Turkey

Despite Growth, Europe Remains Distant

Global Economy
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Justin Siken
Economic Overview
Historic Perspective

- **Volatile Growth**
  - Several Financial Crises
  - Dependent on Foreign Capital

- **Inflation**
  - Recurring Problem
  - Exceeded 100% twice

- **Growth Since 2004**
  - 8% average GDP PPP
  - Inflation <10%
  - Gap with EU reduced

### CPI % Change

<table>
<thead>
<tr>
<th>Year</th>
<th>Turkey</th>
<th>Spain</th>
<th>China</th>
<th>USA</th>
</tr>
</thead>
<tbody>
<tr>
<td>1960-1970</td>
<td>3.37</td>
<td>6.16</td>
<td>0.41</td>
<td>2.92</td>
</tr>
<tr>
<td>1970-1980</td>
<td>1.56</td>
<td>3.43</td>
<td>2.99</td>
<td>2.28</td>
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<tr>
<td>1980-1990</td>
<td>2.94</td>
<td>1.45</td>
<td>4.22</td>
<td>2.07</td>
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<tr>
<td>1990-2000</td>
<td>1.43</td>
<td>4.37</td>
<td>5.47</td>
<td>2.39</td>
</tr>
<tr>
<td>2000-2011</td>
<td>3.26</td>
<td>1.41</td>
<td>7.82</td>
<td>0.49</td>
</tr>
</tbody>
</table>

Sources: PMT Country Data, self calculation
Growth Components Comparison

GDP Per Capita PPP (Y/N)

Workers Per Capita (L/N)

Capital Per Worker (K/L)

Total Factor Productivity (A)

Sources: PMT Country Data, self calculation
The 2000-2001 Financial Crisis

Drivers

- Efforts to control inflation (106% in 1994)
- FDI decline (1989-1996)
- Growing deficit
- Weak banking system
- Recession in Europe

The Crisis

- Interest rate spike (3,000%)
- Currency collapse
- Banking sector bailout

Reliable FDI Outflow data not available before 2004; however, large outflows were seen in 1996 after the IMF warned Turkey’s government borrowing was not sustainable.

Sources: World Bank, PMT Country Data
Post-Crisis Reforms

- Fiscal reforms
  - Controlled deficit
  - Reset expectations

- Structural reforms
  - Privatization
  - New FDI rules
  - Simplified corporate taxes
  - Microeconomic liberalization

- Monetary reforms
  - Central bank independence
  - Inflation targeting
  - Currency rebased

Sources: OECD
Continuing Economic Issues
Low Workforce Participation

- L/N lags Europe
  - Unemployment is average
  - Unbalanced gains from trade and urbanization

- Female workforce participation is very low
  - 29% versus 40-65% for most of Europe
  - Decline since 1990s

Sources: World Bank
Poor Competitiveness

- TFP matches peripheral Europe
- Large “shadow” economy
- Burdensome regulations
- Persistent trade deficit and misaligned capacity

Turkey Trade Balance (% GDP)

Total Factor Productivity Comparison

Sources: World Bank, PMT Country Data, Trading Economics
Capital Gap

- Large gap with developed nations
- Capital base growth
  - Low and declining savings rate in Turkey
- Dependent on foreign investment
- Investment will need to increase substantially to support critical L/N growth

Turkey Savings Rate (% GDP)

Alan * (K/L) Comparison

Sources: World Bank, PMT Country Data
Recommendations to Close the Gap
Encourage Women to Enter Workforce

- Minimal cultural difference
- Educated women
  - Leave workforce after having children
  - Solution: Childcare subsidies, preschool
- Uneducated women
  - Not transitioning from agriculture
  - Solution: Continuing education programs
- Opportunity to increase GDP over 35%

L/N Expansion scenario assumes female participation increases to European average by 2050. TFP growth 2% in both scenarios. Left axis is Y/N, right axis is L/N

Sources: Self calculation
Promote Economic Formalization

- Shrink shadow economy
  - Will expand tax base, company sophistication, worker protections/rights
  - Improve competitiveness

Doing Business in Ranking: Turkey

<table>
<thead>
<tr>
<th>Year</th>
<th>Starting a Business</th>
<th>Getting Credit</th>
<th>Paying Taxes</th>
</tr>
</thead>
<tbody>
<tr>
<td>2013</td>
<td>73</td>
<td>82</td>
<td>74</td>
</tr>
<tr>
<td>2014</td>
<td>93</td>
<td>86</td>
<td>71</td>
</tr>
</tbody>
</table>

Business environment
- Reduce required starting capital
- Strengthen creditor prediction
- Improve labor flexibility
- Reduce wage controls

Size of Shadow Economy (% GDP)

Sources: World Bank, Schneider
Encourage Domestic Savings

- Intermediate-term growth possible from investment
- Barriers to remove
  - Persistent inflation
  - Lack of sophisticated banking products
  - Government instability and corruption

Current savings rate is 14% of GDP. Depreciation rate 5%. TFP, and L growth held at 0%