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Export Losses in the EU Market

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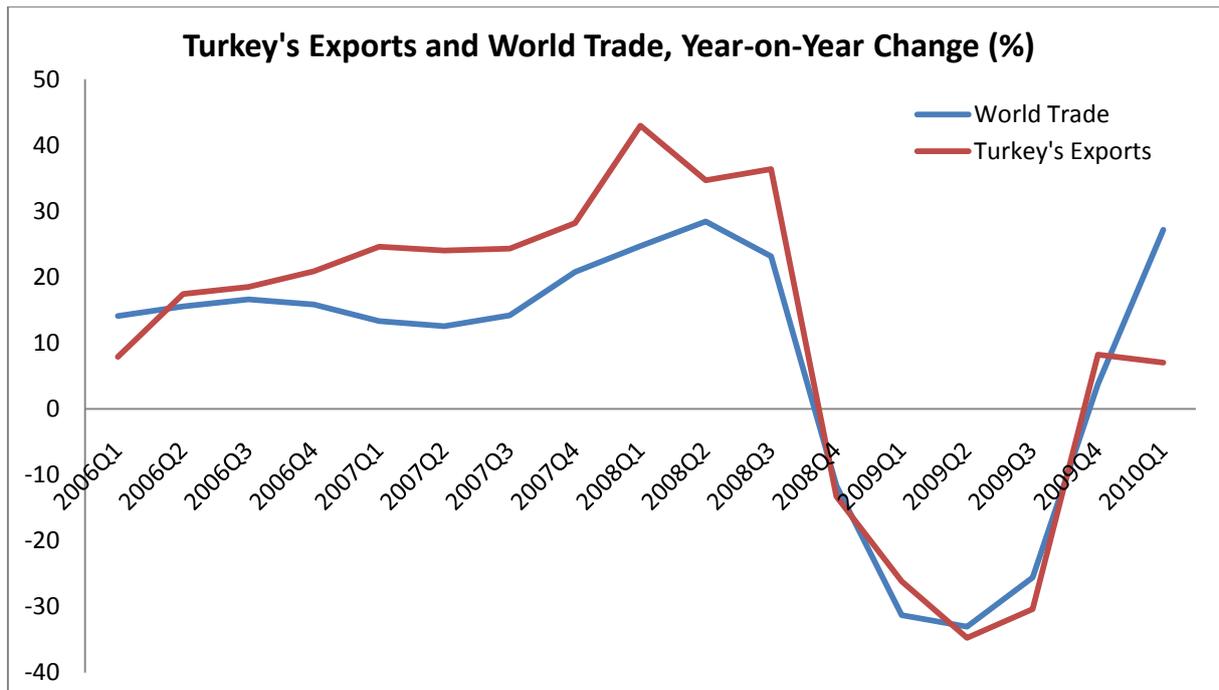
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2008 global crisis had a deep impact on Turkey's export performance and several problems including the problem of export finance, due to the lack of a comprehensive national export strategy, left Turkey behind the world in the process of recovery from the crisis. Figure 1 shows the year-on-year change in total exports of Turkey and the world. According to this, in October 2008 – September 2009 period, Turkey's and world's exports contracted year-on-year by 26 and 27 percent respectively. Another point as striking as the parallel contraction in exports over the crisis period is that Turkey failed to accompany the rest of the world in the recovery in exports that came to place as of the last quarter of 2009. In this period, world exports elevated by 27 percent whereas exports of Turkey rose only by 7 percent.

Figure 1. Turkey's Exports and World Trade, Year-on-Year Change (%), 2006-2010



Source: World Trade Organization (WTO)

The main reason for this divergence can be seen as the fact that European Union (EU) which receives almost 50 percent of Turkey's exports constituted the region that was most severely affected by the crisis. It is of great importance to identify whether the export losses encountered in the EU market stems only from the temporary impacts of the crisis or turns to be permanent in order to design successful export strategies.

This policy note analyzes the exports of Turkey to the EU before and after the crisis with this perspective. In order to eliminate the impact of the crisis, the period between April 2008 and September 2009 representing the period where the crisis was felt most severely was left out of the analysis and the pre-crisis and post-crisis periods were set as October 2007 – March 2008 and October 2009 – March 2010, respectively.

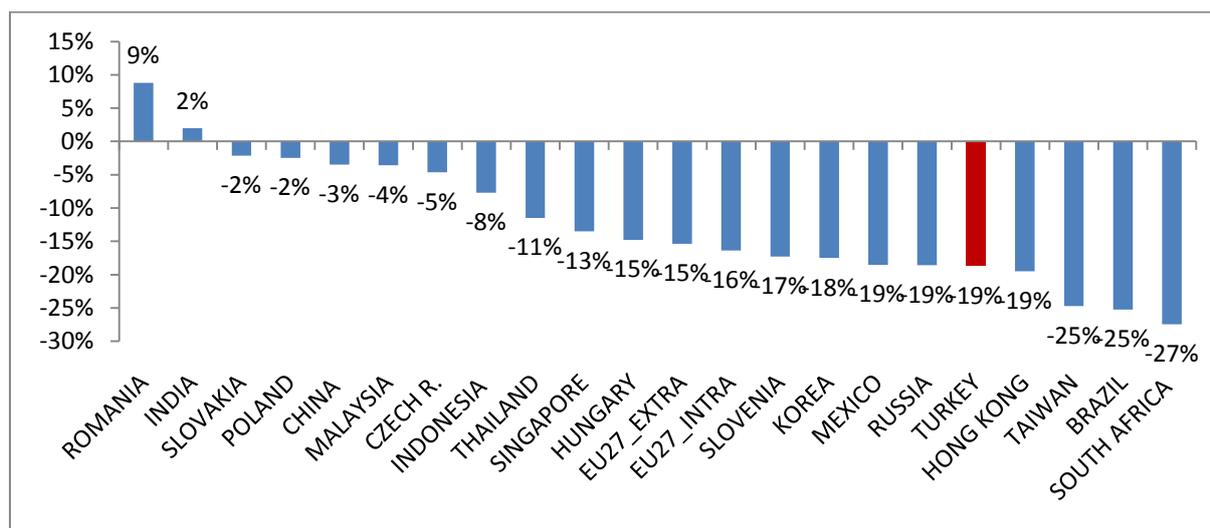
Composition of Turkey's total exports

One important point to note before examining market shares is the regional composition of exports in which the share of the EU dropped from 48 to 46 percent while that of Middle East, Asia and North Africa increased from 2008 to 2009. A reason for this change is that the share of the EU market dropped in general in the world trade as well as the efforts of Turkey's government to diversify export markets as a response to the contraction in the EU market. Another factor which does not get the deserved attention is that multinational firms or domestic firms doing business with multinational firms alter their specialization strategies shifting their production away from EU market. In this respect, it can be concluded that a shift of axis away from EU market to other markets occurred in consequence of corporate strategies redefined during the globalization process.

Change in Turkey's share in exports to the EU market

Figure 2 compares the export data for developing countries which are top twenty exporters to the EU¹. According to this, one striking point is that between October 2009 and March 2010, no countries but Romania and India improved their exports to EU back to the pre-crisis levels. Exports of non-EU countries and exports of EU countries to EU market stand 15 percent and 16 percent below those for the said period, respectively. On the other hand, Turkey's exports to the EU market stood 19 percent below the pre-crisis level, implying that Turkey performed worse than the other two regions mentioned. Furthermore, all new members of the EU (EU-12 countries) recovered more rapidly than Turkey.

Figure 2. Change in Exports to the EU (%), October 2009-March 2010, Comp. to Pre-crisis Period²



Source: Eurostat

¹ Given the fact that only 2% of Turkey's exports to the EU market are energy exports, these twenty countries are ranked according to their non-energy exports to the EU.

² For the elimination of the seasonal effects, exports in October 2009-March 2010 period were compared with October 2007-March 2008 as the pre-crisis period.

Exports to EU and Market Shares: Is There a Shift of Axis?

Table 1 shows the total exports to EU and market shares. The table suggests that, excluding energy, Turkey ranks the fifth following China, Poland, Czech Republic and Hungary, and that Turkey suffers the second highest drop in exports following Russia. As the table also reveals, shares of non-member countries improve and the share of the trade across EU countries falls down. Among these non-member countries, China and India in particular demonstrate an impressive performance while Malaysia, Indonesia, Thailand and Singapore also appear to have increased their market share. Another important result to underline is that new member countries to the EU accomplished to increase their shares in the EU market. Apart from Poland, Czech Republic and Hungary, which have a higher volume of exports to the EU than Turkey, Slovakia and Romania enjoyed an increase in their market share closing the gap between their exports and Turkey's exports. The mentioned significant change in EU's trade composition might imply a short-term post-crisis outlook as well as a long term shift of axis.

Table 1. Exports to the EU and Shares in the EU Market for Selected Countries

	October 2007-March 2008		October 2009-March 2010		Change	
	Exports (billion €)	Market Share	Exports (billion €)	Market Share	Exports (billion €)	Market Share
CHINA	120.9	5.72%	116.7	6.58%	-4.2	0.86%
POLAND	41.2	1.95%	40.2	2.26%	-1.0	0.31%
NON-EU 27	758.7	35.92%	642.3	36.20%	-116.5	0.29%
CZECH REP.	38.3	1.81%	36.5	2.06%	-1.8	0.25%
INDIA	13.9	0.66%	14.2	0.80%	0.3	0.14%
SLOVAKIA	17.4	0.82%	17.0	0.96%	-0.4	0.14%
ROMANIA	9.6	0.46%	10.5	0.59%	0.8	0.13%
MALAYSIA	8.8	0.42%	8.5	0.48%	-0.3	0.06%
INDONESIA	6.4	0.30%	5.9	0.33%	-0.5	0.03%
THAILAND	8.7	0.41%	7.7	0.43%	-1.0	0.02%
HUNGARY	27.3	1.29%	23.3	1.31%	-4.0	0.02%
SINGAPORE	9.0	0.42%	7.8	0.44%	-1.2	0.01%
HONG KONG	5.9	0.28%	4.8	0.27%	-1.2	-0.01%
KOREA	20.3	0.96%	16.7	0.94%	-3.5	-0.02%
TURKEY	24.1	1.14%	19.6	1.10%	-4.5	-0.04%
TAIWAN	13.0	0.62%	9.8	0.55%	-3.2	-0.06%
RUSSIA	83.7	3.96%	68.1	3.84%	-15.6	-0.12%
EU 27	1353.7	64.08%	1132.0	63.81%	-221.8	-0.27%
Total	2112.5	100.00%	1774.0	100.00%	-338.5	-----

Source: Eurostat

Turkey's Export Performance by Sectors

Five sectors that have at least a 5% share in Turkey's total exports to the EU market constitute 60% of Turkey's total exports to EU. Table 2 shows the total export volume of these sectors.

Table 2. Five Sectors with the Largest Volume of Exports to the EU Market in 2009³

Sector Code (SITC Rev. 3)	Sector Definition	Exports (billion \$)		Share of the Sector in the Exports to the EU	
		2007	2009	2007	2009
84	Articles of apparel and clothing accessories	11.3	9.4	18%	20%
78	Road vehicles (including air-cushion vehicles)	12.5	9.2	20%	19%
65	Textile yarn, fabrics, made-up articles, n.e.s., and related products	4.9	3.9	8%	8%
77	Electrical machinery, apparatus and appliances, n.e.s., and electrical parts thereof	3.5	3.3	6%	7%
05	Vegetables and fruit	3.0	2.9	5%	6%

Source: UN Comtrade

Articles of apparel and clothing accessories

Annexed Figure 1 compares the change in exports of the 15 developing countries that have highest volume of exports to the EU in articles of apparel and clothing accessories sector. According to this, Poland, China, Bangladesh, Sri Lanka and India increased their exports compared to the pre-crisis period (October 2007-March 2008) whereas Turkey's exports dropped by 17% compared to the period before the crisis. Concerning the market shares, it is seen that the total market share of non-EU countries and predominantly China, Bangladesh and India, the biggest rivals of Turkey in this sector, increased while Turkey appears to be one of the most severely affected countries. Fall of competitiveness in this sector, as has been voiced for long, coupled with the problems such as the difficulties in export finance, gave way to an unfavorable outlook that can potentially prove to be a long term problem.⁴

Road vehicles (including air-cushion vehicles)

Turkey, which ranks the third among developing countries in exports of road vehicles sector following Czech Republic and Poland, faced a €1.2 billion reduction in exports, ending to be the country facing the biggest loss in this sector. Annexed Figure 2 indicates that in October 2009 – March 2010 period four

³ The share of the iron and steel sector, which was the fourth in terms of the sectors with highest exports to the EU in 2007, dropped from 6% in 2007 to 3% in 2009 and the sector fell down to the 5th rank getting out of the first five sectors. Therefore, the sector was not involved in the analysis.

⁴ For the impact of foreign trade finance in the fall in exports, please see Policy Note by Sarp Kalkan, Hasan Çağlayan Dündar and Ayşegül Dinççağ, May 2010.

countries – India, Romania, South Africa and Taiwan – achieved the pre-crisis levels in exports whereas Turkey stands 23% below the level achieved before the crisis. Even though the loss of exports to the new EU member countries and Asian countries create the impression that there exists structural problems, the reason for the sharp contraction in exports in this sector must be searched in the fact that incentive policies for passenger cars applied by the EU were not applicable for commercial type vehicles that Turkey's production concentrated on and that the commercial vehicle sector narrowed more rapidly due to the investments coming to a halt in the crisis period.

Textile products

As Annexed Figure 3 indicates, Turkey ranks the second among developing countries in terms of textile exports to the EU, following China. Nonetheless, Turkey is the country that faced the biggest drops in exports as a result of the crisis (by €300 million). In this respect, it is unfavorable that the gap not only between the sector leader China and Turkey but also between India and Pakistan widened. In parallel with the export losses in the apparel sector, the reductions in this sector also seem to have a permanent character.

Electrical machinery, apparatus and appliances, n.e.s., and electrical parts thereof

Electrical machinery sector is the only main export item for which the pre-crisis export level was re-achieved. Nonetheless, in this sector Malaysia, Korea and Romania, rivals of Turkey in the sector in terms of quantity and market share, demonstrated a better performance than Turkey. As Annexed Figure 4 shows, reduction in exports between EU countries and the significant increase in the share of Asian countries are striking.

The Usual Suspect: Exchange Rate

The argument that Turkish lira is too valuable that it affects foreign trade balances adversely is frequently voiced nowadays. It is highlighted that higher labor costs compared to Asian countries and appreciation of the lira play the most significant role in the contraction in exports. With this perspective, analyzing the exchange rate dynamics for countries which increased exports to EU and improved share in the EU market in the post-crisis period can furnish us with more concrete information on export-exchange rate correlation.

Turkish lira depreciated in real terms against other currencies from the last quarter of 2008 to the first quarter of 2009. Despite the appreciation in the following periods, TL could not yet achieve the pre-crisis value. Considering the real exchange rates for Asian countries which succeeded an increase in market share in exports to the EU in the period after the crisis, it is seen that currencies of China, Indonesia and Singapore appreciated in the recent period whereas currencies of Taiwan and Korea, which faced fall in exports and loss of market share, depreciated. Only the change in the value of the currency of India depreciated in a direction supporting the above argument⁵.

5 Similar results are obtained when nominal exchange rates against € is used instead of real effective exchange rates.

Table 3. Change in Real Effective Exchange Rate Index, October 2009-March 2010, Compared to Pre-crisis Period⁶

Country	Appreciation of real exchange rate
Indonesia	7%
China	7%
Singapore	3%
India	-5%
Taiwan	-5%
Turkey	-6%
Korea	-18%

Therefore, the argument that exchange rate dynamics had an effect on the exports to the EU is not supported for the period covering the pre- and post-crisis episodes. That Turkey, Taiwan and Korea, the currencies of which depreciated, faced reductions in market share while China, Indonesia and Singapore increased their market share despite the appreciation of their currencies implies that export performance is also affected by structural factors other than exchange rate dynamics. This indicates, measures focusing not only on exchange rate policy must be devised to tackle the export losses.

Results

This policy note examines the determinants of the limited recovery in exports to the EU in the post-crisis period on the basis of market shares and sectors. Results can be summarized as follows:

- EU market goes through a 'shift of axis': With the commencement of the recovery from the crisis, the share of EU's imports from non-EU countries increased whereas the share of imports from member countries diminished. However, Turkey failed to make use of this opportunity. While this change in the trade composition of the EU, which still suffers the negative impacts of the crisis, might imply a flight from quality in the short term, it might highlight a structural transformation in the long term⁷. This issue, which is of significant importance for Turkey's exports to the EU, necessitates further analysis.
- Non-EU countries that achieved highest increase in their market shares in the EU are Asian countries including China, India, Malaysia, and Indonesia. It is striking that new member EU countries (EU-12 countries) also increased their shares in the EU market.
- Apart from some exceptions, Turkey lost market share to Asian countries in labor-intensive apparel and textiles industry and to new member EU countries in more capital-intensive motor vehicles exports. Thus, Turkey competes with different regions in different sectors. On the other

⁶ For the elimination of the seasonal effects, exports in October 2009-March 2010 period were compared with October 2007-March 2008 as the pre-crisis period.

⁷ Flight from quality can be defined as the tendency of countries to direct their import demand to cheaper countries and thus to increase their demand to low-quality products of Asian economies relying on cheap labor.

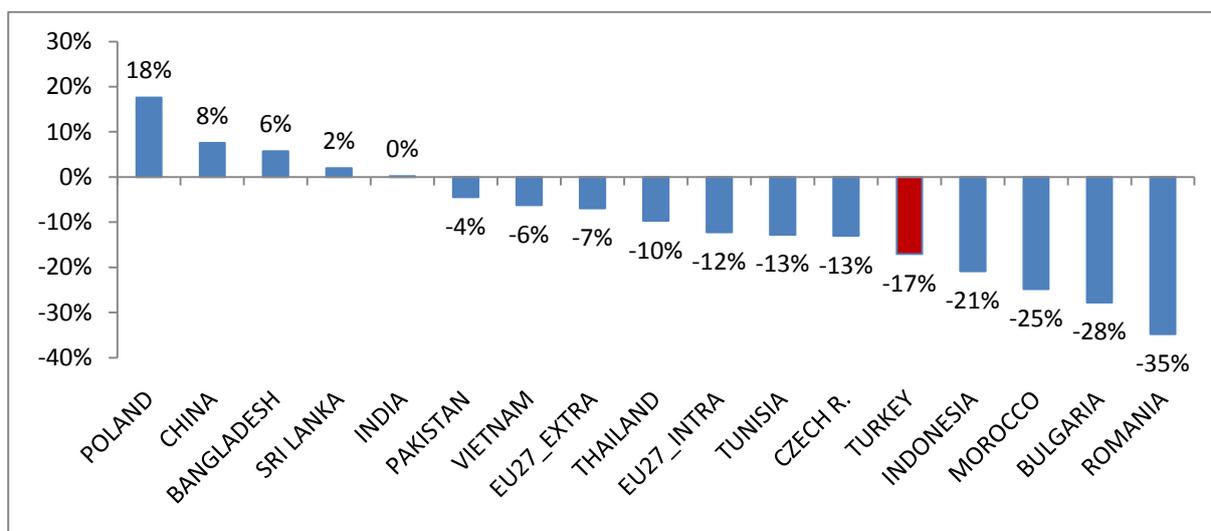
hand, it should be noted that commercial vehicles, which constitute a significant part of Turkey's road vehicles exports, were excluded from the scope of incentives by the EU and that the tightening of investments had a greater impact on commercial vehicles segment.

- A number of Asian countries which achieved a rise in their share in the EU market as well as in volume of exports to the EU achieved these despite the appreciation of the currency. Furthermore, Turkey as well as Korea and Taiwan faced tightening of market shares despite depreciation of domestic currencies. These imply that export losses in the EU market cannot be explained solely by the exchange rate effect and that other structural factors also play a role in this process.
- Market share was lost to emerging Asian economies relying on cheap labor in labor-intensive sectors and to new EU member countries (EU 12) including Poland, Czech Republic, Slovakia, Romania and Hungary in capital-intensive sectors. The losses in the capital-intensive sectors also stem from the recent shift of foreign direct investments from Turkey towards EU-12 countries. The reasons for the losses in all sectors must be analyzed cautiously and long term industrial and export policies accordingly devised must be implemented.
- Another reason for export losses is the problems with respect to trade finance. In order to eliminate these, Eximbank and private banks must increase the credit facilities extended to exporters and eligibility conditions must be loosened taking into account that the impacts of the crisis have eased.
- Finally, the mentioned market share losses can also result from domestic firms setting new specialization strategies in the process of globalization. In this context, domestic firms within the business web of multinational firms might have increased their activities in the markets other than the EU which could have led to a shift of axis in foreign trade. Therefore, it would be of great importance to conduct a 'value chain' analysis that also accounts for this argument in order to design the correct policies.

While world trade recovers after the crisis, Turkey faces considerable losses in the most important export market, which signals a significant problem. In order for the losses in the European Union market not to be persistent in the long term, structural problems in the market must be analyzed keenly and a well-designed and effective export strategy must be put into practice. In addition, this strategy must also solve the problems pertaining to trade finance by reviewing the export support system. The shift of European Union's export demand toward non-EU member countries along with the recovery from the global crisis should be considered as an opportunity for Turkey and efficient and correct policies must be put into force immediately in order to seize this opportunity.

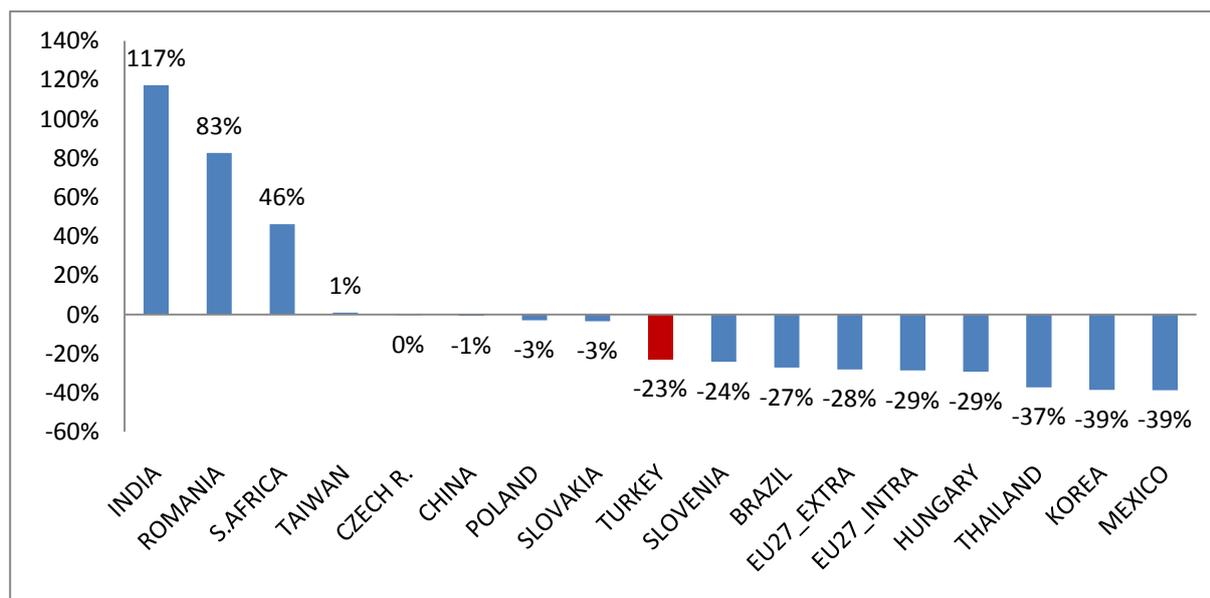
ANNEX: Comparison of pre- and post-crisis changes in export performance in export oriented sectors

Figure 1. Change in Exports to EU in “Articles of Apparel and Clothing Accessories”, October 2009-March 2010, Compared to the pre-crisis Period⁸



Source: Eurostat

Figure 2. Change in Exports to EU in “Road Vehicles” Sector, October 2009-March 2010, Compared to the pre-crisis Period⁹

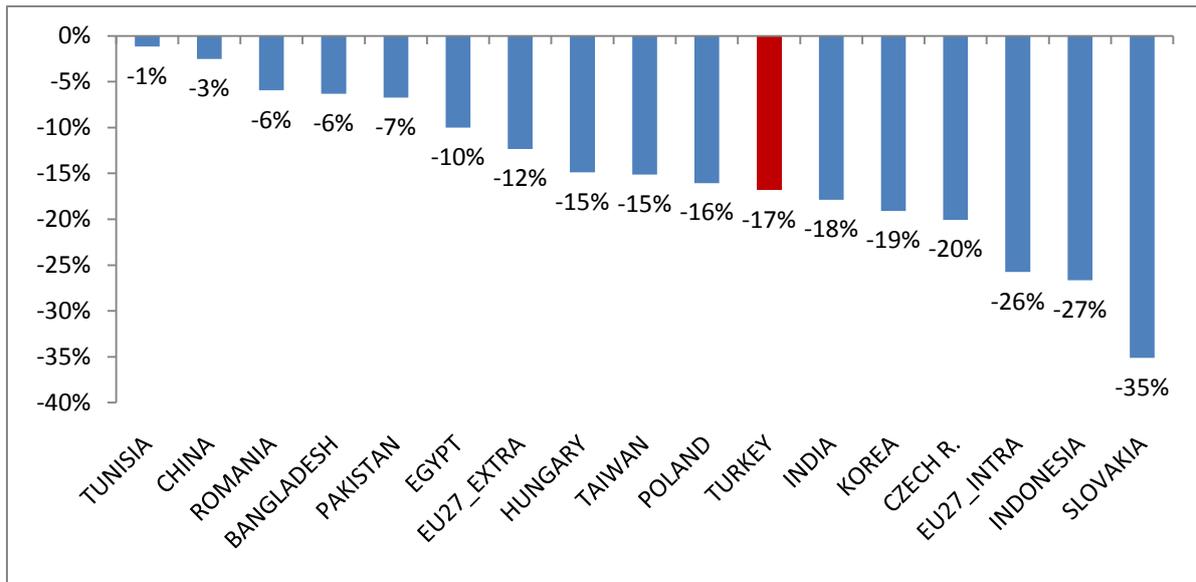


Source: Eurostat

⁸ For the elimination of the seasonal effects, exports in October 2009-March 2010 period were compared with October 2007-March 2008 as the pre-crisis period.

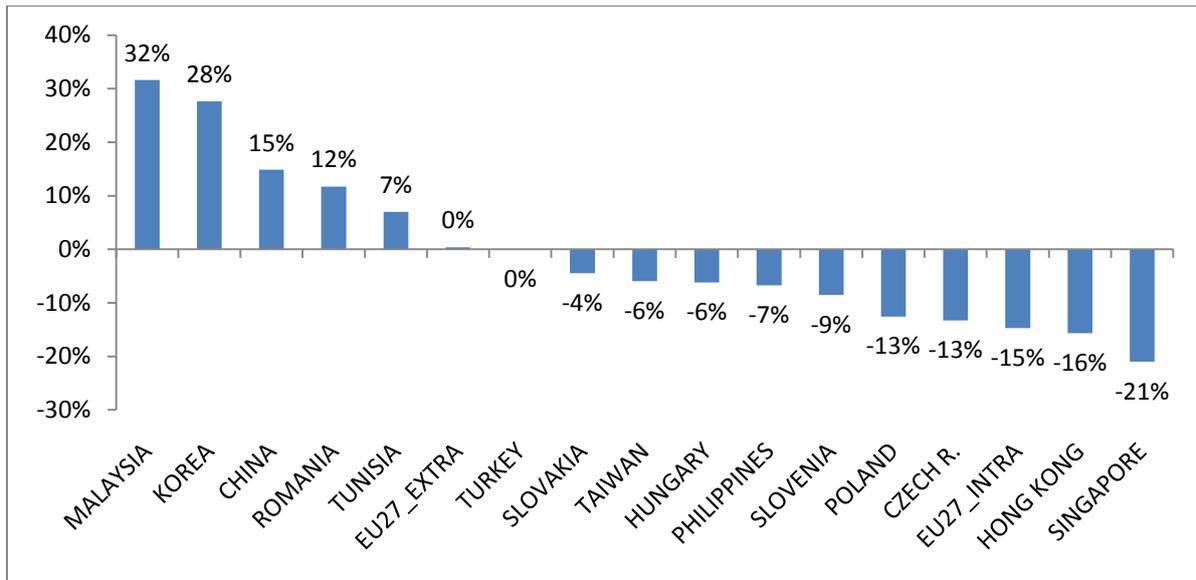
⁹ For the elimination of the seasonal effects, exports in October 2009-March 2010 period were compared with October 2007-March 2008 as the pre-crisis period.

Figure 3. Change in Exports to EU in “Textile Products” Sector, October 2009-March 2010, Compared to the pre-crisis Period¹⁰



Source: Eurostat

Figure 4. Change in Exports to EU in “Electrical Machinery and Apparatus” Sector, October 2009-March 2010, Compared to the pre-crisis Period¹¹



Source: Eurostat

¹⁰ For the elimination of the seasonal effects, exports in October 2009-March 2010 period were compared with October 2007-March 2008 as the pre-crisis period.

¹¹ For the elimination of the seasonal effects, exports in October 2009-March 2010 period were compared with October 2007-March 2008 as the pre-crisis period.