company Size (Number of Employees)	**High**	**Medium-High**	**Medium-Low**	**Low**
Micro (1–19)	0.2	8.3	31.1	60.4
Small (20–49)	0.9	17.6	28.4	53.0
Medium (50–249)	1.5	17.4	31.4	49.7
SMEs (1–249)	0.3	9.1	31.0	59.7
Large (250 +)	2.6	18.8	24.7	54.0

Source: Adapted from Turkstat (2016).

As of 2015, 55.1% of Turkish SMEs are involved in export transactions, whereas 37.7% are involved in imports as their main business model. Examining the size of the companies involved in the export transactions, the share of micro enterprises is 17.7%, that of small enterprises is 20.3%, and that of medium-sized enterprises is 17.1%, whereas large enterprises (employing more than 250 people) account for 44.8% of the total Turkish exports in 2015. On the other hand, in the total imports, the share of micro enterprises is 6.3%, that of small enterprises is 13.1%, that of medium-sized enterprises is 18.2%, and that of large enterprises is 62.3% as of 2015 (Turkstat 2016). These figures underline the dominance of large enterprises in Turkish foreign trade activities, which is closely related to the financing problems of SMEs in Turkey.

3. STATUS OF THE MSME CREDIT GUARANTEE SCHEME IN TURKEY

3.1 ESKKK

In Turkey, there are two main mechanisms that offer collateral support to alleviate the financing problems of SMEs. One of them is the Tradesmen and Craftsmen Credit and Collateral Cooperatives (Esnaf ve Sanatkârlar Kredi ve Kefalet Kooperatifleri (ESKKK)) and the other is the KGF (Duramaz 2017). The ESKKK offers collateral support mainly for micro-sized traders and craftsmen, whereas the KGF offers support for SMEs. The ESKKK was founded in 1951, functioned under Turkish Trade Law until 1969, and

thereafter started to function as a private law legal entity with the Cooperatives Law numbered 1163 (Duramaz 2017, 20). The ESKKK offers loans to micro-sized traders and craftsmen via intermediary banks. The Turkish Treasury provides these funds, and the ESKKK facilitates loans through its collateral (Duramaz 2017, 21). Contemporarily, the ESKKK operates under the Center Union of Turkish Tradesmen and Craftsmen Credit and Collateral Cooperative Unions (Türkiye Esnaf ve Sanatkarlar Kredi ve Kefalet Kooperatifleri Birlikleri Merkez Birliği (TESKOMB)). The ESKKK offers 100% collateral for the Treasury-supported state bank Halkbank's loans to micro-sized tradesmen and craftsmen. Compared with the ESKKK's support for micro-sized tradesmen and craftsmen, the KGF operates for other SMEs of micro, small, and medium sizes. The ESKKK has more than 1.5 million members of tradesmen and craftsmen, who are shareholders of the ESKKK, and this is how the ESKKK can offer collateral for its members. According to Duramaz (2017, 21), the total TESKOMB collateral reached 40 billion TRY by 2016, approximately $10.6 billion.[1]

3.2 KGF

The KGF operates as a joint-stock company, and its shareholders include chambers, public agencies, non-government organizations, and banks. The Union of Chambers and Commodity Exchanges of Turkey (TOBB) holds 29.17%, and the Small and Medium Business Development and Support Administration (KOSGEB) holds 29.16% of the shares; the Confederation of Turkish Tradesmen and Craftsmen (TESK), the Foundation of Small and Medium Sized Enterprises, Self-Employed, and Administrators of Turkey (TOSYÖV), and the Foundation of Vocational Training and Small Industry Support (MEKSA) hold 0.12%, 0.0080%, and 0.0040% of the shares, respectively. Additionally, 27 banks and financial institutions each own 1.54% of the total shares. At the end of 2017, the KGF had 40 branches in 35 different cities in Turkey (KGF 2017a).

3.2.1 The KGF from its Creation in 1994 to 2016

Researchers consider Turkey's KGF as a latecomer to the CGSs in the developing world, because other developing countries started actively to operate these schemes in the early 1970s (Table 4). In particular, Japan is one of the early CGS innovators (Yoshino and Taghizadeh-Hesary 2016). After the introduction of the Japanese CGS in 1937, they spread throughout Europe and the Americas in the 1950s and then to Africa, Asia, and Oceania in the 1960s and 1970s (Yoshino and Taghizadeh-Hesary 2016).[2] Levitsky (1997) provides a comparison of developing countries in terms of the start of CGS operations (Table 4).

Although Turkey founded its CGS, the KGF, in 1993 and it became operational in 1994, the country used historical legislation dating from long before the establishment of the KGF to improve the financing conditions of SMEs and the functioning of the KGF after its establishment. Table 5 summarizes this legislation. It illustrates that, after 2015, Turkey made more efforts to boost the effectiveness of the KGF. Essentially, the efforts to improve the KGF's effectiveness stemmed from the need to address the financing problems of SMEs and the declining economic growth rates. The efforts in 2015 underline the increasing role of the Turkish Treasury in KGF operations; the KGF reform efforts in 2017 also reflect the Treasury's critical role.

[1] For TRY–USD conversions, the study uses the last exchange rate for 2017, 1 USD = 3.77 TRY.

[2] Please see OECD (2018a) for a comprehensive and comparative review of the latest SME finance trends and conditions around the world.

Table 4: Developing Country Credit Guarantee Schemes

Country	Operation Year
Indonesia	1971
Malaysia	1972
Pakistan	1972
Republic of Korea	1974
Taipei,China	1974
Philippines	1976 (originally 1952)
Zimbabwe	1978
Sri Lanka	1979
Peru	1979
Chile	1980
Colombia	1981
India	1981
Thailand	1986
Turkey	1994

Source: Adapted from Levitsky (1997, 6).

Table 5: Historical Legislation Relating to the KGF's Activities in Turkey

Year	Legislation	Content
1964	Act of Fees Tax numbered 492	Credit collateral transactions (excluding judgment fees) are except from the fees stipulated in the law.
1964	Stamp Tax Law numbered 488	Papers that the KGF issues to provide credit collateral are exempt from stamp tax.
1984	Value Added Tax Law numbered 3065	Credit collateral transactions of the KGF are exempt from value added tax.
1993	Cabinet Decree Official Gazette numbered 21637	Establishment of the credit guarantee fund (KGF).
2006	Corporate Tax Law numbered 5520	The KGF is exempt from corporate tax.
2009	Cabinet Decree Official Gazette numbered 27289	The treasury must provide support for credit guarantee institutions.
2015	Regulations, Official Gazette numbered 29267	Amendment to the Regulations on Principles and Procedures regarding Setting the Qualifications of Guarantees and Other Receivables by the Banks and the Reserves.
2015	Cabinet Decree Official Gazette numbered 29281	The treasury must provide support for credit guarantee institutions.
2015	Amendment to Law, Official Gazette numbered 29319	TRY 2 billion is the upper limit of the support that the treasury must provide for credit guarantee institutions.
2015	Cabinet Decree Official Gazette numbered 29396	Increasing the upper limit of treasury support for credit guarantee institutions to TRY 2 billion, the upper limit of guarantees for the ship-building industry to TRY 5 billion, and the upper limit of the guarantees in the scope of the treasury support by the KGF to TRY 15 billion.
2015	Cabinet Decree Official Gazette numbered 29566	Amendment to the "Cabinet Decree on Principles and Procedures regarding the Treasury Support to be provided to the Credit Guarantee Institutions" numbered 2015/7331.

Source: Adapted from KGF (2017b).

The KGF issues guarantees via bank loans either through its own equity or through the Turkish Treasury support funds. Until 2016, on an annual basis, the highest number of firms using authorized guarantees reached the maximum of 23,365 and the total amount of authorized guarantees exceeded 7.3 billion TRY during the same year (almost $2 billion) (KGF 2016). The number of firms to which the KGF granted guarantees in 2016 (23,365) is almost equivalent to the total number of firms that received authorized guarantees between 1994 and 2015 (25,325). Between 1994 and 2016, in total 47,450 firms received authorized guarantees, with a total guarantee amount of 18 billion TRY (equivalent to $4.8 billion). On the other hand, between 1994 and 2016, in total only 37,180 firms used these authorized guarantees, with the total amount of guarantees used reaching 12 billion TRY (about $3.2 billion) (KGF 2016). These figures offer a stark contrast to the revitalization of the KGF in 2017. Yıldırım, Ünal, and Gedikli (2015) examine the effectiveness of the KGF in easing the financing activities of Turkish SMEs between 1990 and 2014. They find that the KGF has boosted commercial loans since 2006 and that a higher level of investments reflects the improvement in commercial loans. In other words, the KGF has been effective in improving Turkey's capital stock by encouraging more investment. Table 6 below illustrates the details of the KFG's activities until 2016.

Table 6: Provision of Guarantees (Equity + Treasury) by the KGF, 1994–2016 (TRY)

	Requested Guarantees (Incoming Demand)		
Period	**Number of SMEs**	**Credit Amount**	**Guarantee Amount**
1994–2012	18.946	10.034.354.834	7.273.973.837
2013	4.107	2.704.616.086	2.017.920.732
2014	5.662	3.115.261.712	2.341.999.214
2015	8.764	5.626.880.473	4.237.564.532
2016	30.220	14.387.448.543	11.388.989.893
1994–2016	65.628	39.697.356.514	30.083.622.049
	Authorized Guarantees (Approved Demands)		
Period	**Number of SMEs**	**Credit Amount**	**Guarantee Amount**
1994–2012	12.615	5.961.117.226	4.230.867.690
2013	2.462	1.467.406.113	1.061.378.253
2014	4.233	1.887.621.435	1.391.917.903
2015	6.015	3.324.047.085	2.445.967.341
2016	23.365	9.579.927.724	7.375.030.469
1994–2016	47.450	24.633.598.216	18.287.718.263
	Guarantees in Use (Opened Demands)		
Period	**Number of SMEs**	**Credit Amount**	**Guarantee Amount**
1994–2012	8.036	3.867.335.534	2.806.833.626
2013	2.118	1.007.778.894	760.575.736
2014	4.579	1.353.449.105	1.049.795.242
2015	4.736	2.417.635.842	1.848.791.475
2016	19.506	6.681.693.217	5.127.824.694
1994–2016	37.180	16.341.609.824	12.316.949.883

Source: KGF (2016).

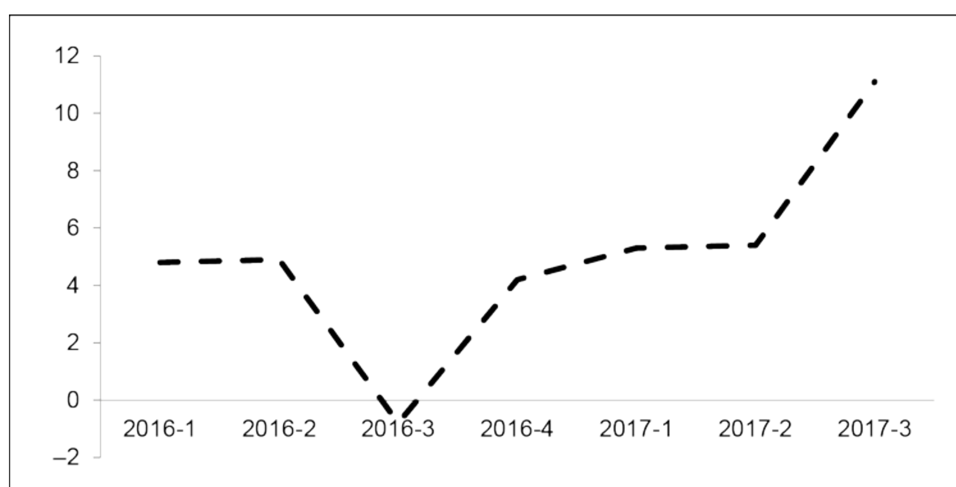
Between 1994 and 2016, micro, small, and medium-sized enterprises accounted for about 27.7%, 40.6%, and 31.7% of all the guarantees that the KGF issued, respectively. In 2015, the non-performing guarantee ratio was 4.67%, and this ratio dropped to 3.65% in 2016. Of the non-performing guarantees, 57.9% were equity guarantees and the remaining 42.1% were treasury-backed guarantees. By the end of 2016, the KGF's total assets stood at 314,9 million TRY, of which 219 million TRY corresponded to liquid assets. Üstün (2016) indicates that only 1% of the SMEs in Turkey take advantage of the KGF's support. Some of the reasons behind this very low rate are the perception that only troubled SMEs use KGF support, the large size of informal activity in SME operations, the high cost of loans even with collateral guarantees, the high application and commission fees, and the long time that it takes to receive bureaucratic approval (Üstün 2016). Despite the efforts until 2016, these problems significantly limited the KGF's activity in Turkey.

3.2.2 The 2017 Revision of the KGF

It is essential to place the significant revision of the KGF within the context of the Turkish political economy. The financial stability orientation of the Turkish central bank starting from 2010 aimed to give the Turkish economy a soft landing in the face of the surge of capital flows and overheating in the economy (Yağcı 2017b). This resulted in a political backlash from within the ruling Justice and Development Party (Adalet ve Kalkınma Partisi) (Yağcı 2018). In addition, the failed coup attempt during the third quarter of 2016 resulted in a sharp decline in the GDP growth. For these reasons, the government intended to stimulate economic growth by easing access to finance for SMEs. The revisions of the KGF occurred against this political economy background.

Figure 1: Turkish Quarterly Gross Domestic Product (GDP) Growth

(%)



Source: Turkstat (2017).

Despite the coup attempt in July 2016, the economic growth rate normalized during the fourth quarter of 2016 and further escalated in 2017. According to the GDP figures, in the third quarter of 2017, the Turkish economy grew by 11.1%. Compared with the same quarter of the previous year, the total value added increased by 14.8% in the industry sector, 18.7% in the construction sector, 2.8% in the agricultural sector, and 20.7% in the service sector (wholesale and retail trade, transport, storage, and accommodation and food service activities) (Turkstat 2017). During the same period,

the exports of goods and services increased by 17.2% and the imports of goods and services increased by 14.5%. While these are exceptional results, it is important to emphasize the role of KGF-supported loans in these economic growth rates.

To improve the operations of the KGF, to ease the financing difficulties of SMEs, and to boost economic growth, the Turkish Government implemented new measures in early 2017, and a new era started for the CGS in Turkey. The Turkish Treasury and the KGF signed a protocol following the Council of Ministers Decree 2017/9969, which amended the treasury support for the KGF in several respects. With these amendments,

- The KGF guarantee limit that the Turkish Treasury supported increased to 250 billion TRY (around $66 billion) from 20 billion TRY.
- The treasury compensation limit in the case of non-performing loans increased from 2 billion TRY to 25 billion TRY ($6.63 billion).
- The guarantee limit ratios for SMEs and exporter SMEs increased to 90% and 100%, respectively.
- The one-time commission for SME loans reduced to 0.03% from the 0.5%–2% range, and the application fee was annulled. The reduction on commission fees aimed to lower the cost of bank loans and incentivize SMEs to take advantage of the new KGF measures.
- The treasury compensation limit for non-performing loans is 7% of the guarantee so that, if the bank non-performing loan ratio is more than 7%, banks bear the credit exposure above 7% (Central Bank of the Republic of Turkey (TCMB) 2017a). This aimed to reduce the moral hazard for the banks, since the guarantee limit ratios for SMEs and exporter SMEs increased to 90% and 100%, respectively.
- The SME and exporter SME loan limits increased to 12 million TRY ($3.18 million) and 50 million TRY ($13.26 million), respectively.

To accelerate the credit utilization process, the KGF removed the credit approval committees instituted and introduced an internal evaluation system (KOBİS) and the "Portfolio Guarantee System" (PGS) so that banks directly evaluate the application and after their approval the KGF only seeks compliance with the beneficiary conditions. With these changes, the loan application closing time shortened to 1 day from 35–40 days. A KGF representative underlines that the new KGF measures are not a cyclical tool but a permanent structural reform for the Turkish economy. Furthermore, the KGF representative indicates that, with the new measures, the KGF became the largest credit guarantee fund in the world, surpassing the Republic of Korea's Korea Credit Guarantee Fund (KODIT) (Para Analiz 2017).

In addition to the amendments to the treasury support for the KGF, the Turkish Government introduced other measures to boost economic activity in 2017. Some of these measures were the KOSGEB's interest-free loan support and the TOBB's low-interest respite credit. Nevertheless, the KGF amendments were the main contributor to the surge of economic growth in the first three quarters of 2017.

The new KGF measures started to influence the loan provisions from the first quarter of 2017, and the annual corporate loan growth surged by 20% by the end of the third quarter in 2017 (TCMB 2017b). By September 2017, the total loan provision of Turkish banks had reached 1 trillion 994 billion TRY (about $529 billion), of which 51% comprised commercial and corporate loans, 25% SME loans, and 24% consumer loans and credit cards (Banking Regulation and Supervision Agency [BDDK] 2017). The sectoral loan provision shares in the total loans in decreasing order were wholesale

and brokerage (8.94%), construction (8.51%), electric, gas, and water resources (6.53%), retail trade and personal products (4.12%), agriculture (4.02%), research, consulting, advertising, and other activities (3.14%), the textile and textile products industry (3.11%), the main metal industry (2.94%), the food, beverage, and tobacco industry (2.89%), and hotels (2.23%). The composition of SME loans was 41.6% for medium-sized, 32.9% for small, and 25.5% for micro-sized enterprises. The non-performing loan ratio for the banking sector was stable at 3.05% by September 2017 (BDDK 2017).

In late 2017, the KGF released some information about the new CGS measures that came into effect in early 2017. As of November 2017, 365,000 firms used KGF-supported loans equivalent to 220 billion TRY ($58 billion), and they used 197 billion TRY ($52 billion) collateral for these loans (Karanfil 2017). Of these transactions, 54% were first-time loans, 33% additional loans, and 5% renewal loans. The average loan value was 532 thousand TRY ($141,000), and the average interest rate was 15.22%. This rate is lower than the average TRY commercial loan interest rate.

With the new KGF measures since early 2017, the average maturity for working capital loans has been 39 months with 9 months with no payment, and for investment loans the average maturity has been 65 months with 29 months with no payment. SMEs have used 74% of the KGF-supported loans, and 31% of the loans have been in the manufacturing sector. Lastly, 7,568 exporters have used loans of 27.7 billion TRY ($7.35 billion), and exporter SMEs have used 7.5 billion TRY of these loans (Karanfil 2017). As a result, KGF-supported loans played an important role in the acceleration of economic growth in the first three quarters of 2017 (Figure 1). KGF representatives estimate that the KGF measures contributed 2% to the overall economic growth in 2017 (Para Analiz 2017).

With the new measures, 314,239 SMEs received authorized guarantees only in 2017, with the total amount of authorized guarantees reaching 238 billion TRY (about $63 billion) (KGF 2017a). With these figures, the number of firms that received guarantees only in 2017 is 6 times higher than those that received guarantees between 1994 and 2016 combined. As a result, the Turkish economy grew at an annual rate of 7.4% in 2017. The KGF contributed significantly to the acceleration of the economic growth rate.

Regarding the composition of KGF activities, the distinction between KGF equity-backed vs treasury-backed guarantees and bank loans is crucial. Table 7 shows that, with the revitalization of the KGF in 2017, the treasury-backed guarantee and loan amounts increased significantly, whereas the equity-backed guarantee and loan amounts remained stable. In other words, treasury-backed guarantees dominated the KGF activities in 2017. The sustainability of the treasury-dominated KGF activities in the long term is highly questionable. Thus, overreliance on treasury support may inhibit the effectiveness of the KGF in the long run. The last section on policy recommendations addresses this and other aspects of the KGF to make it a more effective, sustainable, technology-driven, and current account deficit-reducing financing scheme.

Table 7: Guarantees Granted (Equity Backed versus Treasury Backed)
(Million TRY)

Guarantees Granted (Million TL)						
	Equity Backed			Treasury Backed		
Year	Number	Loan Amount	Guarantee Amount	Number	Loan Amount	Guarantee Amount
2016	4,446	2,392	2,057	18,919	7,188	5,318
2017	6,888	2,381	2,076	307,351	262,601	236,698

Source: KGF (2017a).

Nevertheless, structural obstacles to SME finance persist in the Turkish economy, which challenge the sustainability and long-term contribution of the CGS. Relatedly, the next section considers the major challenges ahead for achieving an effective and sustainable CGS in Turkey. This requires an examination of the structural features of the economy and the way in which it is possible to improve the KGF's operations in consideration of these structural features.

4. CHALLENGES FOR THE DEVELOPMENT AND EFFECTIVENESS OF THE CGS IN TURKEY

4.1 Overview of Challenges for the CGS

As articulated in the previous sections, the Turkish bank-based financial system aggravates the problem of access to finance for Turkish SMEs. In addition to the prevalent difficulties that SMEs face in fundraising from banks, more recently, the Basel capital accord made the financing environment more challenging. Basel III adopted new rules—liquidity frameworks and leverage ratio frameworks—to strengthen the risk management of banks as well as introducing strengthened capital requirements (Yoshino and Taghizadeh-Hesary 2017). These new measures may further restrict banks in providing loans to SMEs.

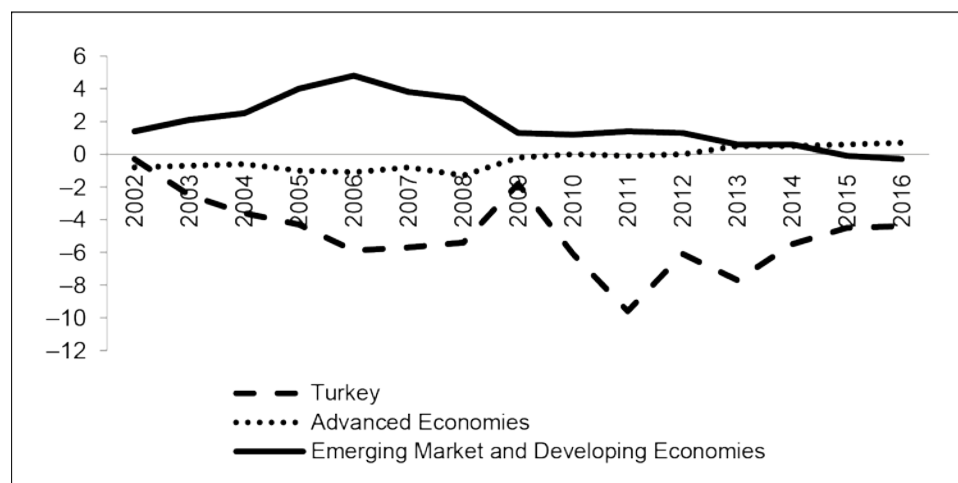
For the Southern and Eastern Mediterranean region, Ayadi and Gadi (2013) underline three key factors in the exclusion of MSMEs from credit markets: information asymmetries arising from MSMEs' lack of transparency, suitable collateral, and track record; poor macroeconomic and regulatory conditions in the region, such as high interest rates; and poorly functioning financial systems as a result of the lack of effective credit information-sharing mechanisms, weak enforcement of creditor rights, and inappropriate collateral regimes. In the Turkish case, the first and second reasons are key contributors to the financing problems of SMEs. On the other hand, for the third reason, it is only possible to cite the banks' inappropriate collateral regime as a major obstacle for SMEs. Another challenge for the proper functioning of CGSs in all countries where they exist is that banks can shift riskier loans away from their normal lending to guarantee schemes (Levitsky and Prasad 1987). It is feasible to address this issue through the monitoring of bank lending and the proper functioning of risk-sharing arrangements in which the public authority, businesses, and banks all share the risk in CGSs so that banks do not have an incentive to shift riskier loans to the guarantee schemes. These difficulties necessitate a properly functioning CGS in Turkey so that SMEs can take an active part in the economy. In addition to these factors, structural problems in the Turkish economy exacerbate SMEs' problems and complicate the effective functioning of the CGS in Turkey.

4.2 Structural Economic Challenges in Turkey and their Impact on SME Financing and the KGF

Some of the key structural problems in the Turkish economy are the chronic current account deficit, the high inflation rates, and the large size of the informal economy (Yağcı 2017a). These structural obstacles, combined with the bank-based financial system and the dominance of large holding companies in the domestic economy and the financial sector, significantly constrain the financing ability of SMEs. This section aims to explain these structural constraints and challenges of the Turkish economy from a comparative perspective to enable a proper examination of the development and effectiveness of the CGS in Turkey.

One of the major structural problems for the Turkish economy is the chronic current account deficit. The main reason behind the unsustainable and chronic current account deficit is the chronic trade deficit, because the Turkish export sector is mainly composed of low-technology products, the Turkish manufacturing sector relies heavily on imported input components, and Turkey is dependent on energy imports, which deteriorate the current account balance (Yağcı 2017a, 99). During times of rapid economic expansion, the current account deficit worsens, and, during times of economic contraction, it tends to improve. The pro-cyclicality of the current account deficit and concerns about the overheating of the Turkish economy obstruct the efforts to ease the financing difficulty of SMEs. The comparison of the Turkish case with other economic groups in the world illustrates this structural constraint much more clearly (Figure 2).

Figure 2: Current Account Balance in Country Groups
(% GDP)

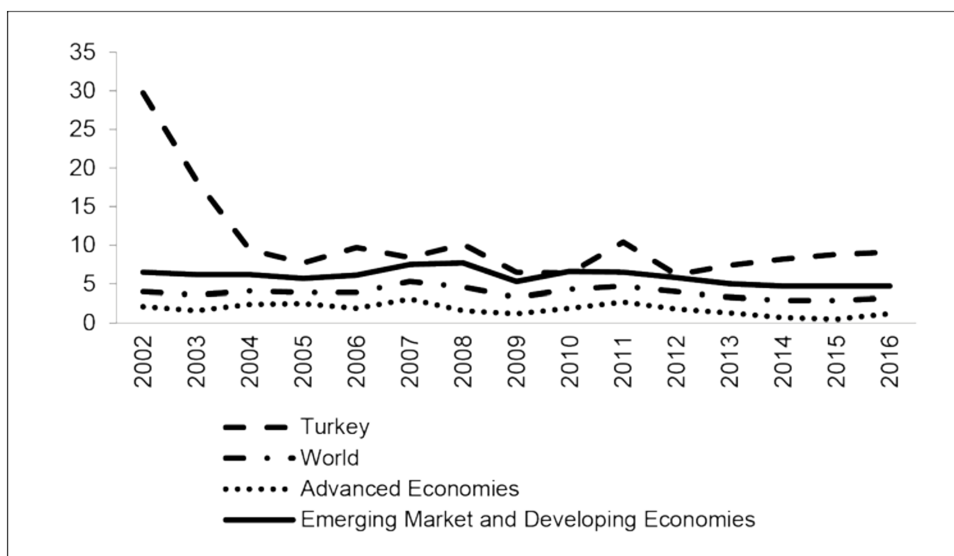


Source: IMF (2017a).

In Turkey, the current account imbalance relies excessively on the domestic demand, and the external savings magnify the foreign financing needs, increase the risk premia, and make the Turkish economy very vulnerable to external shocks (OECD 2018b, 9). In addition, foreign currency loans with very low interest rates in international markets have increased the debt burden of Turkish firms significantly (OECD 2018b, 11). The significant depreciation of the Turkish lira against foreign currencies in 2018 underlines the fragility of the Turkish economy to external shocks.

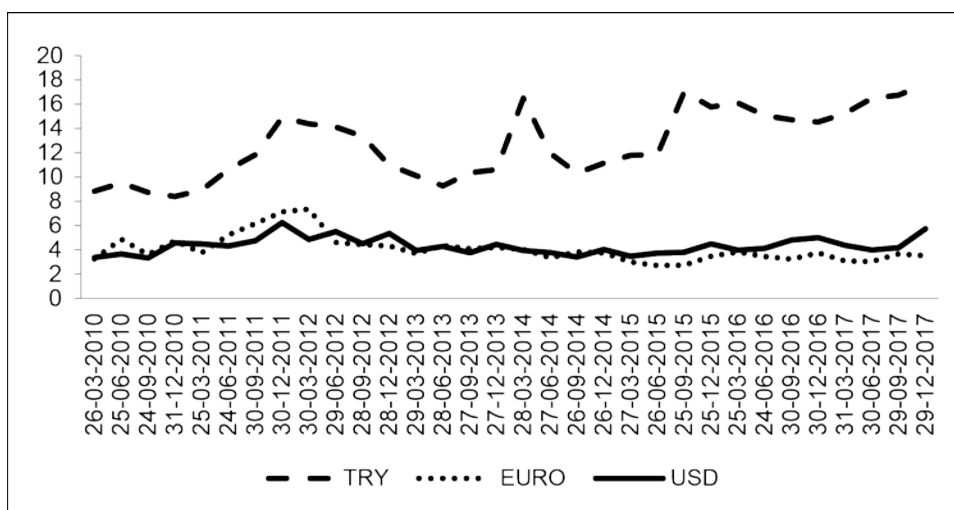
Another structural challenge of the Turkish economy is high inflation rates. The Turkish central bank, the Central Bank of the Republic of Turkey (TCMB), was successful in lowering the inflation rates to single digits in the early 2010s. However, recently the inflation rates have risen, and they surpassed 10% in 2017 (Figure 3).

Figure 3: Inflation (Consumer Prices, %)



Source: IMF (2017b).

Figure 4: Commercial Loan Interest Rates in Turkey
(%)



Source: TCMB (2017c).

As a result, the TRY-denominated commercial loan interest rates are at very high levels compared with US dollar- or euro-denominated loans (Figure 4). The high interest rates for Turkish lira loans have a negative influence primarily on SMEs, because most of them cannot access foreign-currency loans. On the other hand, large holding companies can access foreign-currency loans with ultra-low interest rates in the aftermath of global financial crisis. Nevertheless, these conglomerates have foreign debt and they are taking exchange rate risk with foreign-currency-denominated loans.

The large size of the informal economy is another key challenge that aggravates SMEs' access to finance. According to estimates, the informal economy constitutes 31% of the Turkish economy compared with 18% in OECD economies (OECD et al. 2016, 336). Because of the large size of the informal economy, Turkish SMEs in general cannot provide proper financial reporting and revenue analysis. Consequently, banks, as the key financiers in the Turkish economy, are either unwilling to offer loans to SMEs or charge very high interest rates because the perceived risks are high. Overall, the bank-based financial system contributes to the challenges that SMEs in Turkey face in gaining access to finance as a structural impediment.

Another structural feature of the Turkish economy that exacerbates the financing problem of SMEs is the bank-based financial system. As of 2014, banking sector assets account for 94% of all the financial assets in the Turkish economy (IMF 2017c, 27). With respect to the banking groups in the financial system, private commercial banks, state-owned commercial banks, state-owned development banks, and private development banks have a 57%, 33%, 3%, and 1% share of the overall financial system, respectively. Therefore, SMEs rely heavily on the banking sector to access finance. In addition to these factors, the historical evolution of the Turkish financial system paved the way for "holding banking" (Gültekin-Karakaş 2005). This also limits SMEs' access to finance in the Turkish context. Relatedly, the overreliance on bank financing and the negligible size of alternative financing mechanisms necessitate the active involvement of public agencies, such as the KGF and the KOSGEB, to ease Turkish SMEs' access to finance.

The lack of alternative financing arrangements, high commercial interest rates, and overreliance on the banking sector require CGSs and the Turkish KGF to be more active in easing SMEs' access to finance. In addition to these factors, Basel III has put more pressure on the banking sector regarding SME lending, so banks are less willing to lend to SMEs, which they consider to be riskier than large companies (Yoshino and Taghizadeh-Hesary 2017). Besides, information asymmetry with regard to SMEs' activities and financial reporting difficulties constrain bank lending to SMEs. Therefore, an effectively functioning CGS mechanism is a necessity for Turkish SMEs to overcome the financing hurdle. The next section situates Turkish SMEs in relation to other country groups based on empirical evidence and survey data and examines the views of real and financial sector representatives about SMEs' access to finance.

5. ACCESS TO FINANCE ISSUES FOR SMES IN TURKEY AND OTHER COUNTRY GROUPS: EMPIRICAL EVIDENCE AND EXPERT INTERVIEWS WITH REAL AND FINANCIAL SECTOR REPRESENTATIVES

In the analysis of Turkish SMEs, comparisons with other country groups are critical. These will enable the researchers to identify the context-specific obstacles faced by Turkish SMEs. In this regard, the European Commission's Small Business Act (SBA) offers a venue to examine Turkish SMEs' performance in comparison with their European counterparts. The European Union (EU) initiated the SBA in 2008. The SBA is a comprehensive framework for the EU policy on SMEs. It aims to promote entrepreneurship, reduce the regulatory burden, and improve access to finance, markets, and internationalization for European SMEs (European Commission 2018).

According to the 2017 SBA Fact Sheet, Turkey performs well compared with its European counterparts in promoting entrepreneurship for SMEs. In terms of enhancing skills, innovation, the regulatory environment, internationalization, and responsive administration for SMEs, Turkey performs on a par with European countries. Nevertheless, for Turkish SMEs, the main obstacle appears to be access to finance and "second-chance" opportunities (European Commission 2017b). This was translated in the Turkish Government measures to improve access to finance conditions, and the revitalization of the KGF in 2017 is a case in point in this respect. Nevertheless, the policy interventions for second-chance opportunities remain limited for Turkish SMEs.

The OECD SME Policy Index provides a more detailed study based on survey data and assessments with policy makers that compares policies for Turkish and Western Balkan SMEs. For the Turkish case, the survey sample size is 1,344 SMEs, consisting of 549 small, 484 medium-sized, and 311 large enterprises (OECD et al. 2016). This survey categorizes different aspects of access to finance, and SMEs evaluate each dimension. Accordingly, a score of 1 (the lowest score) indicates the weakest dimension or the worst performance, whereas a score of 5 (the highest score) refers to the strongest dimension or the best performance. The figures below illustrate the dimensions of each challenge. For access to finance, financial literacy and bank and non-bank financing are the lowest-performing categories.

These figures are supplemented with interview research with real sector representatives. Political economy studies widely use the interview methodology (Mosley 2013). Through interviews, it is possible to grasp the perceptions, preferences, and evaluations of key stakeholders and articulate the missing link between survey findings and economic behavior (Yağcı 2018). The cited interviews are part of a research project utilizing the "purposive sampling" strategy in interview research (Yağcı 2016).

5.1 General Assessment of Access to Finance

The low scores for financial literacy and non-bank financing highlight the access to finance challenges for Turkish SMEs. Academic research on Turkish SMEs underlines the financing challenges. These studies on Turkish SMEs mostly concentrate on different cities. For instance, a study on İstanbul-based SMEs with a sample size of 924 firms finds that 53% of SMEs finance their activities with equity, 68% indicate that access to finance is their major problem, and only 7% indicate that they do not have a financing problem (Güzeldere and Sarıoğlu 2014). The respondents highlight high interest rates and collateral as the major obstacles to finance, and these are the main reasons for their preference for equity financing (Güzeldere and Sarıoğlu 2014, 235). Another SME survey with 107 SMEs based in Gaziantep finds that 67% of SMEs express access to finance as the main obstacle and that 46% do not use bank loans for their activities (Civan 2012). Another survey-based study with 200 respondents in Aksaray and Mersin finds that 60% of SMEs encounter funding problems (Çelik and Karadal 2007). These studies underline SMEs' access to finance challenges in Turkey and identify high interest rates and collateral requirements as major impediments to access to finance. The expert interviews with real and financial sector representatives in the section below substantiate these findings.

Figure 5: Access to Finance: Turkish SMEs' Survey Responses

Access to Finance
Lowest score - Highest score
Financial literacy (2.68) Non-bank financing (2.73) Bank financing (3.55) Venture capital (4.19) Legal and regulatory framework (4.28)

Source: OECD et al. (2016, 145).

5.2 Legal and Regulatory Framework

For the legal and regulatory framework, creditor rights receive the lowest score.

Figure 6: Legal and Regulatory Framework: Turkish SMEs' Survey Responses

Legal and Regulatory Framework
Lowest score - Highest score
Creditor rights (3.53) Stock market (4.22) Registers (4.40) Credit information bureaus (4.51) Banking regulations (5.00)

Source: OECD et al. (2016, 147).

According to a real sector representative, one of the major problems that SMEs face in their financing arrangements is the nature of credit contracts, which protect the banking sector 100% but ignore the real sector's interests (Yağcı 2016, 252). In comparison with international examples, in Turkey, the language of credit contracts is very heavy, includes too many details, and, in the words of the SME representative: "Under normal conditions, it is really troublesome and unexpected that two sides sign this kind of agreement" (Yağcı 2016, 252). The international examples from Switzerland and Germany stress that a credit contract should appeal to real sector companies, with language that is very simple, clear, and understandable: "These contracts are not tens of pages with very small letter sizes (like the ones in Turkey). They are very clear. There are differences with respect to the attitude and tone" (Yağcı 2016, 252). According to real sector representatives, this problem is associated with the lack of trust between banks and SMEs. One of them indicates that banks with centralized, top-down decision-making mechanisms and state banks with cumbersome bureaucracies cannot build a trustworthy relationship in the local conditions (Yağcı 2016, 252).

Another aspect of this problem is that SMEs lack the necessary legal assistance in their dealings with the banks. An important implication of this problem is that banks can recall their commercial loans especially during an economic slowdown or for other reasons, even though there is no repayment problem on the part of the SMEs. These kinds of loan recalls usually result in bankruptcy for companies that normally do not have financial problems. Many SMEs refuse to deal with banks because of their bad experiences in the past.

Some of the other legal and regulatory problems that SMEs face in their financing arrangements include letters of guarantee given to the state and the resource utilization support fund, which incur additional costs for SMEs in credit contracts.

5.3 Bank Financing

One of the critical issues in SMEs' access to finance in Turkey is the fact that the banking system relies heavily on fixed-asset collateral for SME finance and does not utilize movable assets for this purpose. Furthermore, due to the short-term deposit base, banks are not willing to provide SMEs with long-term loans (OECD et al. 2016, 339). The comparison of Turkish SMEs with their Western Balkan counterparts illustrates that only in Turkey is there an operational CGS run by a dedicated agency (OECD et al. 2016, 149). However, the above analysis indicates that only since 2017 has the Turkish CGS, the KGF, been actively engaged in overcoming SMEs' problems in gaining access to finance.

On the issue of bank financing for SMEs, another important distinction is between suppliers and distributors or retailers. A former high-level executive of a large business group indicates that his or her group could provide assistance to suppliers for their financing problems, but this is not the case for distributors or retailers. Hence, banks can allocate supplier SMEs low-risk loans with the collateral of large holding company payments (Yağcı 2016, 251). On the other hand, distributor SMEs cannot take advantage of low-risk loans.

Figure 7: Bank Financing: Turkish SMEs' Survey Responses

Bank Financing
Lowest score - Highest score
Credit guarantee schemes (3.44) Banking statistics (3.61)

Source: OECD et al. (2016, 149).

5.4 Non-bank Financing

The low scores for alternative financing mechanisms in Turkey, such as savings and loan associations and microfinance, explain Turkish SMEs' overreliance on bank loans.

Figure 8: Non-bank Financing: Turkish SMEs' Survey Responses

Non-bank Financing
Lowest score - Highest score
Savings and loan associations (SLAs) (1.00) Microfinance (2.33) Factoring (3.67) Leasing (3.92)

Source: OECD et al. (2016, 151).

The most common form of non-bank financing is leasing, and SMEs constitute 40% of leasing clients (OECD et al. 2016, 339). Turkish banks own many of the leasing companies. Factoring is another instrument that SMEs utilize for their financing activities, but the factoring costs remain much higher than the traditional lending rates. In Turkey, the KOSGEB attempts to fill the gap in non-bank financing for SMEs and start-ups. For this purpose, the KOSGEB offers financial aid and grants in categories of general support, project-based support, entrepreneurship, and loans of emergency support and machinery and equipment support.

Real sector representatives maintain that the Development Bank of Turkey can take more responsibility for assisting the financing needs of SMEs via alternative financing schemes. Although they indicate the Industrial Development Bank of Turkey to satisfy the financing needs of SMEs to some extent, they do not see this as adequate. Another aspect that requires improvement in the Turkish context for financing activities of SMEs is project-based financing, which is not a developed element of the financing option available to Turkish SMEs. With project-based financing, SMEs will not look for a mortgage or real estate as collateral, but they can utilize the project itself for this purpose (Yağcı 2016, 253).

A real sector representative also emphasizes that SMEs can enhance their financing arrangements by approaching alternative finance tools, such as bond and stock issuance, going public, establishing strategic alliances, or making use of Islamic finance, tools such as sukuk and mudarabah. The central bank policies in the aftermath of the global financial crisis caused political backlash from within the ruling government in Turkey, and the monetary policy received harsh criticism from leading politicians for generating high interest rates in the economy (Yağcı 2018). The real sector representative reaffirms that the financing problem of SMEs cannot be solved by mere reliance on low interest rates, which is why they bring alternative financing tools to the attention of SMEs (Yağcı 2016, 254).

5.5 Venture Capital

It is also possible to consider venture capital as an alternative financing mechanism for Turkish SMEs and start-ups. Nevertheless, venture capital is at a very early stage in Turkey, and more legal and regulatory developments are necessary to incentivize venture capital financing mechanisms.

Figure 9: Venture Capital: Turkish SMEs' Survey Responses

Venture Capital
Lowest score - Highest score
Monitoring and evaluation (2.33) Legal framework (4.33) Design and implementation (4.90)

Source: OECD et al. (2016, 152).

5.6 Financial Literacy

Financial literacy is an essential element of the access-to-finance obstacle for Turkish SMEs. Many SMEs cannot access the financial system because they lack proper legal and financial literacy in their line of business. The large size of the informal economy in Turkey exacerbates this challenge, and banks consider SMEs to be very high-risk clientele because of their legal and financial literacy limitations.

Figure 10: Financial Literacy: Turkish SMEs' Survey Responses

Financial Literacy
Lowest score - Highest score
Monitoring and evaluation (1.00) Design and implementation (3.10)

Source: OECD et al. (2016, 152).

6. CONCLUSIONS AND POLICY RECOMMENDATIONS

This chapter examines the recently revived KGF in Turkey from a comparative historical case study perspective. For the KGF to be a long-term, sustainable, effective CGS mechanism, it is necessary to address several issues. This section presents the key findings from previous research on CGSs and lists concrete policy recommendations for the Turkish KGF to tackle Turkey's structural economic problems.

Roper (2009) underlines the necessary steps to improve CGSs. These suggestions include offering targeted CGSs so that the system is more effective in support of SMEs' transition to innovation, designing both technical and commercial approval processes (dual approval) to reduce the default rates, and establishing an independent guarantee approval process to improve the efficiency of the overall CGS. Moreover, the government should play an active role in setting the agenda, ensuring coordination, providing support, and developing a market for guaranteed loans so that this market can attract international investment.

Levitsky (1997) indicates that CGS mechanisms need to ensure "additionality" in their operations. Additionality refers to the "additional loans made possible due to the guarantee against loss provided to the lender" (Levitsky 1997, 14). Thus, if the provision of guarantees creates additional loans for SMEs, CGSs and their costs are justifiable. On the other hand, if SMEs could access similar loan amounts without a guarantee mechanism, then the operations of CGSs would become questionable.

Saadani, Arvai, and Rocha (2010, 6) assert that the literature on CGSs converges on the principals of attractiveness, additionality, well-designed eligibility criteria, proper coverage ratios and fees, sound risk management, and efficient operational procedures. Furthermore, CGS outcome assessment should be based on the balance between three dimensions: outreach (the scale of the guarantee scheme), additionality (guarantees are extended to firms that are credit constrained), and financial sustainability (CGS activities are long term and not constrained by financial difficulties).

According to Beck, Demirgüç-Kunt, and Martinez-Peria (2008), credit guarantee mechanisms are the most effective government support programs for banks to increase SME lending instead of directed credit, interest, or regulatory subsidies. Beck, Klapper, and Mendoza (2010), in their analysis of credit guarantee funds, find that these mechanisms in developing and developed economies differ significantly in terms of their organizational structure, the role of the government and the private sector in the operations, and risk management and pricing mechanisms. Moreover, most of the funds do not utilize risk-based pricing or proper risk management practices to improve their operations.

Moral hazard is indicated as one of the most important challenges for the implementation of CGSs in several countries (Levitsky 1997). In addition, there is an expectation that the 100% coverage for the guarantee scheme observable in some countries will increase the moral hazard risk. As Levitsky underlines, in countries where the financial system is functioning much more efficiently and effectively, where risk management mechanisms are well developed, this may not constitute a major concern. Nevertheless, in countries where the financial system is not functioning well, where risk management practices are not properly utilized, this is a major risk for CGSs.

The literature above indicates crucial lessons for the Turkish KGF. First, the KGF should ensure sustainability, additionality, accountability, and efficiency in its operations. Secondly, for an innovative, technology-driven financing scheme, the KGF should ensure that it targets SMEs' specific needs and monitors the financing outcomes for continuous improvement. Lastly, the KGF should reduce the moral hazard risks both for the SMEs and for the financial sector. Otherwise, the KGF support may not yield a long-lasting impact on the Turkish economy.

Based on these findings, this study offers the following policy recommendations for the Turkish KGF under the headings of governance of operations and targeting SMEs for technology and innovation orientation.

Governance of KGF operations:

- To improve the KGF's coverage and effectiveness with an SME credit rating service and reduce the information asymmetry, the KGF needs to construct a rich, nationwide SME database. It can utilize the Turkish credit registry bureau for this purpose, and increasing collaboration and cooperation with the KOSGEB may yield better results in terms of reducing the knowledge gap regarding SMEs. Furthermore, proper risk management and diversification mechanisms can reduce moral hazard-related problems. In this respect, the Japanese case can offer lessons for Turkey (Kuwahara et al. 2015).
- There needs to be a mechanism for rating Turkish banks on their performance on KGF guarantees. This would enable banks to have different guarantee ratios based on their performance so that the KGF can avoid moral hazard and reduce the non-performing loans ratio (Yoshino and Taghizadeh-Hesary 2016). The case of the Japan Credit Guarantee Scheme can guide the Turkish KGF for this purpose.
- The KGF needs to take the additionality principle into consideration and to evaluate loan guarantees systematically for this purpose.
- The KGF should focus on ensuring the sustainability of its operations to be a long-term endeavor. The revival of the CGS in 2017 relies heavily on treasury-backed guarantees. The diversification of KGF funders and the participation of more private entities in its transactions would improve the sustainability of the assistance for SMEs. This would also relieve the treasury from the extra burden and ease the public finances. Correspondingly, the KGF can evolve into a more profit-oriented endeavor in the long term without limiting its operations.

Targeting SMEs for technology and innovation orientation

- Şener, Savrul, and Aydın (2014) contend that, while SMEs represent more than 99% of all the enterprises in Turkey, only 55% of them operate in value-added sectors. The structural features of the Turkish economy necessitate a higher technology-oriented CGS, which can improve the current account balance in the long term. A KGF mechanism that evaluates technology-oriented SMEs with scoring of multiple criteria would be helpful in this regard. The Republic of Korea has instituted the Technology Credit Guarantee Fund for this purpose, and its experience can shed light on the Turkish case (Sohn, Moon, and Kim 2005).

- Previous research suggests that credit guarantees have an important role in improving firms' ability to maintain their size and enhance their survival rate (Oh et al. 2009). Nevertheless, the same research shows that credit guarantees do not necessarily increase research and development spending, investment, and growth in productivity, and firms with lower productivity also receive guarantees. Thus, a consistent focus on enhancing guarantee systems for higher technology-oriented SMEs would be beneficial in ensuring long-term gains from the KGF measures. This may require the designing of specific guarantee products for technology-intensive companies.
- Sectoral and regional specialization in KGF activities, periodically monitoring firms with guarantees, and assessing CGSs in Turkey with key stakeholders would significantly improve the KGF's effectiveness in Turkey (Değirmenci 2011).
- The KGF should pay more attention to the evaluation of its guarantee program so that it can continuously improve its operations (Meyer and Nagarajan 1996). The evaluation process should consider several issues, such as whether the guarantees result in the expected outcomes and how the guarantee measures affect lender behavior and the financial system (Meyer and Nagarajan 1996, 14–15).

The recent revival of the KGF underlines that political willingness is critical to enhance SME financing in emerging economies. The Turkish experience further illustrates that public agencies, such as the KGF, should be more actively involved in easing access to finance for SMEs, especially in countries where banks dominate the financial system. Nevertheless, sustainability, additionality, accountability, and efficiency considerations should be at the heart of CGSs. For the Turkish economy to achieve sustainable, high productivity-enhancing growth with lower unemployment rates, the KGF should focus on tailoring its operations to spur high-technology investment, production, and increasing productivity levels for SMEs. This would not only justify the activities of the KGF but also improve its funding resources so that it can become an essential component of the economy policy in the long term.

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