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The Economic Policy Research Foundation of Turkey

Strengthening the Connectivity and Business Synergies in the SEE

Session Three

Business Opportunties

Sarajevo, July 21, 2015

Hypotheses we're working on:

Which business models could be more feasible?

Model 1

GVC integration.

- Similar to what happened in comparable transition economies / New EU member states.
- Industrial decentralization from Istanbul and its hinterland (relocation)
- Flying Geese Paradigm.
- Subcontracting
- Outsourcing

Model 1a
Access to raw material

Model 1b
Access to EU markets

Model 1c
Capability or asset driven.

Model 1d
Going global / internally driven

Model 2

Trilateral cooperations

- Italy-Turkey-Albania
- Germany-Turkey-Kosovo*
- Other?

Model 3

Business services

- ICT, BPoutsourcing
- Product development & commercialization
- Turkish market as a testing ground for SEE developers

Model 5

Tapping into existing trade routes

- Turkey-Germany trade
- 190.000 trucks in 2014

Model 4

JVs for third markets.

- Russia and MENA
- Low hanging fruits from trade

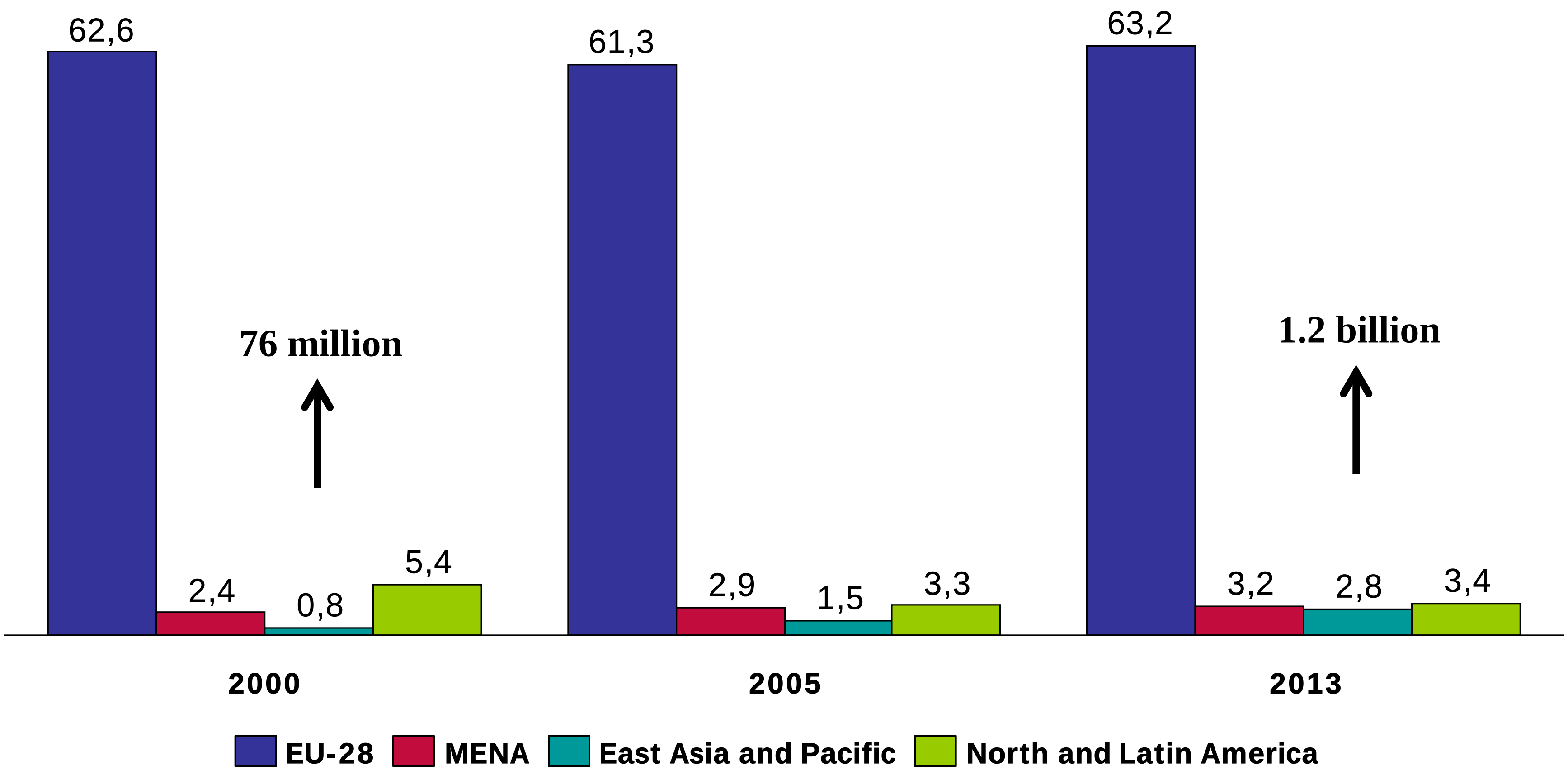
PE/VC

Energy, constructin etc.

SEE's export destinations

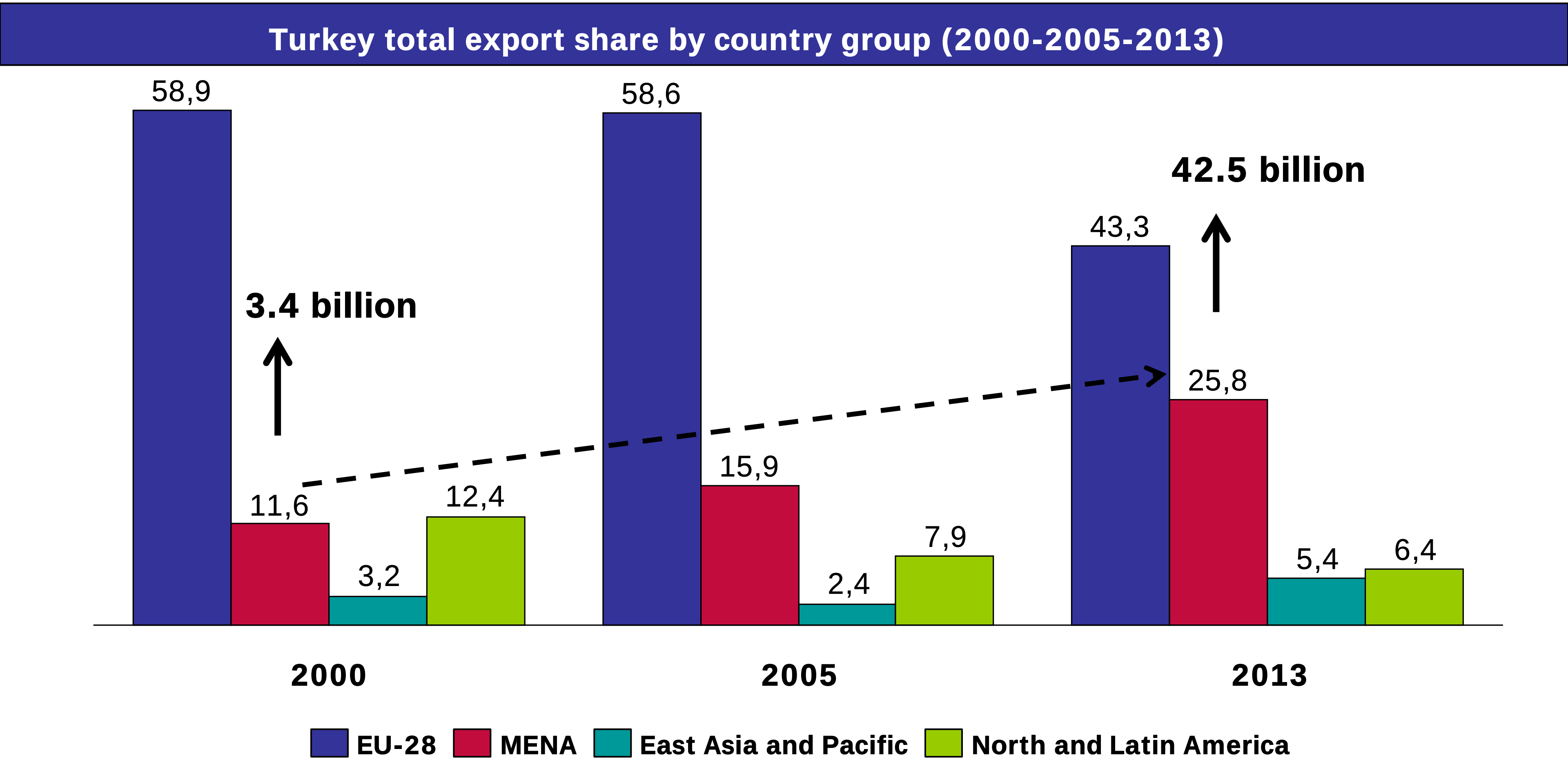
Significant reliance on the EU market

SEE Total Export share by country group (2000-2005-2013)



Source: BACI ,Tepav Calculations

Can Turkey be SEE-6’s gateway to MENA?



Source: BACI ,TEPAV calculations

Hypotheses we're working on:

Which business models could be more feasible?

Model 1

GVC integration.

- Similar to what happened in comparable transition economies / New EU member states.
- Industrial decentralization from Istanbul and its hinterland (relocation)
- Flying Geese Paradigm.
- Conditional on investment climate reforms. Cost & quality of doing business

Model 1a
Access to raw material

Model 1b
Access to EU markets

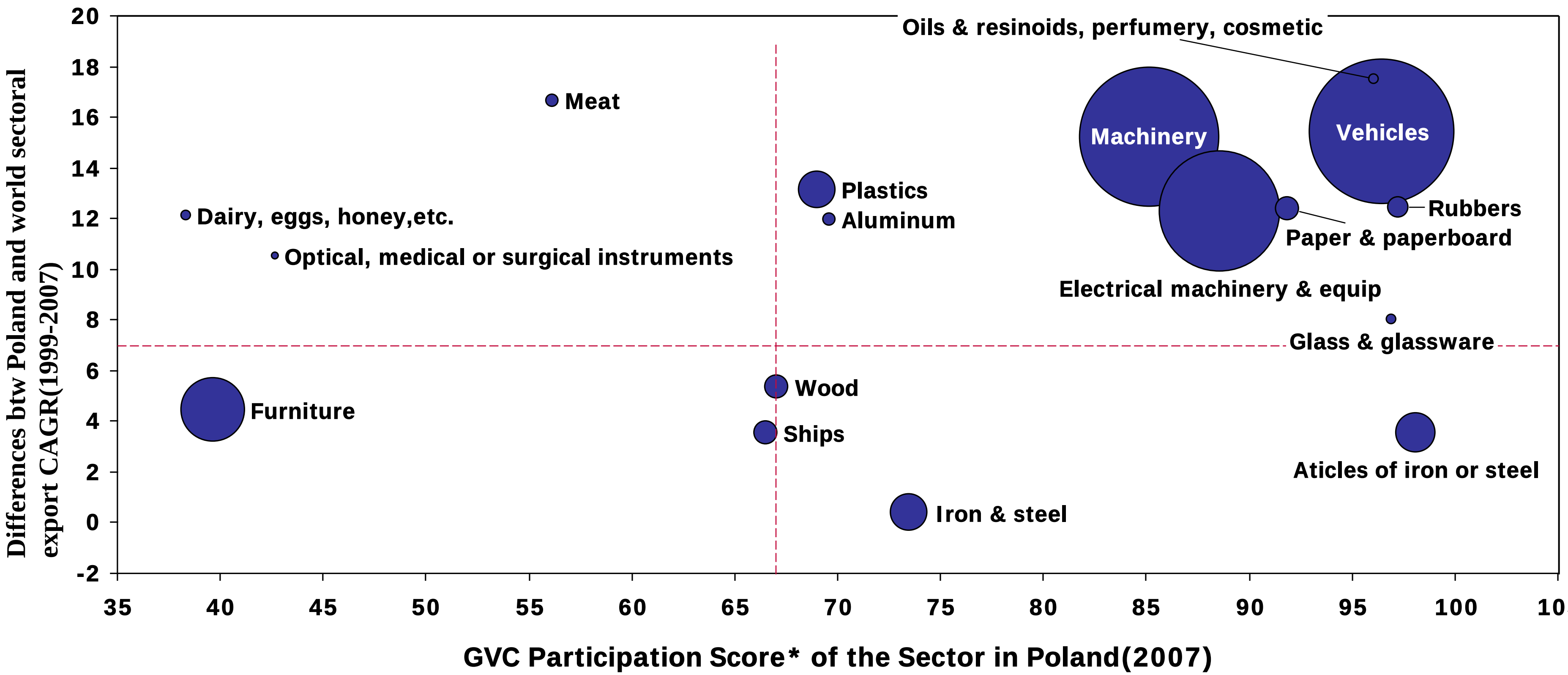
Model 1c
Capability or asset driven.

Model 1d
Going global / internally driven

A GVC integration case: Poland

Any lessons / implications for SEE's future?

GVC participaiton and growth rates of sectors in Poland (1999-2007)



* We use Grubel Lyold Index as a proxy for global value chain (GVC) participation
Note: Bubble sizes (diameter sizes) represent Poland's export in the sector in 2007.
Selection filters: For these sectors, growth rate of the sectoral export in Poland is more than sector's world export growth between 1999 and 2007. In 2007, Poland exports more than 1 billion US $ in the sector .

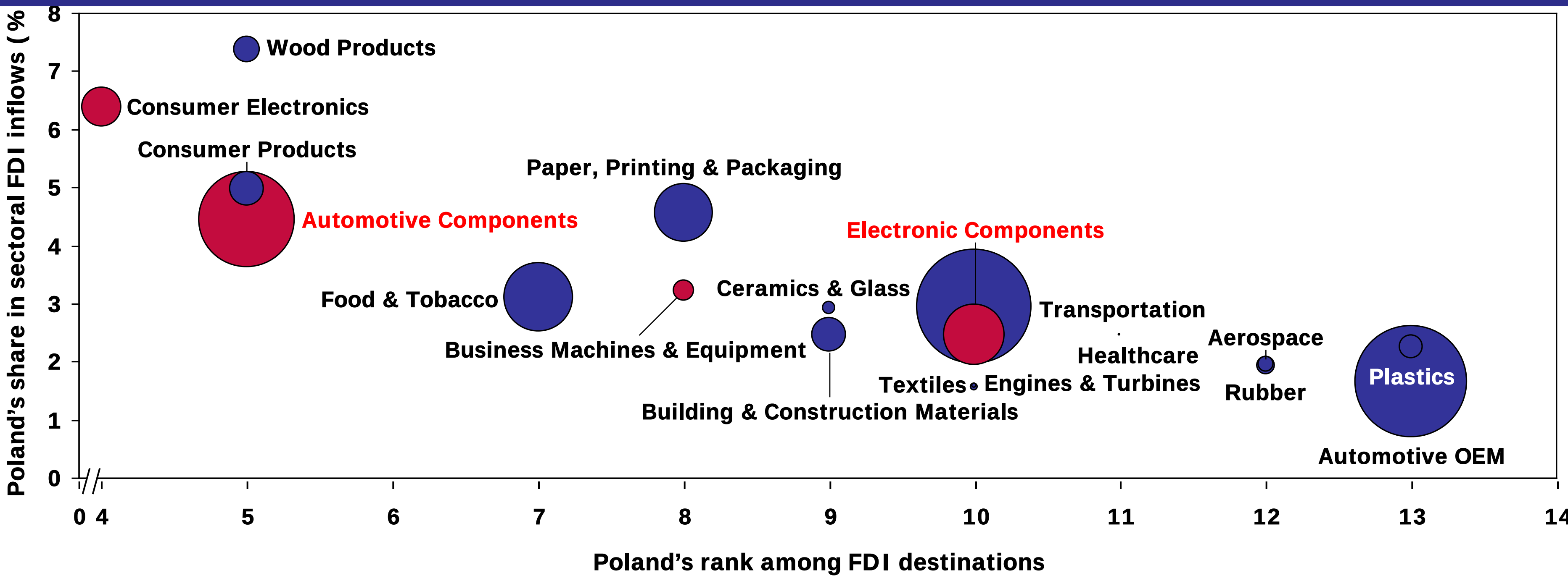
Source: BACI, TEPAV calculations

Poland case con’t.

Structural transformation mostly driven by FDI inflows

- Poland is the 16th demanded destination according to FDI inflow sizes with 145 billion US $ between 2003 and 2014 (1.6% global share)
- However, for some sectors Poland has become a global attraction center.

Poland’s FDI inflows by sectors* (2003-2014)

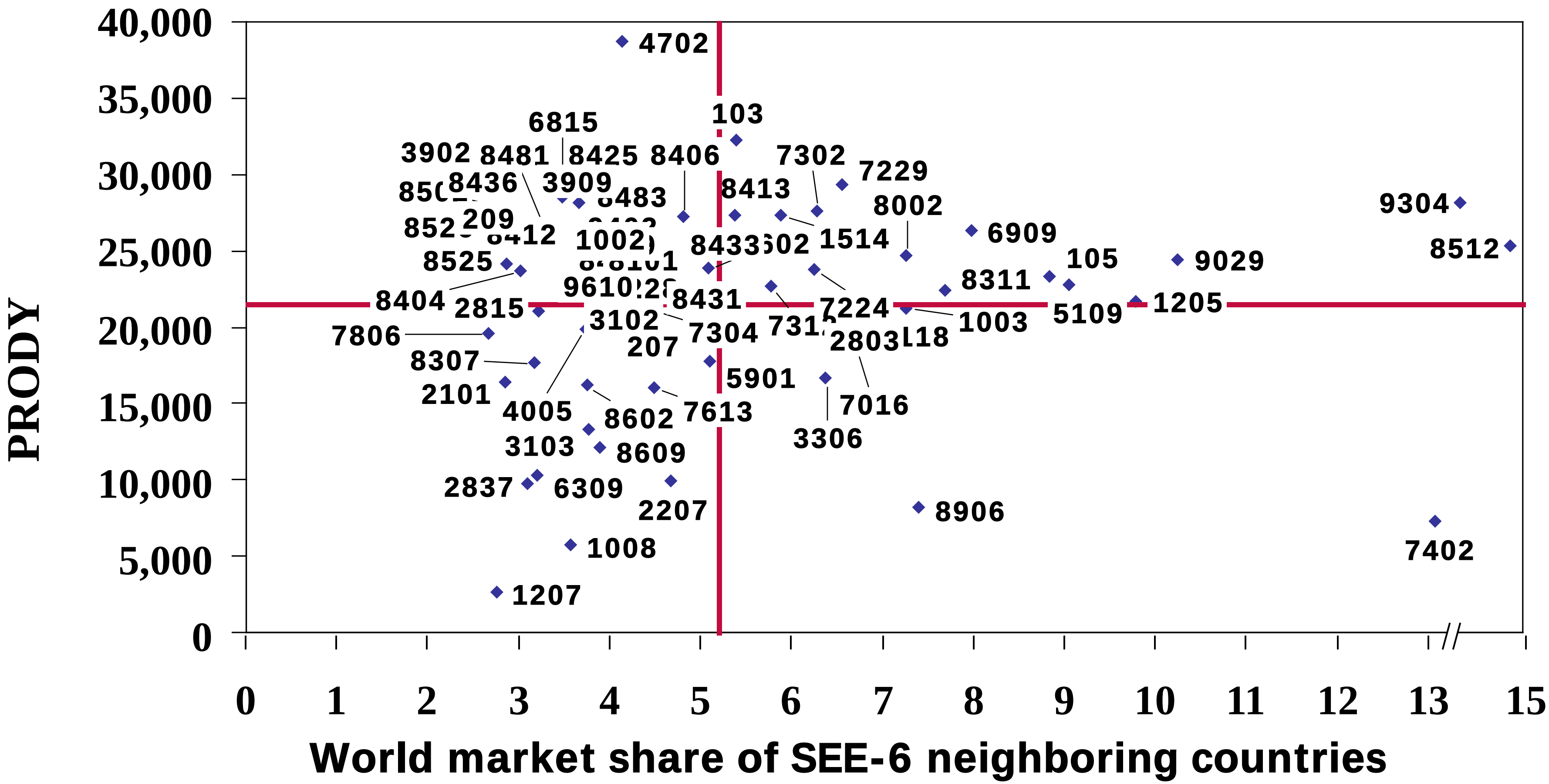


Note: Bubble sizes (diameter sizes) represent Poland’s cumulative sectoral FDI inflows (2003-2014).

Source: FDI Markets, TEPAV calculations

*** Filters: Sectoral FDI inflow share is greater than total share of Poland’s, and real estate is excluded.**

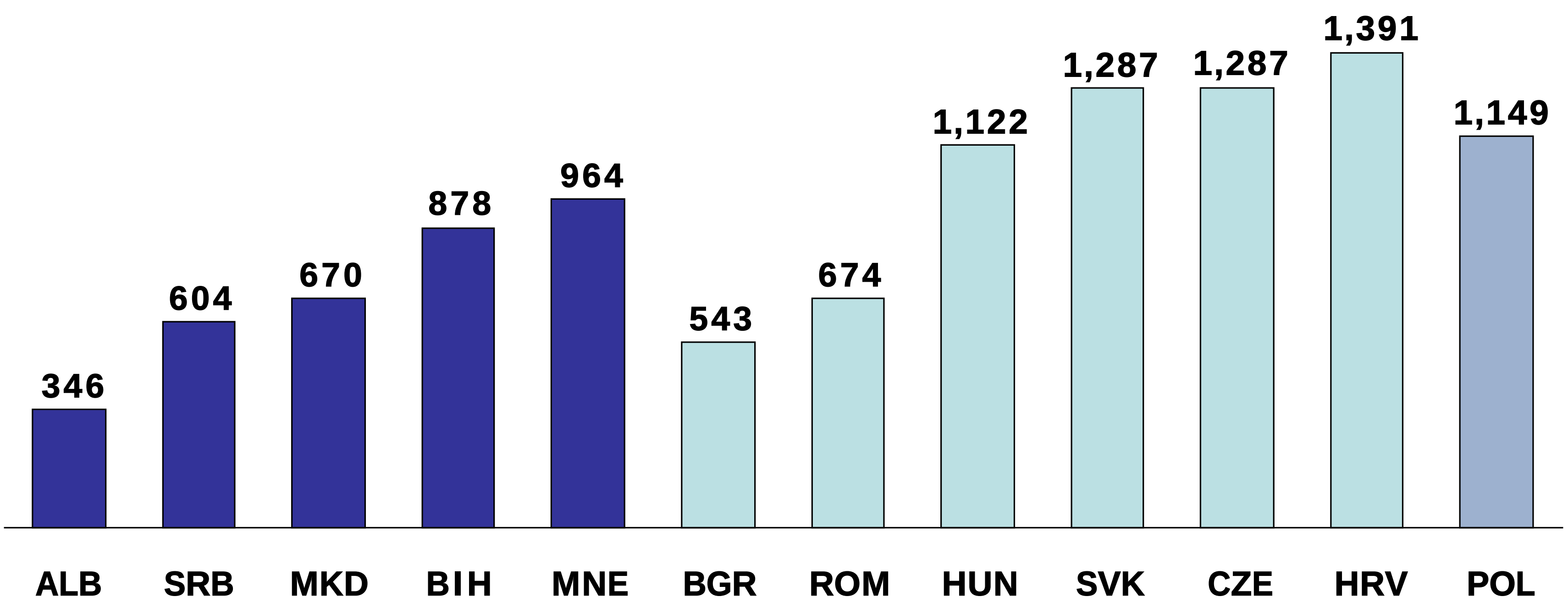
Areas of potential economic integration and capability spillovers from neighbor countries* to SEE-6's



*Neighbor of SEE-6 includes Croatia, Bulgaria, Czech Republic, Hungary, Romania, Slovakia and Slovenia.
Filters: Countries in the neighborhood of SEE-6 are significant exporters as region (RCA ≥ 1), SEE-6 region does not have same significance as exporter (RCA ≤ 1),
Trade volume of the product is growing more than the average (CAGR of the product ≥ CAGR of the world export).
Source: BACI, WDI, TEPAV calculations

Time for the neighborhood to move up, and SEE-6 to take over?

Gross Average Monthly Wages (US $) (2013)



Note: Latest available data for Serbia and Albania are respectively 2010 and 2012.

Source: United Nations Economic Comission for Europe (UNECE) Statistical Database, TEPAV calculations

Hypotheses we're working on:

Which business models could be more feasible?

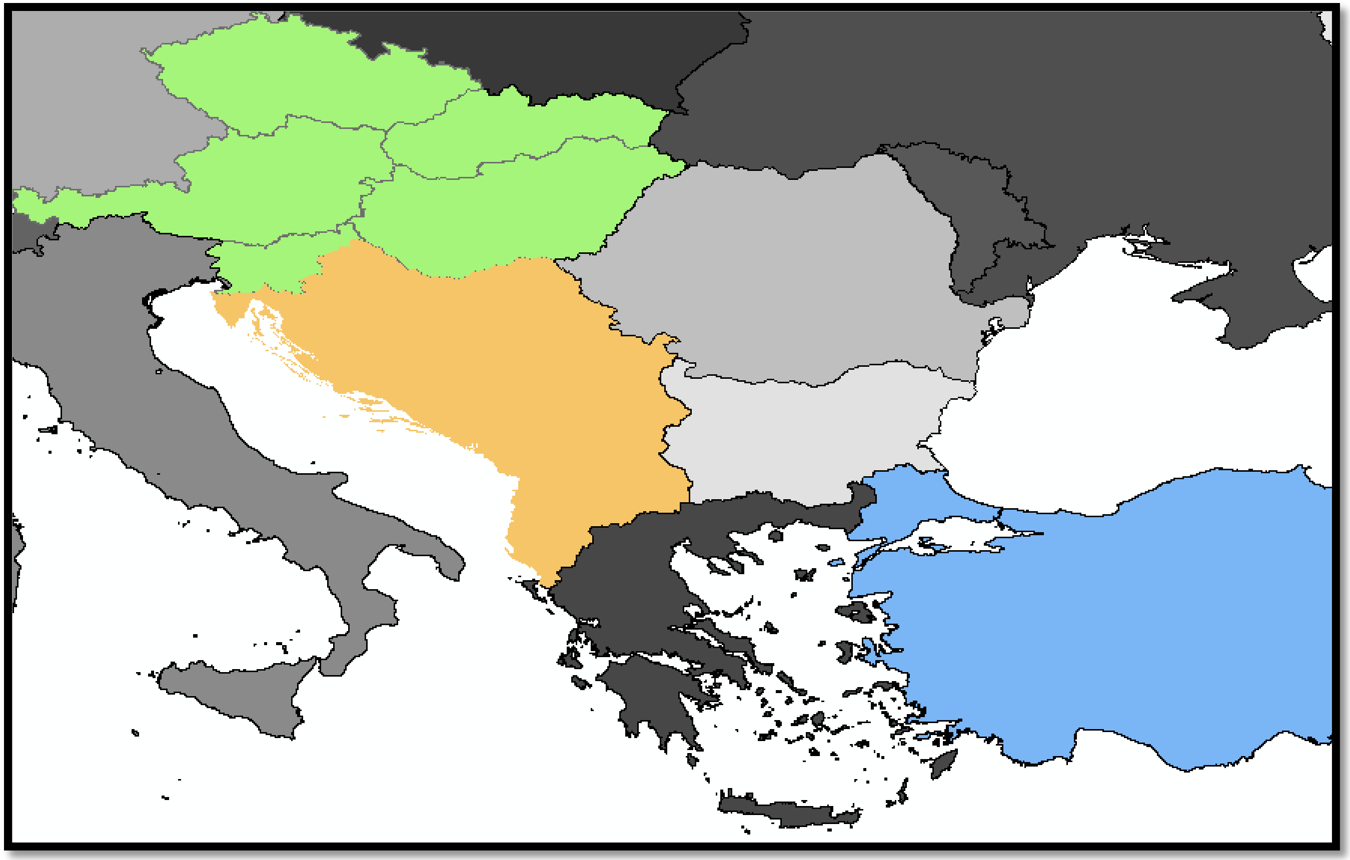
Model 5

JVs for third markets.

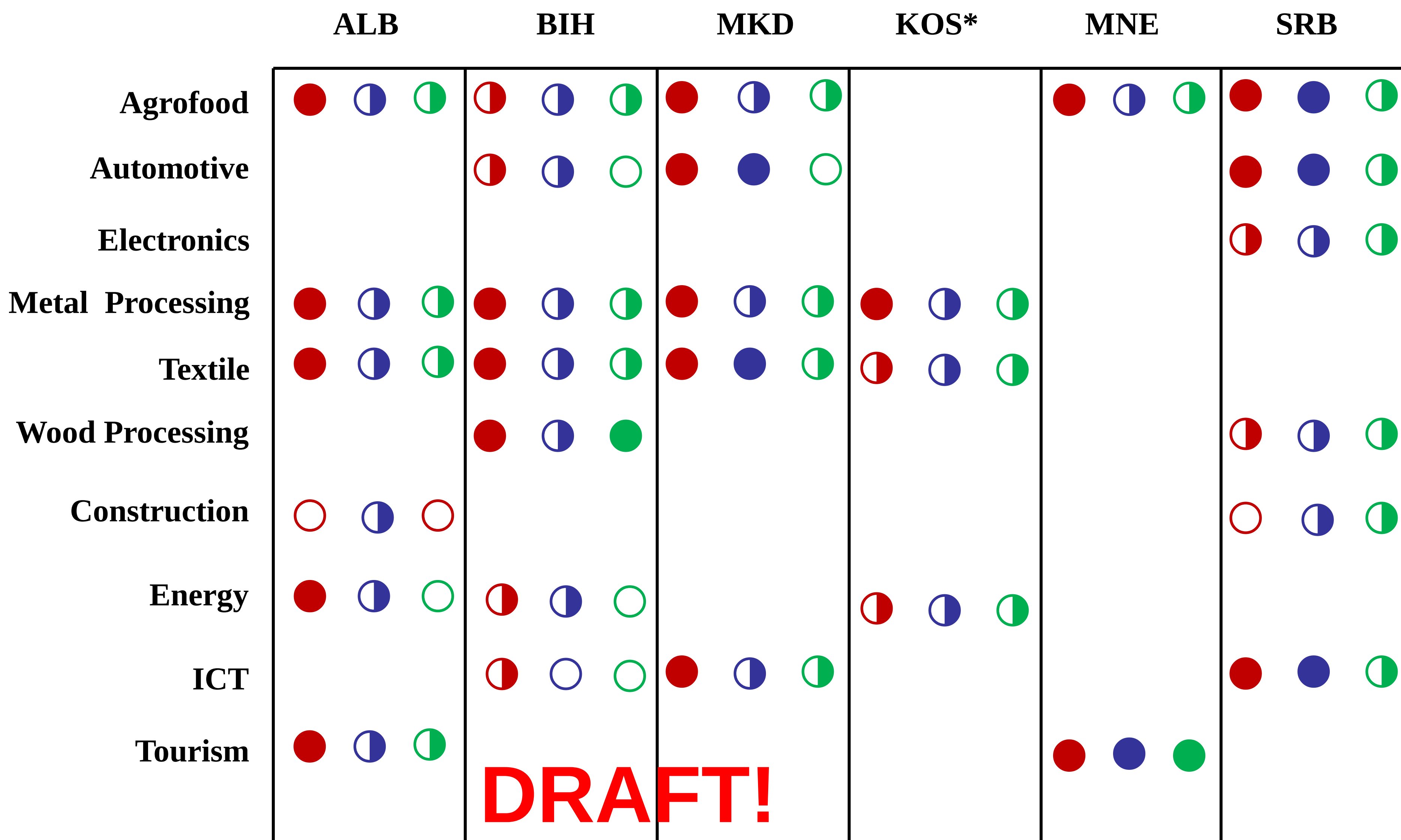
- Russia and MENA
- Low hanging fruits from trade

Can SEE-6 be Turkey's gateway to Central Europe?

Export in million USD	Slovenia	Austria	Czech Republic	Hungary	Slovakia
SEE-6	2,265	1,782	785	753	622
Turkey	460	1,489	1,111	757	506



- Government Priority
- Growth Potential
- VC Connectedness



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Strengthening the Connectivity and Business Synergies in the SEE

Session Three

Opportunity Areas

Textile

Sarajevo, July 21, 2015

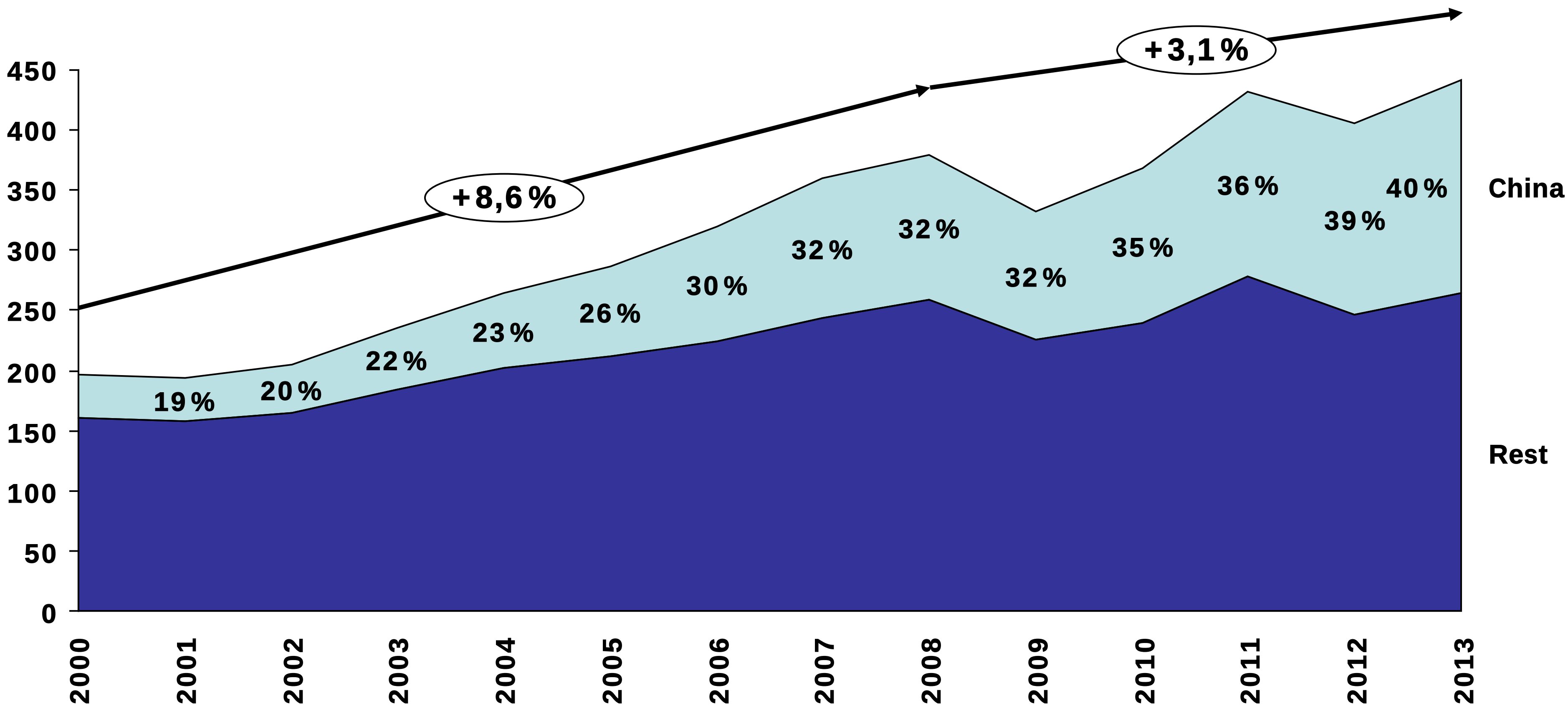
Framework

- Global trends in textile sector
- The region's competencies in textile sector
  - ➔Historical narrative
  - ➔Current trade profile
  - ➔Heavily traded sub-sectors
- Is there room for improvement?
  - ➔China: the elephant in the room?
  - ➔Potential pockets of growth
  - ➔What is SEE's level of price competitiveness?

Global textile trade trends

Even the recession could not slow down China

World textile exports, 2000-2013



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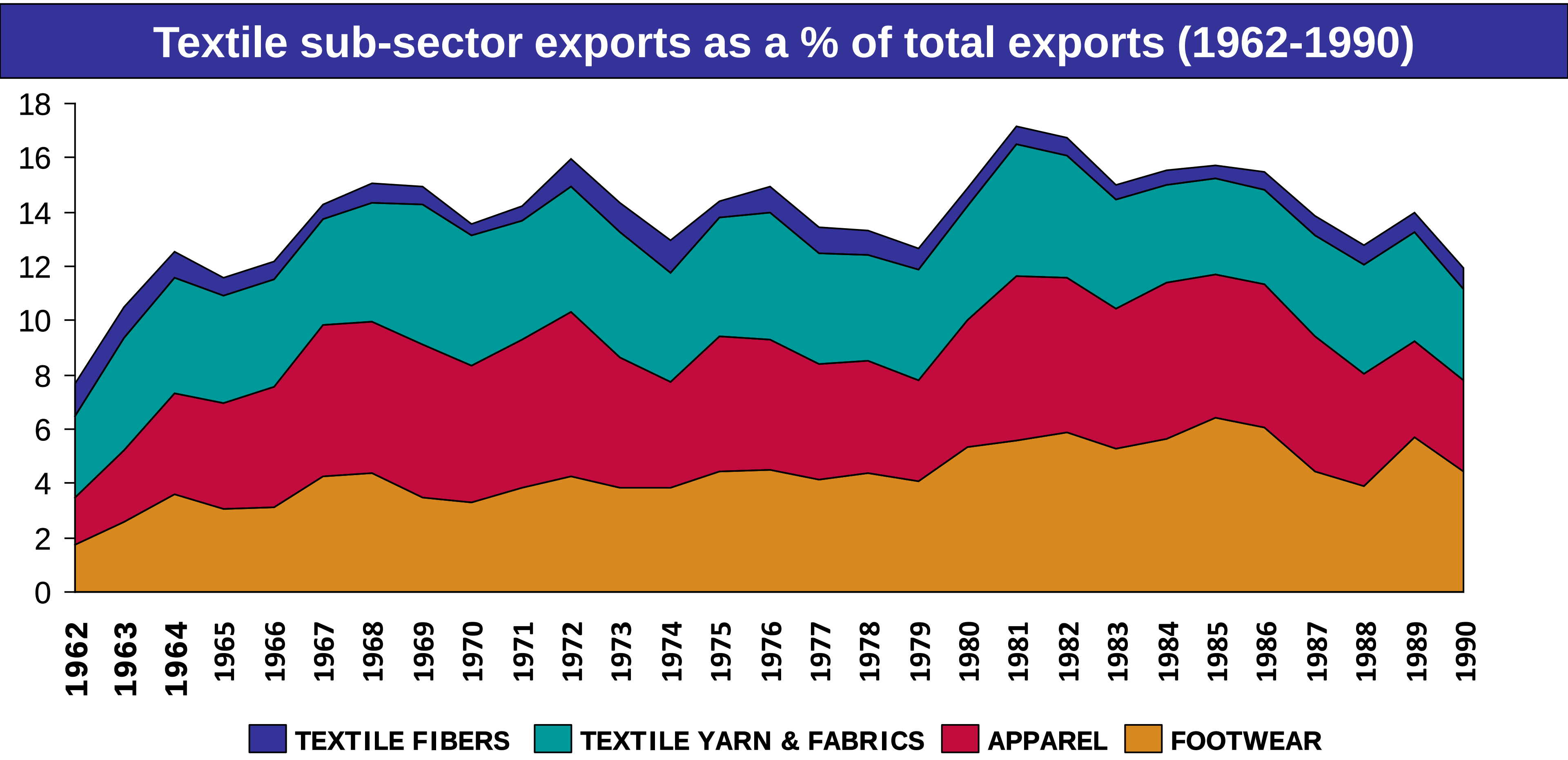
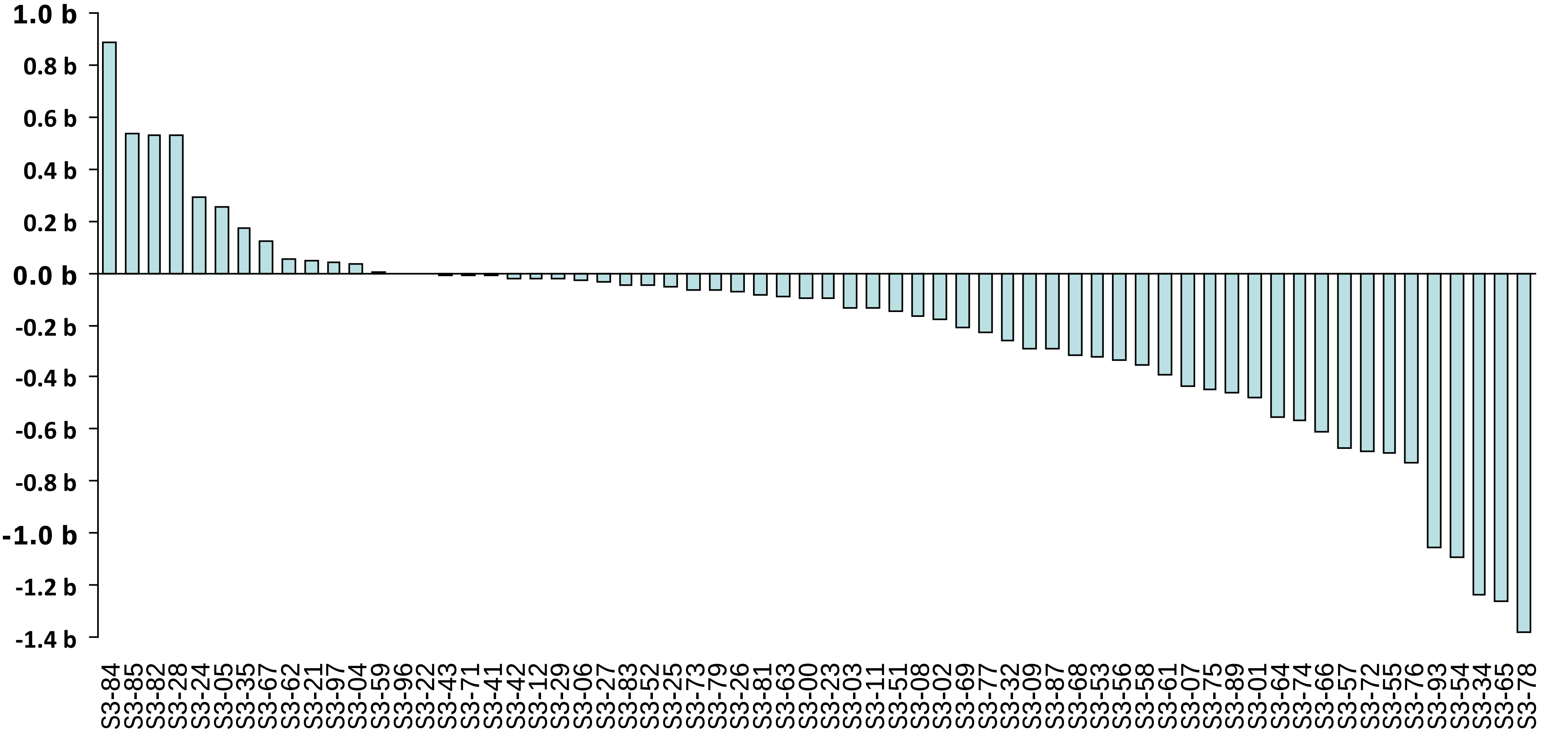
Textile was important during the Yugoslavia times as well



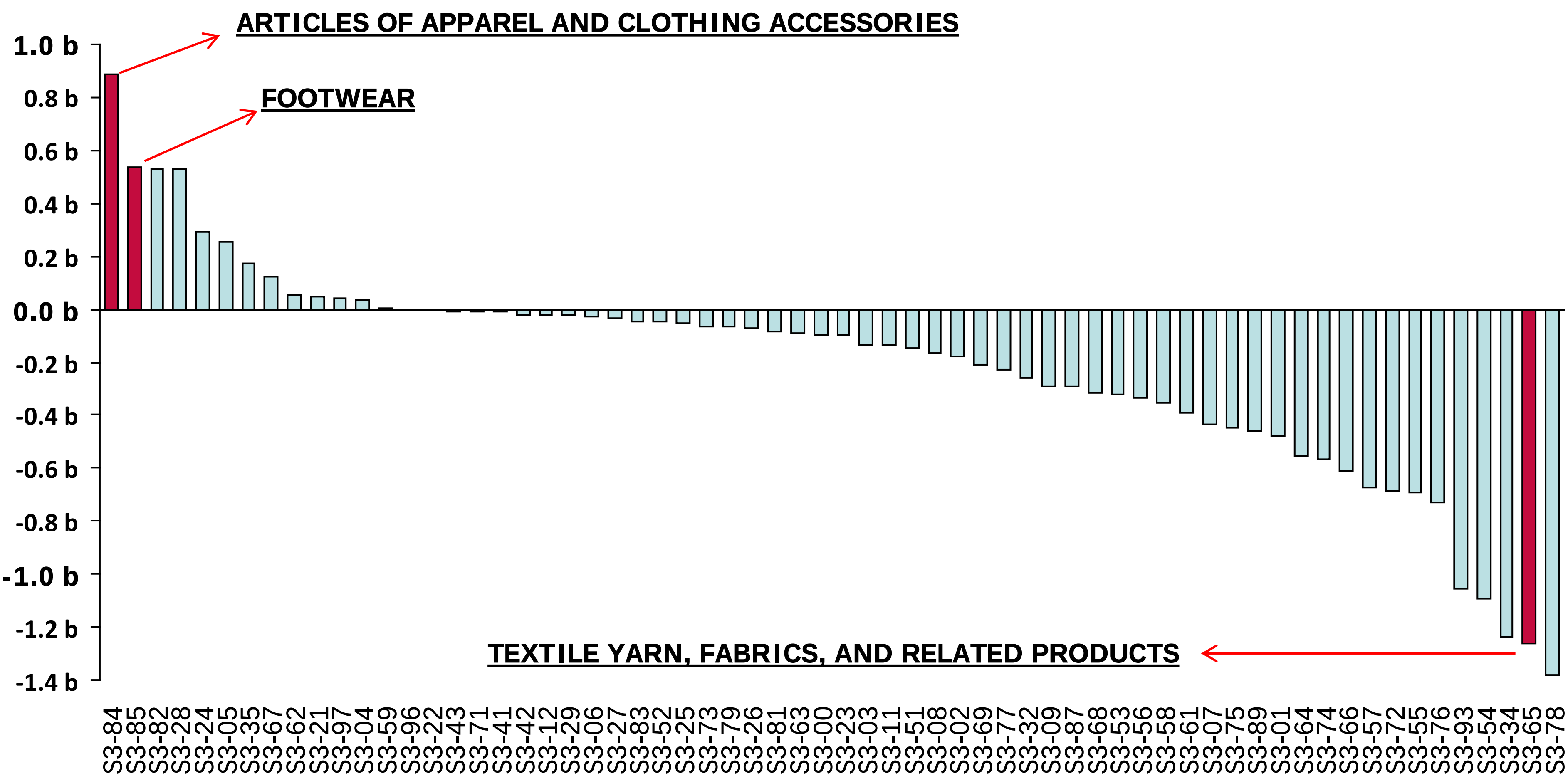
How important is textile for the region today?

SEE-6 sectoral trade balances, 2013, billion USD

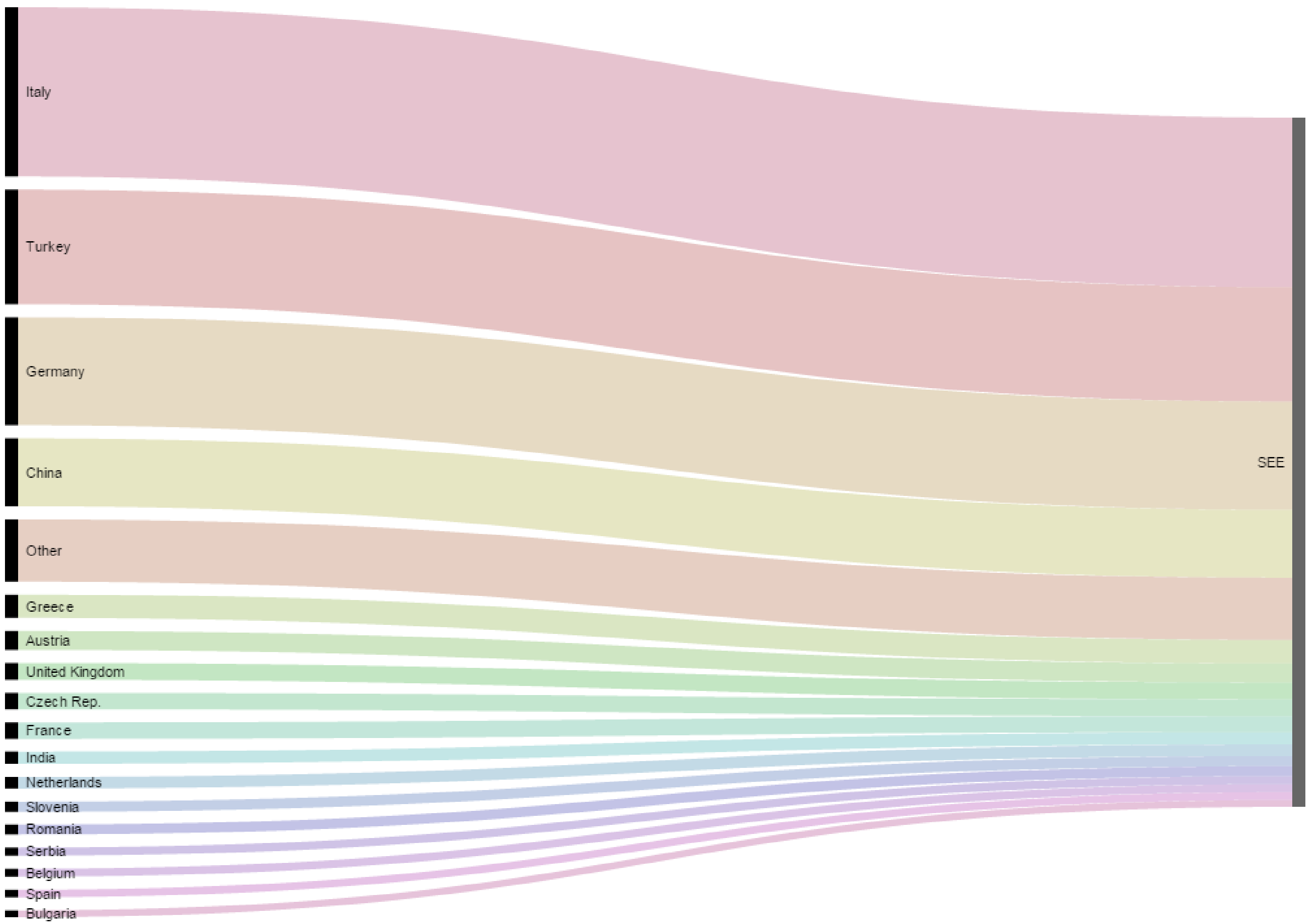


Extremely.

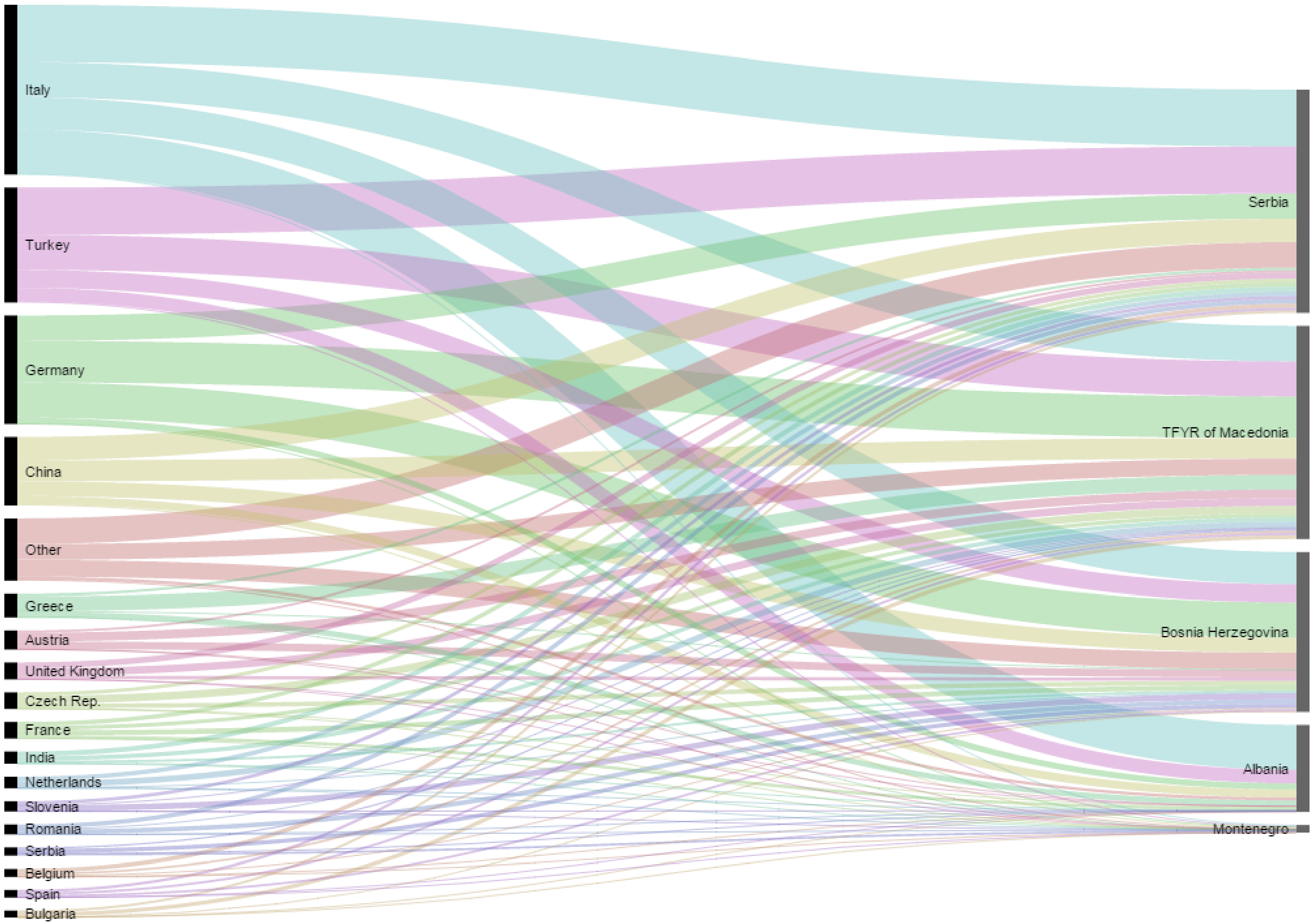
The region imports primary products, exports finished goods.



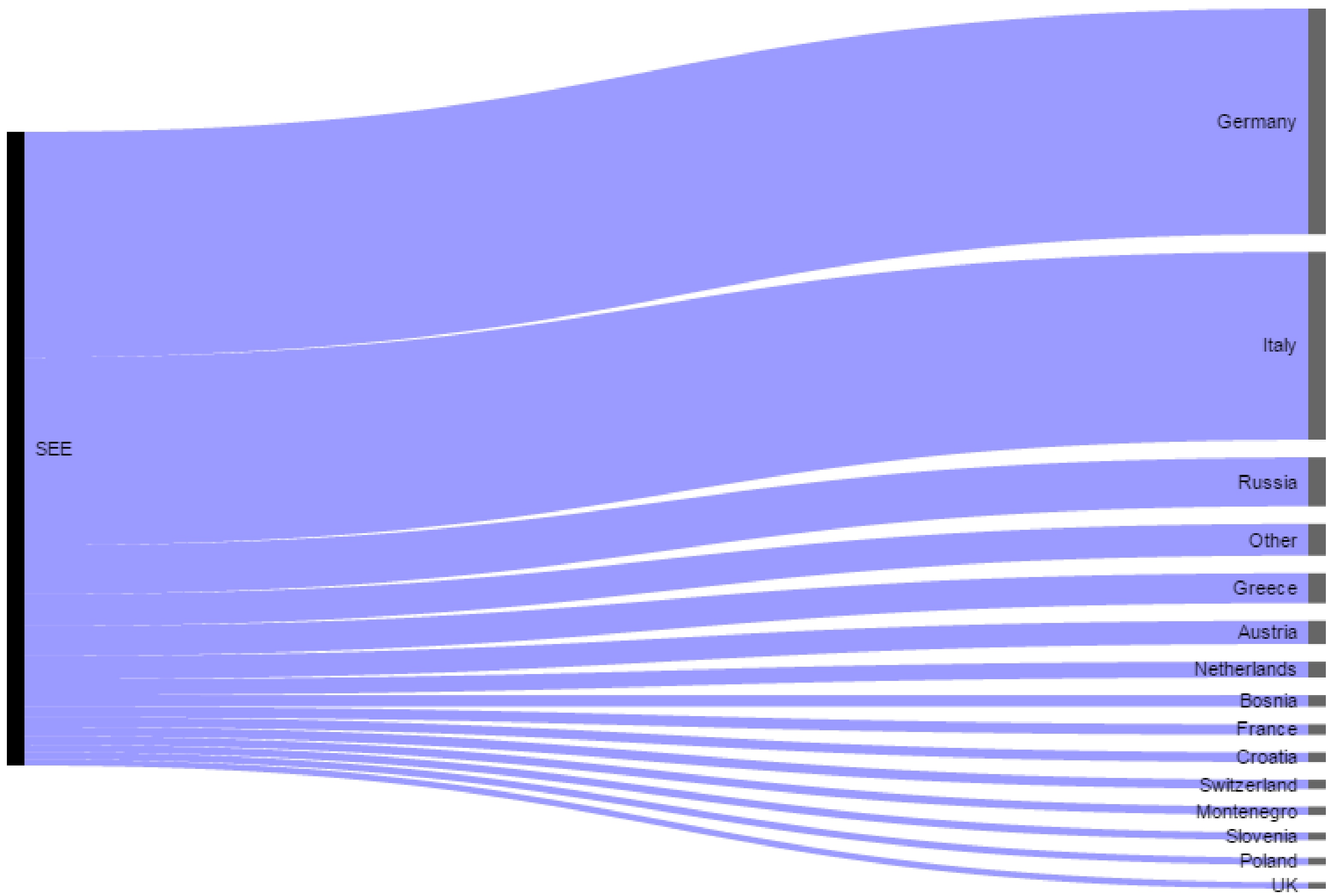
Sources of primary product imports:



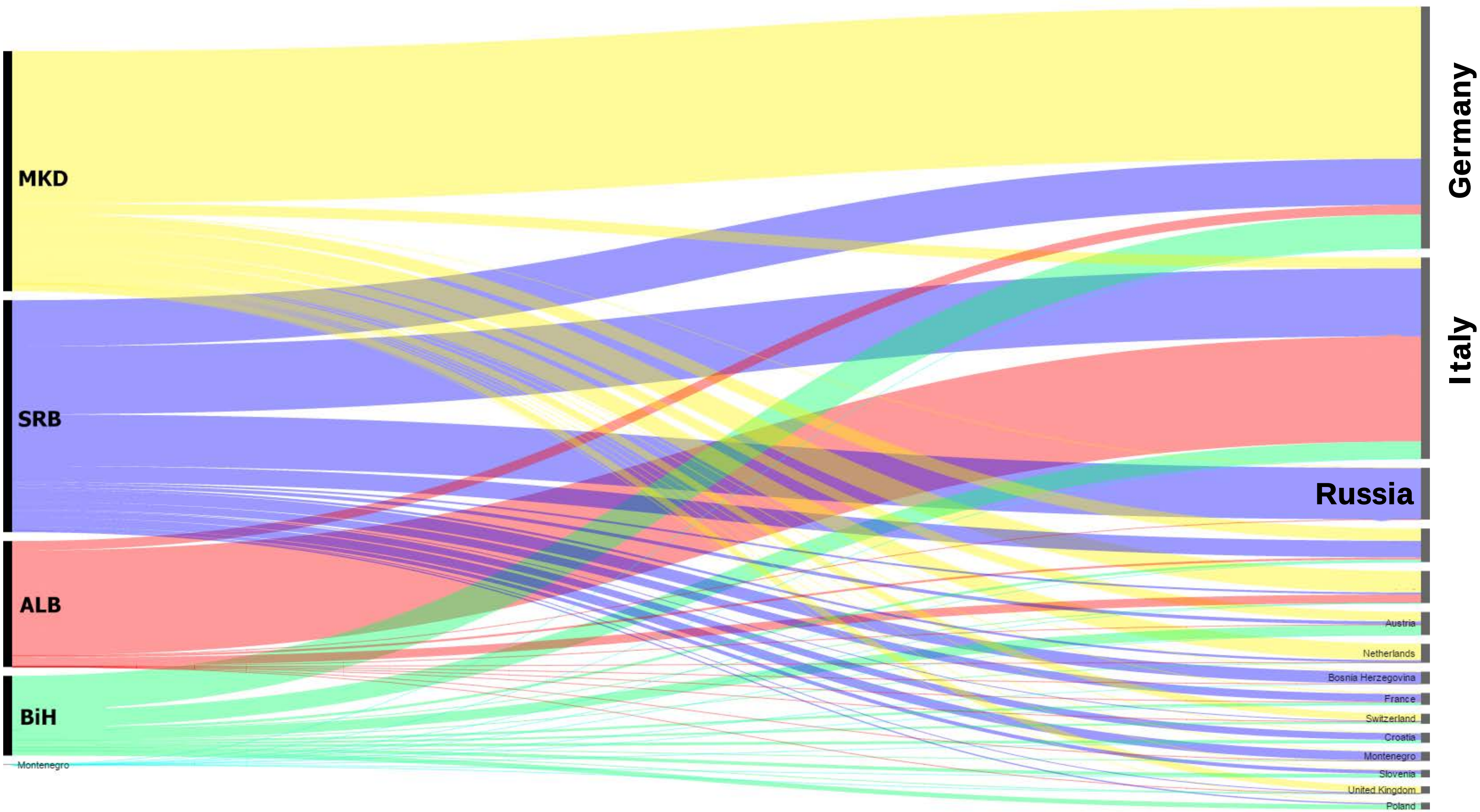
Sources of primary product imports:



Destinations of apparel exports

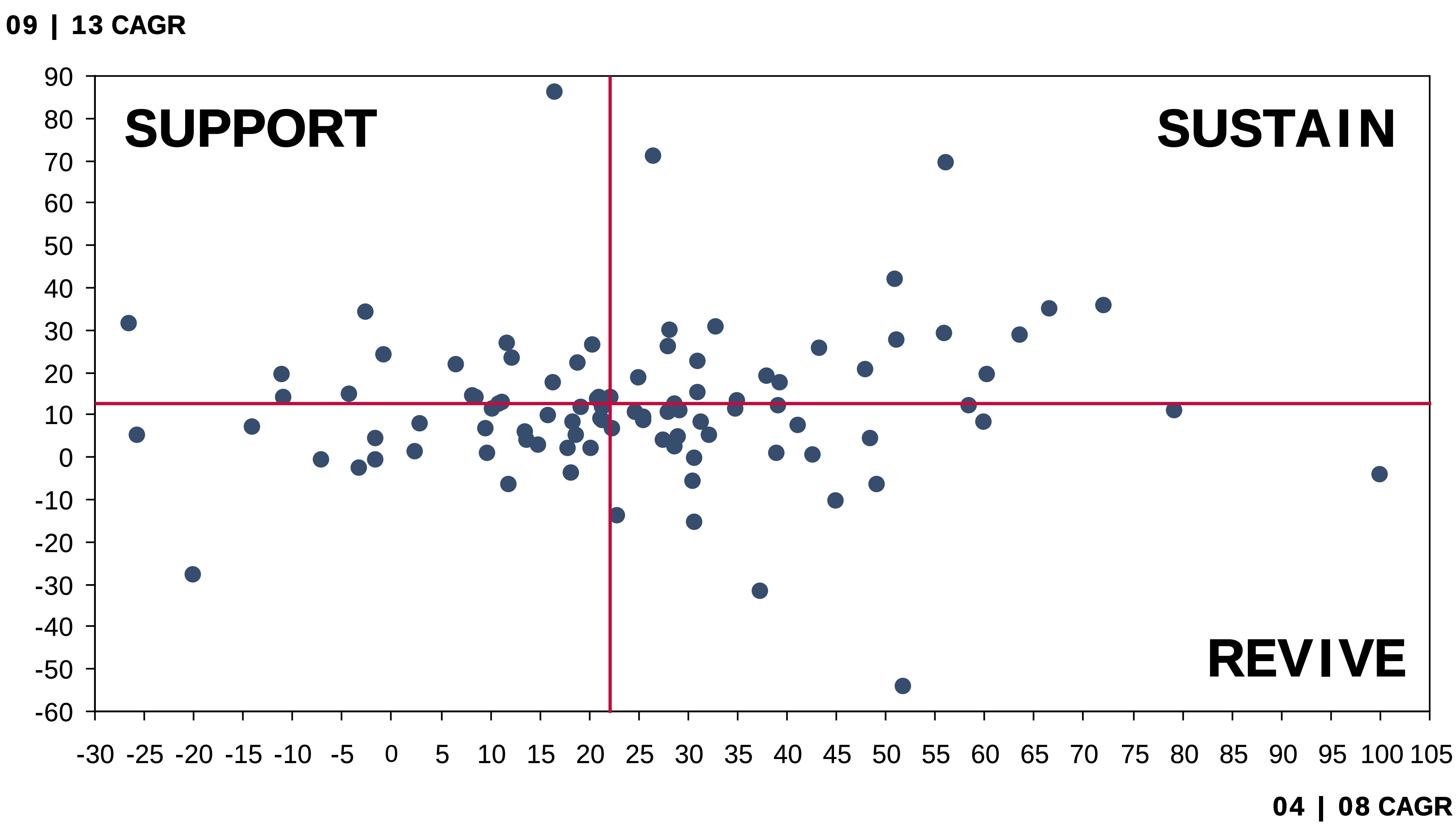


Destinations of apparel exports



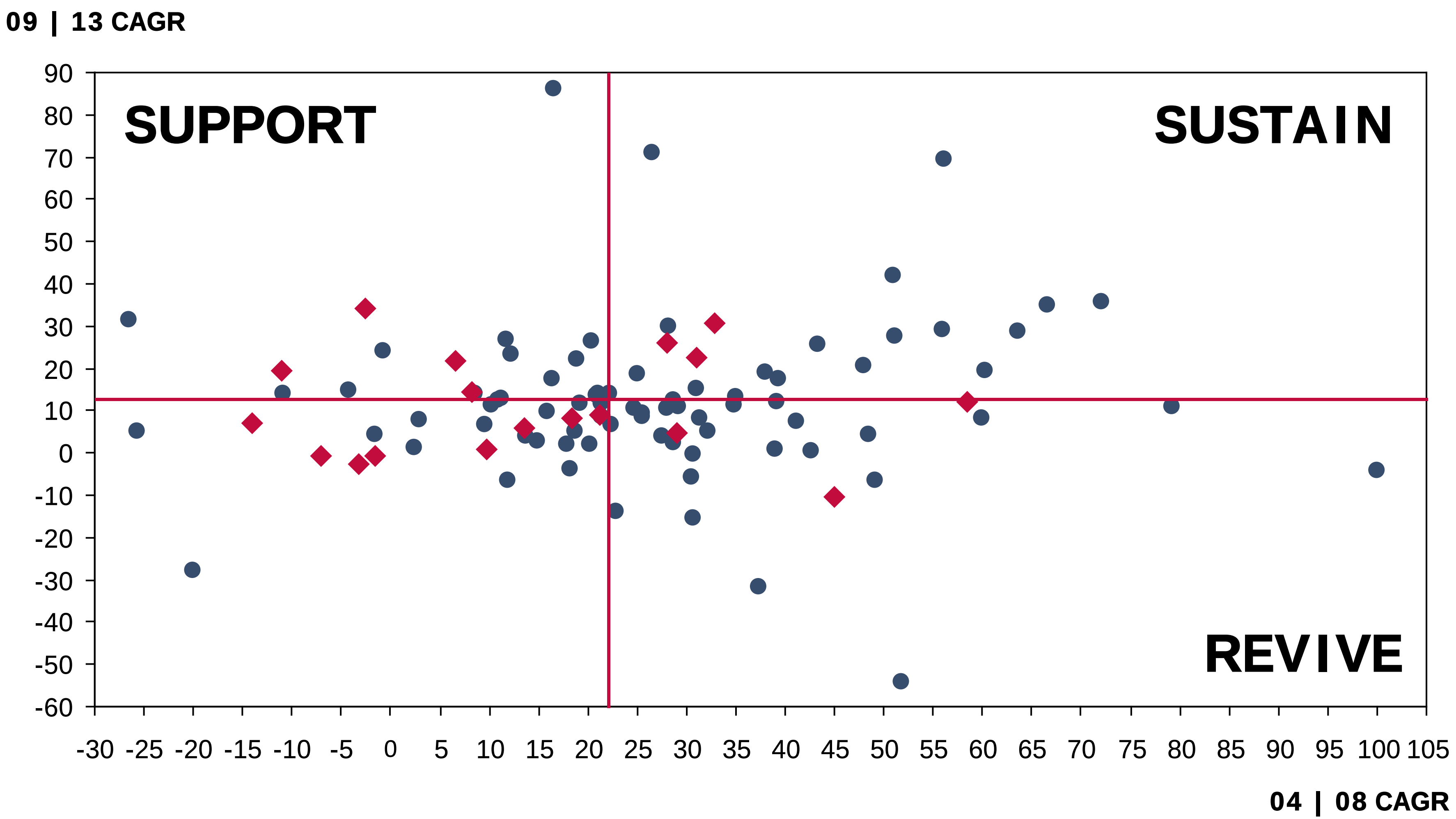
A closer look at SEE's exports

Two digits, XX products



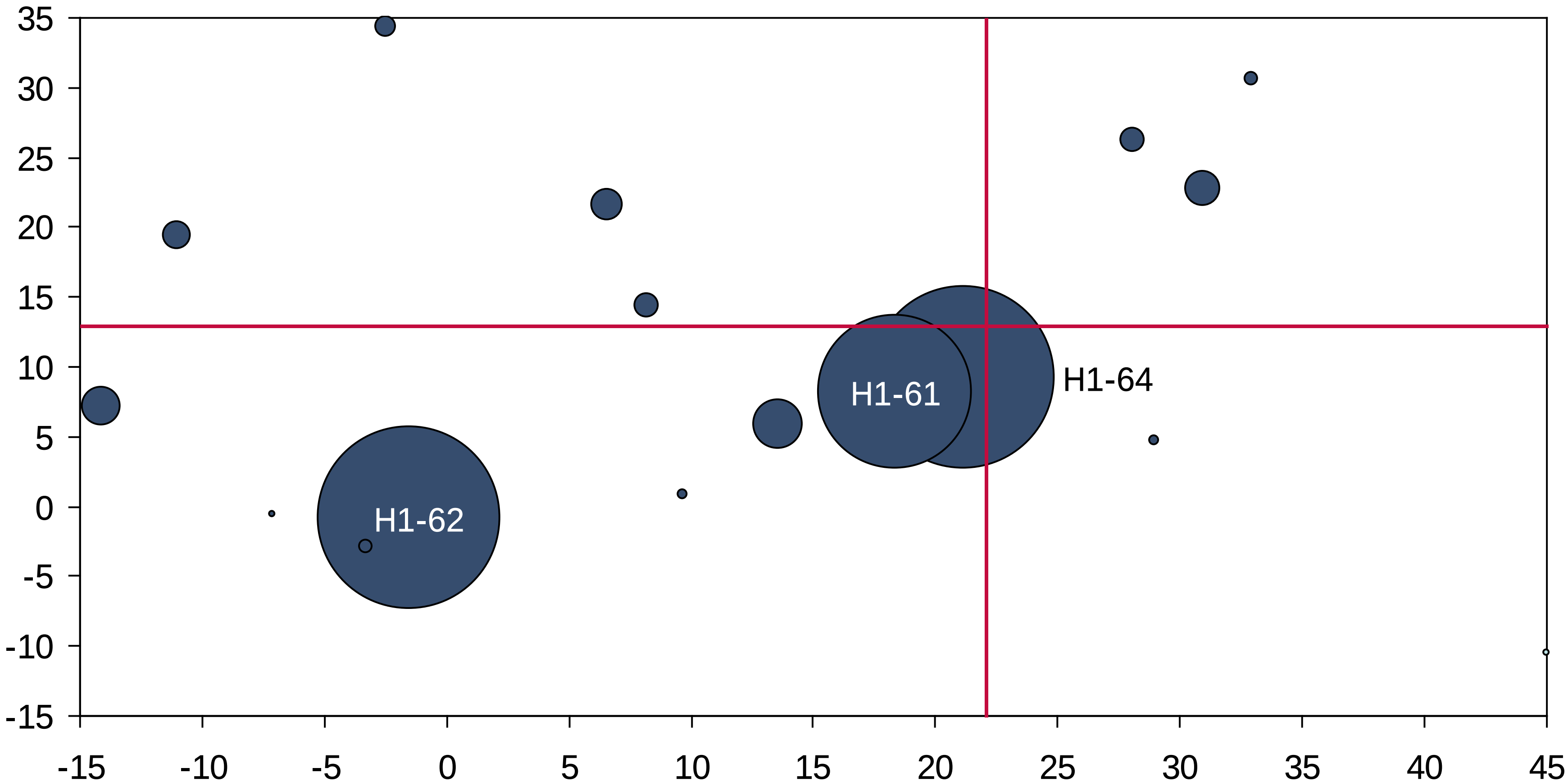
Where are textile sub-sectors?

Not clustered, varied performance.



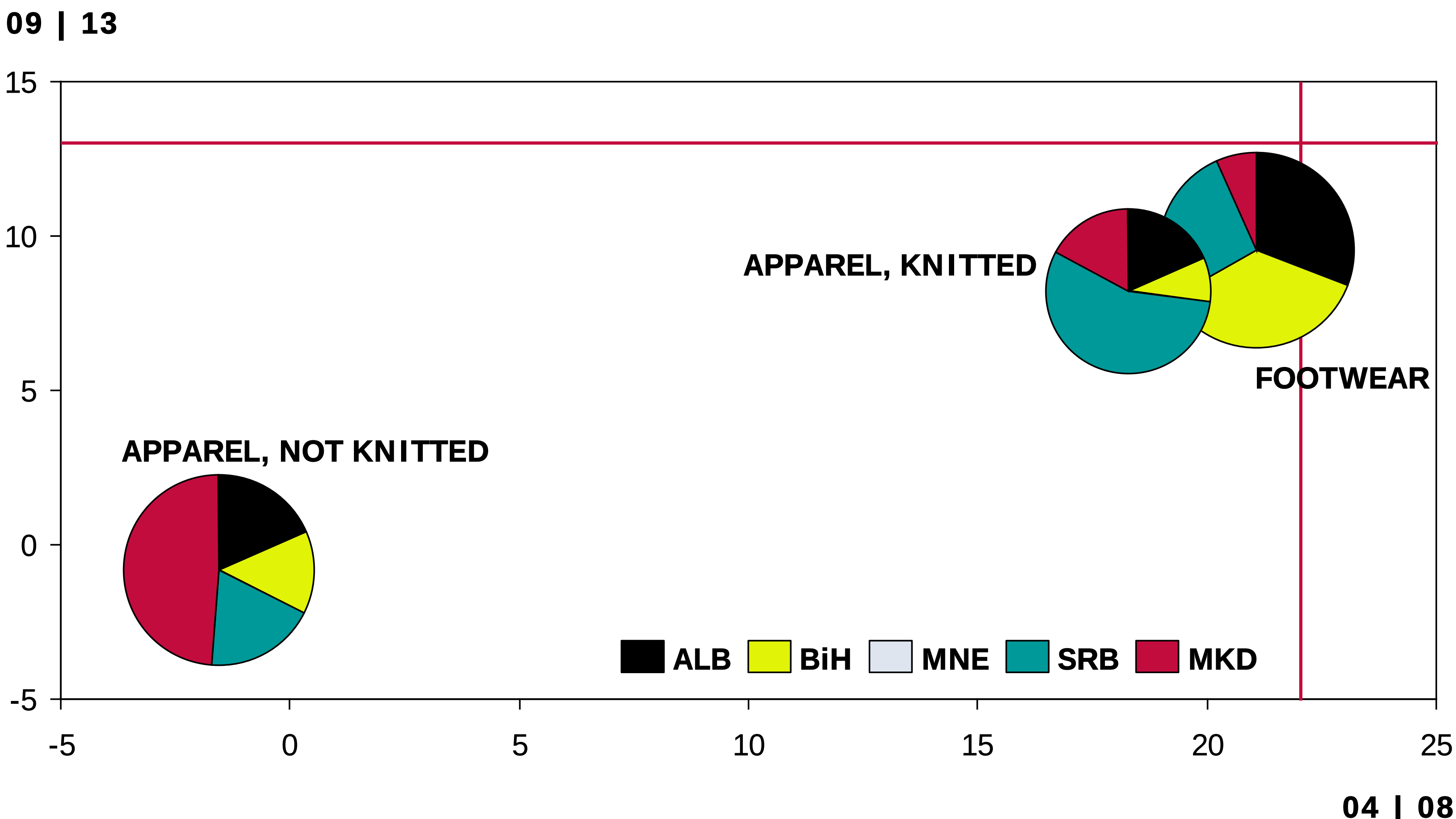
Zooming into textile sub-sectors (1)

Large sectors grow at regional average rates.



Zooming into textile sub-sectors (2)

Export breakdown of three major sub-sectors.



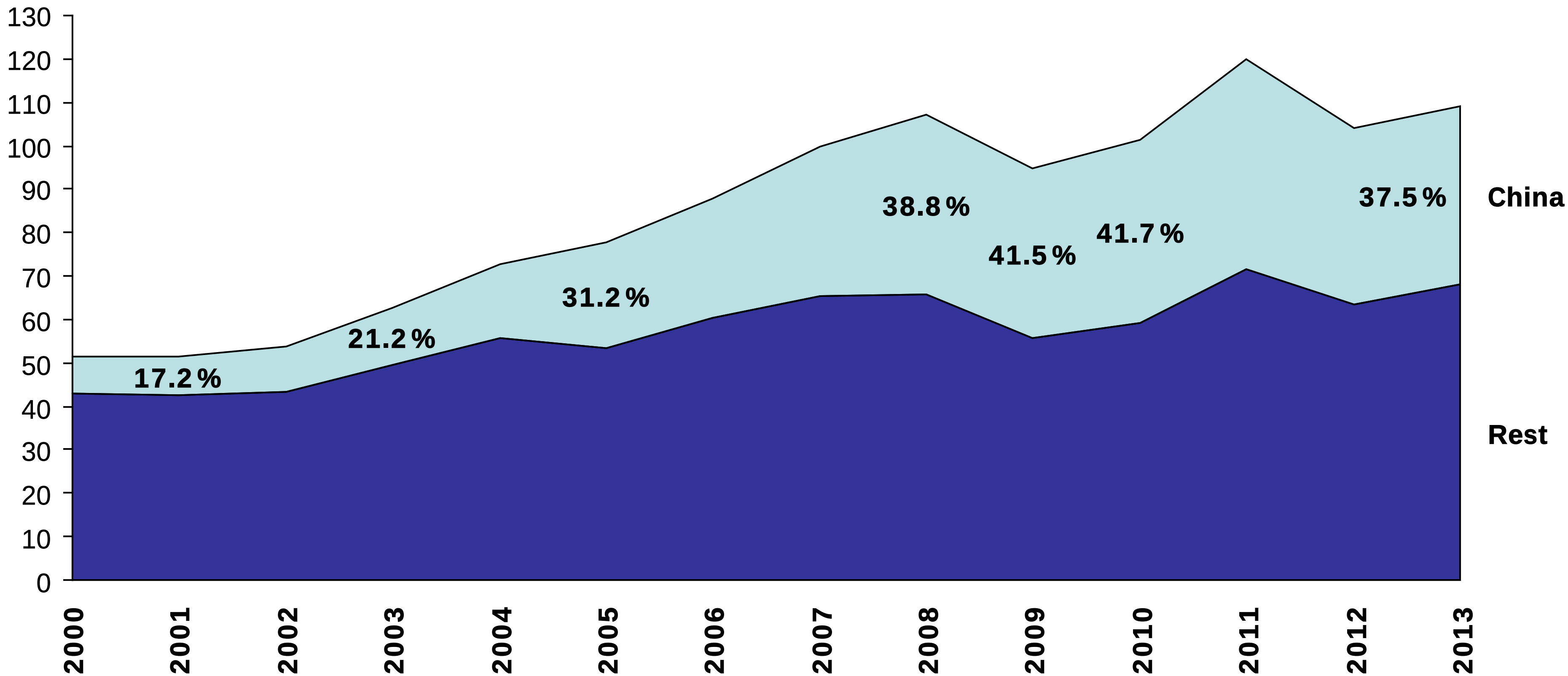
Is there room for improvement?

- Definitely.
- Albeit slowly, China’s market share in the EU-28 has been declining since 2010.
- A more nuanced analysis at product level is necessary to identify opportunities.
- SEE-6 is near some of the top apparel importers in the world, but does not utilize this to its advantage.

China's share is decreasing

Can capitalize by acting fast

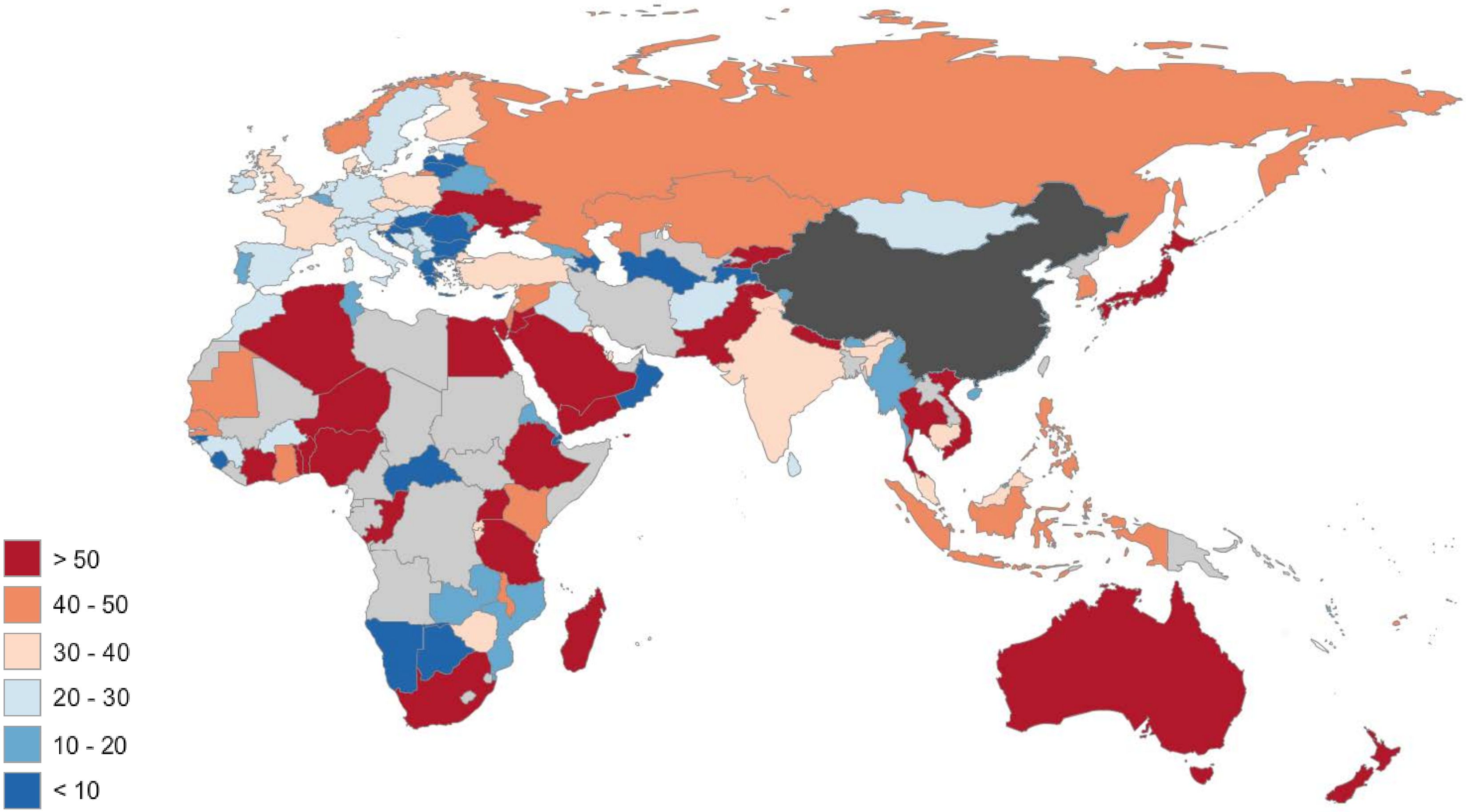
EU-28 textile imports, 2000-2013, billion USD



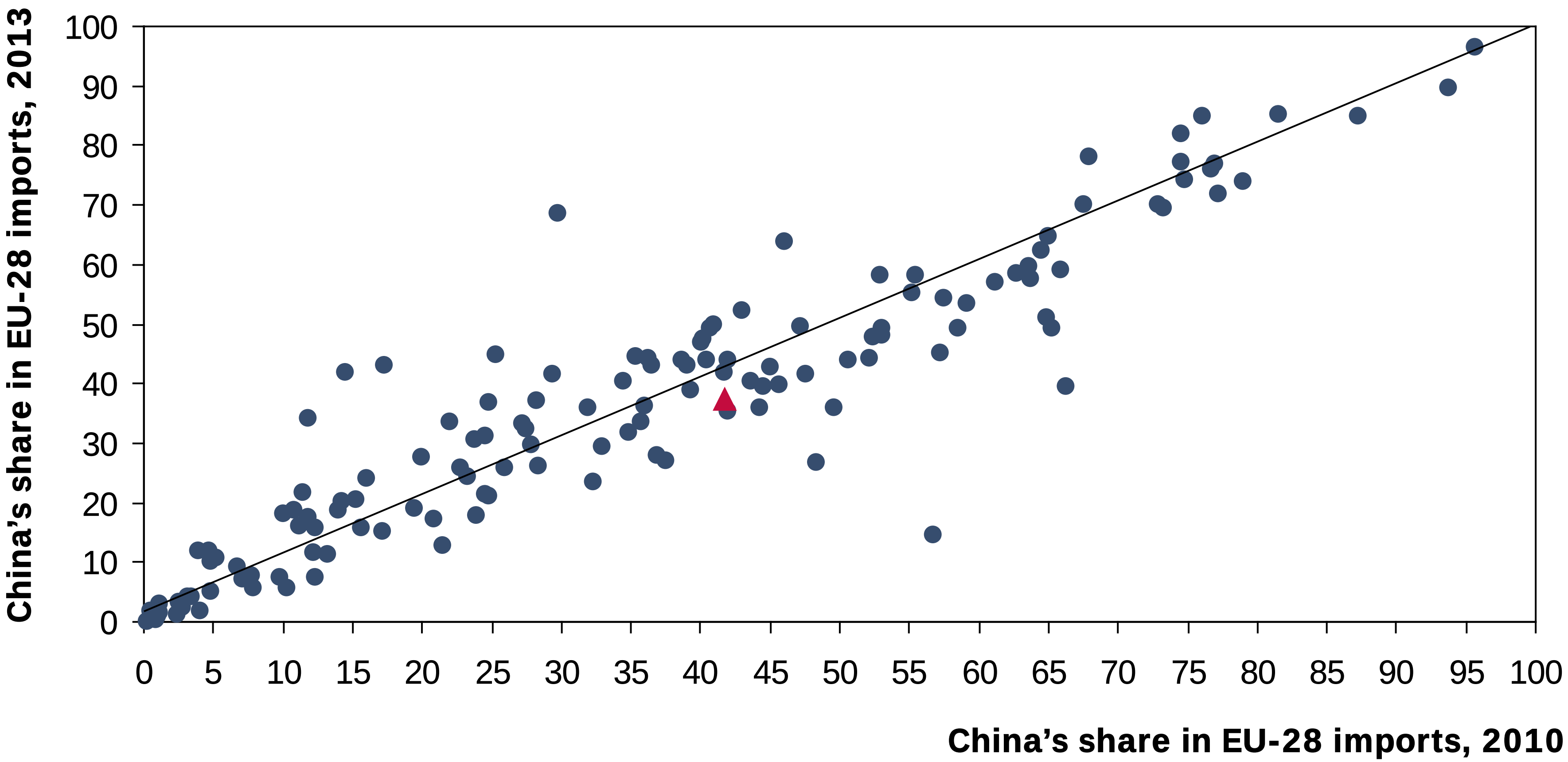
China's weight is not uniform

SEE-6's immediate surrounding is very opportune

Share of Chinese exports in countries' textile imports (2013)

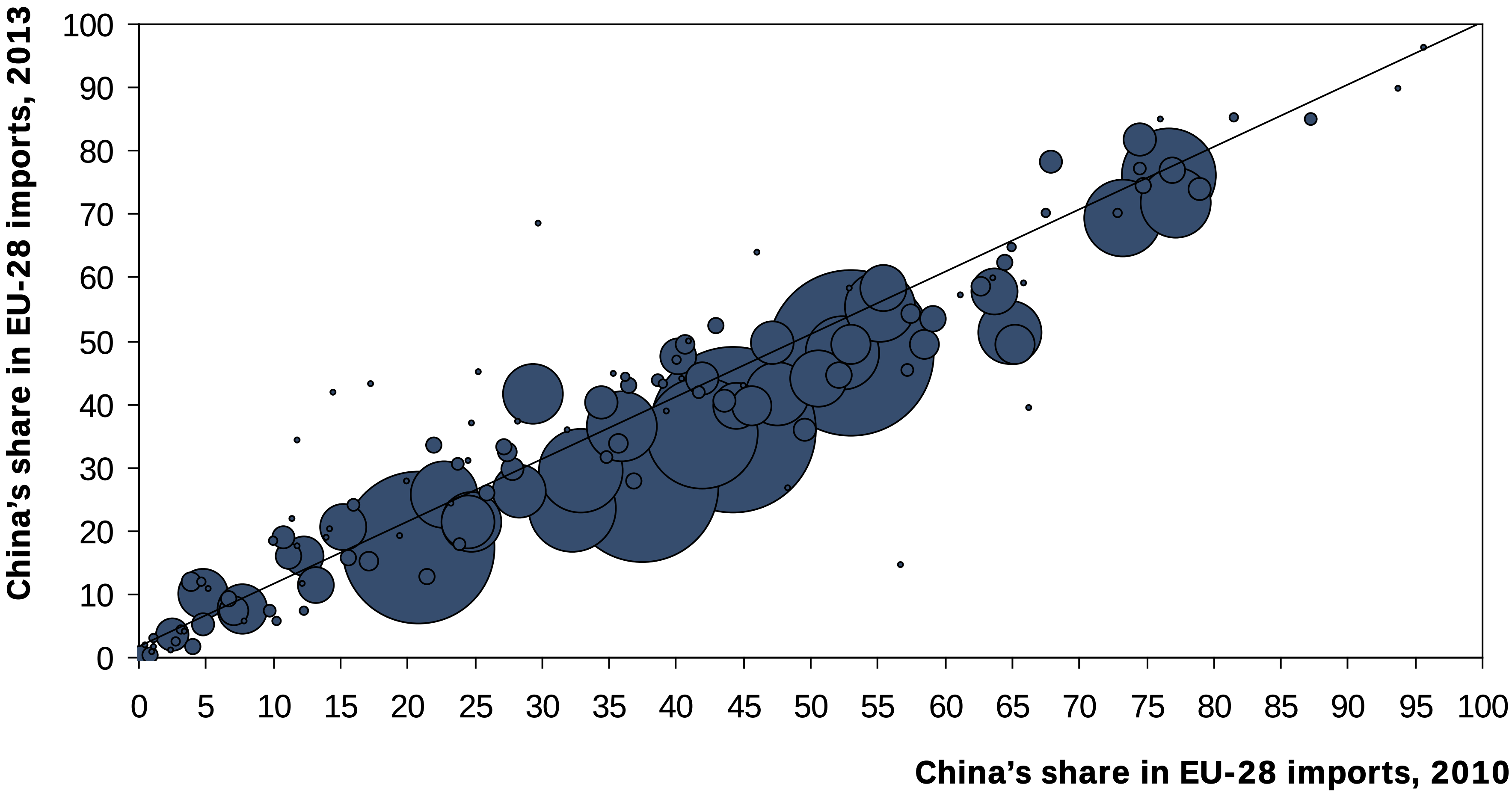


Looking at China's EU-28 performance at product level:
No patterns observed?

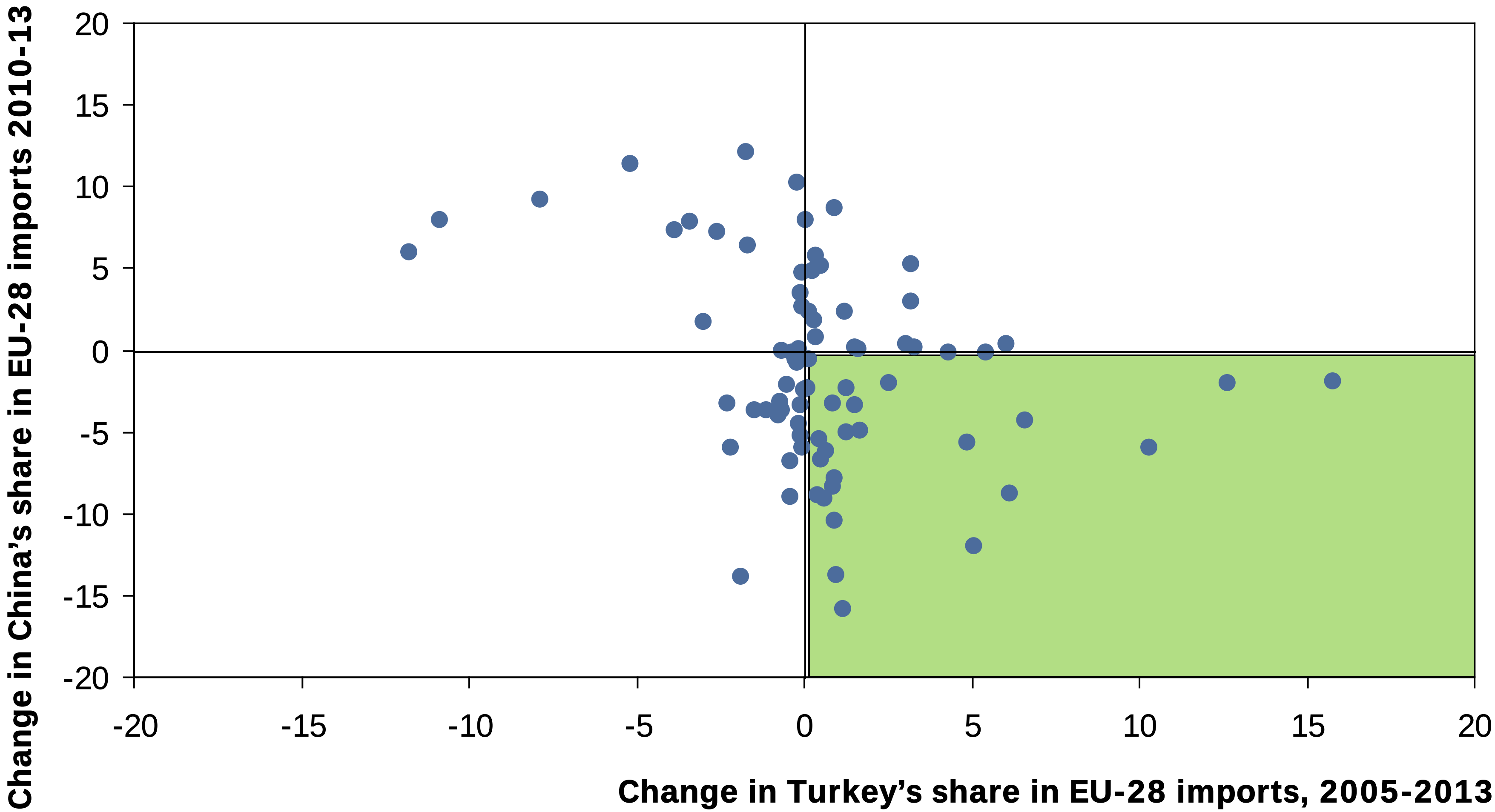


Looking at China's EU-28 performance at product level:

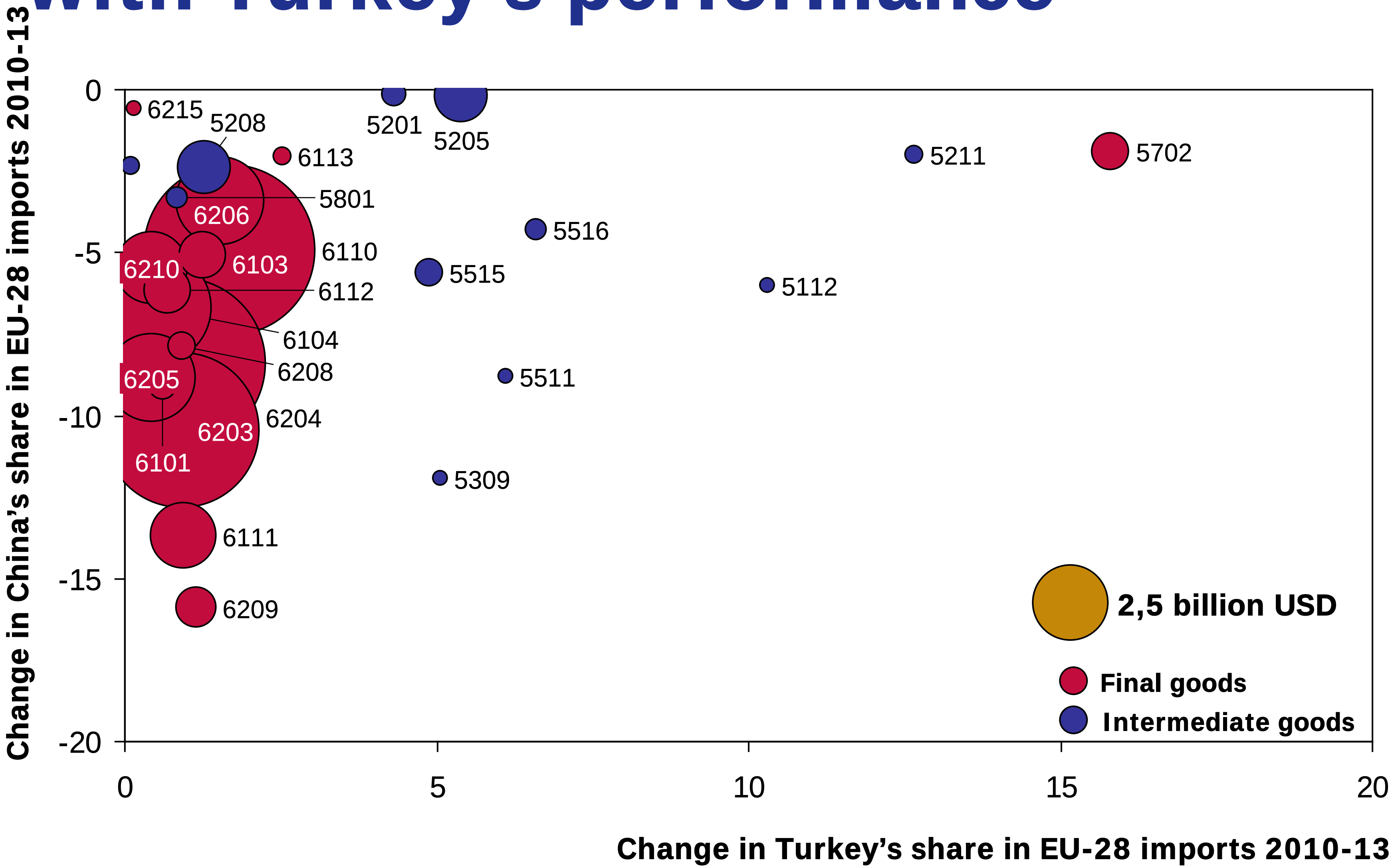
Important products are shifting away



Juxtaposing China's drift in textile with Turkey's performance



Juxtaposing China's drift in textile with Turkey's performance



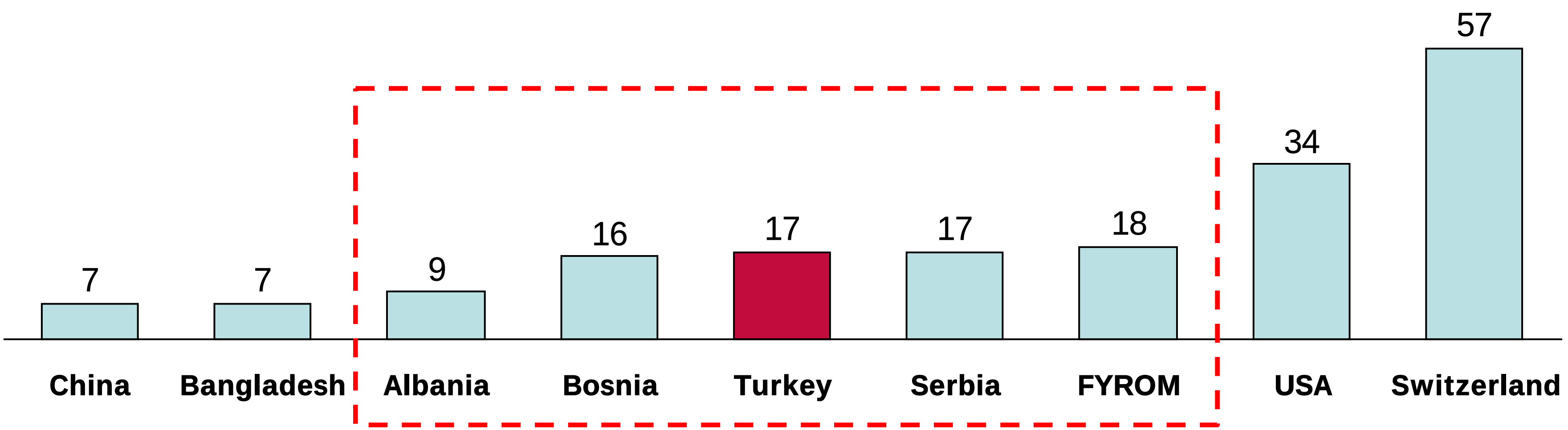
Opportunity areas for Turkish investors in SEE

Product	EU-28 import volume 2013, USD	China's share in EU-28 imports	Turkey's share in EU-28 imports	SEE's share in EU-28 imports
Sweaters, knitted	12 billion	48,1%	11,5%	0,6%
Women's suits, not-knitted	11.9 billion	35,9%	14,5%	2,1%
Men's suits, not-knitted	10.2 billion	27,1%	13,3%	2,1%
Women's suits, knitted	5.5 billion	35,2%	20,5%	1,1%
Men's shirts, not-knitted	3.3 billion	23,5%	11,8%	3,7%
Women's blouses, not-knitted	3.2 billion	29,5%	14,6%	3,1%
Babies' garments, knitted	1.9 billion	51,1%	5,3%	0,3%
Sports suits	1 billion	57,6%	3,1%	2,2%
Men's suits, knitted	960 million	39,5%	16,2%	0,6%
Babies' garments, not-knitted	740 million	49,3%	3,8%	0,2%
Men's overcoats, knitted	398 million	49,4%	7,3%	0,5%
Woman's slips	382 million	44,3%	20,8%	0,6%

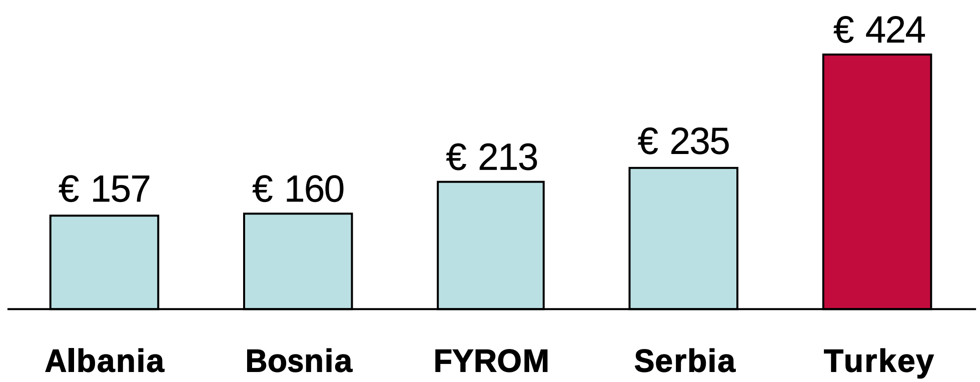
What about price competitiveness?

Like Turkey, SEE is positioned between developing Asia and developed countries

Unit price of a pair of exported jeans, 2013, USD



Minimum wage in SEE and Turkey



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Opportunity Areas

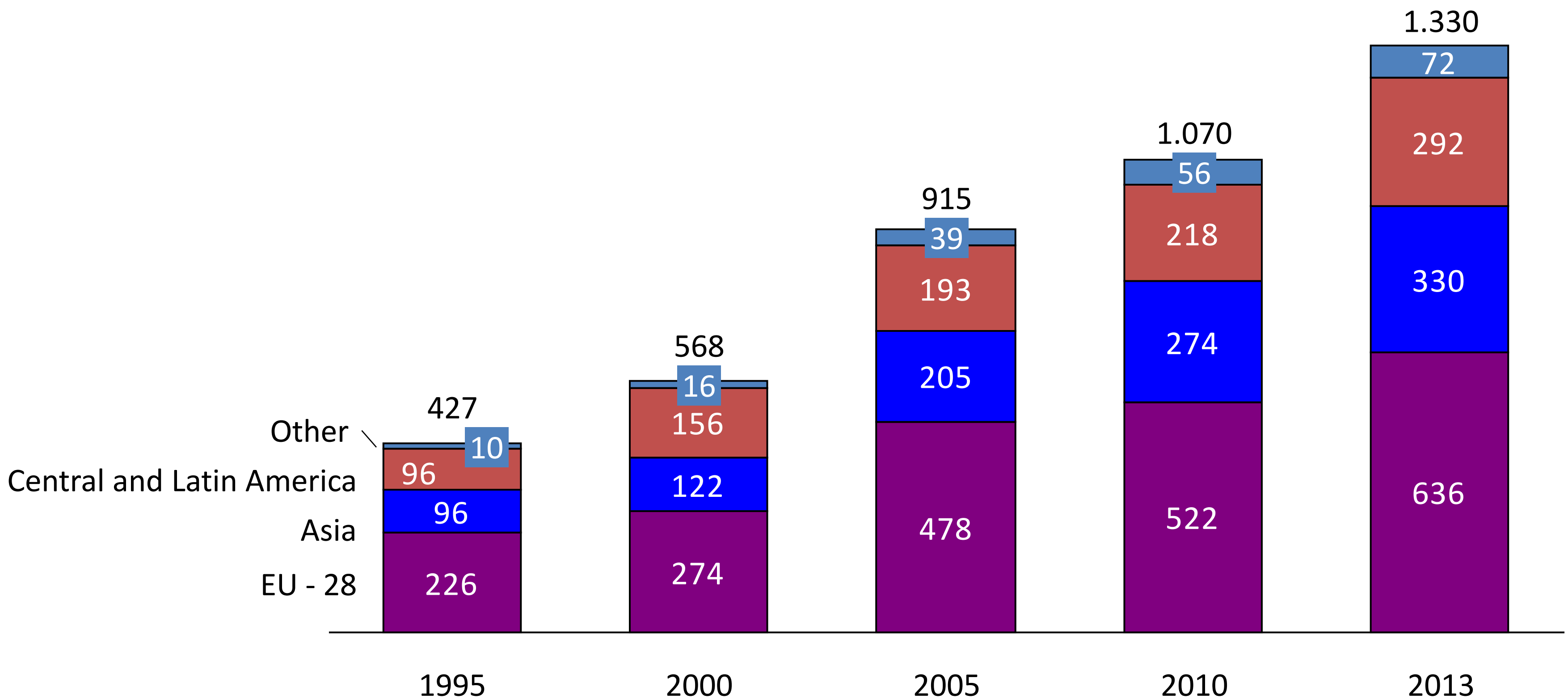
Automotive

Sarajevo, July 21, 2015

Global automotive trade trends

Playground of the EU..

Total World Export of Automobile Industry by country groups, billion $ (1995-2013)

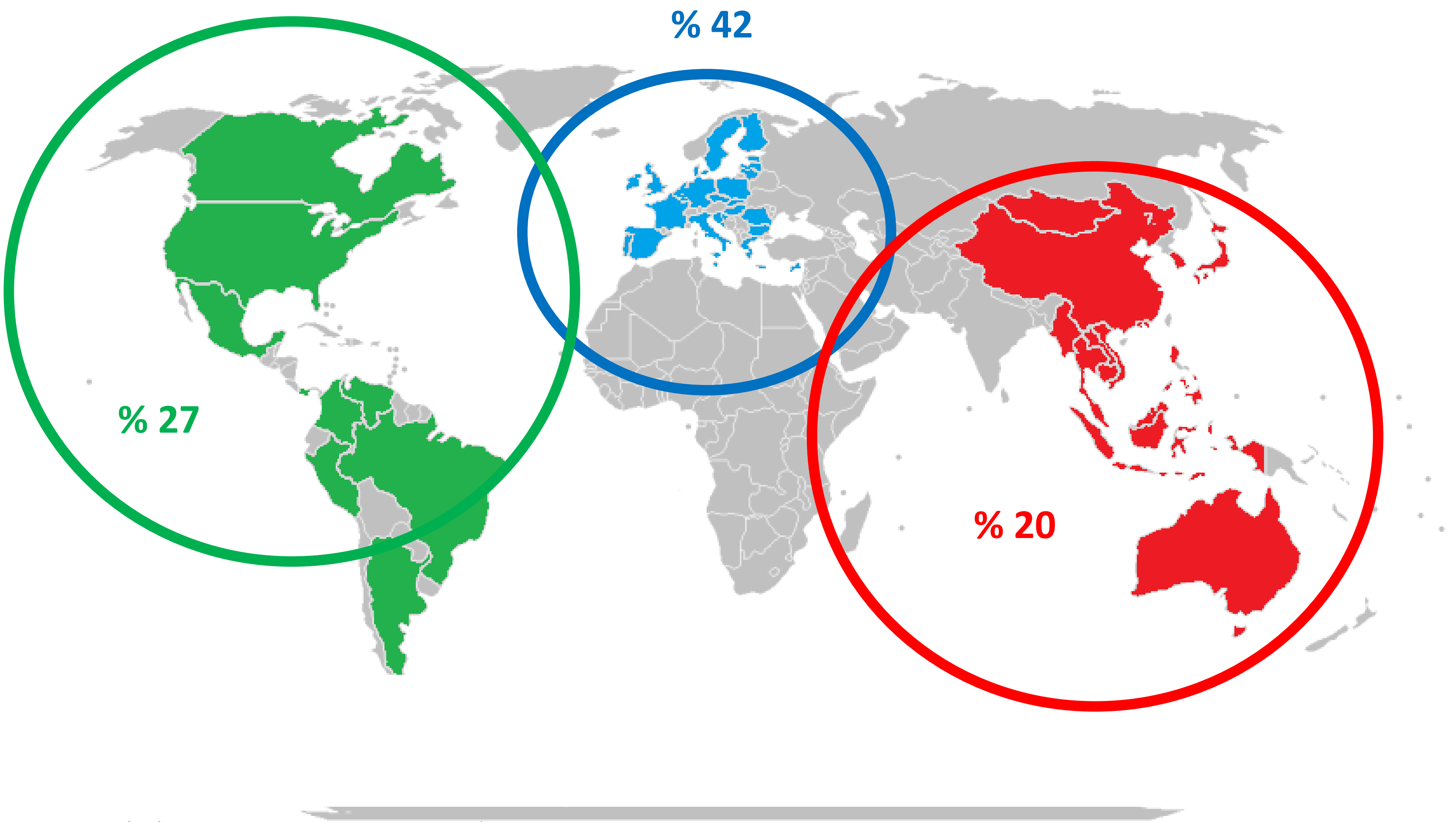


Share from world total export*	%10	%10.2	%10.4	%8.8	%9.1

Source: BACI, Tepav Calculations, HS2-87 Automotive Industry

42 percent of all automotive sector trade occurs within the eu-28

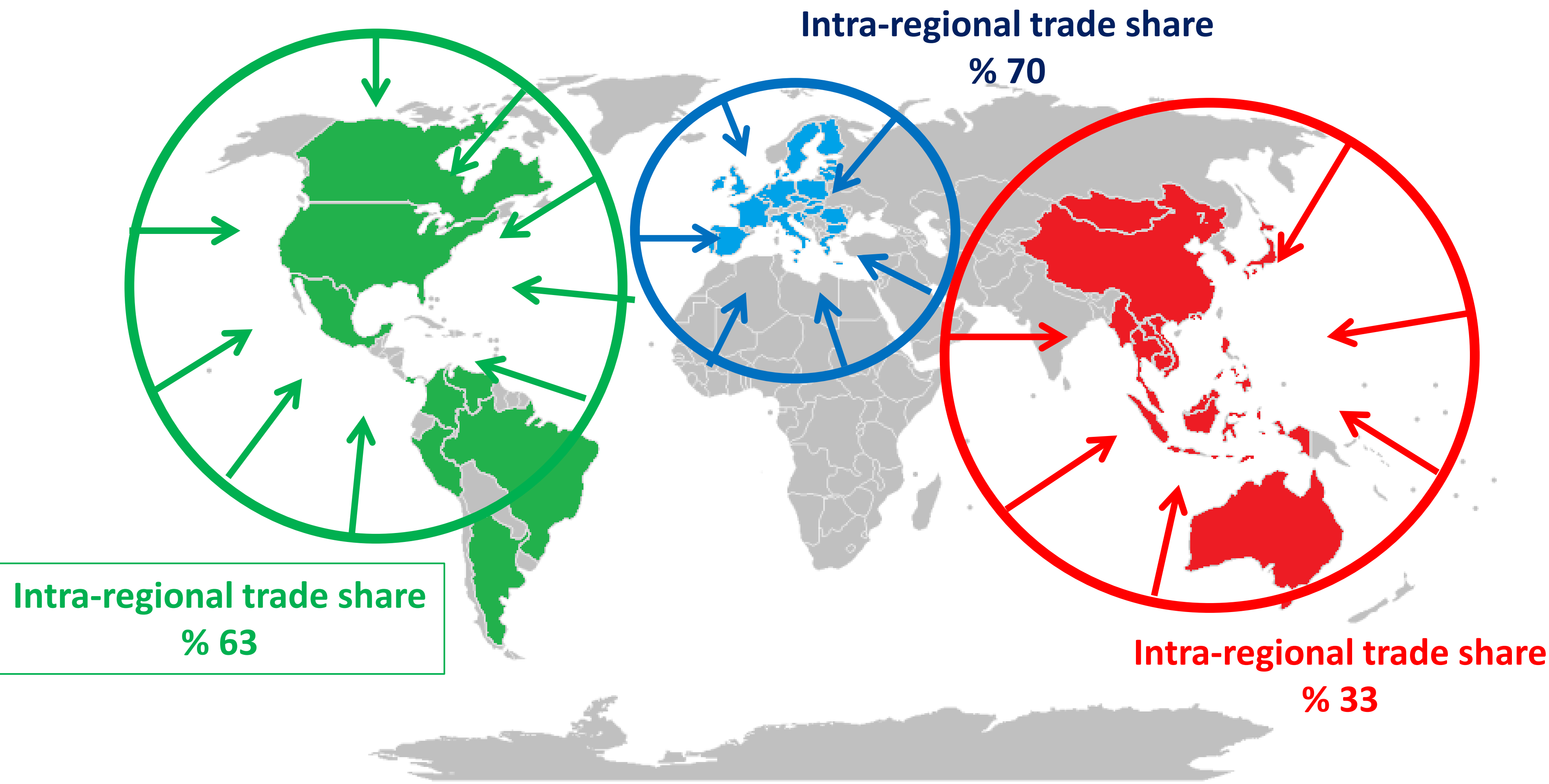
1 of 5 cars produced worldwide is produced in EU



Source: BACI, Tepav Calculations, HS2-87 Automotive Industry - 2013
*Total automotive trade (export + import)

EU-28's intra-region automotive trade was 70 percent in 2013

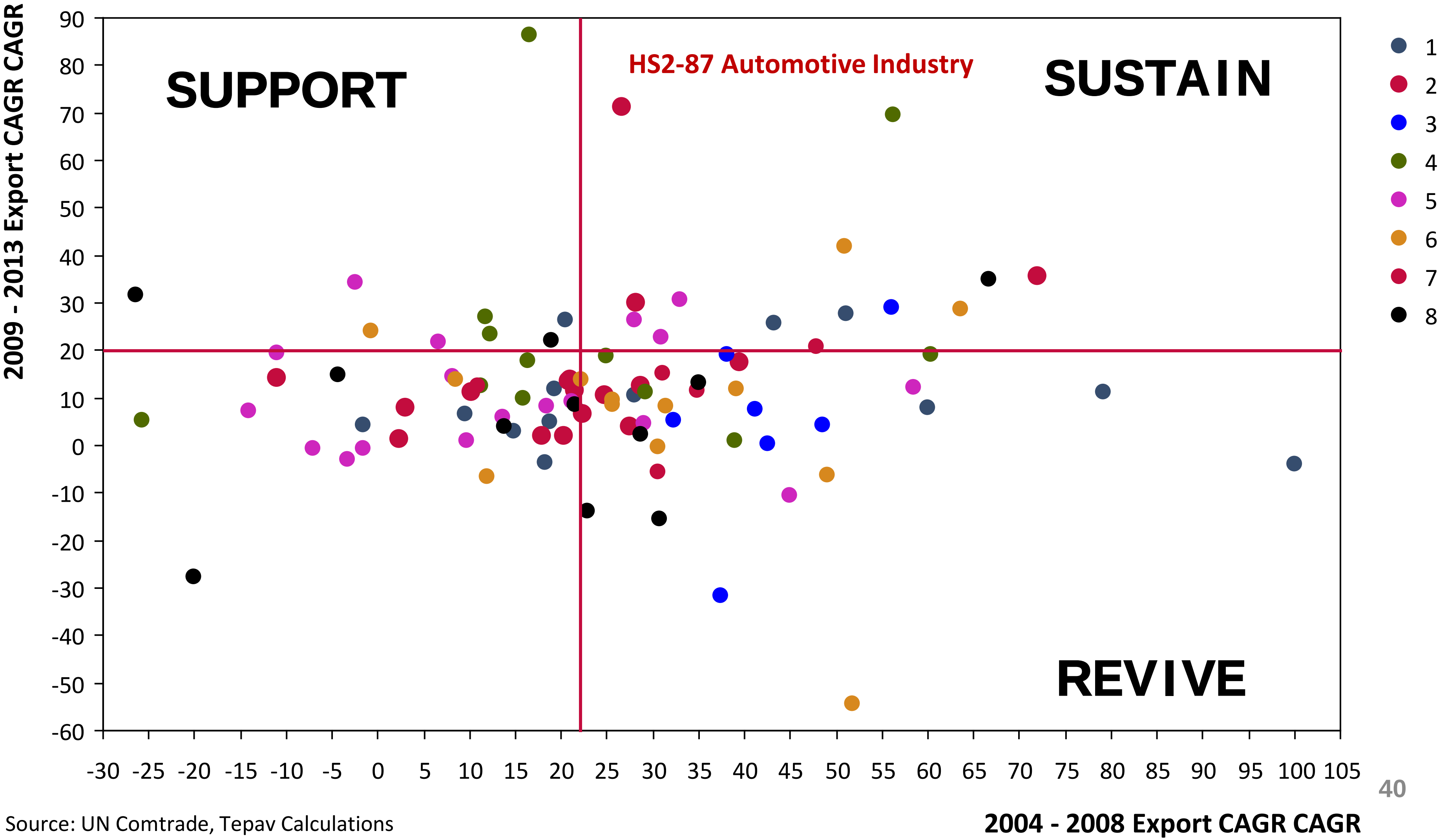
Both demand and supply sides of the equation



Source: BACI, Tepav Calculations, HS2-87 Automotive Industry

A closer look at SEE's exports

Where is the automotive sector?

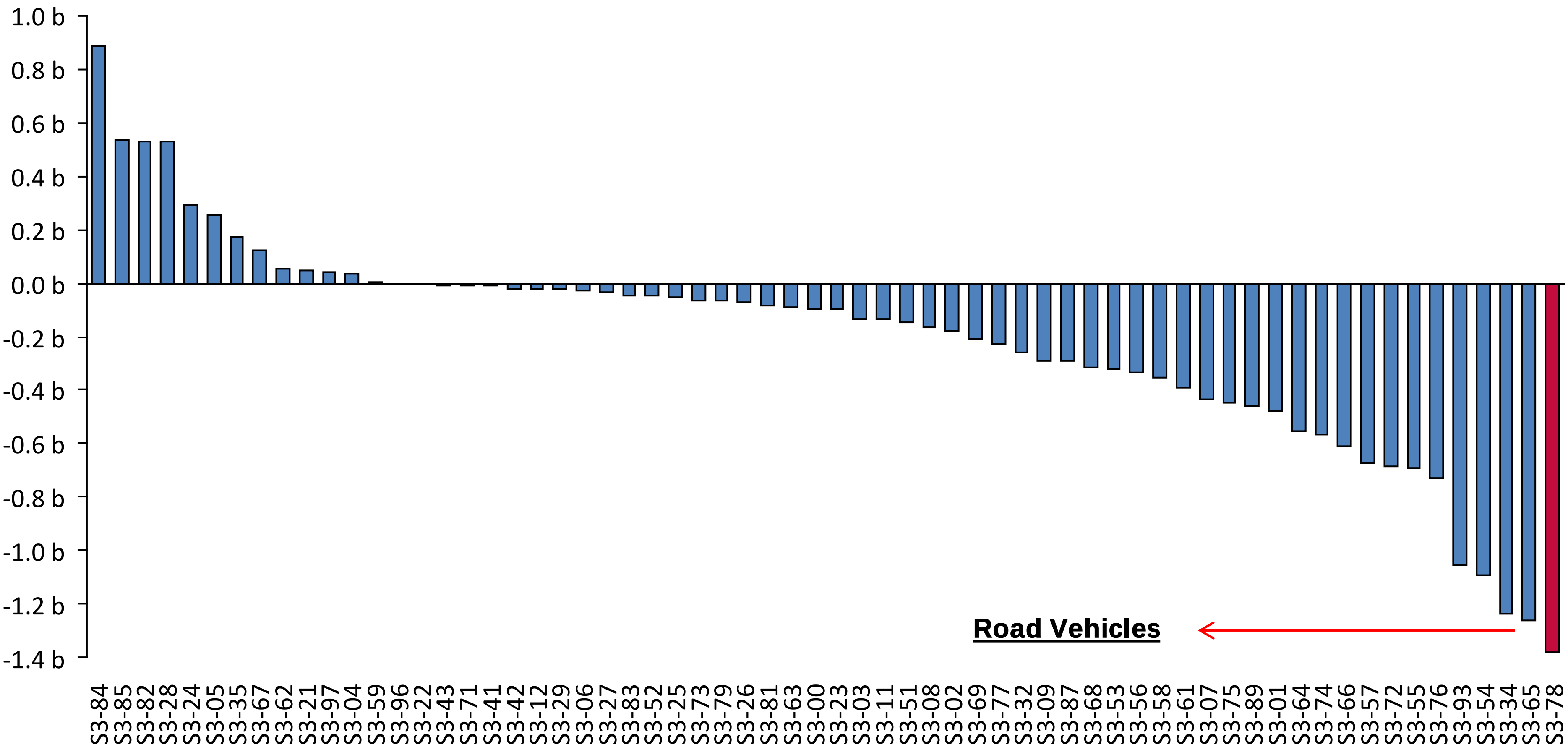


Source: UN Comtrade, Tepav Calculations

How important is automotive sector for the region today?

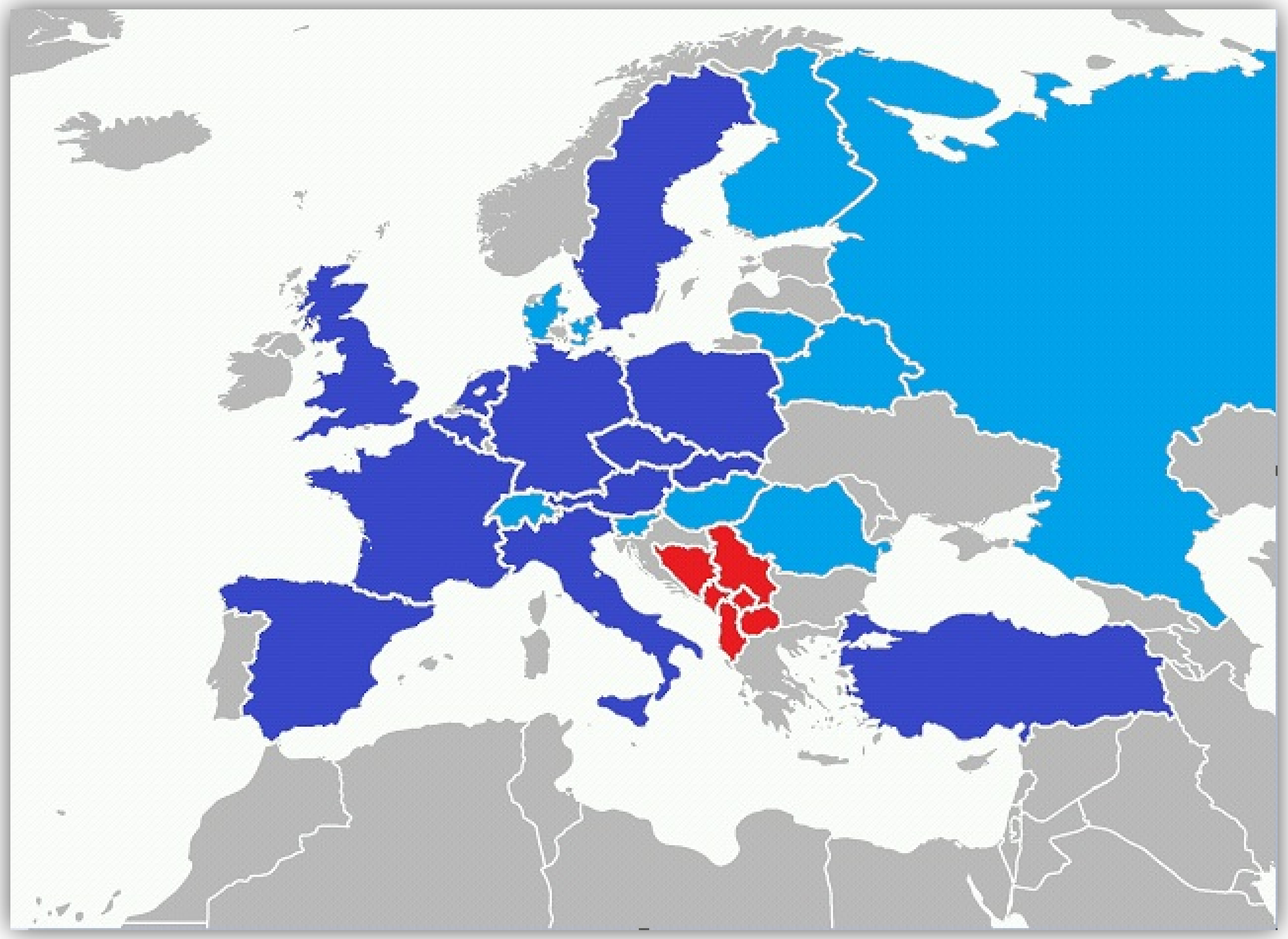
The single largest deficit item in the trade balance sheet

SEE-6 sectoral trade balances, 2013, billion USD



Source: UN Comtrade, Tepav Calculations, SITC – 78 Road Vehicles

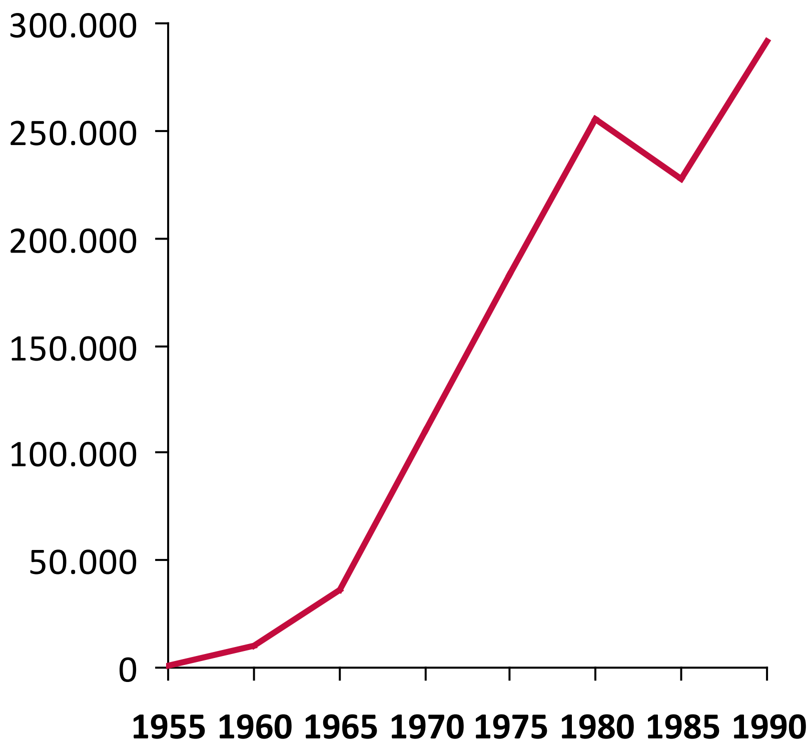
...SEE is surrounded by the largest producers



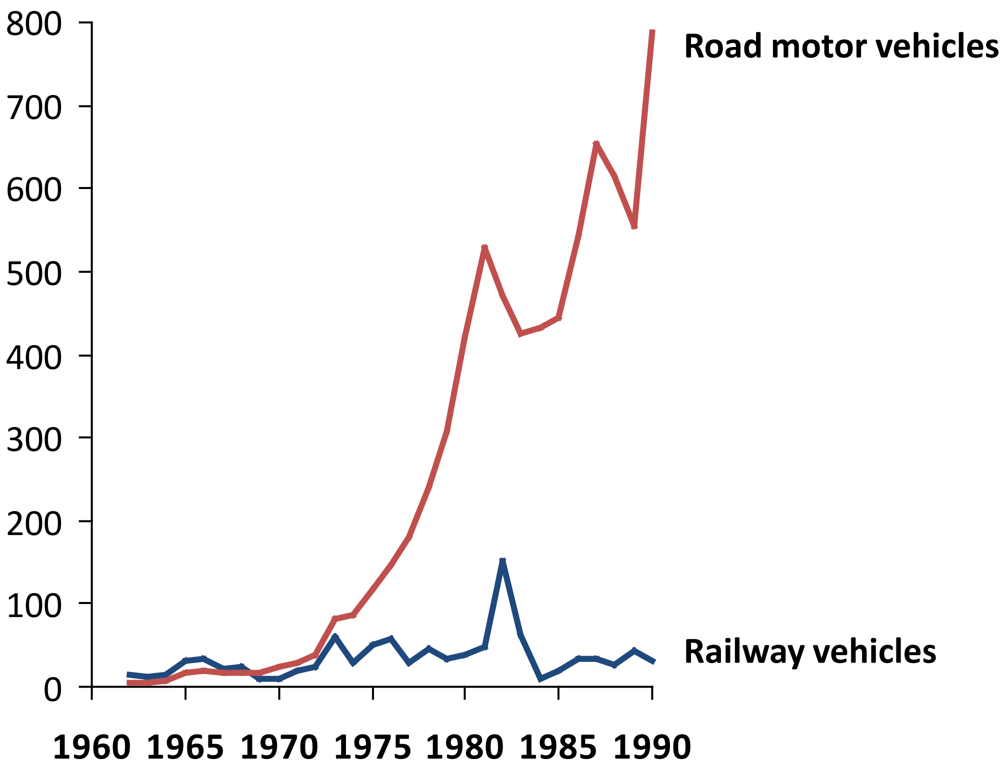
Source: BACI, Tepav Calculations, HS2-87 Automotive Industry

Automotive was an important sector for Yugoslavia since 50s…

Fmr Yugoslavia's Automotive Production (1962—1990)
Unit



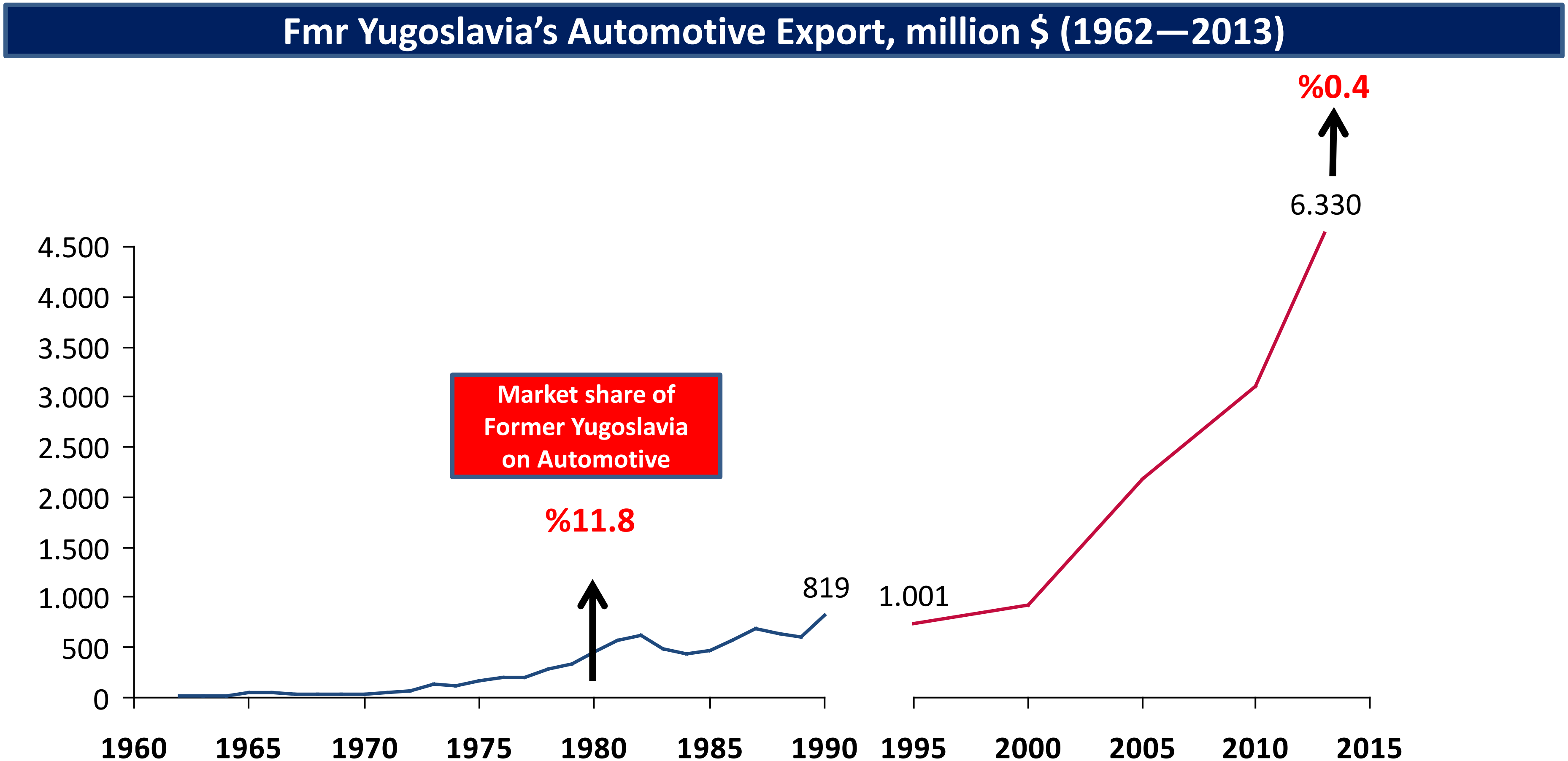
Fmr Yugoslavia's Automotive Export (1962—1990)
million $



Source: http://trade.ec.europa.eu/doclib/docs/2007/june/tradoc_134826.pdf
UN Comtrade, Sitc rev1 731,732

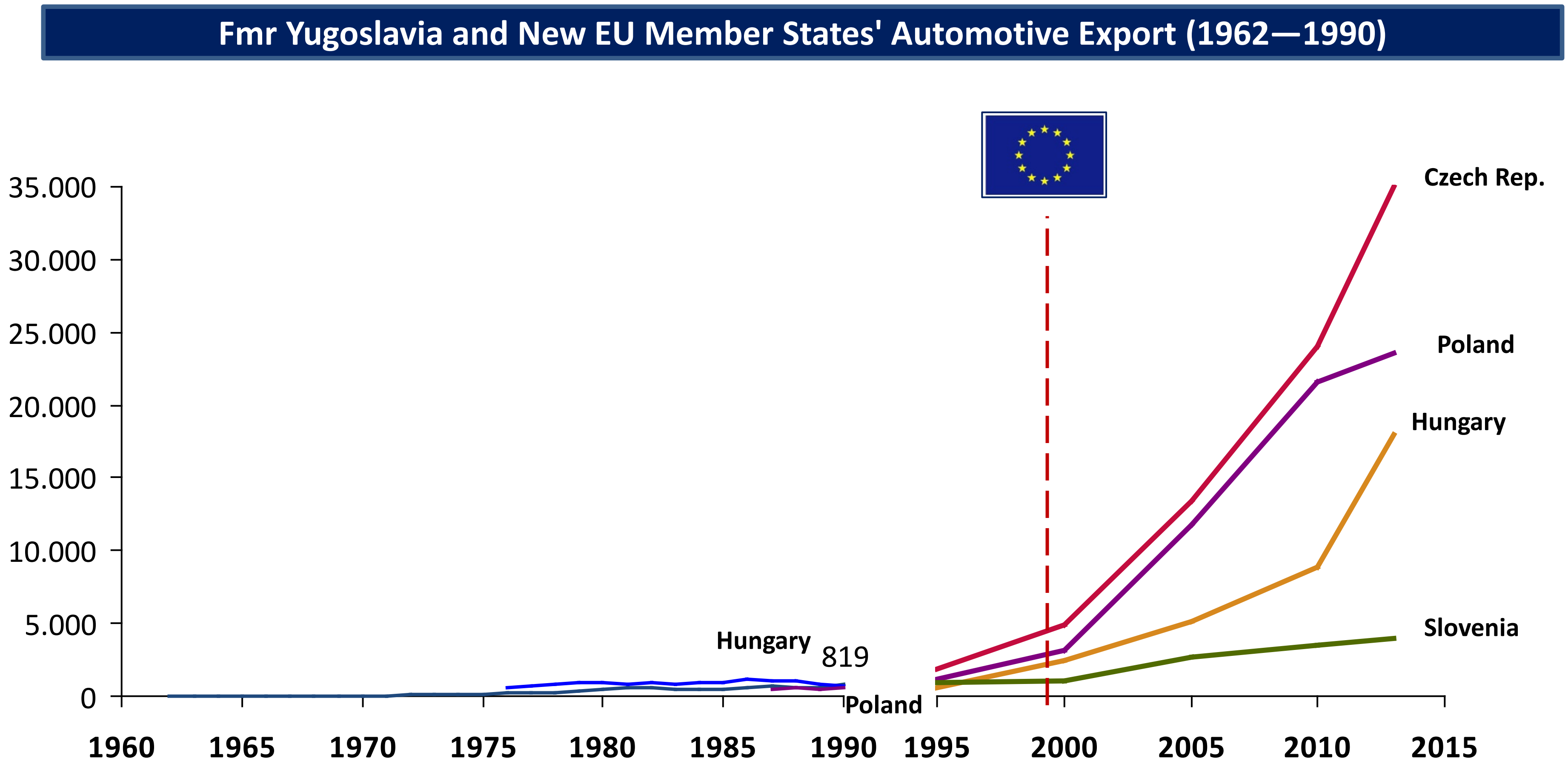
Lackluster performance following the breakup

The region could not keep up with market growth...



Source: http://trade.ec.europa.eu/doclib/docs/2007/june/tradoc_134826.pdf
Sitc rev1 731,732

...as well as the new member states

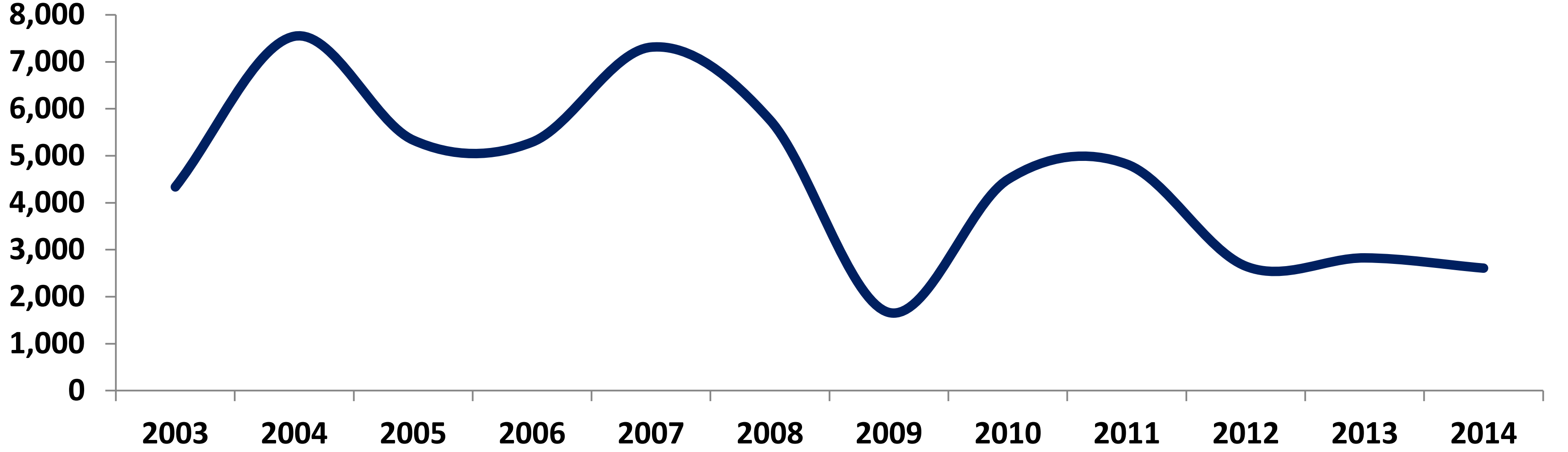


Source: http://trade.ec.europa.eu/doclib/docs/2007/june/tradoc_134826.pdf
Sitc rev1 731,732

EU harmonization process was the anchor for automotive FDI inflows

New EU Member States Inward Automotive Investment ,million $ (2003-2014)

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	
Poland	1,071	2,023	2,390	1,451	1,703	2,115	271	1,475	949	918	1,896	1,285	**17,547**
Slovakia	980	2,159	1,112	2,028	1,721	844	502	403	2,948	85	78	263	**13,121**
Hungary	1,792	567	738	614	1,231	2,214	446	2,239	352	460	448	601	**11,703**
Czech Rep.	489	2,108	1,082	1,071	2,557	588	338	374	554	1,155	366	455	**11,136**
Slovenia	5	687	11	126	100	0	107	4	18	31	38	5	**1,132**
Total	4,336	7,543	5,333	5,290	7,311	5,761	1,664	4,494	4,821	2,650	2,826	2,608	**13,652**



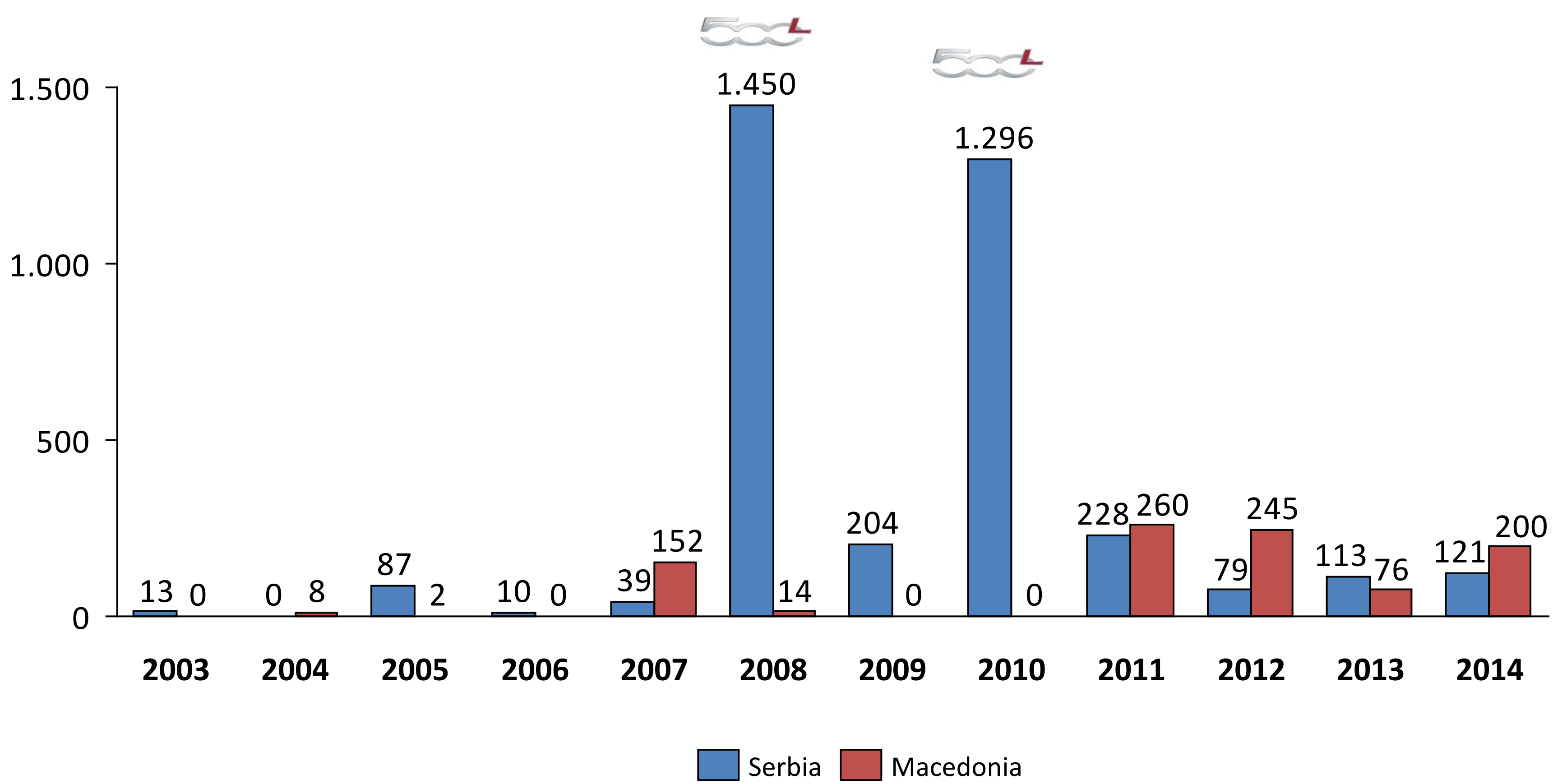
Source: FDI Markets Database

10 of top 20 automotive FDI destinations are in Europe

These 10 countries attract almost 177 billion us $ automotive FDI… = China (167 b $)

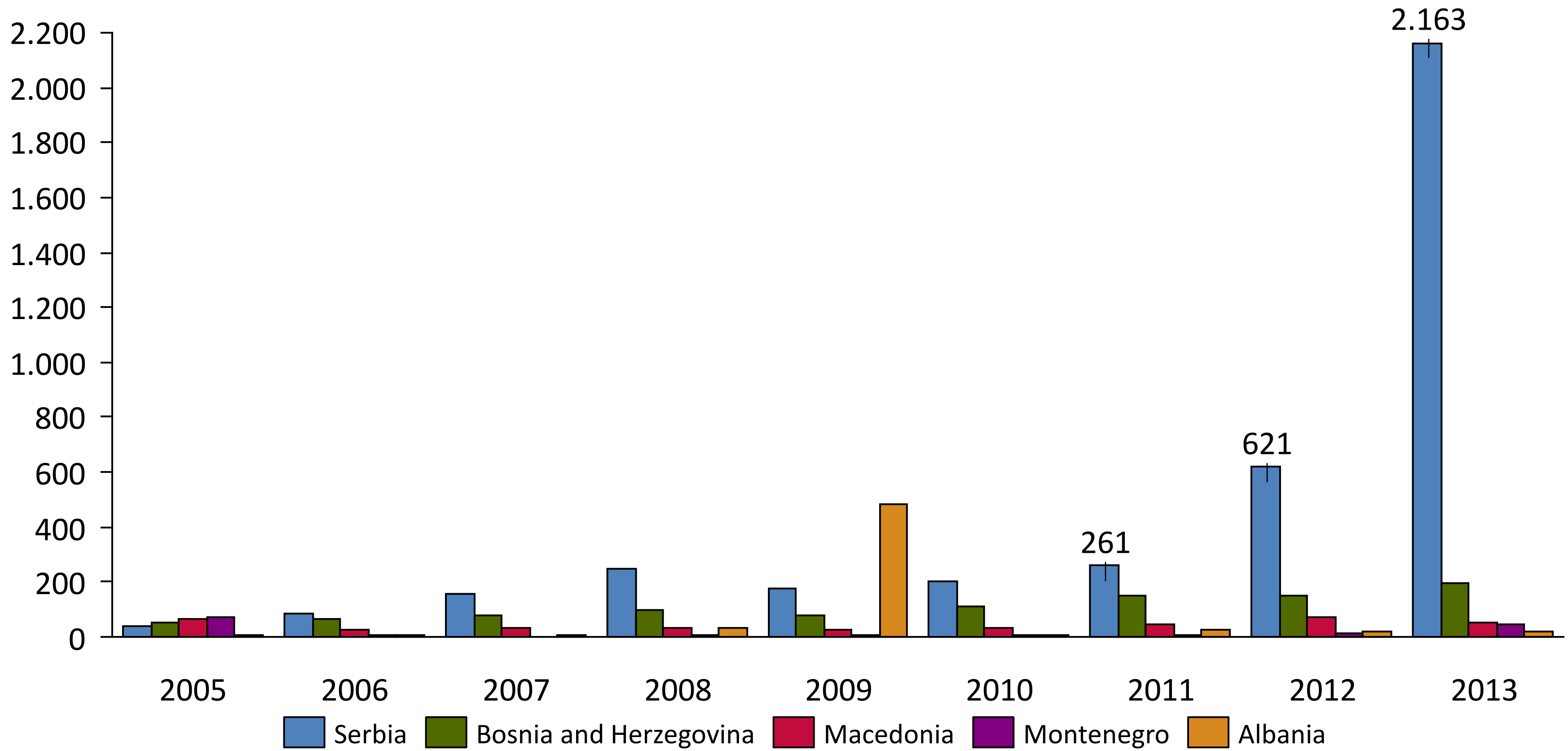
Source: FDI Markets Database (2003-2013 total FDI)

SEE's Inward Automotive Investment by country ,million $ (2003-2014)



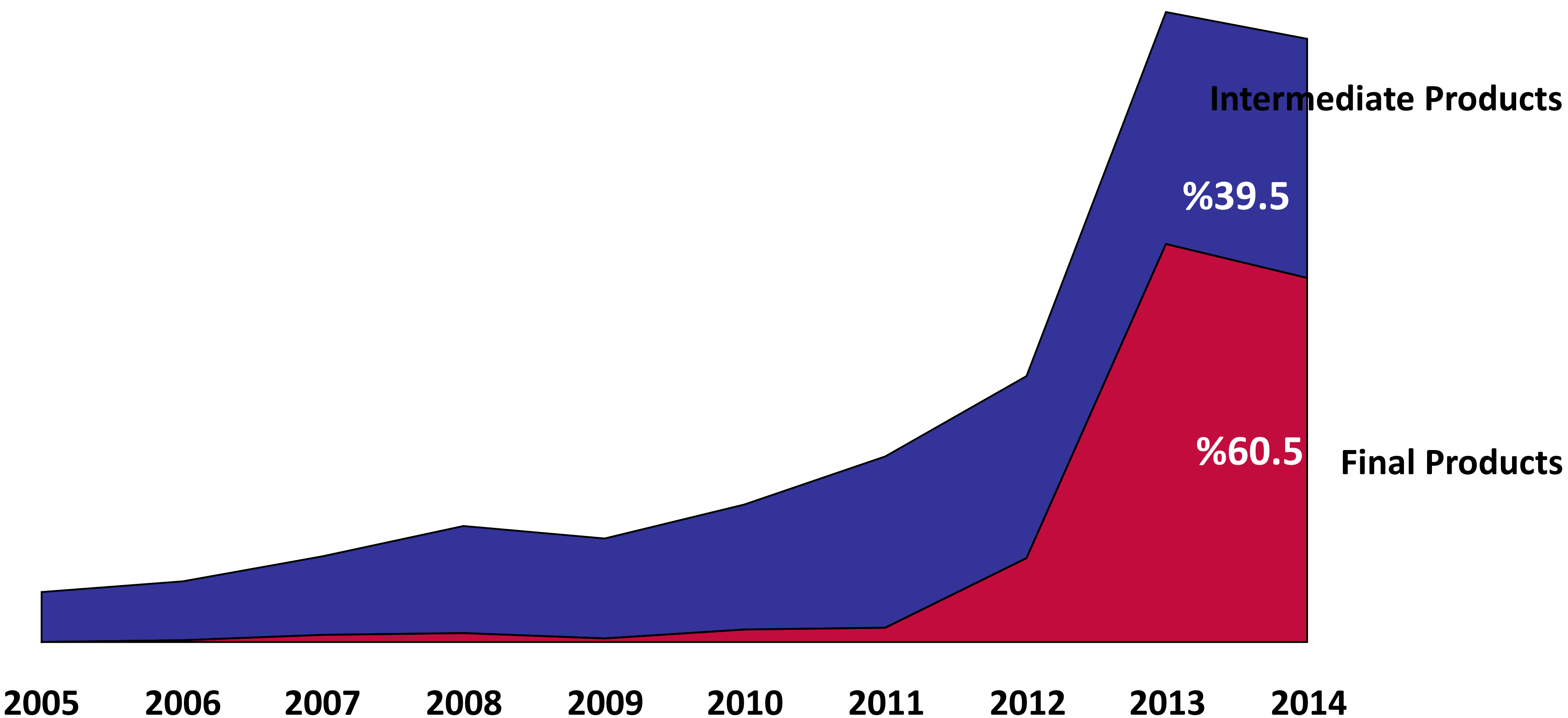
Source: FDI Markets Database

SEE's Automotive Export by country ,million $ (2003-2014)



The value chain could not yet cluster around the flagship investment

Serbia's Automotive Value Chain Export ,billion $ (1962—1990)

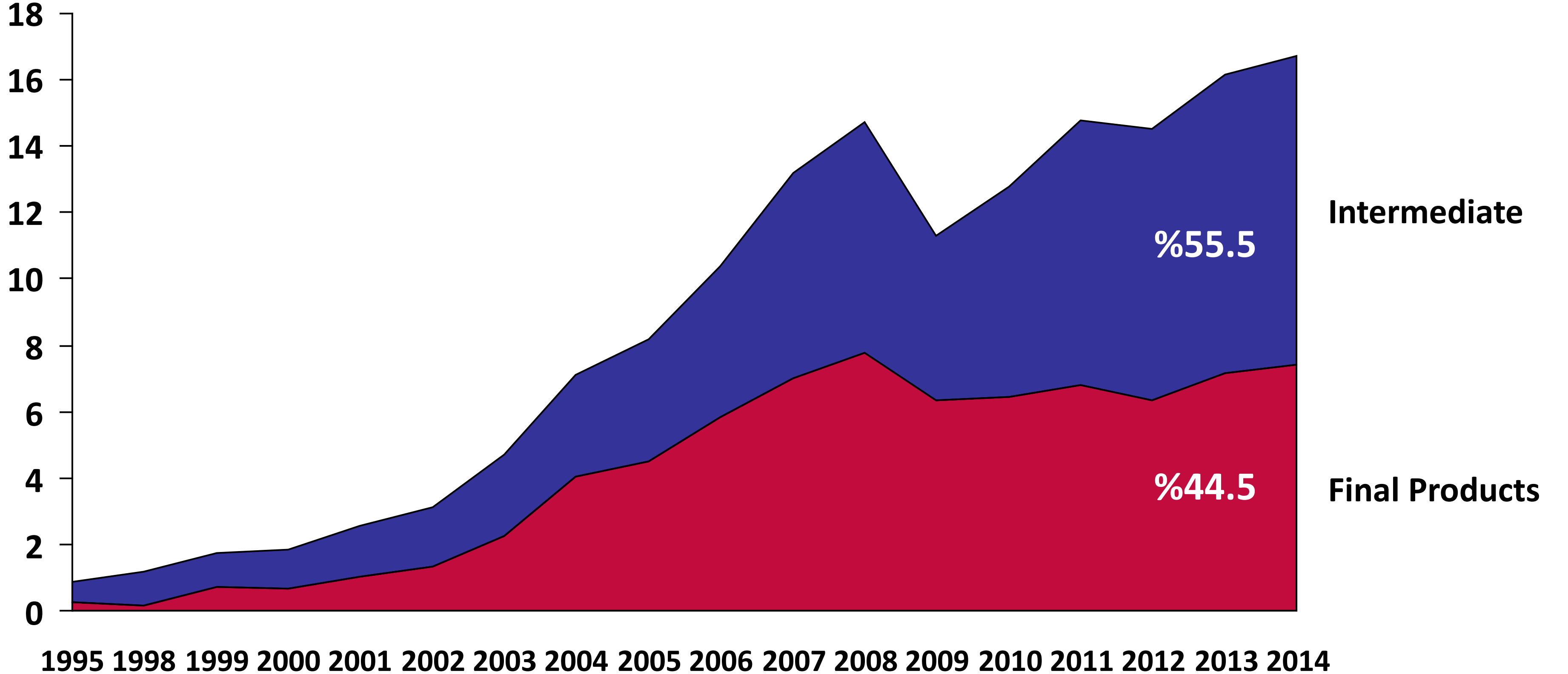


Source: Comtrade, BEC

Sign of a prospering automotive sector

A healthy balance between intermediate and final products

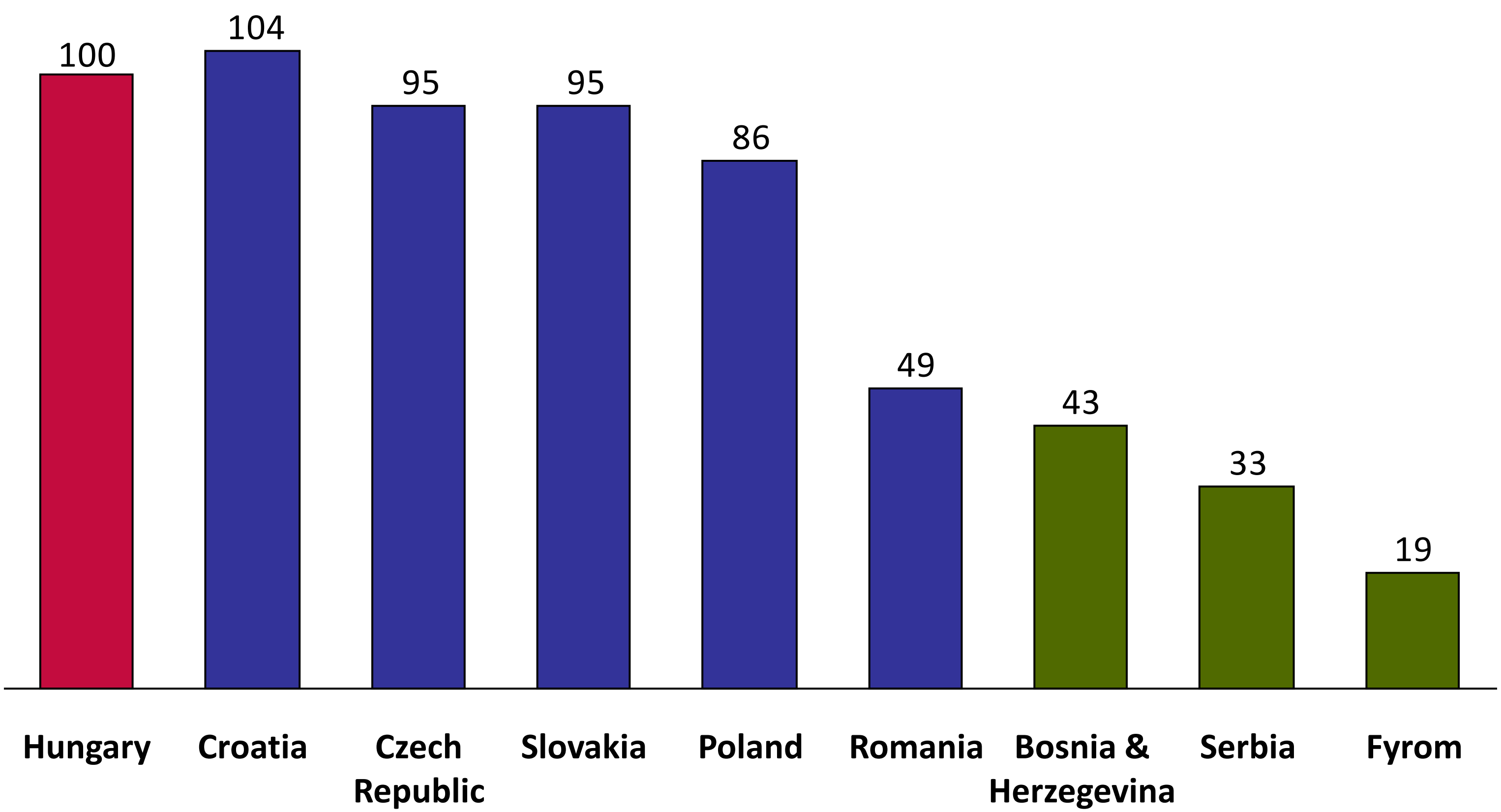
Turkey's Automotive Value Chain Export ,billion $ (1962—1990)



Source: Comtrade, BEC

Time for the neighborhood to move up and SEE-6 to take over?

Average Wages in the Automotive Industry, 2006 (indexed on Hungary's wage levels)



Source: OECD analysis based on ILO Bureau of Statistic

The ways in which SEE could become a regional hub of automotive manufacturing

1. Attracting FDI from EU-28

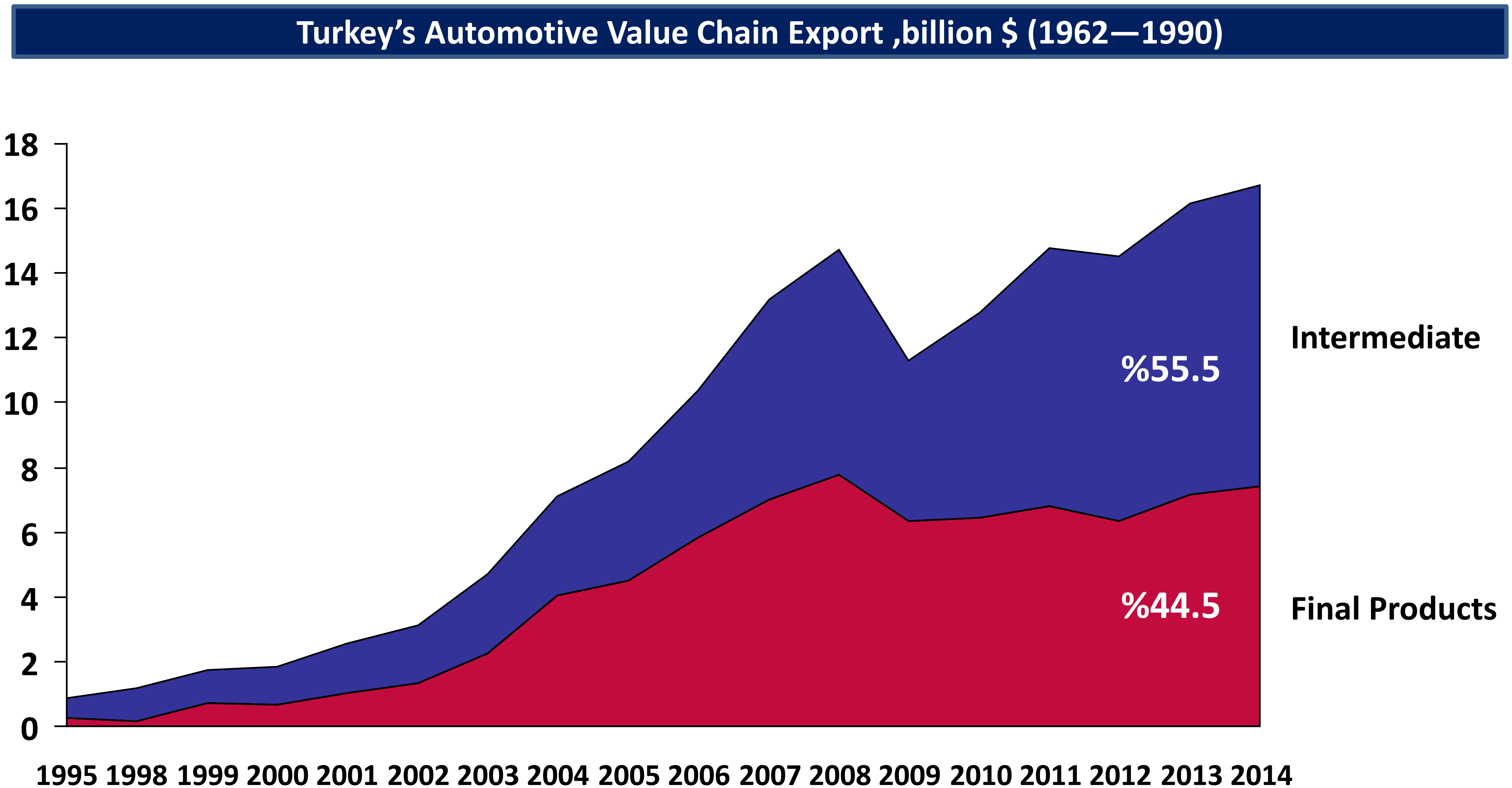
2. Attracting FDI from new rising exporters; East Asia and Pacific

3. Attracting FDI from Value Chain Suppliers

- Turkey

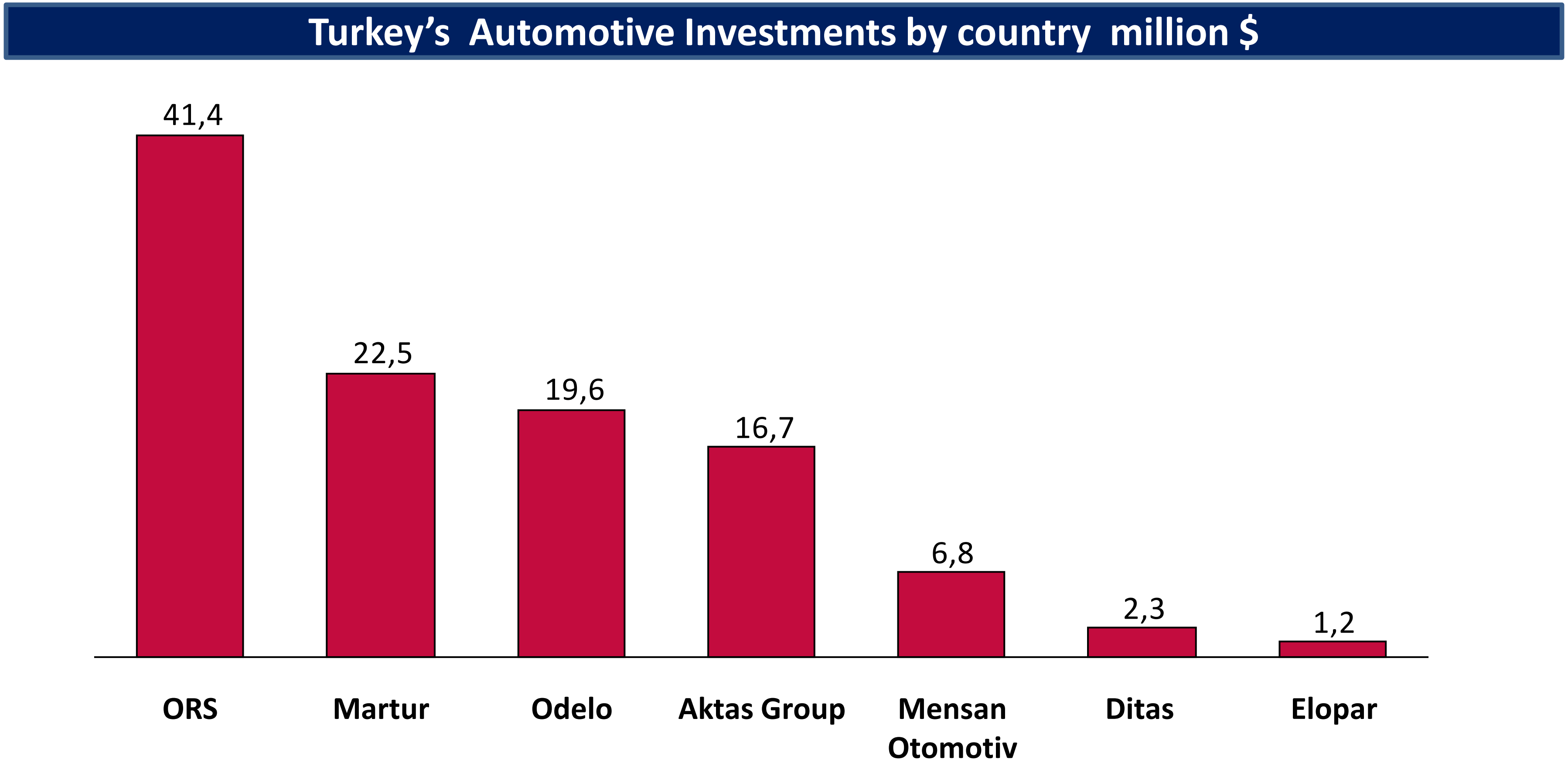
Sign of a prospering automotive sector

A healthy balance between intermediate and final products



Source: Comtrade, BEC

Potential Turkish investors in SEE's automotive sector



Bulgaria	**Macedonia FYR**	**Poland**	**Romania**	**Russia**	**Russia**	**Slovenia**

Source: FDI Markets Database

tepav

The Economic Policy Research Foundation of Turkey

Strengthening the Connectivity and Business Synergies in the SEE

Session Three

Opportunity Areas

Energy

Sarajevo, July 21, 2015

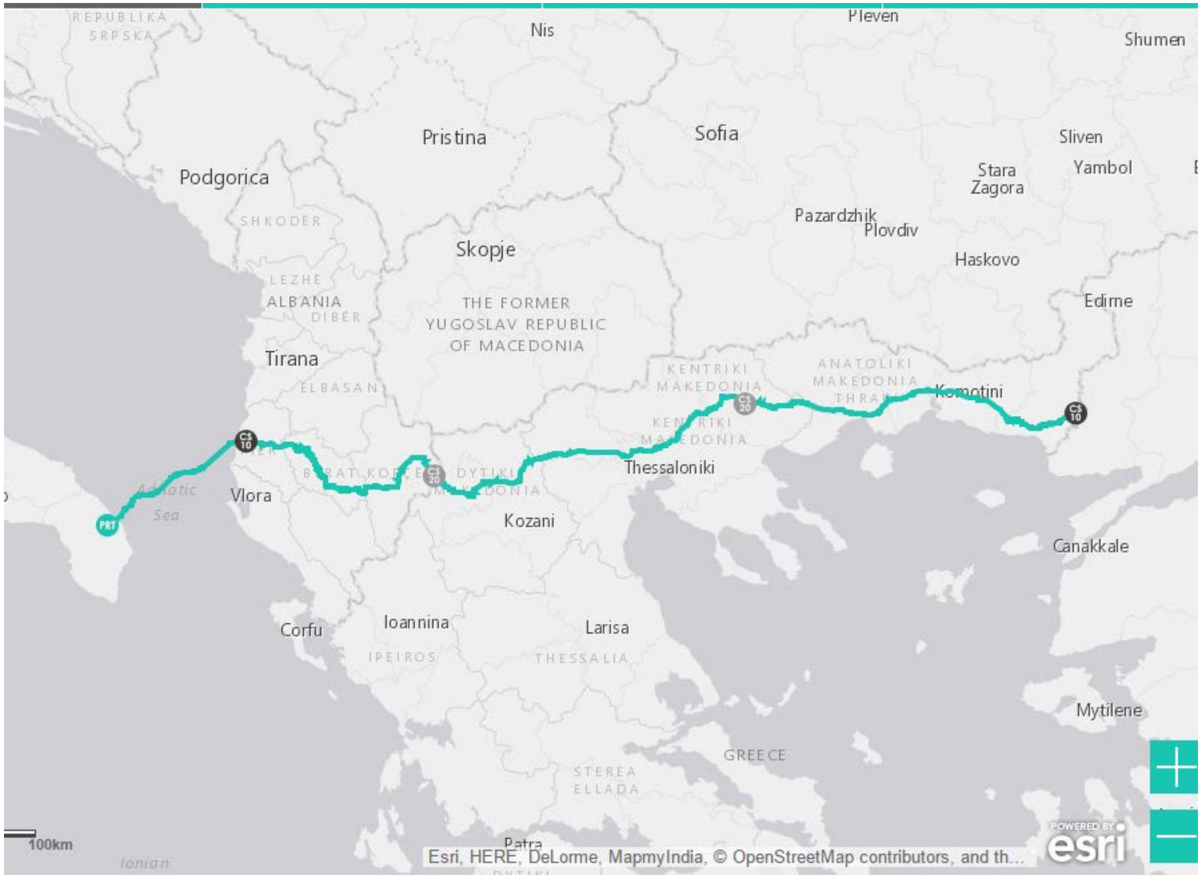
Framework

- The SEE economies importance for ensuring the energy security of the broader region
- What does current state of energy consumption in the SEE economies tell us?
- What could Turkish companies do in the region?
  - → Energy efficiency
  - → Electricity production investments
  - → Exploration and drilling and mining

The SEE is critical for Europe's energy security

Trans Adriatic Route Map (a win-win project)

- An important project of the Southern Gas Corridor
- Bringing natural gas from the Caspian region to Europe
- Diversification away from Russia
- Connects with TANAP on the border of Turkey and Greece,
- 10 bcm initially, potential to double the capacity
- TAP and Ionian Adriatic Pipeline (IAP) to carry Caspian gas to Croatia, Albania, Montenegro, and Bosnia and Herzegovina



Turkey has a higher per capita GDP than the SEE economies

Country	GDP per capita (current US$)
Turkey	**10542.8**
Montenegro	7370.9
Serbia	6152.9
Macedonia, FYR	5370.7
Bosnia and Herzegovina	4796.2
Albania	4619.2
Kosovo	3989.7

Source: World Development Indicators

But the SEE economies consumes more electricity pc than Turkey does

Country	GDP per capita (current US$)	Electric consumption (kWh pc)
Turkey	**10542.8**	**2709.3**
Montenegro	7370.9	5752.5
Serbia	6152.9	4489.6
Macedonia, FYR	5370.7	3880.9
Bosnia and Herzegovina	4796.2	3188.6
Albania	4619.2	2195.0
Kosovo	3989.7	2947.0

Source: World Development Indicators

CA balances of the SEE countries and Turkey are negative

Country	GDP per capita (current US$)	Electric consumption (kWh pc)	CA balance (% of GDP)
Turkey	**10542.8**	**2709.3**	**-7.9**
Montenegro	7370.9	5752.5	-14.7
Serbia	6152.9	4489.6	-6.1
Macedonia, FYR	5370.7	3880.9	-1.8
Bosnia and Herzegovina	4796.2	3188.6	-5.8
Albania	4619.2	2195.0	-10.7
Kosovo	3989.7	2947.0	-6.4

Source: World Development Indicators

Energy imports is part of the CA deficit problem in both Turkey and the SEE

Country	GDP per capita (current US$)	Electric consumption (kWh pc)	CA balance (% of GDP)	Energy imports (% of energy use)
Turkey	**10542.8**	**2709.3**	**-7.9**	**71.5**
Montenegro	7370.9	5752.5	-14.7	33.0
Serbia	6152.9	4489.6	-6.1	31.0
Macedonia, FYR	5370.7	3880.9	-1.8	42.8
Bosnia and Herzegovina	4796.2	3188.6	-5.8	34.9
Albania	4619.2	2195.0	-10.7	31.6
Kosovo	3989.7	2947.0	-6.4	29.0

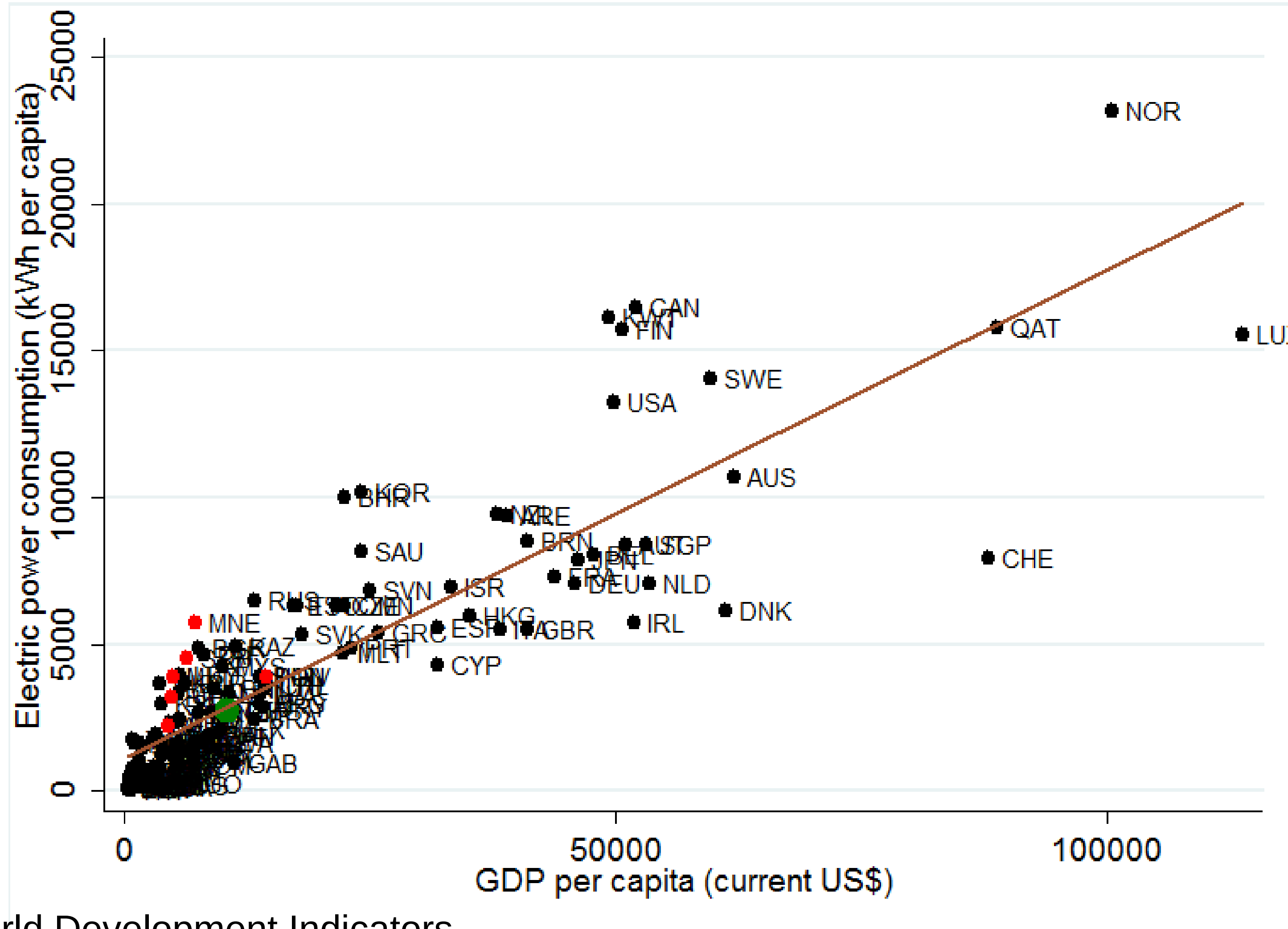
Source: World Development Indicators

There is room for decreasing the energy intensity (increasing EE) of the SEE economies

Country	GDP per capita (current US$)	Electric consumption (kWh pc)	CA balance (% of GDP)	Energy imports (% of energy use)	Energy intensity (MJ/$2011 PPP GDP)
Turkey	**10542.8**	**2709.3**	**-7.9**	**71.5**	**3.6**
Montenegro	7370.9	5752.5	-14.7	33.0	5.2
Serbia	6152.9	4489.6	-6.1	31.0	7.1
Macedonia, FYR	5370.7	3880.9	-1.8	42.8	5.1
Bosnia and Herzegovina	4796.2	3188.6	-5.8	34.9	7.9
Albania	4619.2	2195.0	-10.7	31.6	3.0
Kosovo	3989.7	2947.0	-6.4	29.0	6.6

Source: World Development Indicators

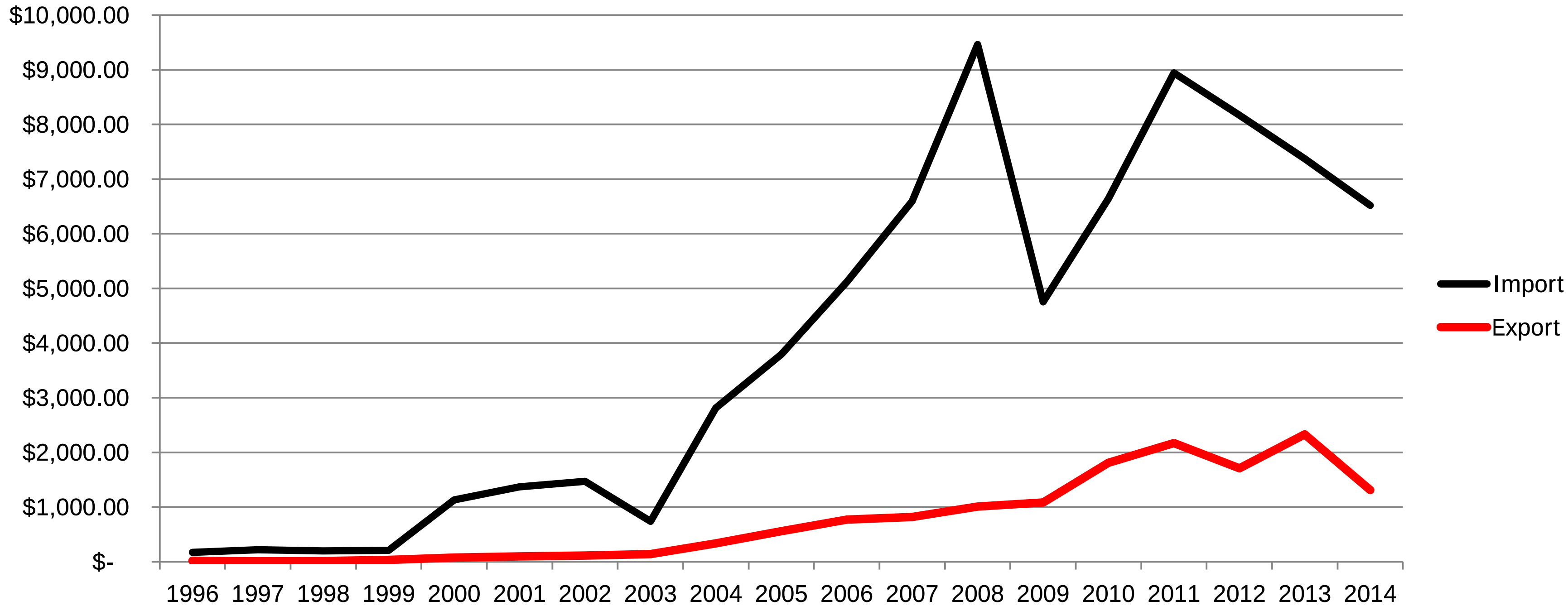
Electiricty consumption pc in the SEE is higher than the countries with similar GDP pc



Source: World Development Indicators

EE for decreasing the hydrocarbon import bill

Mineral fuels, mineral oils and products of their distillation exports and imports of the SEE economies (million USD)



Source: UN COMTRADE

Sizeable energy efficiency improvement potential in different sectors

Table 1 Energy-saving potential in the Western Balkans[1]

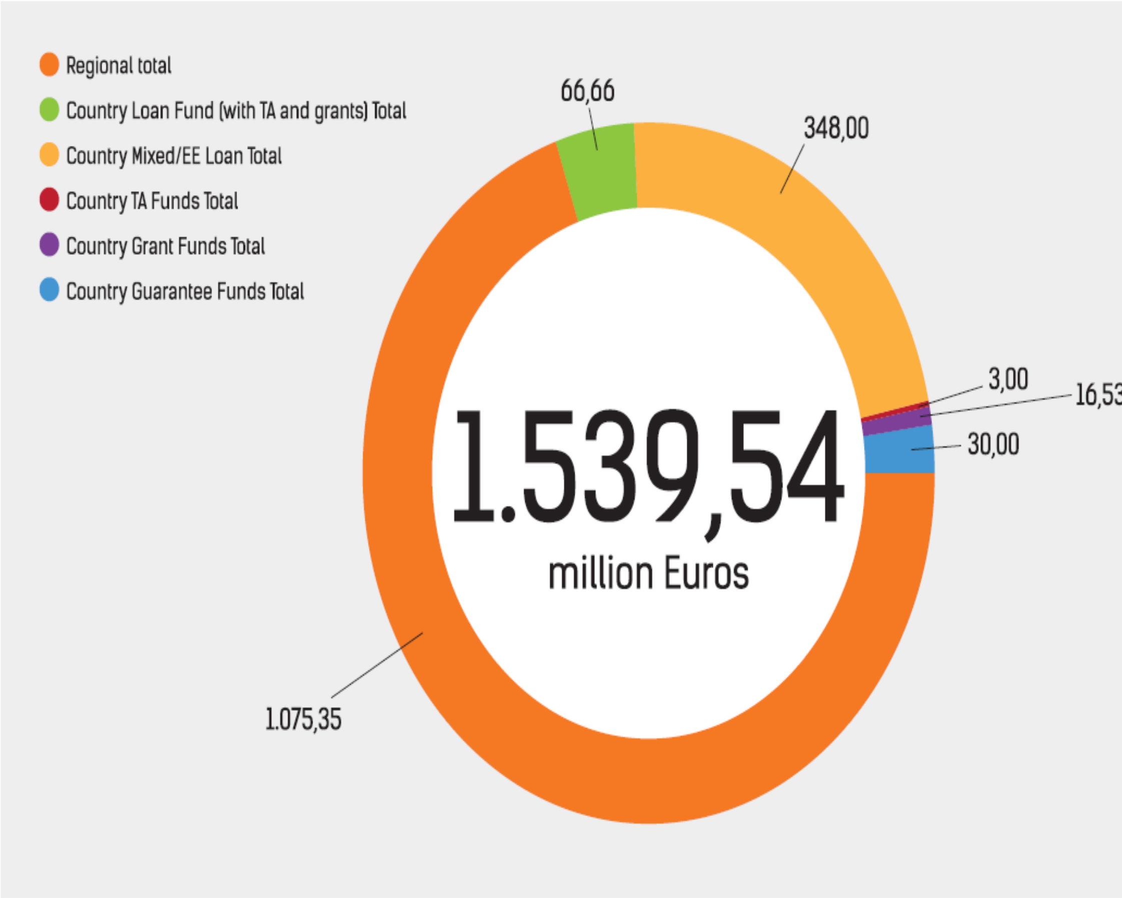
Sector	Energy-Saving Potential %
Transport	10
Residential	10–35
Public	35–40
Service	10–30
Industrial	5–25

Source: EBRD

More than 1.5 billion euros funding available for EE projects

- Several Turkish companies could benefit from this opportunity in cooperation with their SEE counterparts
  - Construction material producers
  - Insulation companies
  - Energy service companies
- Building business partnerships is important
  - Capability transfer

Figure 1 Available EE financing by type of fund (2013) (EUR mil.)

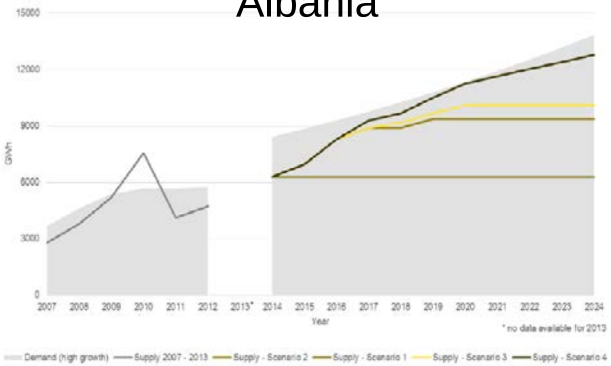


Source: EBRD

All the SEE economies plan to expand their electricity generation capacity

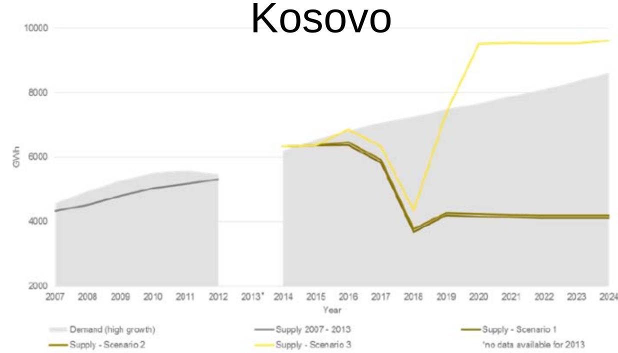
The Turkish private sector could bring capital and expertise. But

Albania

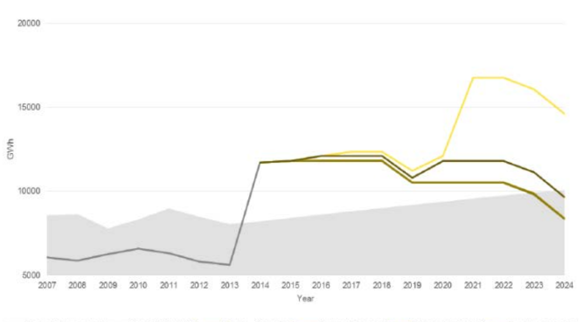


Bosnia and Herzegovina

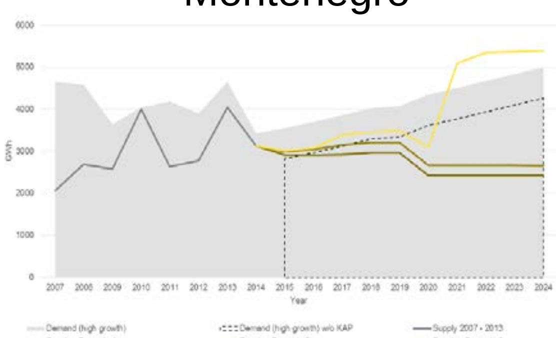
Kosovo



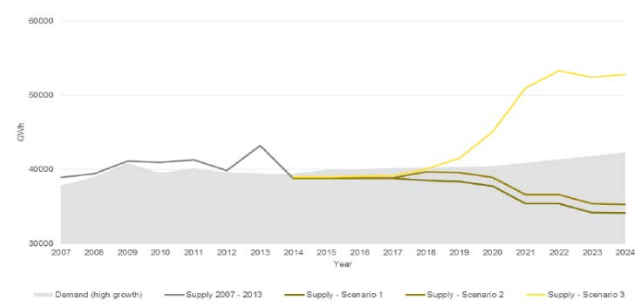
Macedonia



Montenegro

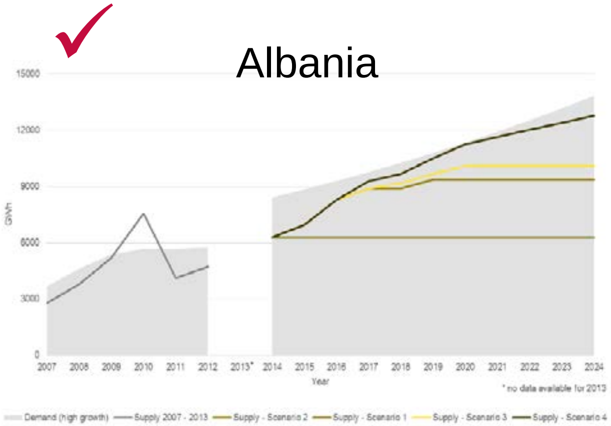


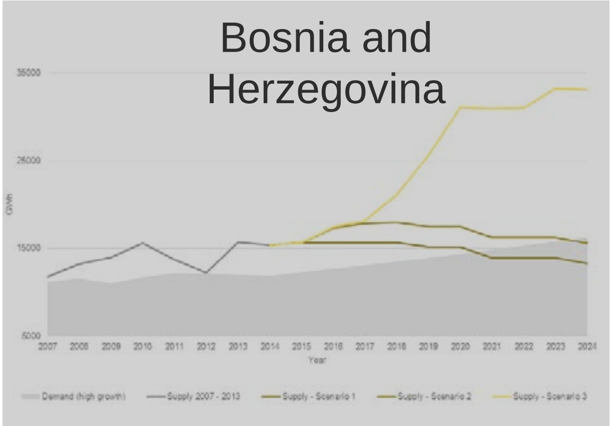
Serbia

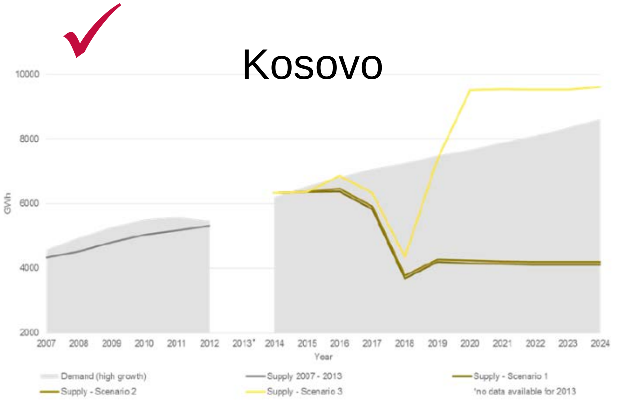


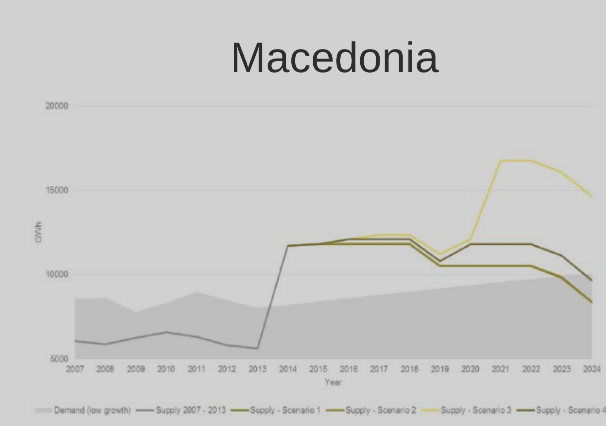
Source: University of Groningen

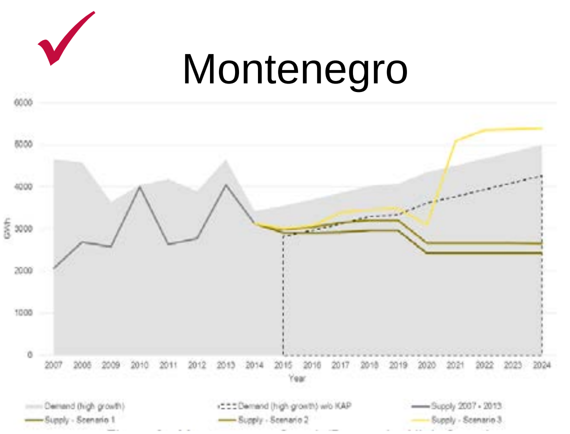
Albania, Kosova, and Montenegro are projected to have strong demand for electricity

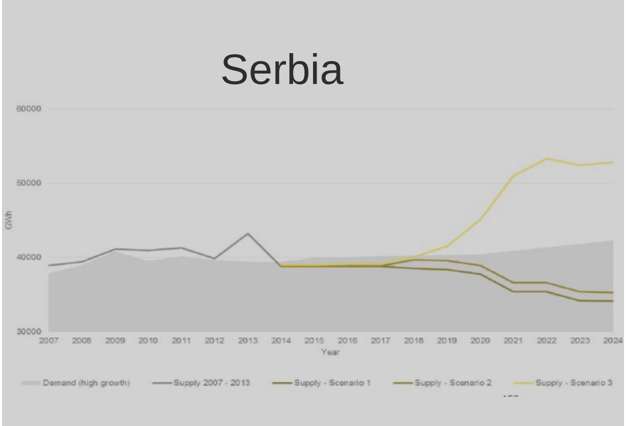






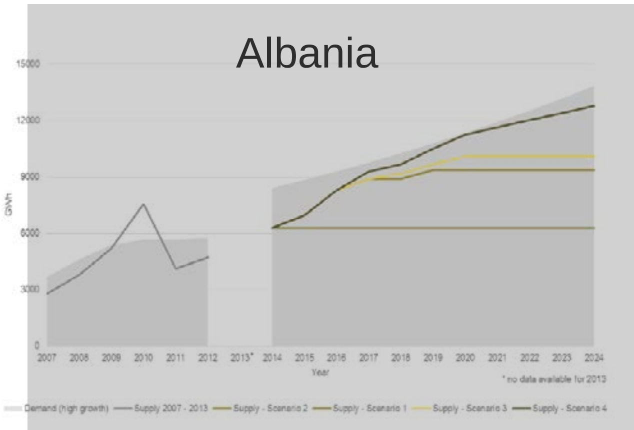


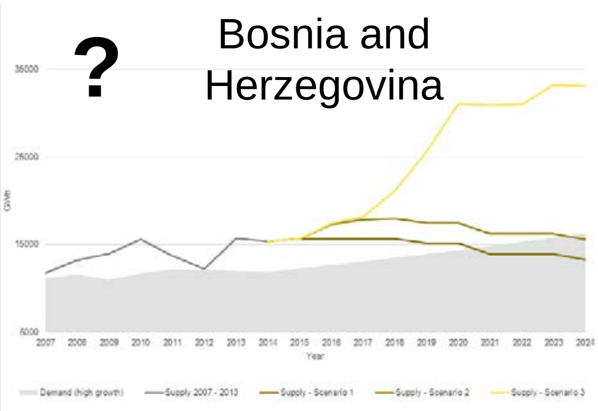


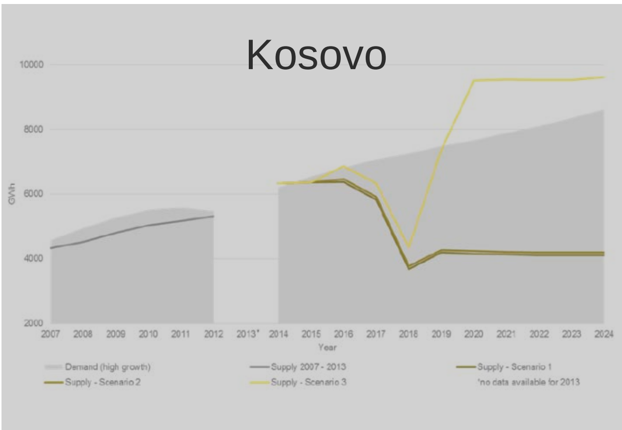


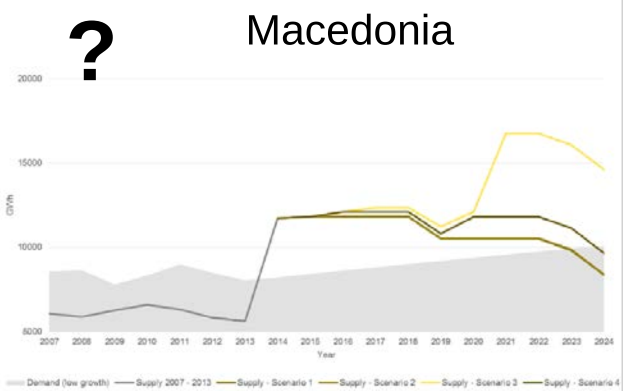
Source: University of Groningen

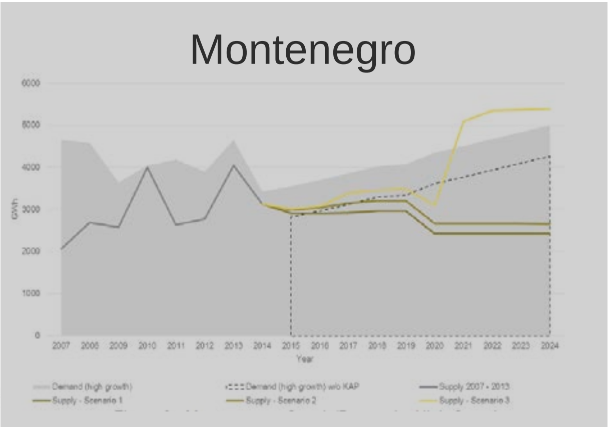
But the others will have to rely on exports if the planned investments are realized

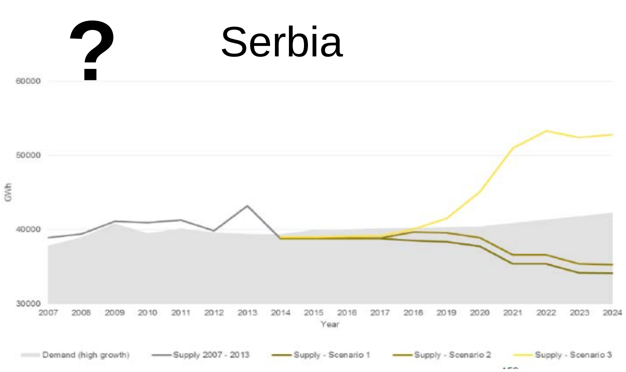












Source: University of Groningen

The risk of stranded electriciy production assests in the region

- There is the need for a better energy cooperation among the SEE economies
- Otherwise a race to the bottom is inevitable. Not enough market for excess electricity energy in Europe
- Turkish companies are used to invest in electricity production assets in case they have state guarantee
  - ➔ A similar arrangement should be put in force

The region needs more oil and gas exploration and drilling activities

- Some proven reserves and high interest from big international oil companies
- Being part of the Energy Charter Treaty is a plus to attract more investments
- The Turkish oil and gas companies could be interested in investing into the region
  - → TPIC, Genel Energy, TURCAS etc...