

# tepaV

Economic Policy Research Foundation of Turkey

## **An overview of Turkey's developmental journey: full side and empty side of the glass**

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# Framework

- Experience sharing:
  - “Experience is a collection of past mistakes...”
- What has Turkey achieved in terms of structural transformation?
  - Full side of the glass
- What are the current challenges?
  - Empty side of the glass
  - What is it that reforms shall fix?
- Way forward?
  - How to get out of the middle income trap?

# What has Turkey done in terms of policy reform so far?

- 1980 policy reforms
  - Price reforms
  - Financial liberalization
  - Trade liberalization
  - Convertibility of the Turkish lira
- 2001 policy reforms
  - Banking reform—prudence etc.
  - Privatization
  - Independent authorities
  - Fiscal and monetary discipline

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**First  
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- Public administration reform
- Tax reform
- Operational problems of the legal system
- Education reform-curriculum
- Labor market rigidities
- Health reform

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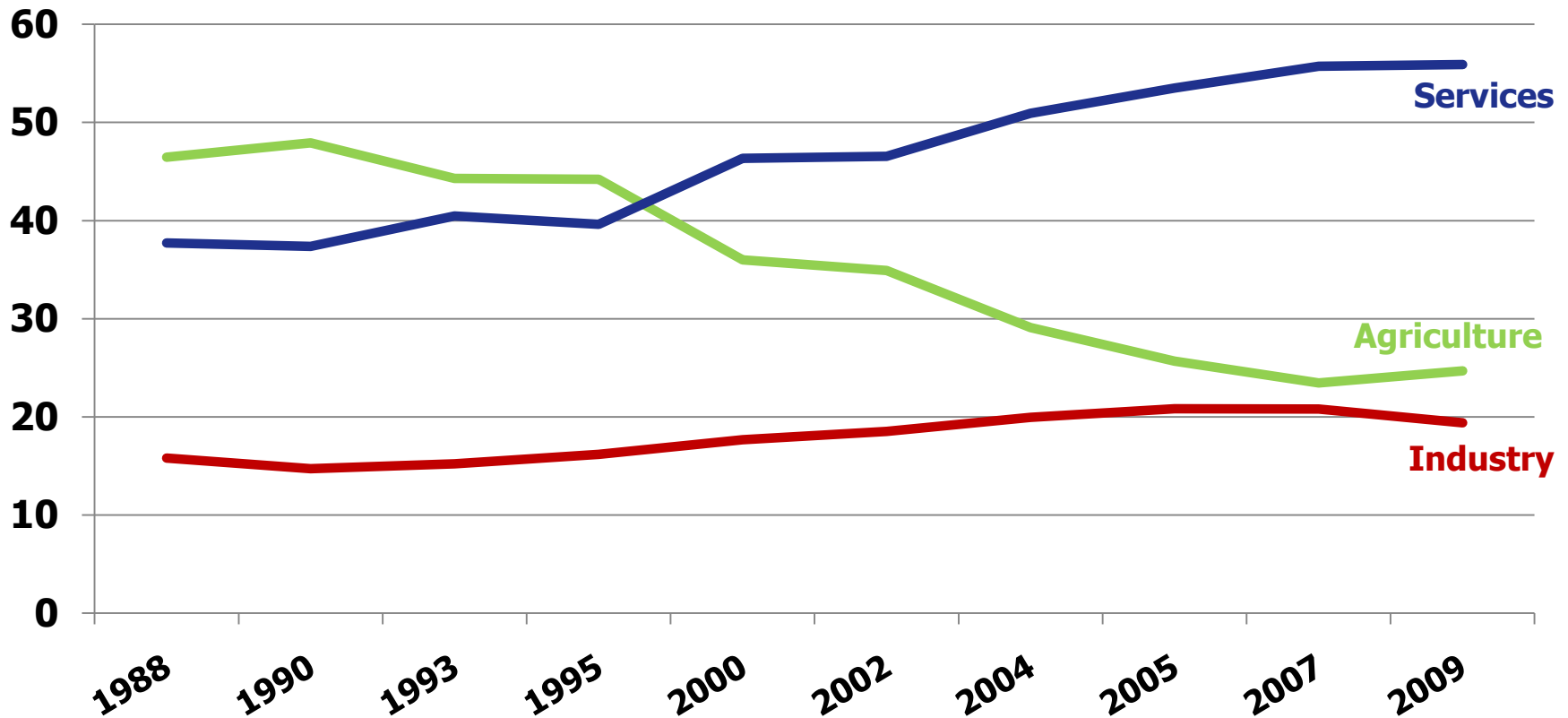
**Second  
generation  
reforms**

# An overview of the recent progress of Turkish economy

	1980	2001	2008
<b>GDP (billion \$)</b>	70	509	700
<b>Per capita GDP (USD)</b>	1,500	2,906	9,000
<b>Number of enterprises</b>	90,000	723,503	1,170,248
<b>Exports (USD billion)</b>	3	31	132
<b>Exports per worker (USD)</b>	65	1,456	6,229
<b>Industry share in exports</b>	10%	92%	92%
<b>Number of exporters</b>	1,000	25,000	47,000
<b>Tourism revenue (billion \$)</b>	0,3	8	21
<b>Ranking in the world (in terms of GDP)</b>	25th	21st	17th

# Transformation is still ongoing; along with rapid urbanization

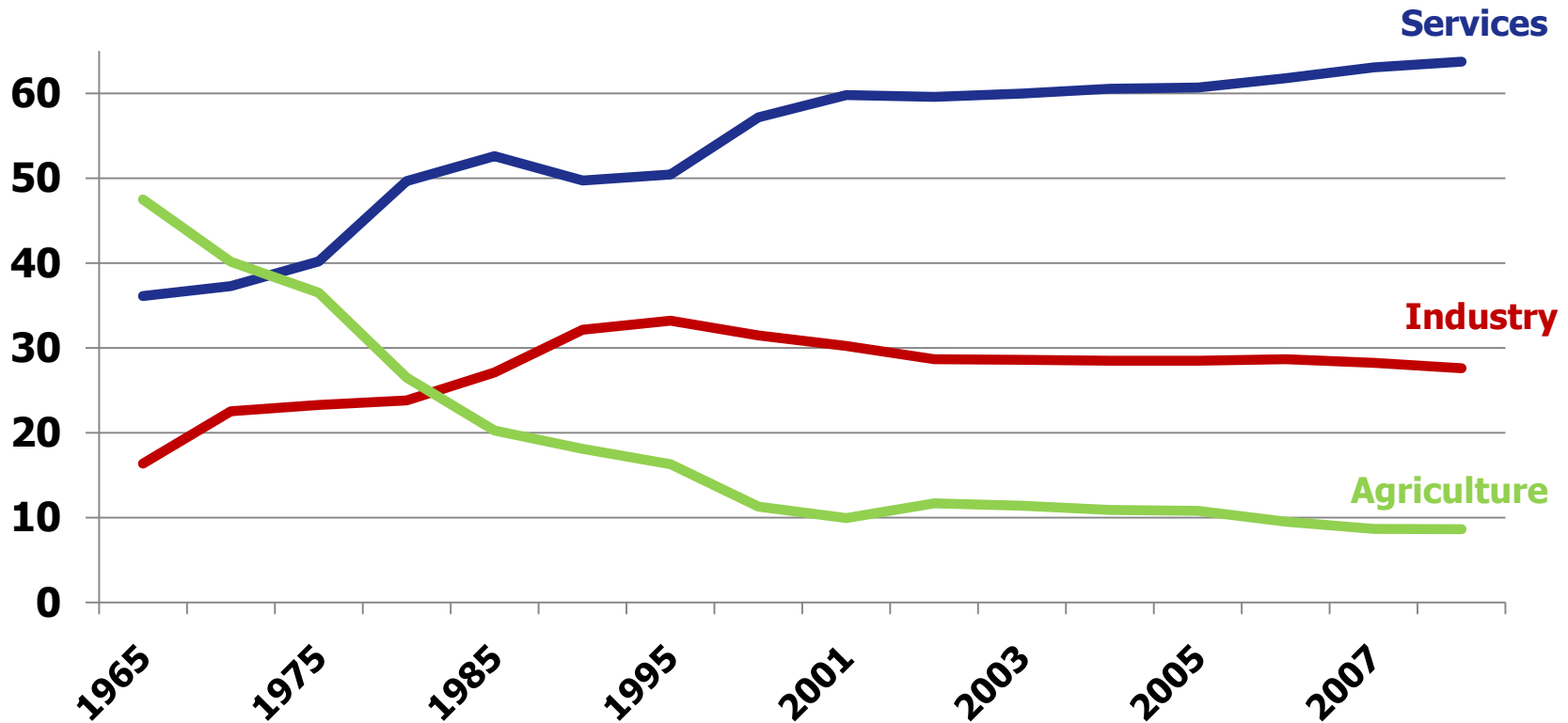
Sectoral distribution of labor (%) 1988 - 2009





# No structural change after 2001?

Sectoral composition of GDP (%) 1965 - 2009

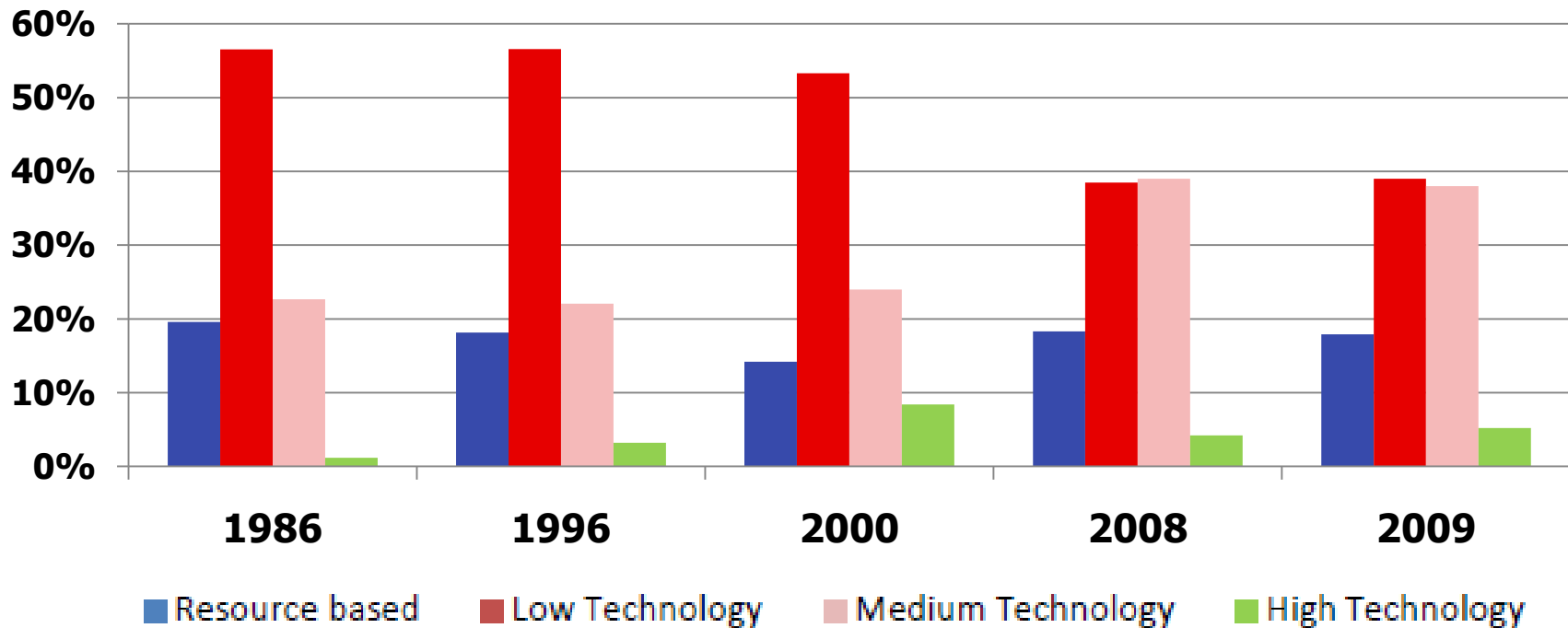


# Transformation and diversification

- Diversification is increasingly becoming the key element of Turkey's economic transformation
- A three dimensional process / three aspects of diversification:
  - Sectoral and technological
  - Geographical (within Turkey)
  - Market diversification (globally)

# Technological transformation: declining low-tech, rising mid-tech

## Technological composition of Turkey's exports 1990-2009

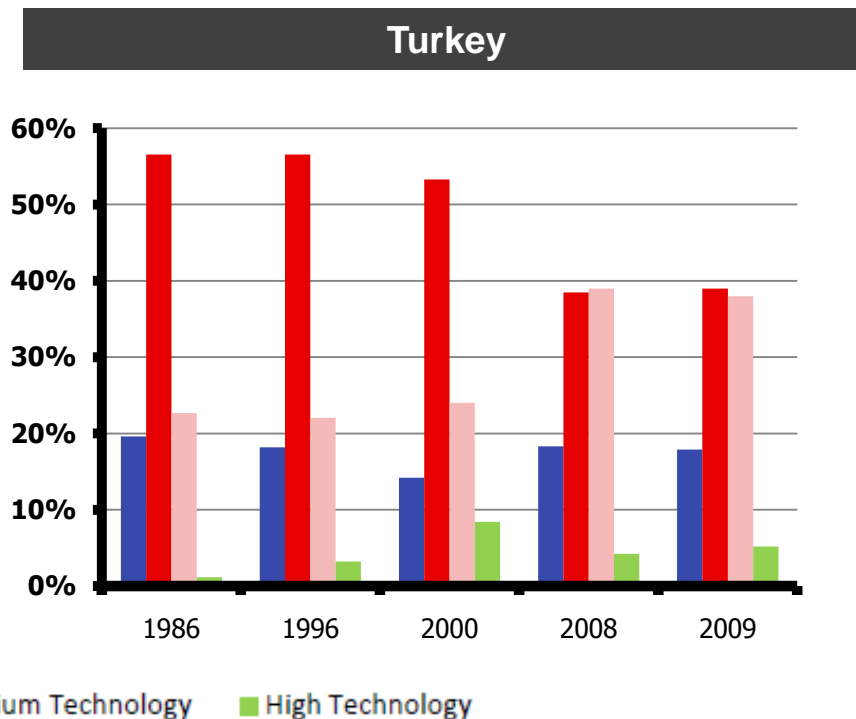
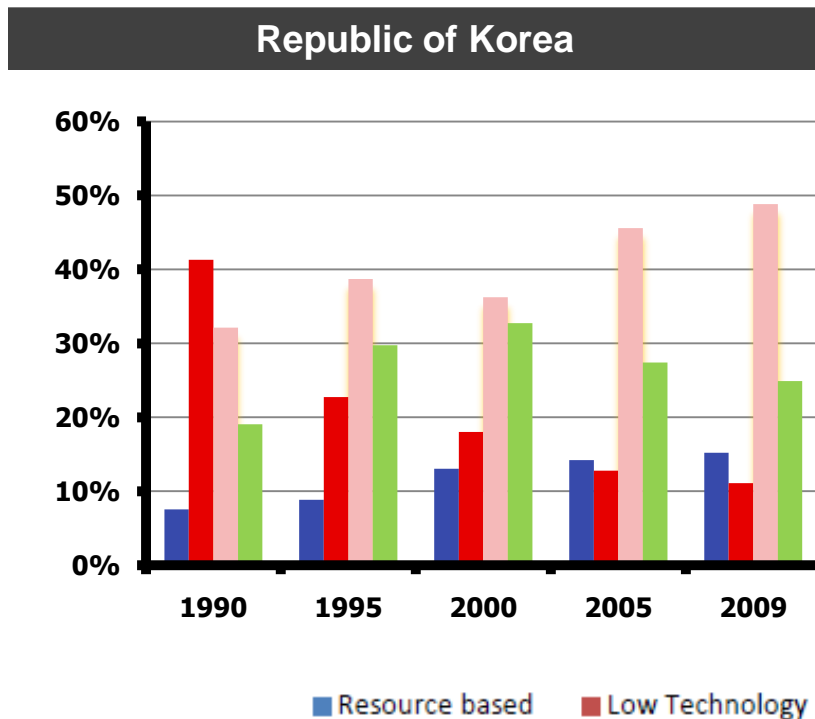


# What does Turkey produce now?

- Emerging sectors:
  - White goods
  - Automobile and parts
  - Consumer electronics
  - Ships
  - Machinery and equipment
- Traditional sectors:
  - Textile, apparels, leather
  - Food and agro-industry
  - Construction materials
  - Furniture

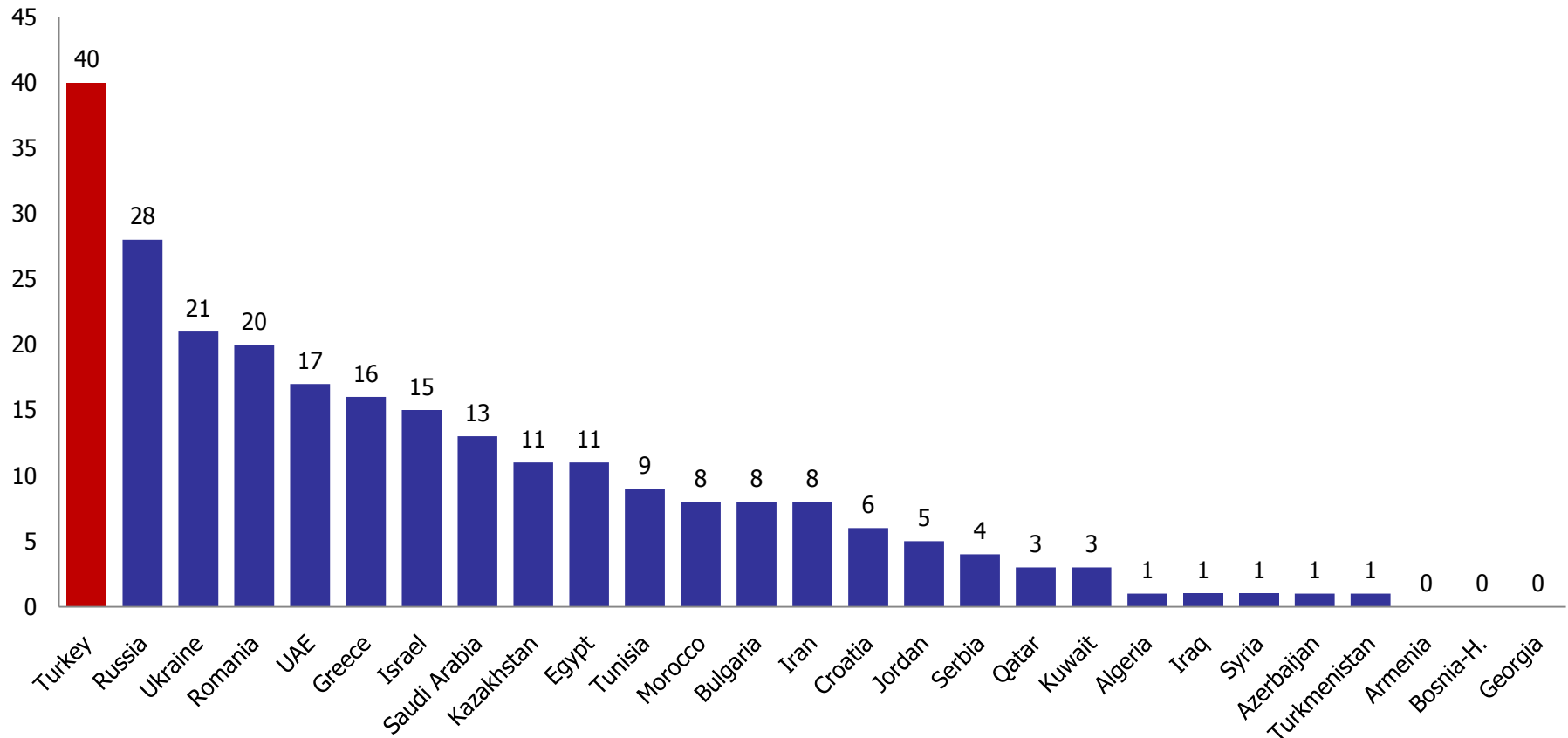
# When it comes to high-tech, Turkey has a long way to go

## Technological composition of exports of Korea and Turkey (1990-2009)



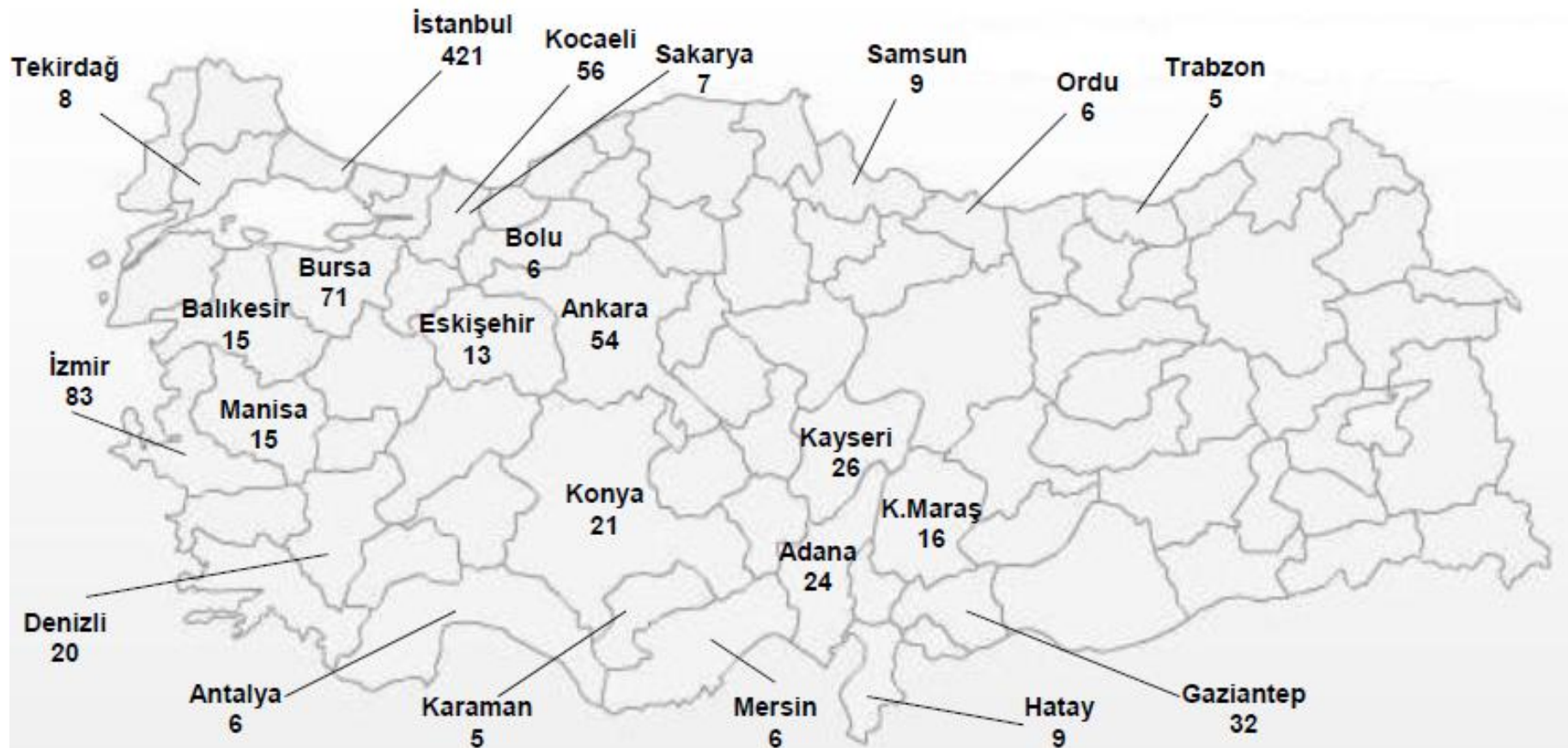
# Sectoral diversification is increasingly a critical feature of Turkish economy

Number of sectors with above \$ 500 million exports (HS4 classification, 2 digit, 2007-2008)



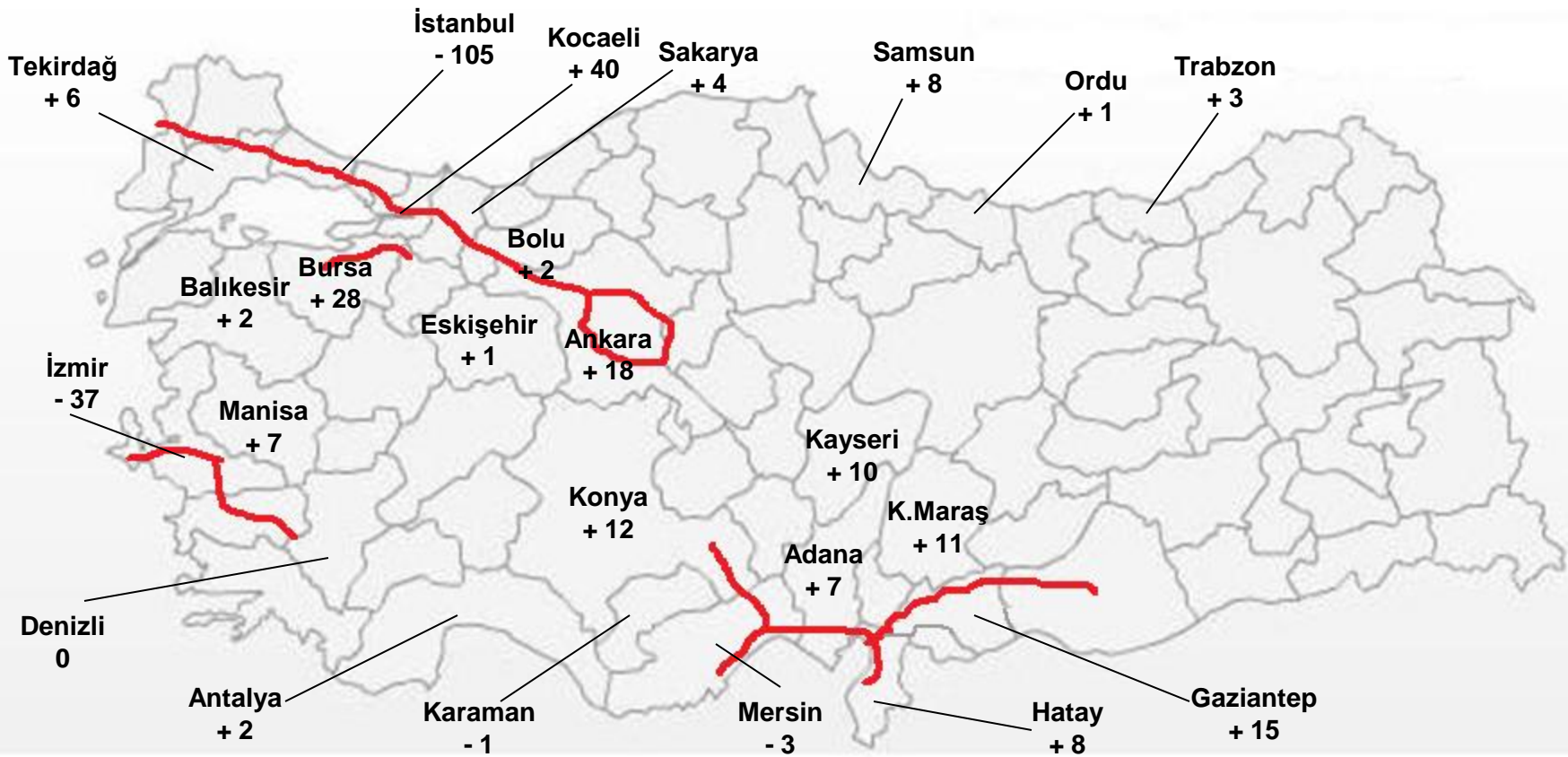
# Geographic diversification process: "the emerging Anatolian tigers"

Cities with 5 or more firms among the largest 1000 industrial firms in Turkey, 2009



# Industry's move from west to east?

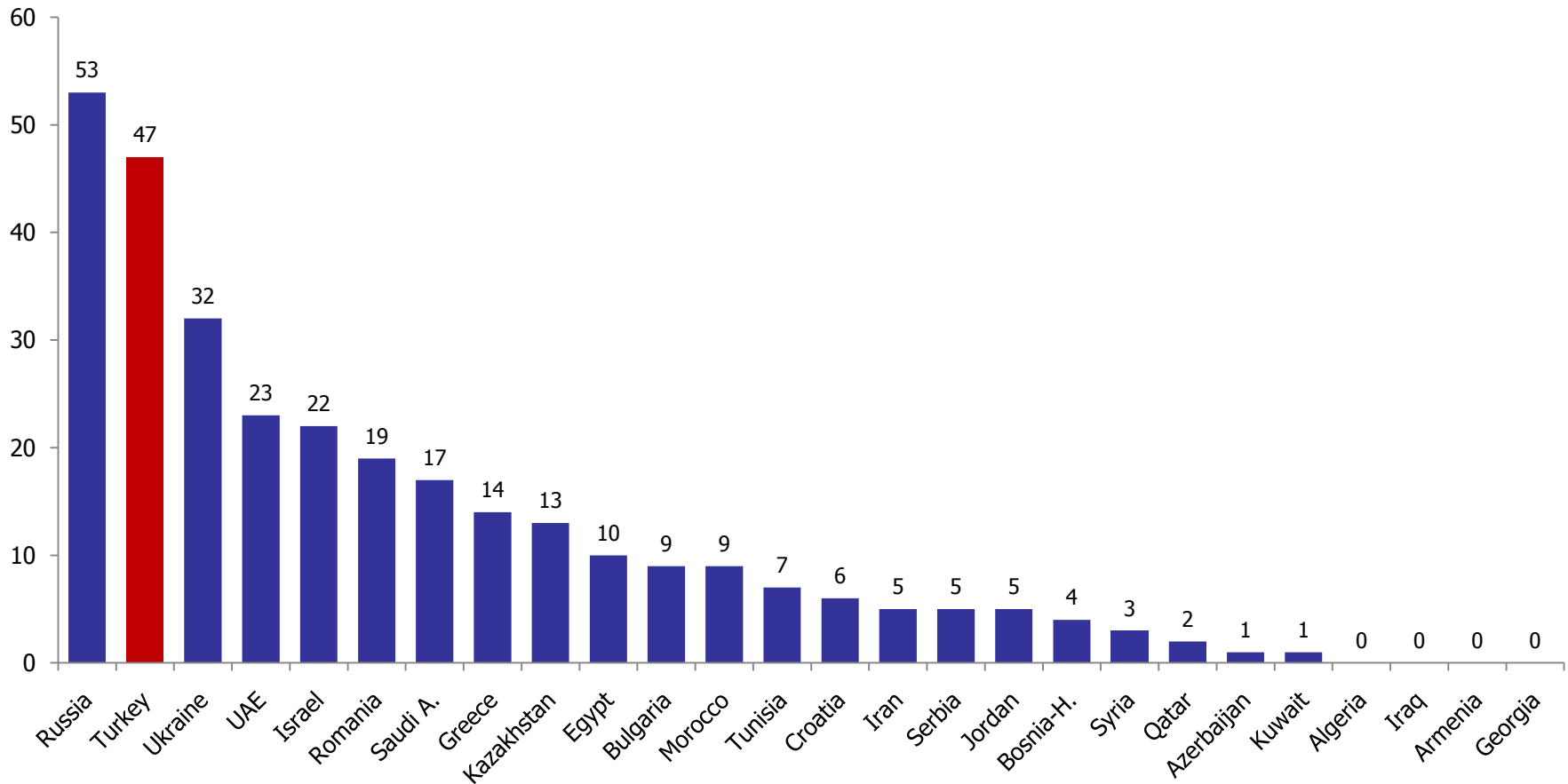
Expressways in Turkey (red lines, as of 2010) and change in the number of firms listed in largest top 1000 industrial companies between 1997-



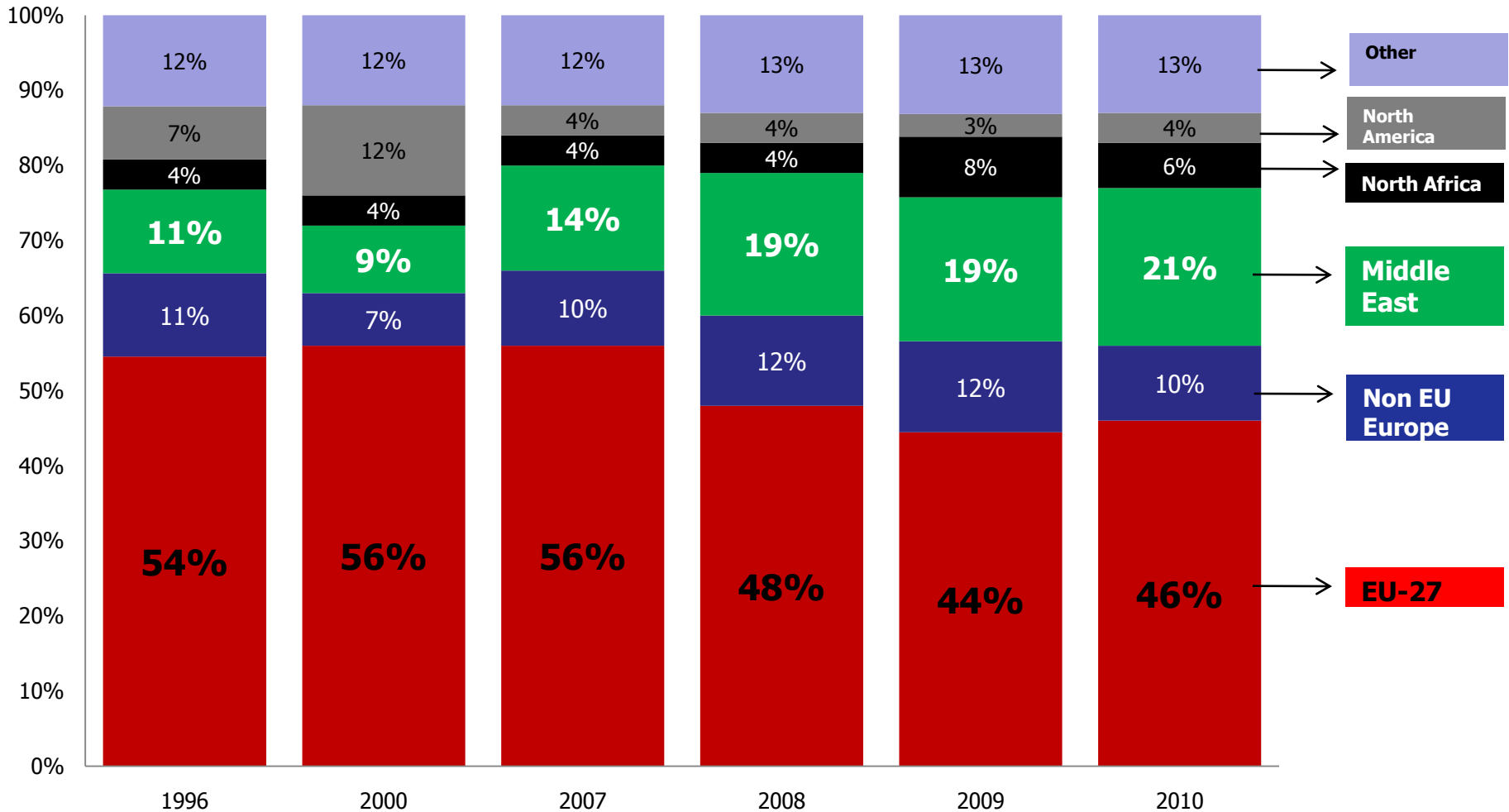


# Geographically diversified export portfolio: presence in various different markets

Number of export destinations (non-energy) over \$ 500 million volume, 2007-2008

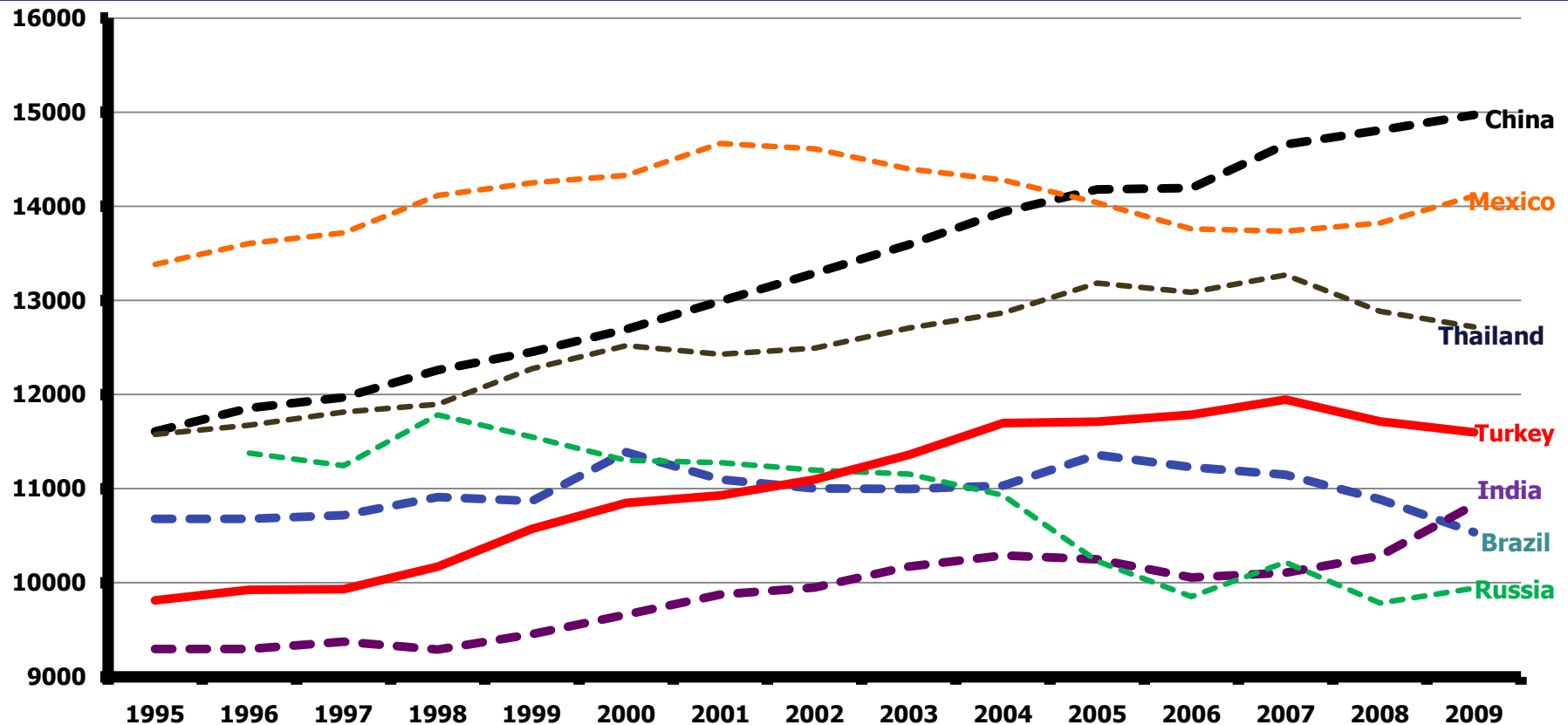


# Market diversification for export markets; declining share of the EU, rising MENA



# Decreasing share of EU implies low sophistication for Turkish exports...

## Export Sophistication Index (EXPY) Turkey and selected countries (1995-2009)



# To sum up the transformation story

- Transformation is happening and changing the Turkish society more than ever before
- Not a coherent growth strategy but rather the outcome of the interplay of several factors
  - ➔ Internal structural factors:
    - Geographical location
    - EU Customs Union and accession process
    - Demographic structure / entrepreneurship potential
  - ➔ External factors:
    - Global economic and technological trends
    - Vertical specialization strategies of MNCs
    - Rising foreign direct investment flows

# Empty side of the glass? Major policy challenges waiting to be tackled...

## ■ Achieving convergence

→ Increasing the economic growth capacity from 4 to 7 percent

→ *A coherent growth story?*

## ■ Tackling SME growth problem

→ Productivity and innovation issues

→ *An ambitious eco-system renovation strategy?*

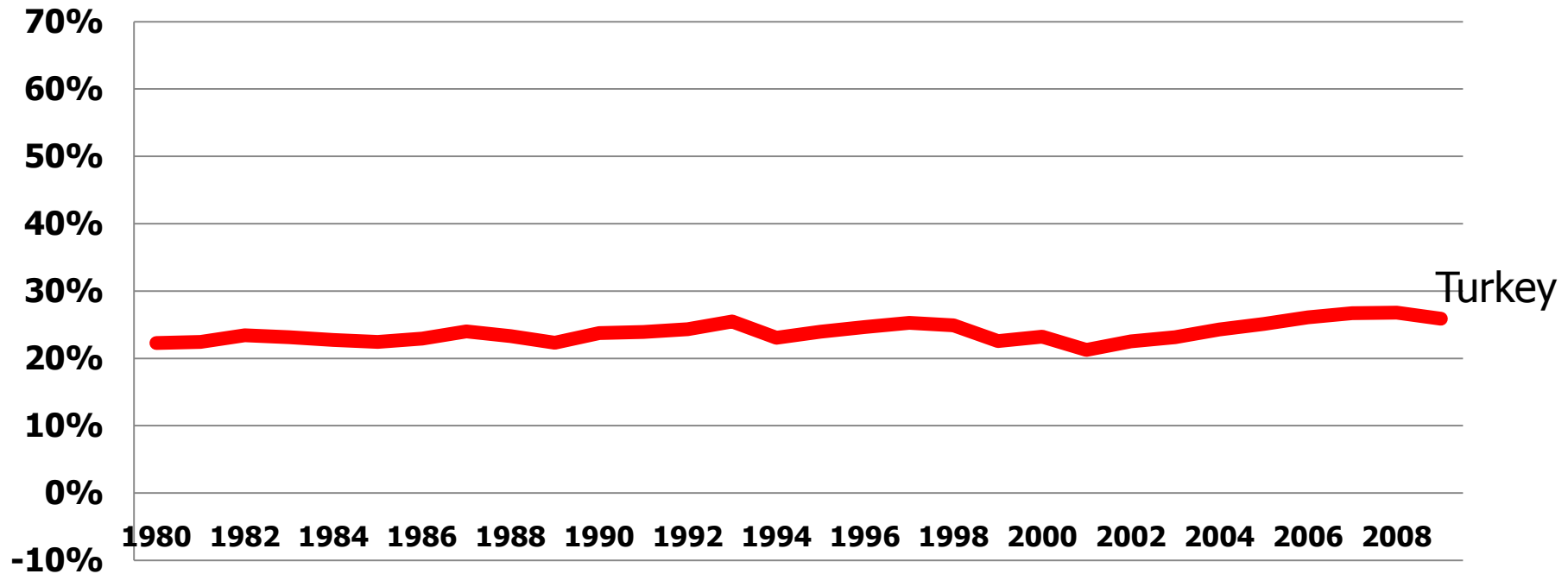
## ■ Fighting skills mismatch and unemployment

→ Urban-rural transformation

→ *An education reform strategy in line with growth and competitiveness strategy?*

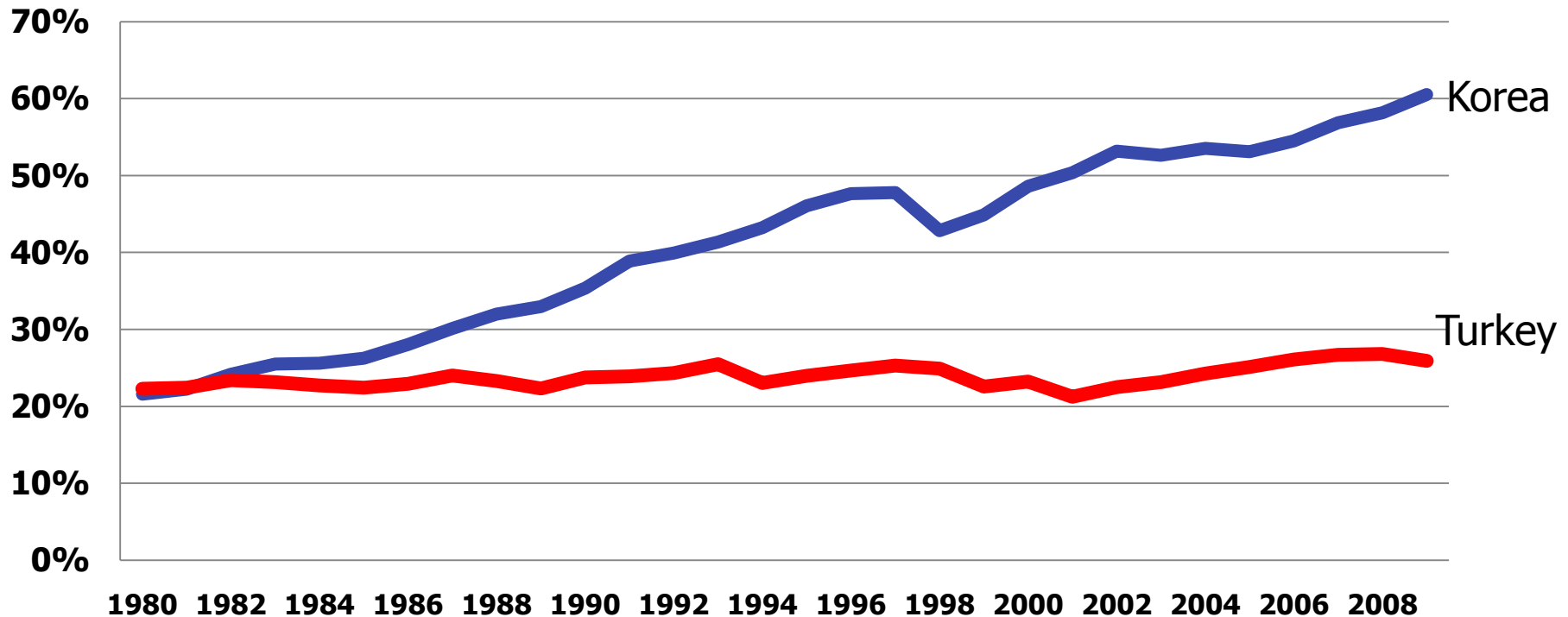
# A very stable convergence performance! Structural change with no (relative) results?

GDP per capita in Turkey as percentage of GDP per capita in U.S., (PPP, 1975-2008)



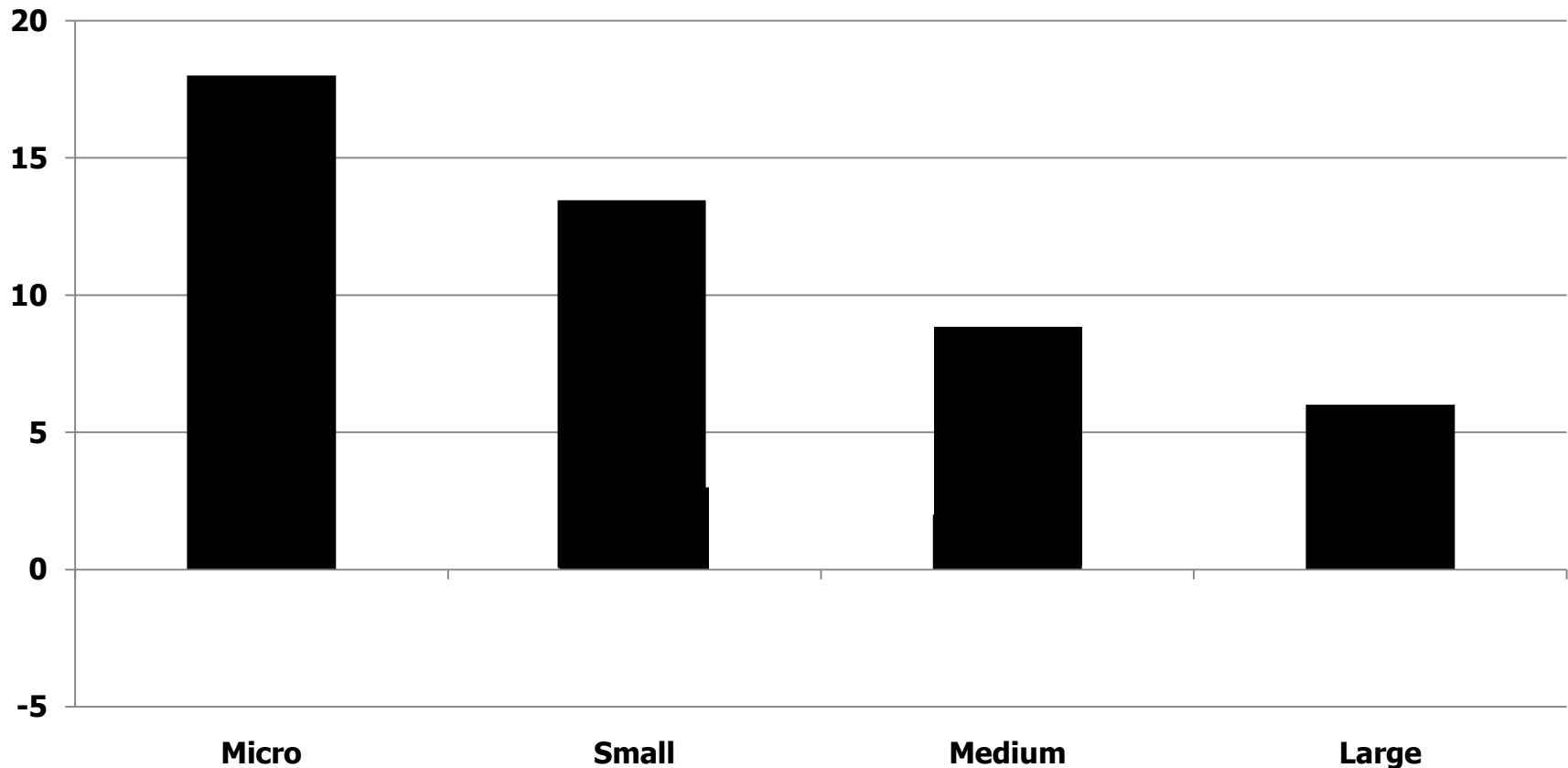
# Though non-convergence is not destiny. A coherent growth story is what Turkey needs...

GDP per capita in S.Korea and Turkey as a percentage of GDP per capita in U.S., (SAGP, 1975-2008)



# Growth of firms in a healthy, private sector driven economy...

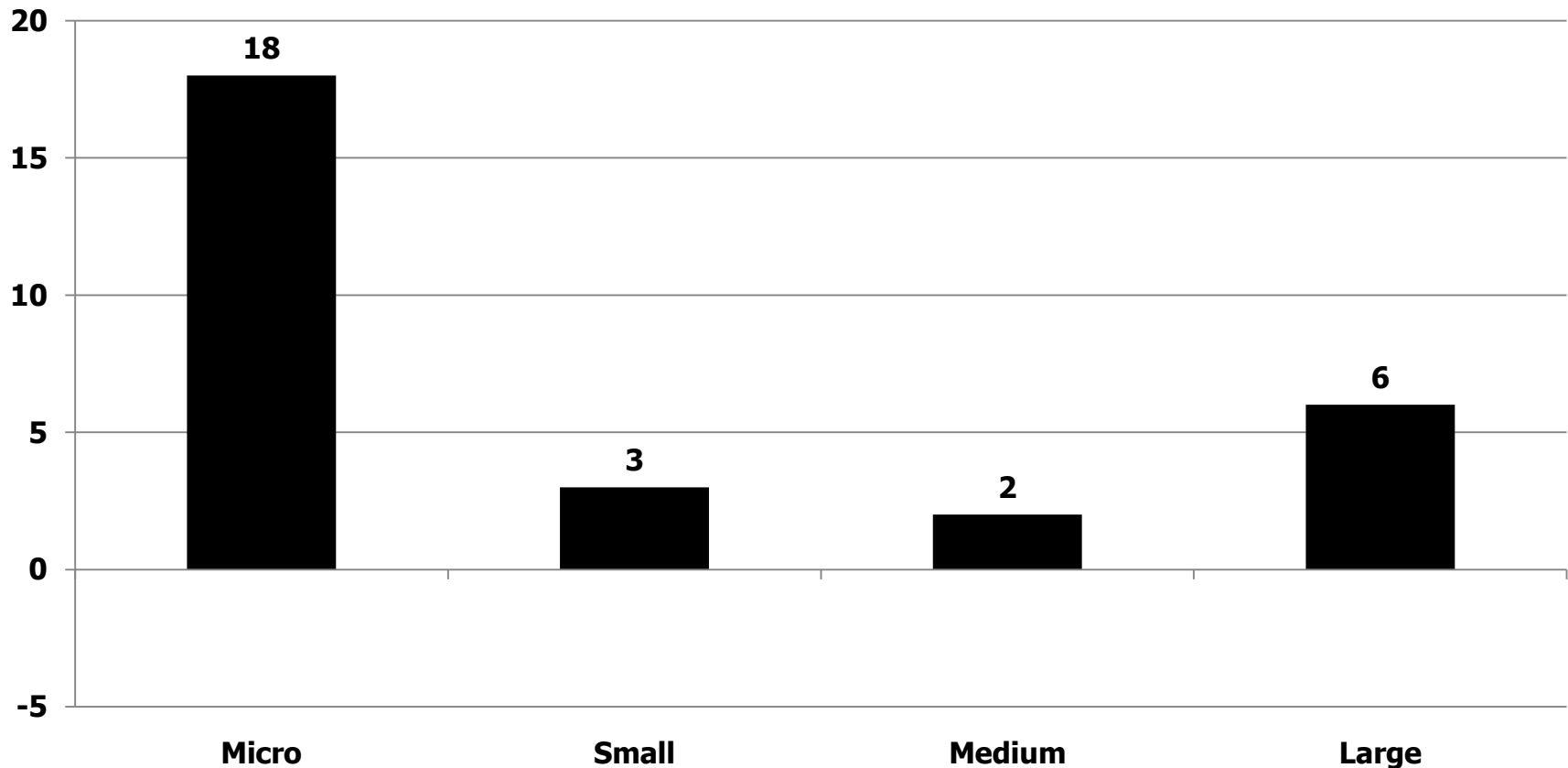
Employment Growth across firm size





# Growth problem in Turkish SMEs

Firm-level employment growth across different sizes, percentage increase (2004-2007)



# Dual structure of the economy is a big problem

## ■ Registered (modern) firms

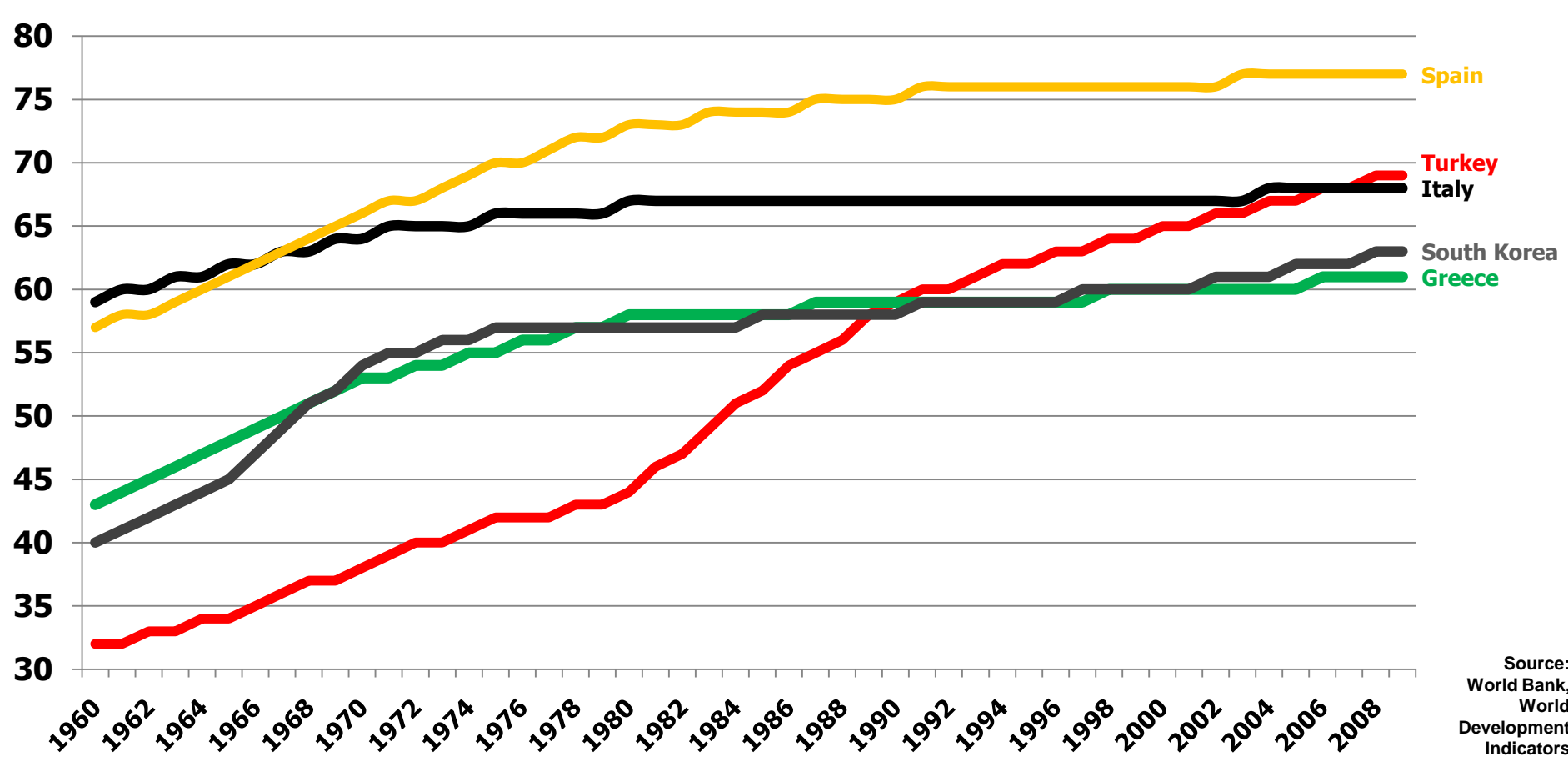
- Productivity levels: 62% of firms in USA
- Economies of scale; new technologies, quality products
- Spread over Anatolia; export oriented

## ■ Unregistered (traditional) firms

- Productivity levels: 25% of firms in USA
- Old technologies, low quality; domestic oriented
- Being unregistered provides a cost advantage of around 20%

# Rapid urbanization puts pressure on labor market and skill needs

Urban population as a percentage of the total population in Turkey, Spain, Italy, Greece and South Korea, (%), 1960-2009

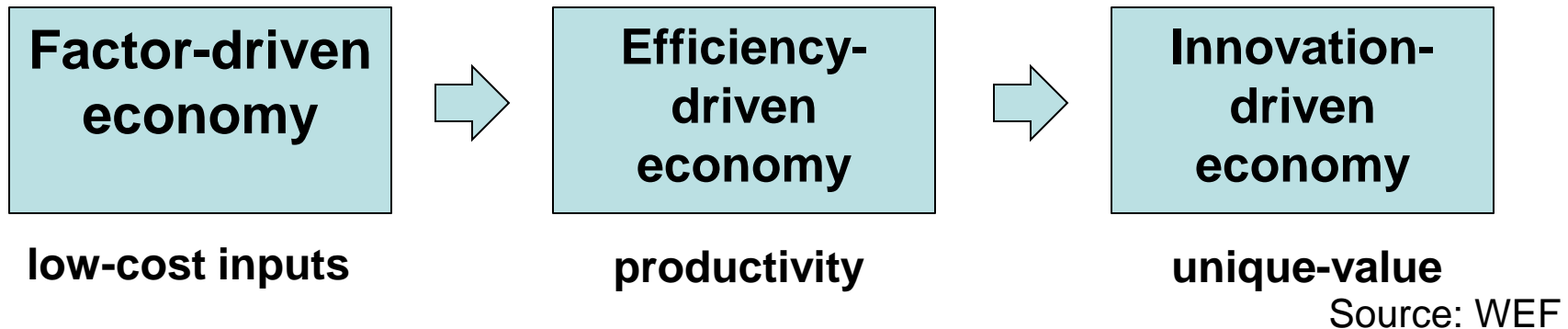


Source: World Bank, World Development Indicators

# What sort of growth strategy needed for Turkey?

- Larger context: A coherent growth story that would tackle the binding constraints with ambitious reforms (eco-system renovation for innovation)
  - Access to finance (PE and VC focus)
  - Education
  - ... (second generation reforms to upgrade institutions)
- A supporting industrial policy framework as part of the overall growth strategy
- Process more important than policy: focus on governance of industrial policy

# Turkey's major risk: middle income trap...



- Where does Turkey stand?
  - Turkey was a transition economy from efficiency-driven to innovation-driven in 2009.
  - In 2010, WEF downgraded Turkey to efficiency-driven.
- Upgrade to an innovation-driven economy? Delayed reforms
  - Tax system, education, judiciary, public administration -- ecosystem
- Risk: no-reform political climate
  - The period ahead will be even less conducive for reforms: elections in 2011, 2012, 2013, 2014, 2015 ....

# Conclusions and takeaways...

- Turkey has a lot to offer for the policy debate in Egypt
  - lot of “experience” to share. So many mistakes.
- We are yet to see the adoption of a new growth strategy, with a strong reform focus
  - Risk is obvious: middle income trap. Stuck in between two worlds...
    - Hard time converging to US and EU income level.
    - Hard time competing with low-cost East Asian producers
- Easier for Egypt to attract capital by focusing on policy reforms. Turkey's experiment is a good case.
  - Harder for Turkey to do the jump. Continue the growth process in its old pace – most likely scenario...