Is Turkish Growth Sustainable?

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Outline

1. Comments

2. A few additional points

But before I go on, for those who are in a hurry:
Is Turkish growth sustainable?

NO! (Can the country grow >5% if there is indeed the “new normal”? Middle-income trap arguments…

Capital Account and GDP Growth (%)
Comment 1: Jobless Growth?

Unemployment and Employment Rates (%)

- Unemployment Rate
- Unemployment rate (seasonally adjusted)
- Employment rate (%)
- Employment Rate (%)

Graph showing trends from 2005.01 to 2013.06.
Comment 1: Jobless growth?

**Turkey’s employment-generating growth** (November 15, 2013)

From 2004 to 2008, annual growth was 5.1 percent, whereas employment rose by 390,000 on average. In other words, we got 76,000 new jobs for each percentage point of growth. From 2010 to 2012, on the other hand, the corresponding figures were 5.4 percent and 1,100,000, which would translate to 204,000 jobs for each percentage point of growth.

By the almost continuous rise in unemployment since June 2012, you could think the trend has been reversed. Nothing could be further from the truth. While third-quarter national income accounts are to be released on Dec. 10, the economy grew 2.6 percent annually during the four quarters before. Employment rose by 742,000 during this period. Using Gürsel's back-of-the-envelope calculation, 290,000 jobs were created for each percentage point of growth.
Comment 2: The export diversification miracle

Two ways to think about this

1. Goods

2. Geography
Economic transformation: a lot of diversification and a little bit of sophistication

<table>
<thead>
<tr>
<th>Turkey’s top-5 export items (1980, share %)</th>
<th>Turkey’s top-5 export items (2010, share %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>13.57</td>
<td>5.45</td>
</tr>
<tr>
<td>11.09</td>
<td>3.47</td>
</tr>
<tr>
<td>7.95</td>
<td>3.01</td>
</tr>
<tr>
<td>6.16</td>
<td>2.93</td>
</tr>
<tr>
<td>4.48</td>
<td>2.42</td>
</tr>
</tbody>
</table>

Source: TEPAV and UN COMTRADE
Comment 2: The export diversification miracle
Comment 2: The export diversification miracle

*Diversification at the expense of sophistication?*

**Orwellian Economics (March 5, 2012)**

IMF paper “*Structural Transformation and the Sophistication of Production*”. The authors build indices for countries’ “sophistication of exports”, as measured by the average income and productivity level associated with all products exported by a country.

Turkey has not been able to increase its export sophistication like China and India. Incidentally, this lack of progress is highlighted in a report from the Economic Research Forum, “The Transformation of International Production Linkages and Turkey” by Erol Taymaz and Kamil Yilmaz.

The billion-dollar question: Why?? Education?
How to make Turkish growth sustainable?

Two ways to think about this:

1. Decrease the current account deficit
2. Manage to live with the deficit
How to make Turkish growth sustainable? 1

Let’s decrease the current account deficit

\[(S-I) + (T-G) = X-M\]

• S-I

• T-G

• X-M
How to make Turkish growth sustainable? 1

Let’s decrease the current account deficit
How to make Turkish growth sustainable? 1

Let’s decrease the current account deficit 1: S-I

Saving Private Savings:

I (October 18, 2009):
- Murat Üçer and Caroline Van Rijckeleghem paper: relate the decline in savings to the post-crisis credit growth and housing price increases.
- Turkey’s middle-class boom

II (March 19, 2012):
- Correlation with women’s LFP and education

III (March 26 2012):
- Demand and supply policies
- How to channel savings into investment
How to make Turkish growth sustainable? 1

Let’s decrease the current account deficit 2: T-G

• Is fiscal policy tight enough?
• Tax reform?
How to make Turkish growth sustainable? 1

Let's decrease the current account deficit 3: X-M

- The misconception on the reasons behind dependency on imports: Cry, the beloved country (November 22, 2009) on
  - Central Bank exporter survey.
  - Too much obsession with the nominal exchange rate: The Admiral has sunk (July 17, 2011)
How to make Turkish growth sustainable? 1

*Let’s decrease the current account deficit* 3: $X-M$

- Transition to high-value added exports?
  - Not only we do not export high value-added products, we are not present in high value-added supply chains. Why?
    - Education
    - Innovation
What is Missing? Education policy is economic policy for Turkey

<table>
<thead>
<tr>
<th>Country</th>
<th>Average age of the population</th>
<th>Female labor force participation rate (%)</th>
<th>Average years of education</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>USA 36.9</td>
<td>58</td>
<td>12.4</td>
</tr>
<tr>
<td>2</td>
<td>China 35.5</td>
<td>67</td>
<td>7.5</td>
</tr>
<tr>
<td>3</td>
<td>Japan 44.8</td>
<td>48</td>
<td>11.5</td>
</tr>
<tr>
<td>4</td>
<td>Germany 44.9</td>
<td>53</td>
<td>12.2</td>
</tr>
<tr>
<td>5</td>
<td>France 39.9</td>
<td>51</td>
<td>10.4</td>
</tr>
<tr>
<td>6</td>
<td>UK 40.0</td>
<td>55</td>
<td>9.5</td>
</tr>
<tr>
<td>7</td>
<td>Brazil 29.3</td>
<td>60</td>
<td>7.2</td>
</tr>
<tr>
<td>8</td>
<td>Italy 43.5</td>
<td>38</td>
<td>9.7</td>
</tr>
<tr>
<td>9</td>
<td>India 26.2</td>
<td>33</td>
<td>4.4</td>
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<tr>
<td>10</td>
<td>Canada 41.0</td>
<td>63</td>
<td>11.5</td>
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<tr>
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<td>Russia 38.7</td>
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<td>Mexico 27.1</td>
<td>43</td>
<td>8.7</td>
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<tr>
<td>14</td>
<td>S. Korea 38.4</td>
<td>50</td>
<td>11.6</td>
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<tr>
<td>15</td>
<td>Australia 37.7</td>
<td>58</td>
<td>9.8</td>
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<td>16</td>
<td>Netherlands 41.1</td>
<td>60</td>
<td>11.2</td>
</tr>
<tr>
<td>17</td>
<td><strong>Turkey 28.5</strong></td>
<td><strong>24</strong></td>
<td><strong>6.5</strong></td>
</tr>
<tr>
<td>18</td>
<td>Indonesia 28.2</td>
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<td>Switzerland 41.7</td>
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<td>10.3</td>
</tr>
<tr>
<td>20</td>
<td>Poland 38.5</td>
<td>46</td>
<td>10.0</td>
</tr>
</tbody>
</table>

Source: TEPAV
A couple of words on education

PISA scores actually undermine the gravity of the situation

- **Bad (and unequal) education** (September 9, 2013):
  - Especially weak in general skills and thinking: [TIMMS study by Education Reform Initiative](#)

Higher Education:

- Again too much inequality
- Not much link to business: [TEPAV- World Bank study](#)
A couple of words on innovation (1)
You need more than creative spelling for Innovation (December 2, 2013)

• Global Innovation Index: Regulatory environment, business environment and education are its weakest input sub-pillars. These deficiencies are well-known, but others that are less so may be equally important: Turkey is also weak in knowledge diffusion, which could, according to recent research conducted at Harvard University, have a huge impact on long-term growth.

• Education: More than meets the eye

• Why would you support start-ups?

• Research has shown, empirically as well as theoretically, that stifling individualism hinders innovation and growth.
What is missing? Turkey’s connectivity problem
(+ prioritization problem: carrying passengers vs. carrying containers)

Regional Picture

Six-lane Expressways (red lines, as of 2010) and the change in the number of firms located in the provinces that had more than 5 firms in the largest 1000 industrial enterprise rating of the Istanbul Chamber of Industry by 2009, between 1997 and 2009.

Source: Istanbul Chamber of Industry and TEPAV
How to make *Turkish growth sustainable? 2*

Learning to live with the current account deficit…

1. Change the composition of financing

2. Try to create buffers against capital reversals
How to make Turkish growth sustainable? 2

(Summary Capital Account Balance (million USD) (12-m rolling)

- Portfolio & Short-term
- Direct Investment & Long-term
How I learned to live with the current account deficit

Why can’t Turkey attract FDI?

• Business Environment: Doing Business, Competitiveness, etc:
  – Doing Business or don’t do business (October 29, 2012)
  – A level playing field? Value of political links, a la Turca

• Policy Uncertainty: Mey and variants...
How I learned to live with the current account deficit

Try to create buffers against capital flow reversals

IMF latest World Economic Outlook Chapter IV- also summary in IMF blog

Countries where volatile capital inflows are balanced by offsetting resident outflows have:

• Strong institutions, such as independent inflation targeting central banks as well as fiscal policy rules that result in lower inflation and more countercyclical fiscal policy outcomes
• Stronger financial supervision and regulation
• More flexible exchange rate regimes and limited restrictions on capital flows
• Large domestic financial systems: e.g. Chile
Just an addendum
A different way of thinking about “sustainable growth”

(UNDP, 1996): Is growth:

- Jobless – growth that does not create new employment opportunities with it.
- Ruthless – growth that only benefits the rich, and leaves the poor in their poverty.
- Voiceless – growth without improvement in democracy or social inclusion.
- Rootless – growth at the expense of cultural identity, or the loss of minority identity.
- Futureless – growth that undermines future generations by depleting resources or destroying biodiversity.
Is Turkish growth ruthless: Inequality

Simple Gini Coefficient hides some of what is going on.

Recent World Banks blog post summarizes
Is Turkish growth ruthless: Poverty

Poverty Statistics

Number of poor (Thousand)

Index

Poverty gap
Poverty rate (%)
Thanks for listening!
Questions & Discussion

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Hurriyet Daily News columns