

Turkey Urbanization Review

Financing Cities in Turkey

Issues and Options for Solutions

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Outline

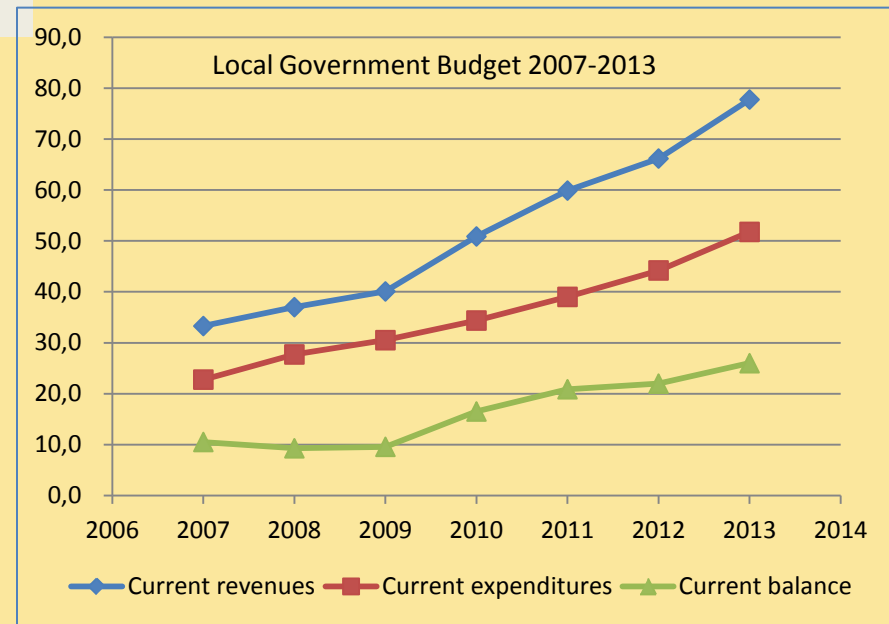
- The state of the LG sector
- Own-source revenues
- Development finance
- Municipal borrowing and debts



The State of the Local Government Sector

Budget situation

- Predictable transfers
- Robust current balance
- Strong debt financing, but substantial short-term debt
- Debt stock=121% of Total Revenues

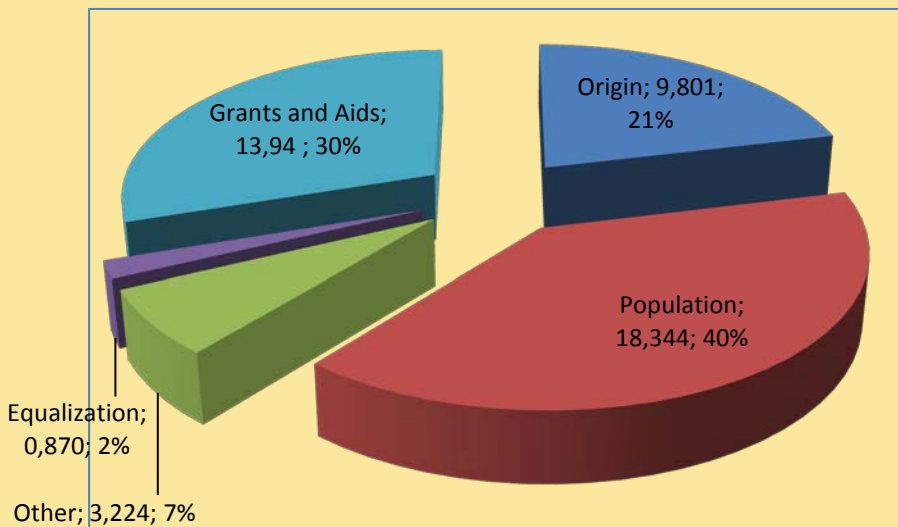


Budget Snapshot	2007	2008	2009	2010	2011	2012	2013
Current revenues	33.3	37.0	40.1	50.9	59.9	66.2	77.8
Current expenditures	22.8	27.7	30.5	34.4	39.0	44.2	51.8
Current balance	10.5	9.3	9.6	16.5	20.9	22.0	26.0
Non-recurrent Revenues	2.2	1.9	2.4	2.7	3.5	3.1	5.6
Capital Expenditures	16.6	18.2	17.7	17.9	22.0	25.1	35.8
Capital balance	(14.4)	(16.4)	(15.3)	(15.2)	(18.5)	(22.0)	(30.2)
Debt financing net	9.0	4.2	(6.9)	10.1	(0.9)	2.2	1.0
Balance total	5.0	(2.9)	(12.6)	11.5	1.5	2.2	(3.2)
Budget Total	39.4	45.9	48.2	52.2	61.0	69.3	87.6

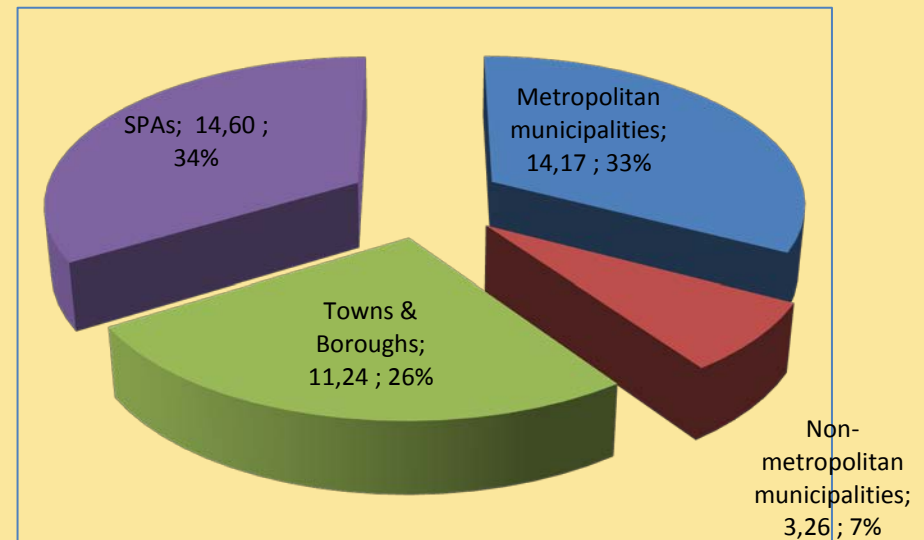
Intergovernmental transfers

- Predictable, buoyant transfers
- Transfer pool 11.5% of Central Budget tax revenues
- Transfer system supports urbanization;
- Moderate equalization of development disparity;

Allocation of transfers 2013 TRL bn. and %

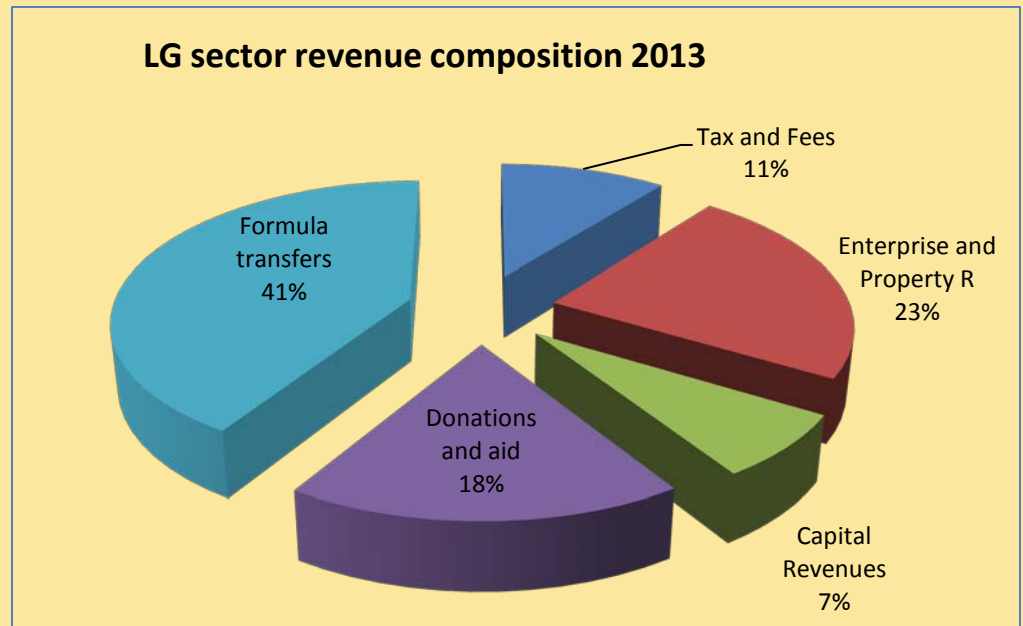


Share of LG entities in total transfers 2013 TRL bn.



LG Revenues

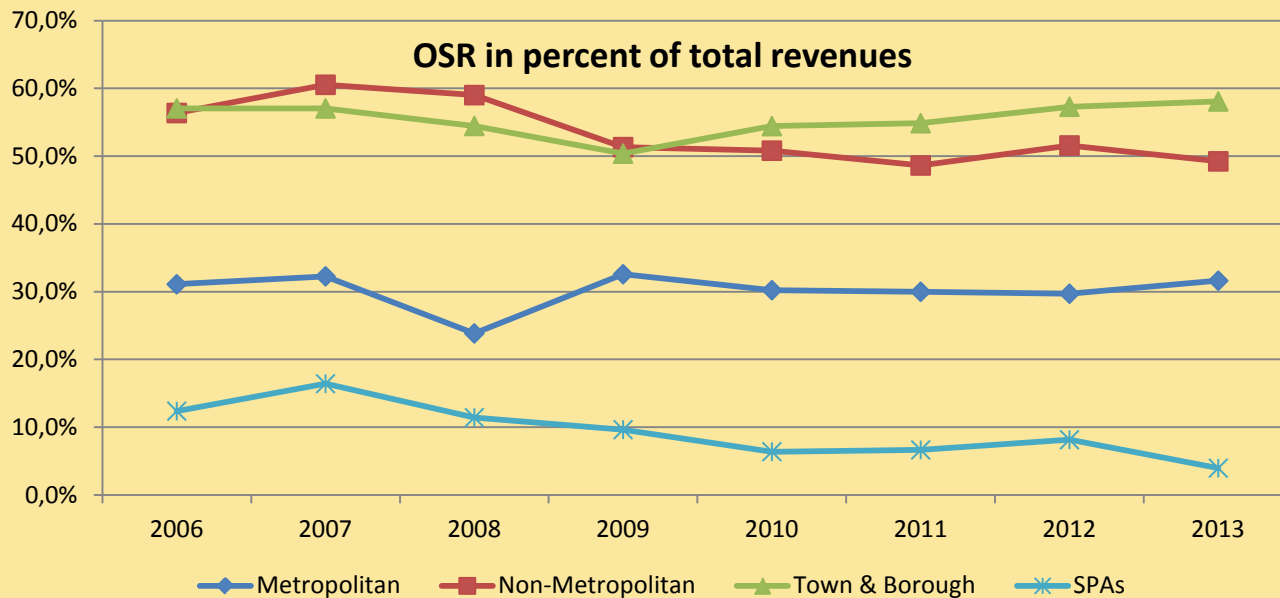
- Reliance on central government 2/3 of total
- Enterprise and property revenues largest in OSR
- Taxes and fees too small in international comparison
- MuEs impact OSR
 - Collect fees
 - Funds to from Ms.
- Rev Classification?
- Need more OSR!



Own-source Revenues

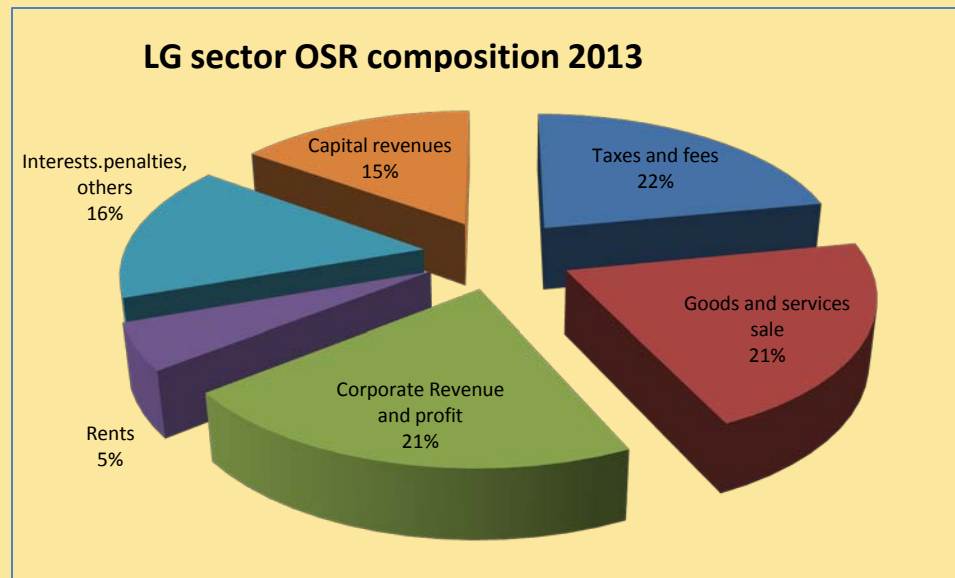
Own-Source Revenues in Declining Share

- Own-Source Revenues have not kept pace with transfers;
- Own-Source Revenues share is declining;
- Non-metro Municipalities and SPAs stronger decline



Own-Source Revenue Composition

- Enterprise and property revenues bulk of OSR
- Taxes and fees very small - 22% of OSR
- Interests and penalties nearly as large as taxes or fees each



Property taxes

- Low revenue in international comparison
- Low rate: 1‰ for land and residential buildings, 2‰ for other buildings, and 3‰ for empty plots;
- EU 10 times higher 1% for buildings + land,
- Developing countries around 3‰ - 5‰
- Underlying issues
 - Low collection efficiency?
 - Adequate valuation?
 - Adequate fiscal databases?

Gap in Incentives and Coordination

- Metropolitan Municipalities have no buoyant own revenues, towns collect property tax
- Disconnect between Metro planning, zoning, investments and Property tax revenues
- The largest investor (Metro Municipality) can't benefit from the investment impact => property tax;
- Property tax windfall revenue for towns in Metro Municipalities; and Property tax not used for supporting large metro level investments

Options for OSR Improvement

- Levy more local taxes:
 - Tourism tax,
 - Local Business tax;
 - Tax surcharge (e.g. small trade tax on VAT);
 - Motor vehicle tax (100% local);
- Improve coordination between Municipal entities
 - Increase property tax rate, expand base
 - Coordinate collection Metro Municipality level, tax developers at using-permit date
 - Share Property tax between Metro and Towns
- Land-based financing – DEVELOPMENT FEE
- Improve accounting, budget classification (consolidation) and cost control (fund accounting, cost centers)

Planning and Financing Development



Planning for Development

- Poor municipal records on long term vision and planning;
- Even some mega-projects seem ad-hoc
- Low coordination btw local bodies in metro jurisdictions
- Rolling Capital Improvement planning w adequate financing is rare/nil;
- Need to improve responding to local needs, community participation, development options

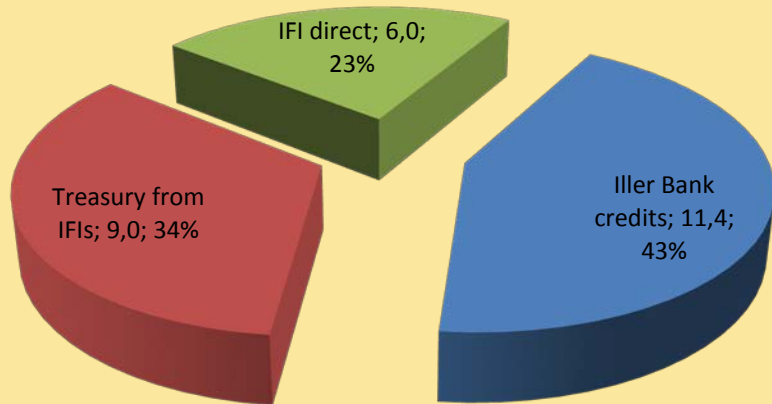
Development Finance

- Municipalities use Cash or Debt,
- Municipalities may use enterprises to incur debt
- Development grant only for SPAs;
- Large programs by central government agencies – unreported contribution
- Land-based financing underutilized;
- PPP underutilized

Financing sources and entities

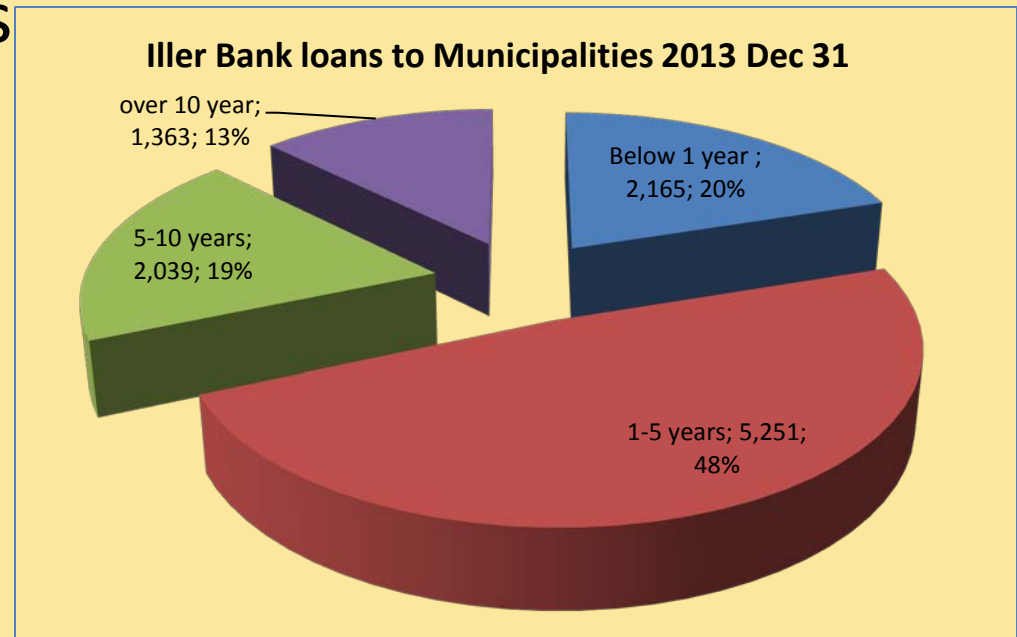
- Foreign funds and mega-projects dominate M investments and debt stock;
- Pressure on Treasury: $\frac{3}{4}$ of funds through or with Treasury guarantee;
- General obligation finance; Project finance rare
- Iller Bank is growing
- Local banks nil
- No domestic bonds for municipalities

Stock of infrastructure Debt 2013 TRL bn. and %



Iller Bank – Local Financier

- Local currency finance,
- Equity finance limits funding capacity
- Preferential rate (6% - well below market rate)
- Maturity term 5 years or less;
- Long term ¼ of loans
- Testing distribution of funds of foreign Agencies
- Options to expand



Options for Iller Bank

- Step over the equity financing
 - Test Project-based finance
 - Test Syndicate finance with domestic entities
 - Financial intermediary for medium and small Municipalities
 - Test bonds
- Need strengthening procedures;
- Need improving portfolio,
- Need insourcing some key capacities
 - appraisal, risk management, loan recovery,
 - business promotion, fund management
- Improve IT and capacity building

Land-based Financing

Land-based financing: procedures to generate funds for infrastructure from land related actions.

- **Selling** land strategically to generate revenues for infrastructure;
 - **Taxing** or charging to tap into private gains;
 - **Regulatory power:** charging against regulation
- Negligible revenue from land transactions** are in the budgets of Turkish municipalities;

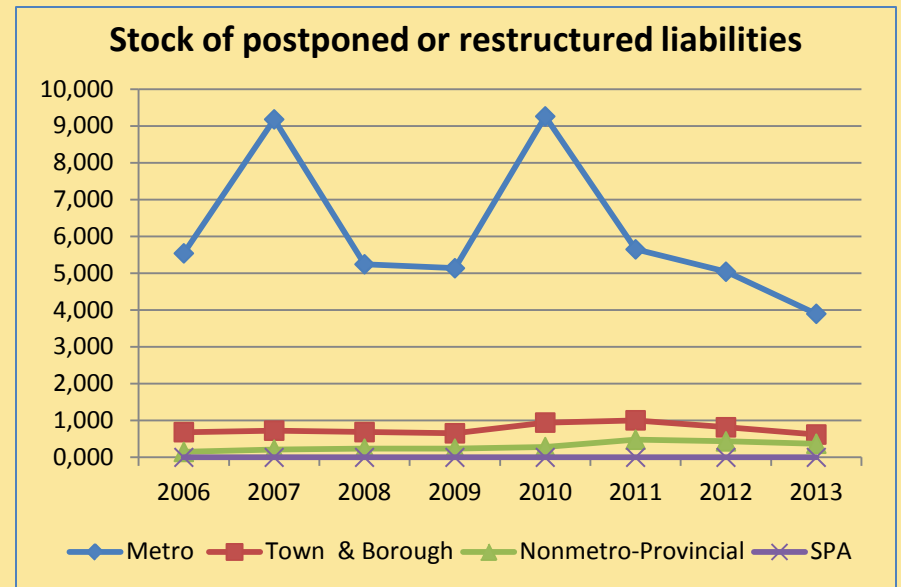
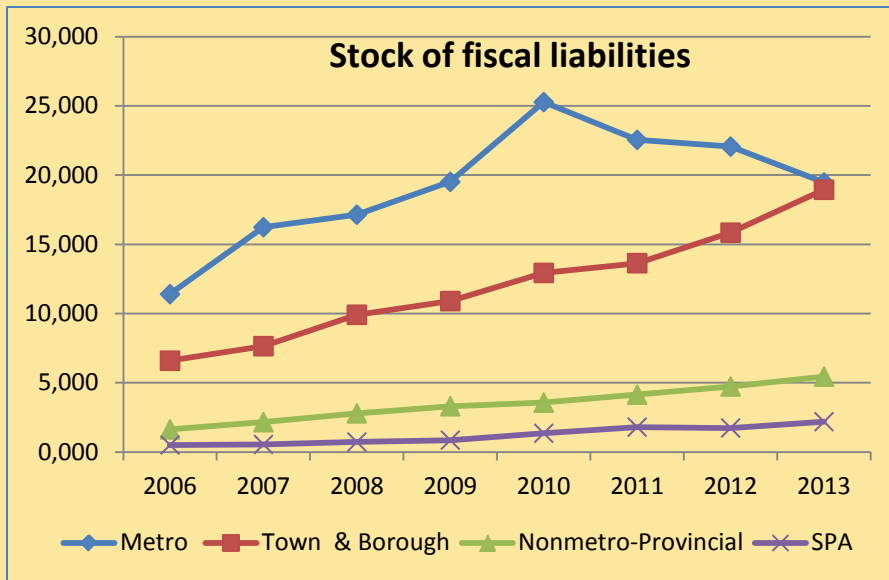
Municipal Borrowing and Debts

Debt financing

- Municipal debt financing 10% of Total budget;
- Great volatility
- Short maturity
- Debt stock is about 120% of Municipal sector budget total;
- Domestic capital or savings play no role in municipal development finance;
- Unclear debt transactions between Municipalities and affiliated entities (enterprises)

Debt snapshot

- The bulk of overdue or restructured debt is vs. the public entities
- Metropolitan Municipalities owe the bulk of restructured public debt;
- Bulk of fiscal liabilities are non-bank debt



Options for improvement

- Reducing short-term Municipal liabilities,
- Build fiscal space for long-term borrowing
- Improve accounting and budget classification,
- Introduce rolling CIP and borrow strategically
- Boost funding and borrowing capacity by increasing OSR and
- Use Land-based financing instruments incl. PPP for boosting funding infrastructure