

tepav

Economic Policy Research Foundation of Turkey

Turkey's structural transformation and prospects after the Referendum & Role of TEPAV

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Framework

- What does TEPAV do?
- A few words about the referendum results
- Turkey's structural transformation
- EU and the transformation of Turkish economy
- How can Turkey get out of the middle-income country trap?
- Any low hanging fruits?

What is TEPAV?

- A private, nonpartisan, nonprofit think tank devoted to independent research
- Founded in December 2004 by the five year trust fund donation of The Union of Chambers and Commodity Exchanges of Turkey (TOBB)
- Board of trustees comprised of TOBB representatives and experts

TEPAV's comparative advantage

■ Knowledge production

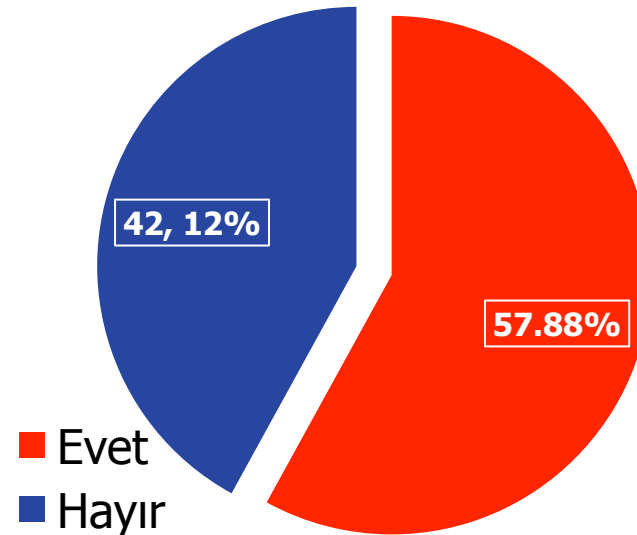
- A strong in-house research capacity
- Network with academics and experts
- Strong ties with the international organizations (The World Bank, OECD, The Brookings Institute etc)

■ Knowledge distribution

- Close contact with TOBB's grassroots organizations (364 chambers all around Turkey)
- Network with the public administration (Former and prominent technocrats among TEPAV staff)
- Strong impact on the media (daily columns, press releases and briefings)

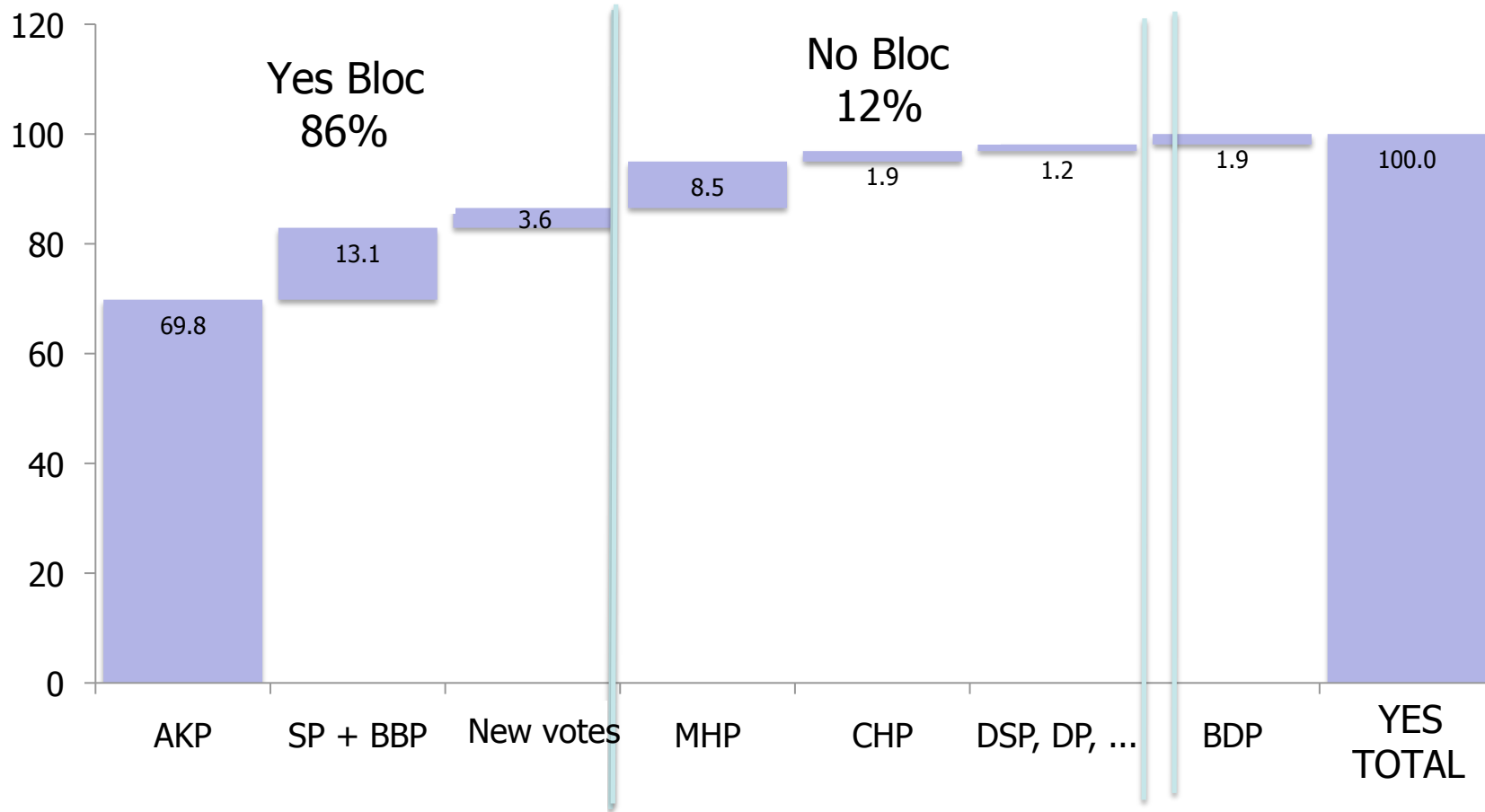
■ Strong and diversified financial resources to sustain activities

Referendum results: 3 million voters seem to have switched from one side to another....



	# of Registered Voters	# of Voters Participated	Yes Votes	No Votes	Turnout Rate (%)
Referendum (2010)	52,051,828	38,368,995 ↓	21,788,267 ↑	15,855,279 ↓	73.71 % ↓
Provincial Council Elections (2009)	48,049,446	40,932,260	Yes Bloc Total	No Bloc Total	85.19 %
			18,445,566	18,244,439	

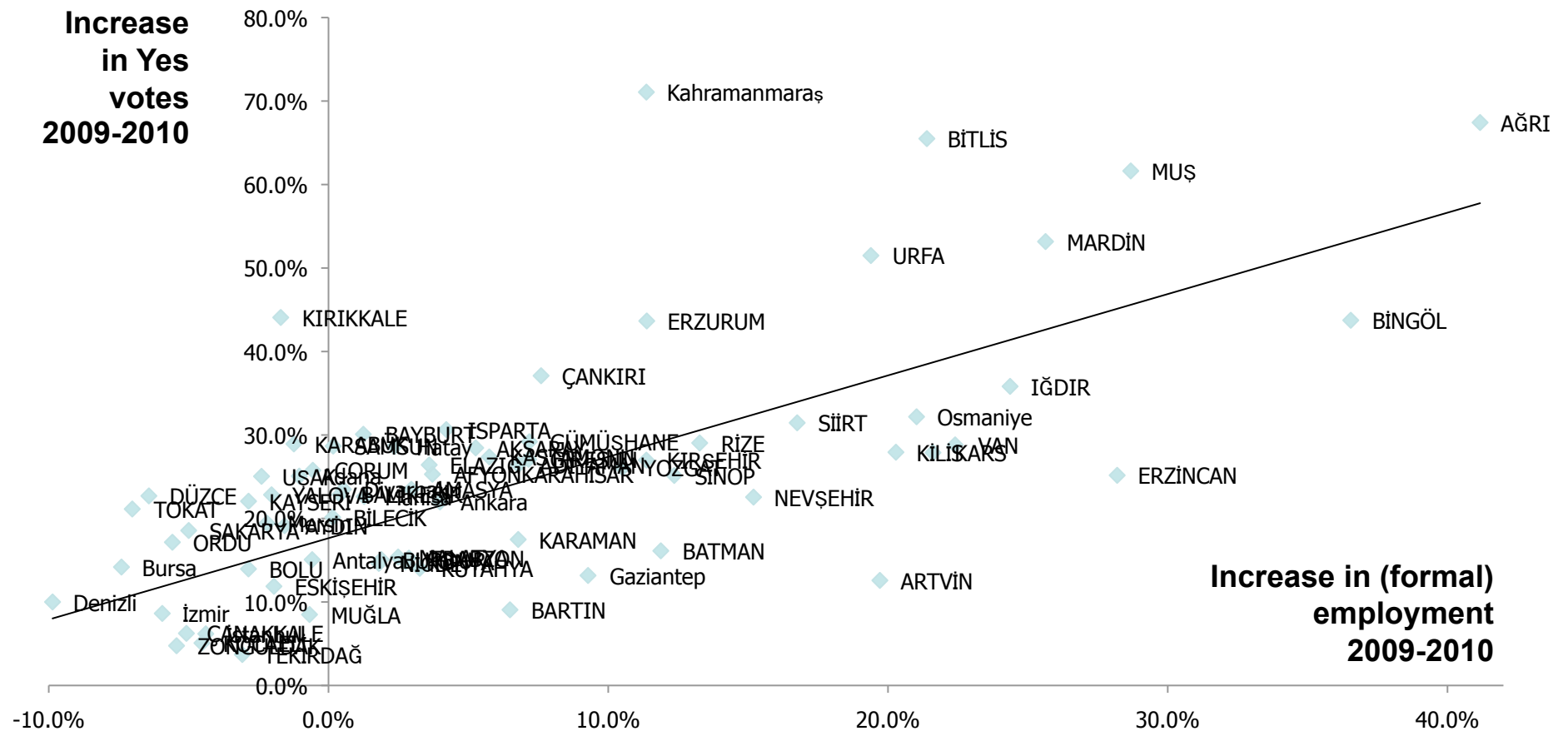
Where did the yes votes come from?



Party voted for in the 2009 Provincial Council Elections

Source: Calculations based on Supreme Election (YSK) Council and A&G data

Economic activity is one of the determinants of Yes votes



After the referendum

- Risk of political uncertainty decreases:
 - AKP seems to create a new 50+ percent voter base with the referendum coalition.
 - The process must be read out politically:
 - Political is due to a large voter not due to the 10% threshold
 - 2011 general elections/2012 presidential elections/2014 local elections
 - Possible debates on a constitution centered around presidential system
 - A parliament with two and a half parties possible for 2011.
- Political stability does not necessarily bring policy stability
 - No nominal anchor: No fiscal rule no IMF
 - Elections almost every year

An overview of the recent progress of Turkish economy

	1980	2008
Number of companies	90,000	640,000
GDP (billion \$)	70	700
Per capita GDP (USD)	1,500	9,000
Exports (USD billion)	3	132
Exports per worker (USD)	65	1,800
Industry share in exports	10%	92%
Number of exporters	1,000	47,000
Tourism revenue (billion \$)	0,3	21
Ranking in the world (in terms of GDP)	25th	17th

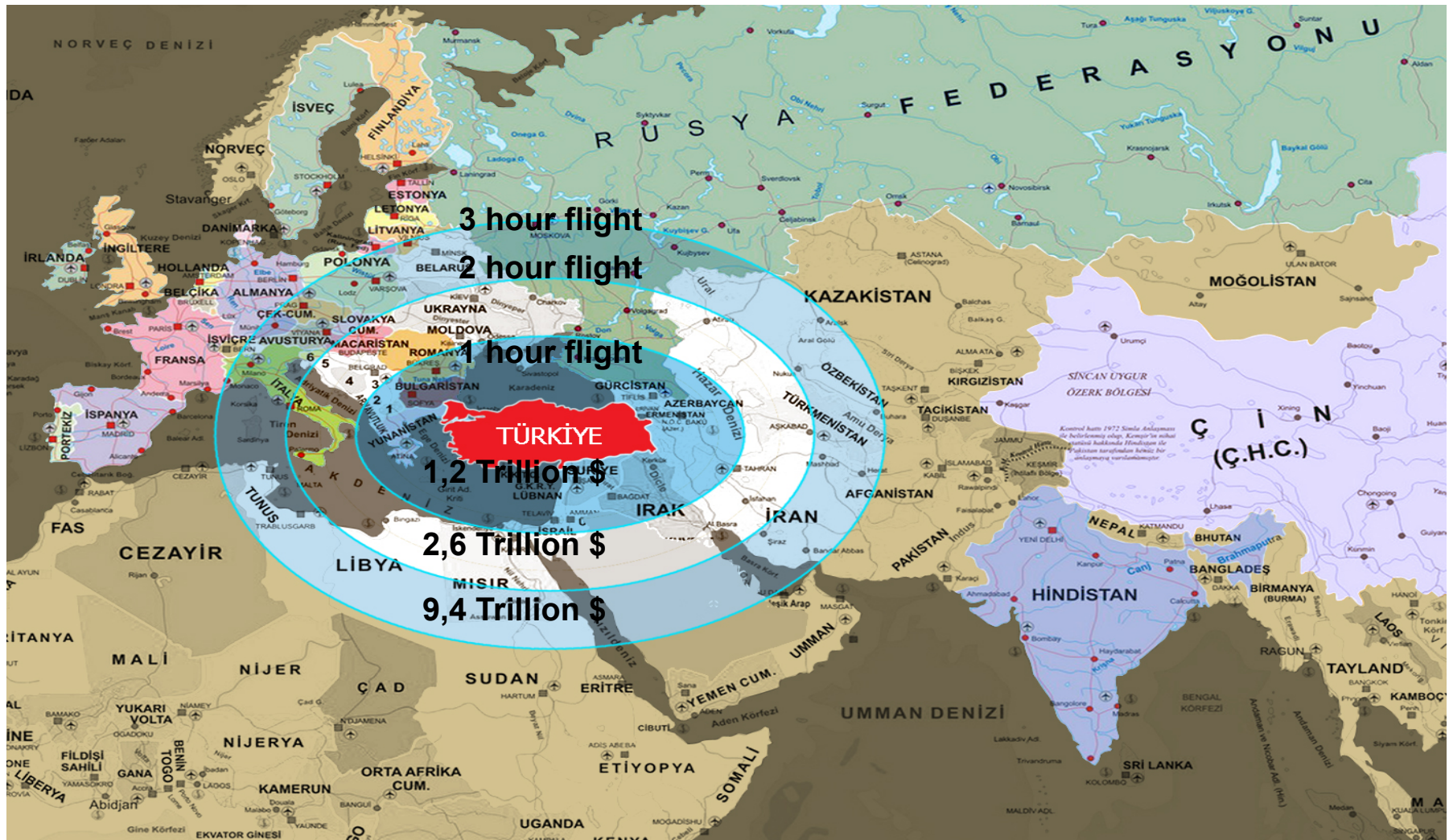
It is a process of total transformation:

- **Mass urbanization**
 - Migration from rural to urban areas
 - Reversal of 75 to 25 percent distribution
- **Proliferation of industry in Anatolia**
 - Gaziantep, Denizli, Konya, Kayseri, Kahramanmaraş
- **Organised industrial zones experience**
 - Gebze as the manufacturing base of Istanbul
- **Transformation in retail sector**
 - Shopping malls and new urban life
 - **IKEA in 3 cities**
- **An Unintended consequence: Political transformation**
 - Periphery comes to the center

Emergence of a new middle class

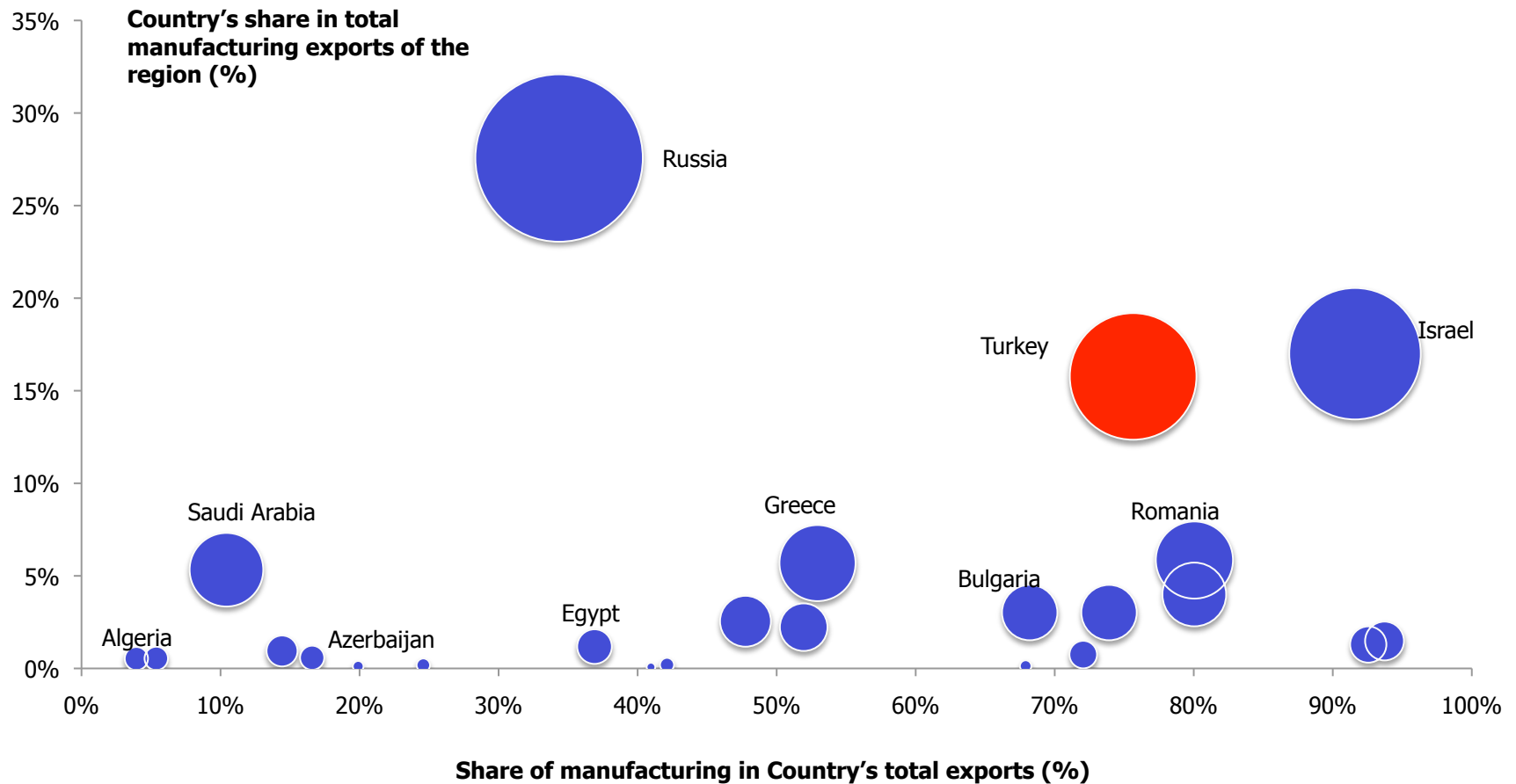
	1999	2003	2006	2008
Automobile Sales (in thousands)	-	359	622	494
White Good Sales (in millions)	4	3	5.5	5.2
Airline Passengers (in millions)	30	34	59	75
Mobile Phone Network Subscribers (in millions) (Swedish investments in Turkcell)	-	26.6	51.4	64
# of People Getting House Loans (thousands)	14	43	268	237
Consumer Credit + Credit Cards (billion TL)	-	12.8	67.7	114

Turkey's global storyline: An investment hub and a logistics center for 1 billion people between EU and China



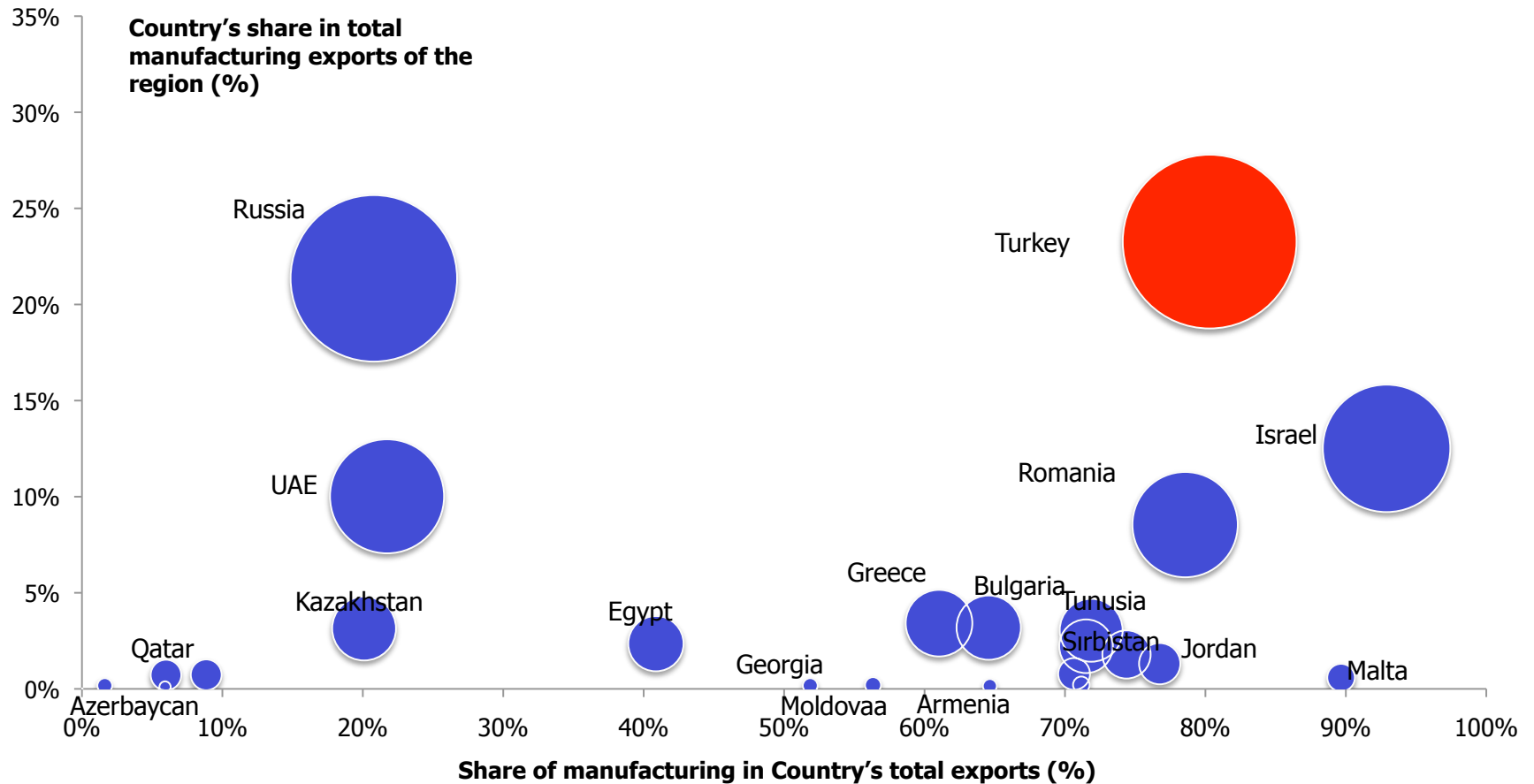
Rapid growth in manufacturing after mid-90's

Export indicators of the countries in the region (1996)

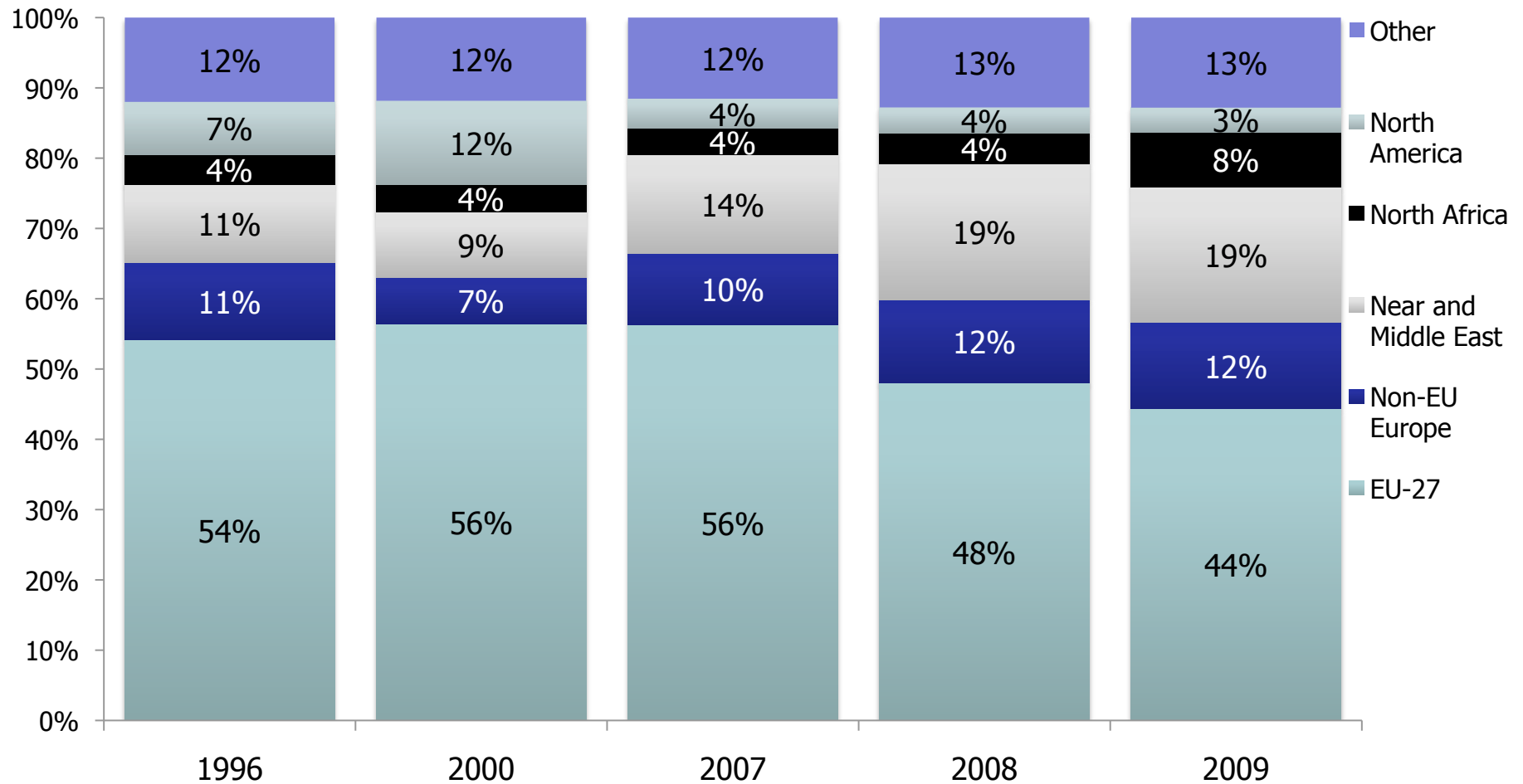


Today Turkey is the largest manufacturer in the region

Export indicators of the countries in the region (2008)



Geographic composition of Turkey's exports: EU-Turkey Customs Union brings Turkey closer to her region



The Ankara Forum and TEPAV

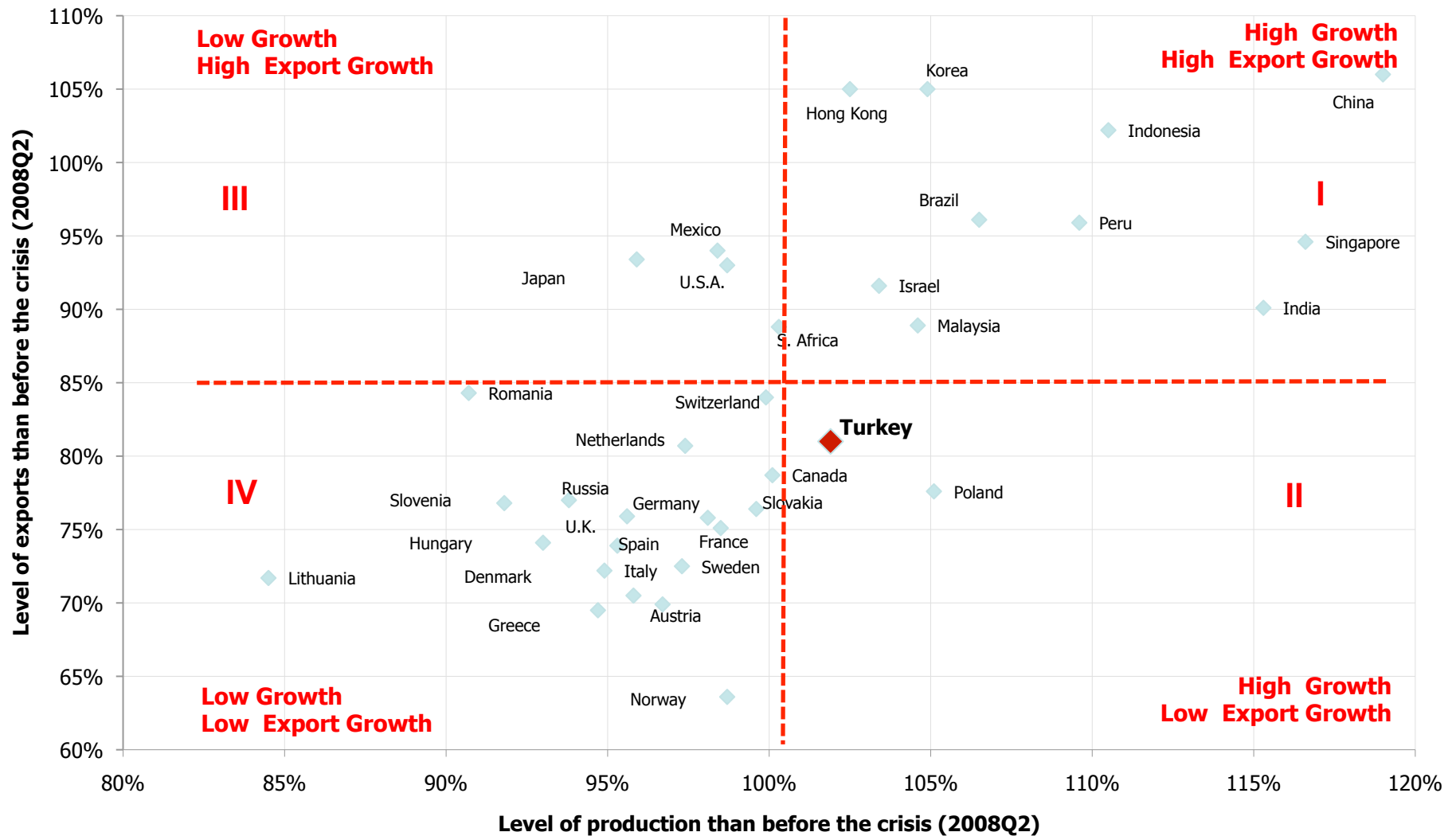
- TEPAV executes and coordinates the activities of the Ankara Forum on behalf of TOBB
 - Technical reports, network coordination and negotiations
- An industrial estate is under construction in Jenin.
 - Opportunity for Turkish businesses to move parts of their value chains to lower cost locations.
 - More opportunities for the growing Palestinian economy
- A similar zone in Yemen



Eastern Anatolia is another priority for TEPAV

- Regional income disparities is critical for the future of Turkey
- Cross-border projects with Armenia and Georgia
 - Tourism clustering around new possible gates: Aktas to Georgia, a special zone in Ani
- Regional development in Mardin – Batman region
 - Links with Northern Iraq

Slow Turkish export recovery because of the EU!



Sources: TEPAV calculations, WTO, Eurostat, EIU, BEA, Statistics Canada, Bank of Israel, Banco de Brasil, tradingeconomics.com

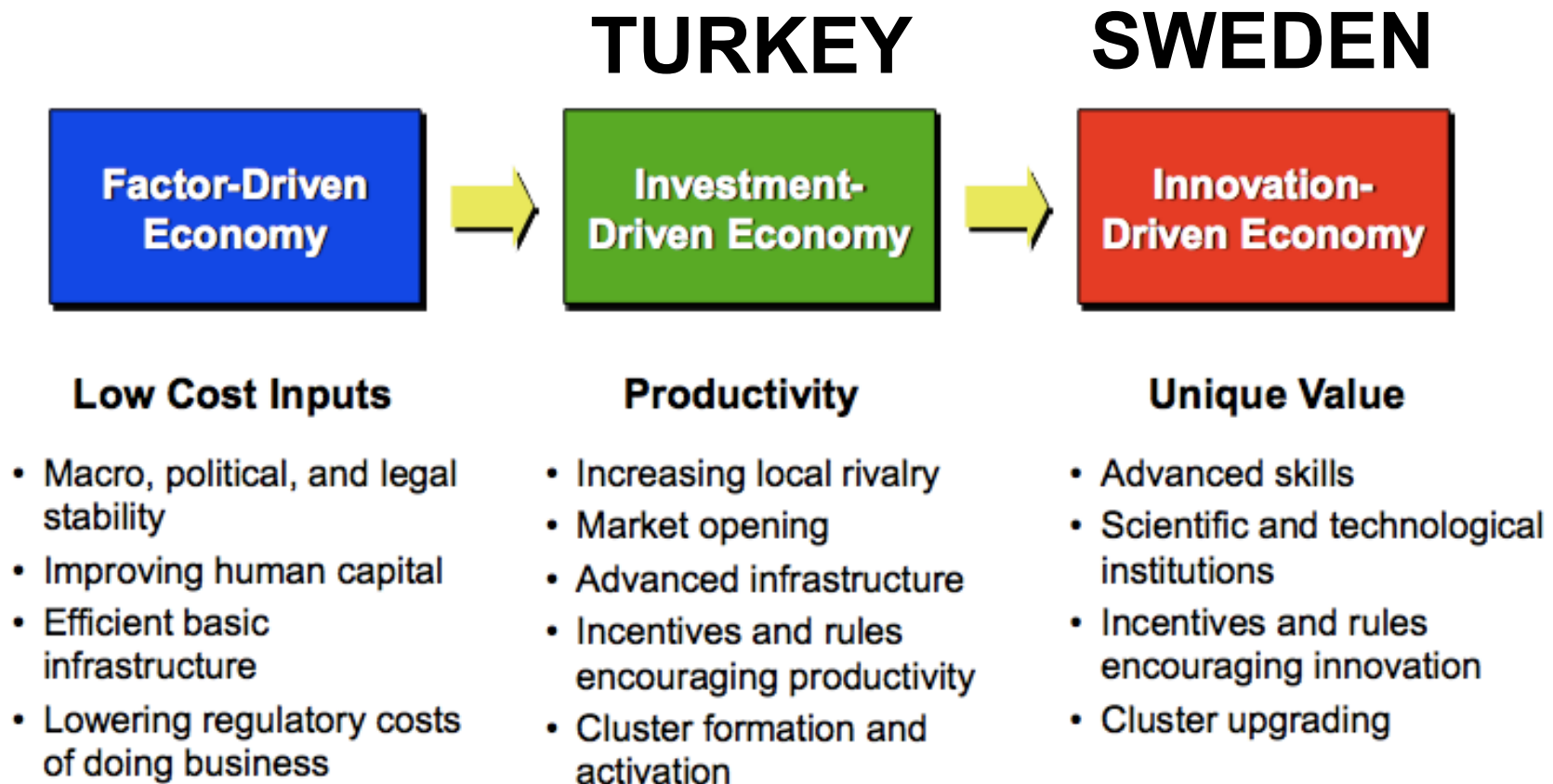
We have to diversify into non-EU markets

- MENA was a good bet
- But we also need sophisticated, high value-added markets
 - United States? (high transport costs, specific products, strong buyers)
- European market is a big experience for our firms, but it also creates a hold-up problem: standards, distribution channels, etc
 - **How did Volvo penetrate into U.S. market?**
 - We only have Ford Transit (which uses Ford's network)

Is EU a tool for sustaining our competitive advantage?

- Back in days:
 - Customs Union with the EU has been a force in structural transformation
 - automobile and TV industries
 - EU was an anchor for reforms
- In the WTO framework, particularly after China's accession, we lost the advantage of the Customs Union
 - Lack in industrial policies to keep our competitive advantage
 - Is location really an advantage?
- Challenge of transforming into an innovation-driven economy

Investment-driven v Innovation-driven economies: is there a trap?



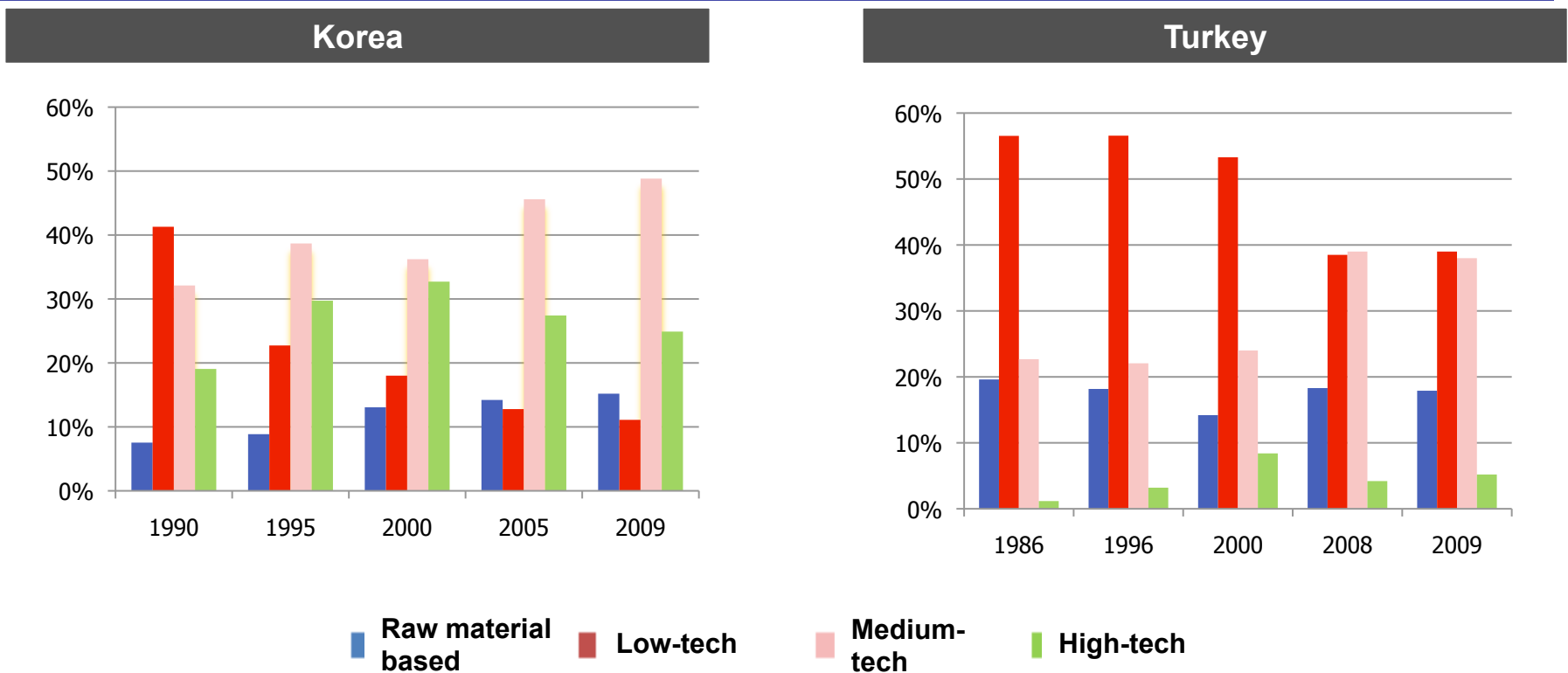
Is there a middle income trap? Turkey might be trapped as an investment- driven middle-income country

- What is the trap?
 - Losing competitive edge to poor countries with low labor cost
 - Yet cannot converge to innovation-driven rich economies
- Who has escaped from this trap?
 - Korea, Taiwan, Poland, Czech Republic
 - Chile?
- Who was trapped?
 - Mexico, Argentina, Malaysia, Vietnam
 - Brazil? Turkey?
- We need a strong and diverse reform agenda as well as infrastructure investments

Innovation is critical

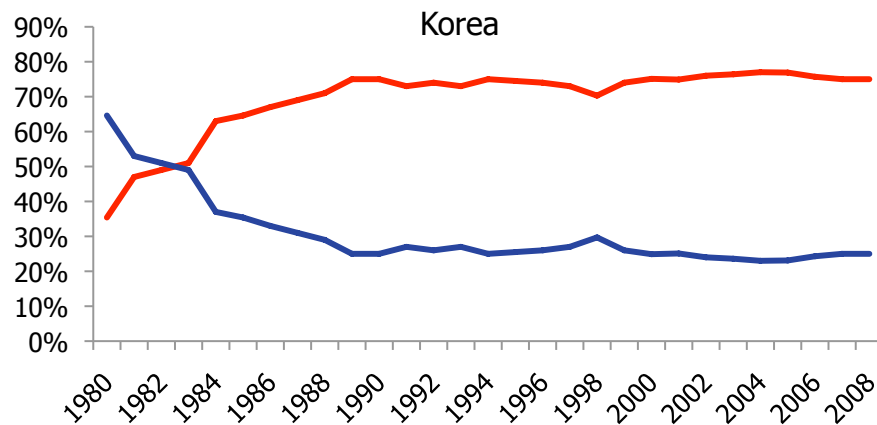
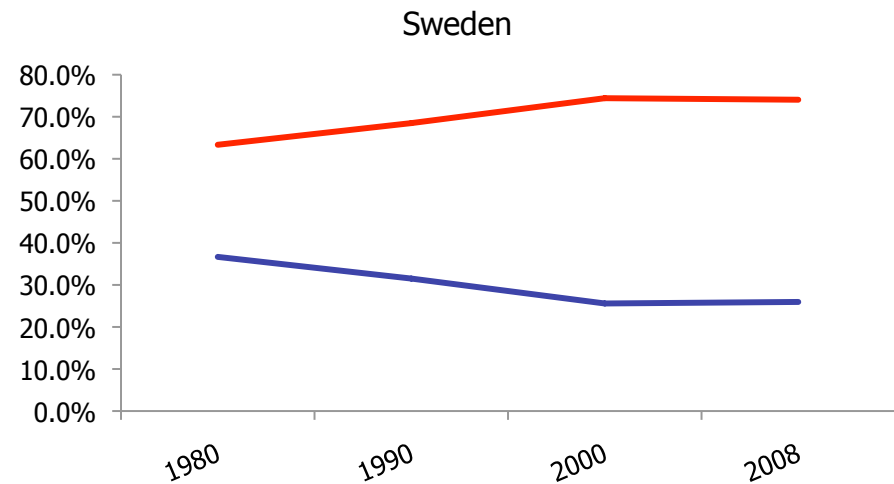
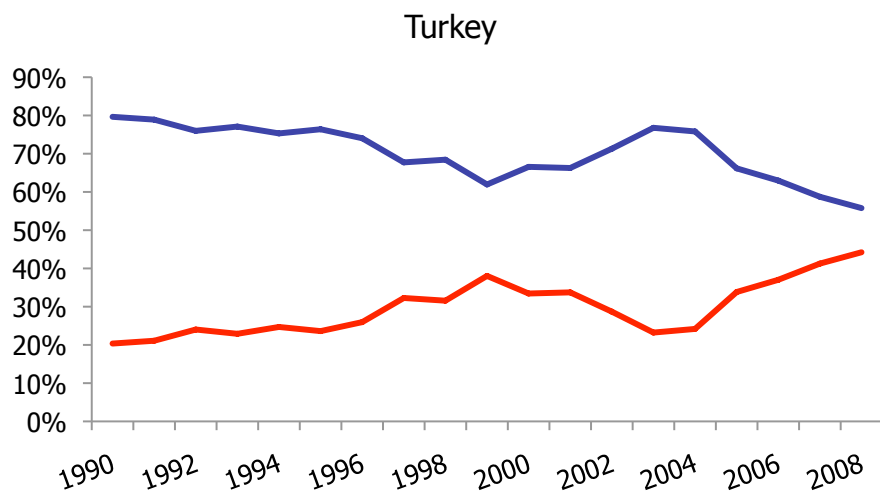
How can we increase the share of the green?

Technological structure of exported goods: Korea and Turkey compared, 1990-2009



Source: COMTRADE database, TEPAV calculations
(Based on technological classification of UNIDO goods)

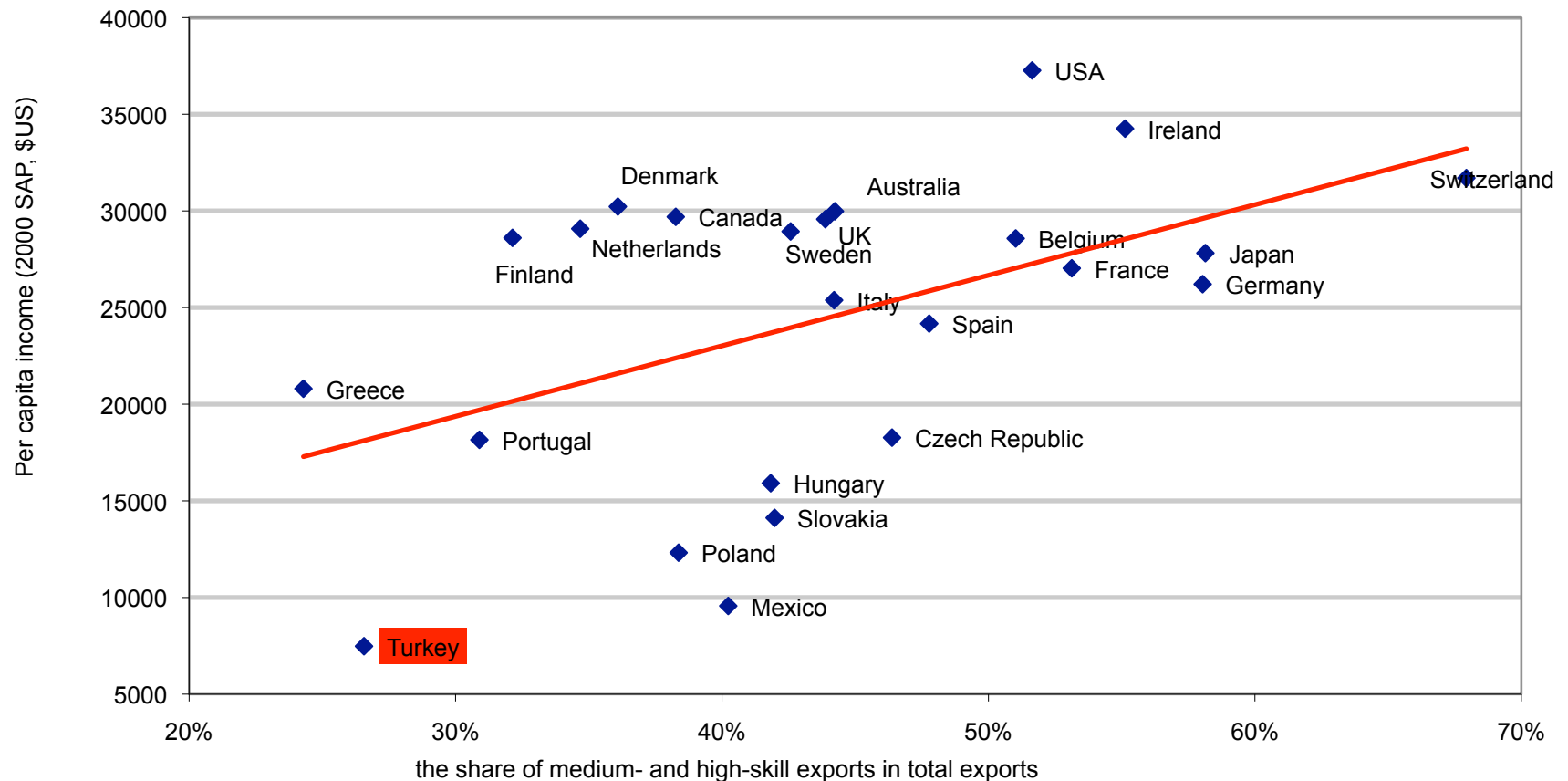
Turkish R&D expenditures are dominated by public



— Private — Public and Universities

How different is the export structure of economies Turkey seeks to converge than Turkey?

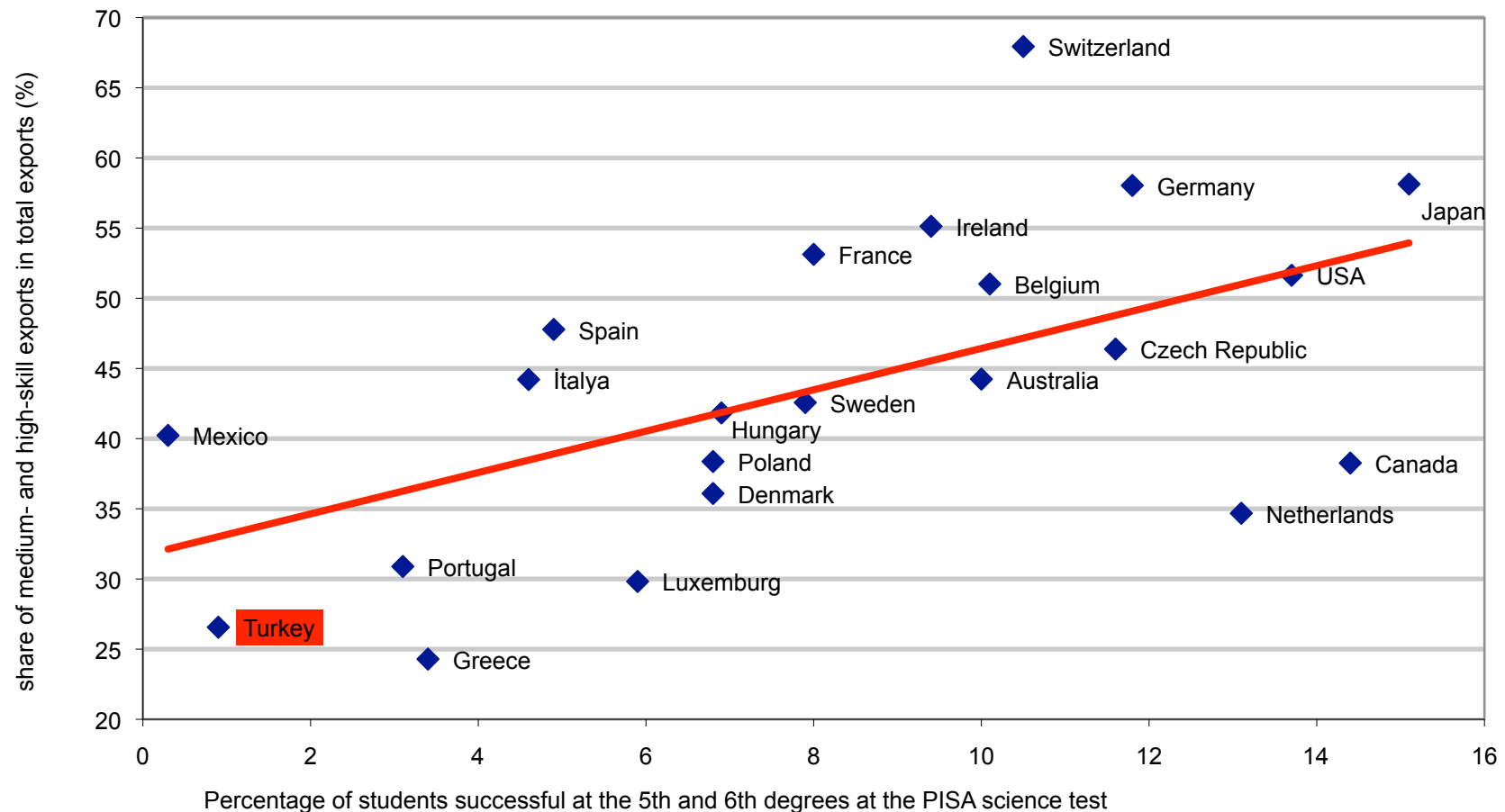
Per capita income and the share of medium- and high-skill exports in total exports in OECD countries, 2005



Source: UNCTAD classification, COMTRADE database, TEPAV calculations,

It is hard to upgrade the production pattern without with a lack of skilled labor force

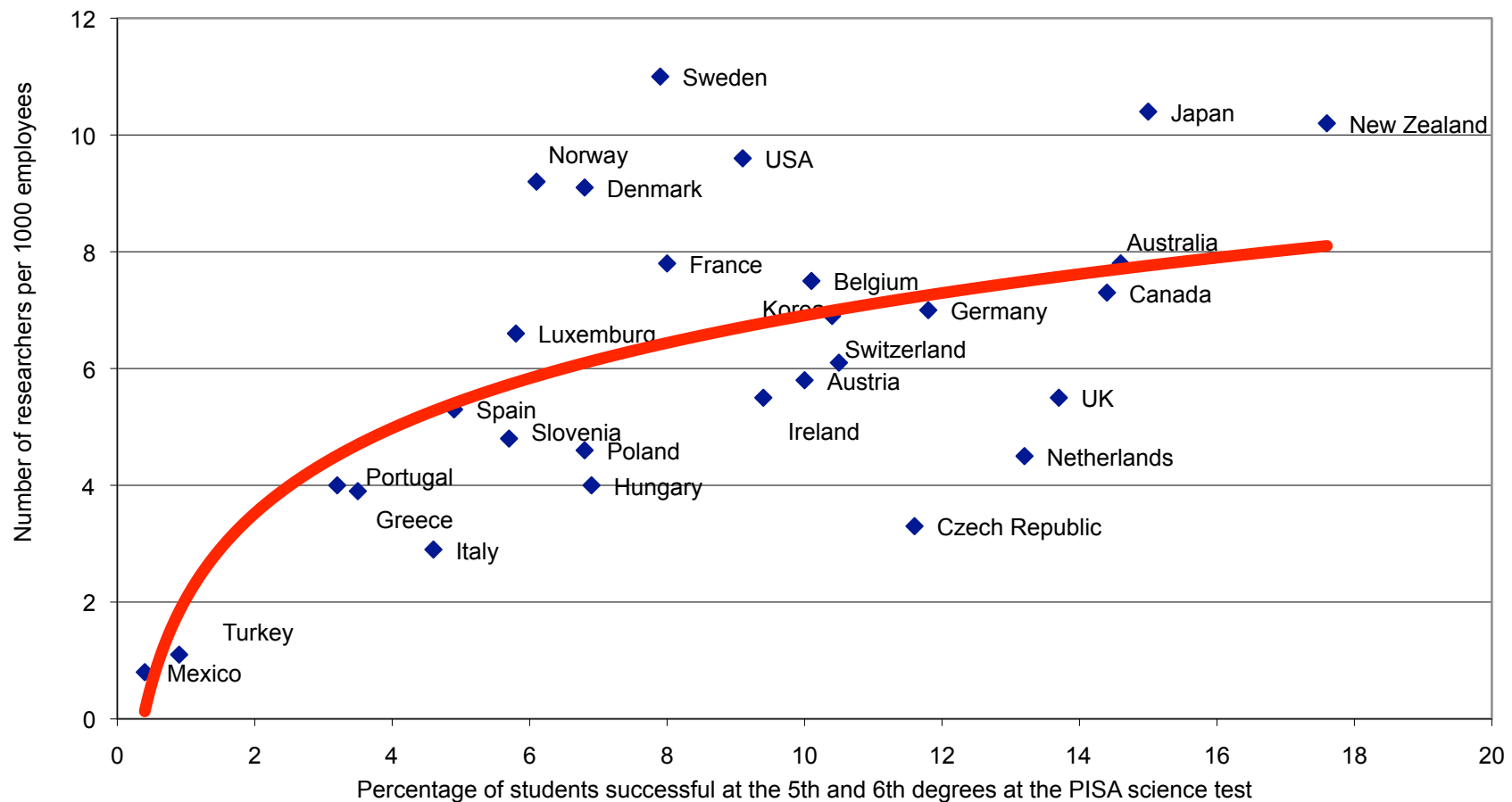
Success at the PISA test and the share of medium- and high-skill exports in total exports, 2005



Source: UNCTAD classification, COMTRADE database, PISA 2006, TEPAV calculations

Success at the PISA tests also correlated with the number of researchers

Level of success at PISA science tests and researcher population in OECD countries



Source: OECD-PISA 2006, TEPAV Calculations

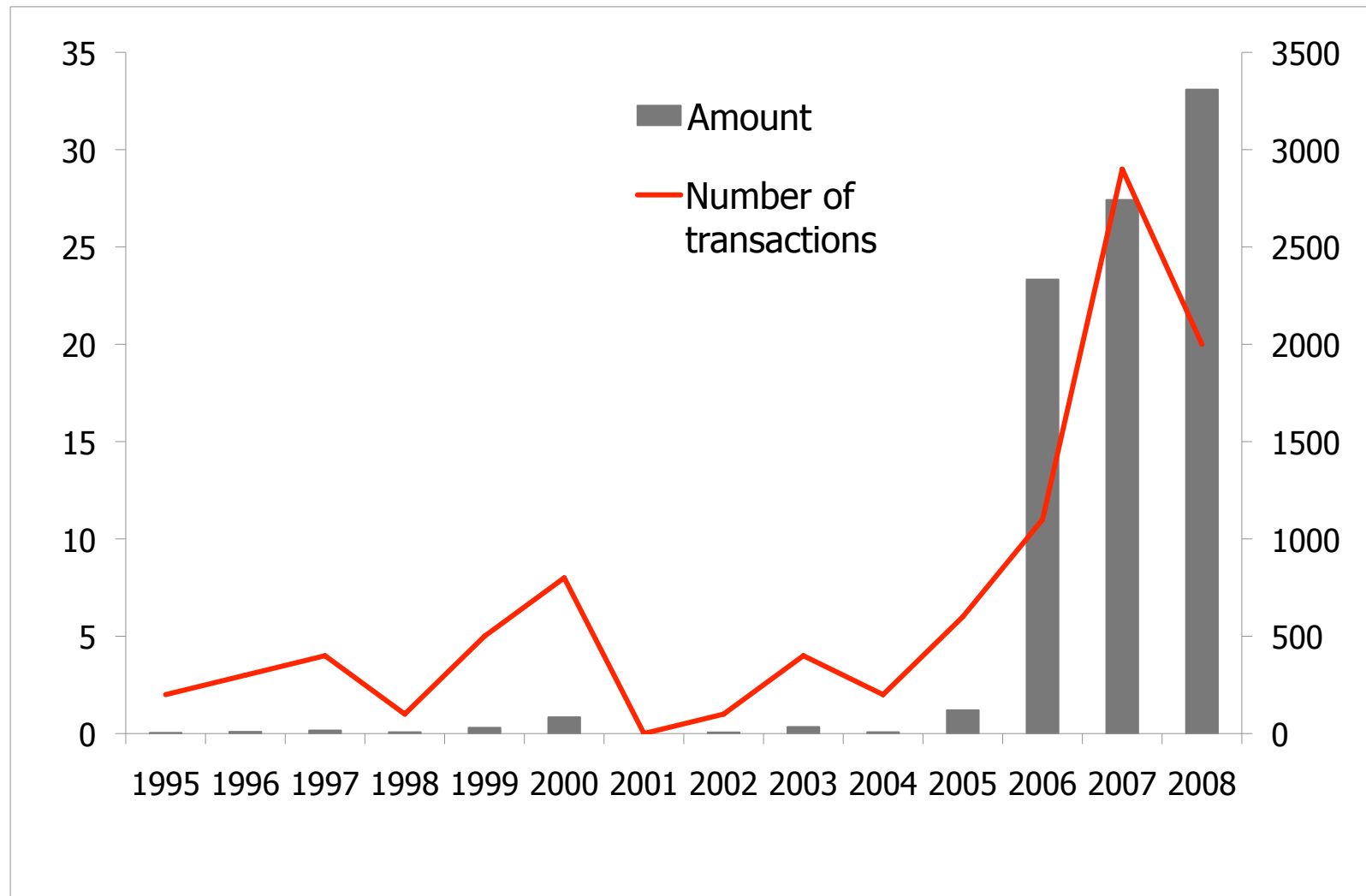
What does TEPAV recently do for innovation?

- All-World Project with Harvard: “Turkey 25”
 - Identification of most rapidly growing 25 firms of Turkey (visibility economics)
- Preparation of a new policy framework for financial innovations
 - Risk capital, securization issues
- Vocational training project for Ministry of Labor and TOBB
 - Content support for the new vocational training attack
 - Training programs tailored for the demands of the private sector
- Regional development projects
 - Both in Turkey and in the surrounding region
 - Efforts to define competitiveness at local environment



Wrap-up

- In 2000s: Turkey had an impressive performance thanks to:
 - 1980 reforms by Ozal (equivalent of Deng reforms)
 - 2001 reforms by Dervis
- At 2010:
 - Turkey is full of opportunities
 - But also struggling to upgrade to an innovation-driven rich economy in an uncertain policy environment
- Challenges:
 - Institutional restructuring in companies in all industries to increase efficiency
 - Firm-based innovation
 - Internationalization of Turkish companies

For example, private equity is a tool for corporate restructuring

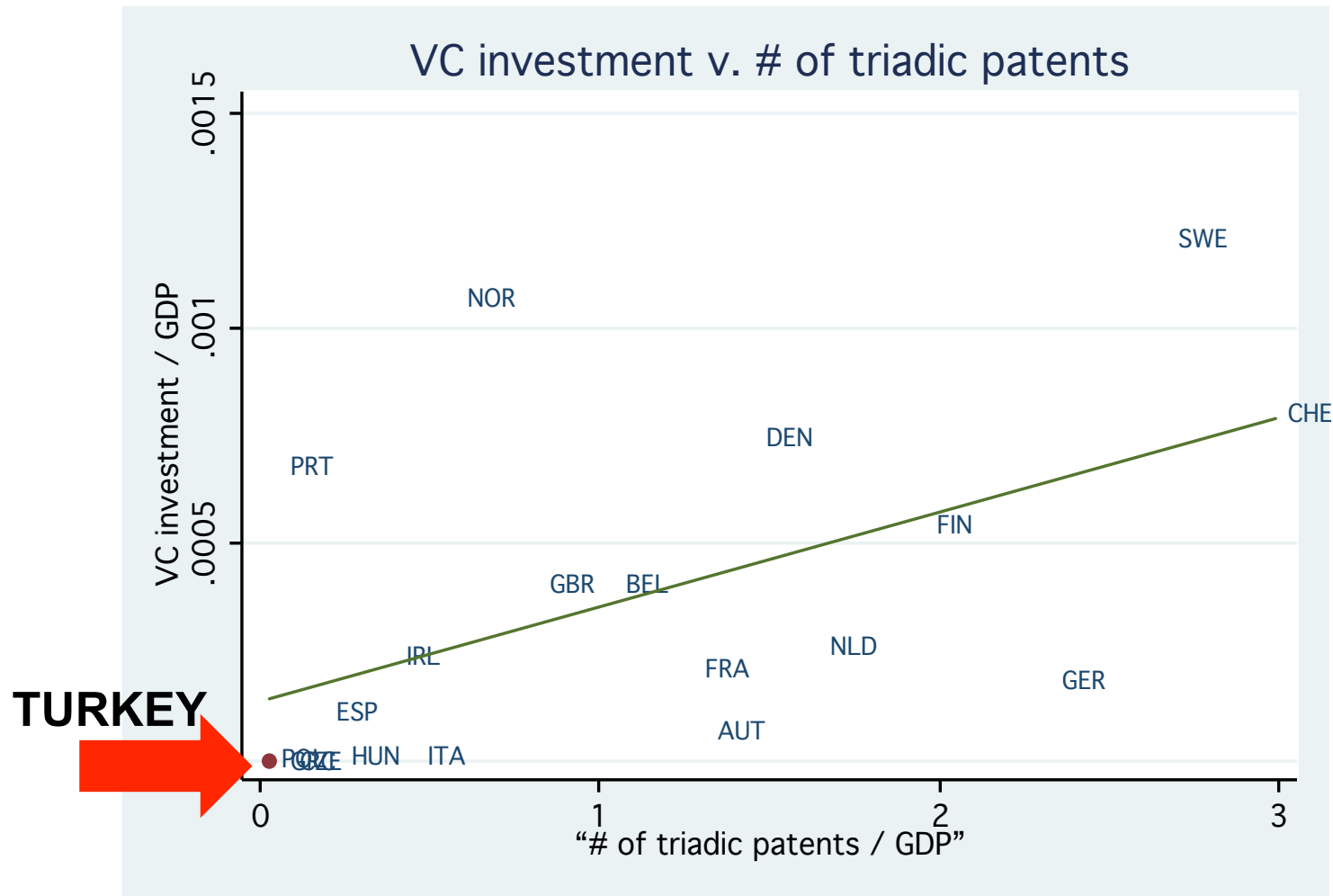


..in a diverse set of industries
(there are companies of high potential everywhere)

 Services
 Manufacturing

Airport Services	Entertainment	Mobile Marketing
Arts & Ent. & Recreation	Eyewear	Motion Picture
Automotive	Factoring Services	Multiplex Operator
Biotech	Fairs and Exhibitions	Paper & Packaging
Broadcasting	Fleet Rental	Payment Systems
Brokerage House	Food & Beverage	Pharmaceuticals
Cargo Carrier	Furniture & Carpets	Plastics
Ceramic Tiles	Health Care	Real Estate
Construction	Household Appliances	FMCG Retailing
Cosmetics Retail	Information and IT	Security Services
Dental Hospital	Leasing	Ship Building
Edible Oil Production	Logistics	System Integrator
Electrical Accessories	Media	Textile
Electronics Retail	Medical Equipment	Travel Accessories
Electronics	Mineral Products	Vehicle Inspection

Turkey ranks low both in innovation and its finance



Concluding remarks / questions

- How to use finance / PE as a tool for corporate restructuring in all industries?
- How to use finance / PE as a tool for internationalization of Turkish firms:
 - Cross-border acquisitions
 - Cross-border green field investments in lower cost locations to keep our competitive advantage in traditional industries
- How to improve venture financing for an innovative economy?