

In Brief: This brief investigates Turkish foreign economic policies with special reference to the post-Arab uprisings. Relying on the “trading state” framework, it offers a critical analysis as to whether the economic dimension of Turkey’s foreign policy proactivism actually functions as envisaged. It claims that substantial state capacity challenges undermine Turkey’s trading state potential. On the external side, the new regional security environment including the civil war in Syria and failed states in the Middle East and North Africa pose enormous challenges to utilize trade and investment as a practical hand in Turkish foreign policy. On the domestic side, Turkey is approaching the middle-income trap that puts the sustainability of its growth and export performance into jeopardy.

Whither the Turkish Trading State? A Question of State Capacity

by Mustafa Kutlay

Introduction

One of the hallmarks of Turkish foreign policy over the last decade has been the increasing importance of the economy. The utility and function of the economy in foreign-policymaking processes has increased to the extent that some scholars have even called Turkey a “trading state.”¹ Turkey, the argument went, started to rely on trade-driven integration strategies rather than military-driven hard-power supply in its foreign relations. In the post-Arab uprisings, however, this picture has changed dramatically; mounting instability undermines Turkey’s trading state potential. Accordingly, state capacity-related problems — both external and internal — now interrupt Turkey’s trade routes with its neighbors and curtail the growth and export potential of the Turkish economy.

The first and external dimension of state capacity, which is relevant in terms of Turkey’s changing regional security environment, concerns the “stateness” of a state. Strong states are ones that have control over their territory and maintain government authority even in scarcely populated and mountainous areas. Weak or failed states lack this capability. This stateness is crucial in the context of existing debates concerning Turkish foreign policy because the

¹ Kemal Kirişçi, “The Transformation of Turkish Foreign Policy: The Rise of the Trading State,” *New Perspectives on Turkey*, no. 40 (2009): 29-57.

regional security environment changed so radically following the Arab uprisings. The Middle East and North African region, which enjoyed relative political stability pre-2011, has plunged into such volatility that even the stateness of several states in the region was put into jeopardy. Turkey's major economic partners were at the epicenter of spectacular state failures. For instance, the devastating civil war in Syria paved the way for the collapse of the Syrian state, with the death of more than 200,000 people, and the exodus of 4.6 million refugees. The Syrian economy also spiraled into total chaos. According to an United Nations Relief and Work Agency report, "even if the conflict ceased now and GDP grew at an average rate of 5 percent each year, it is estimated that it would take the Syrian economy 30 years to return to the economic level of 2010."² The havoc in Syria, a country that had been considered the poster child of Turkey's transformative success as a regional trading state, has had dramatic negative spillover effects on the Turkish political economy, such as suspended visa-free travel, decreased trade volumes, more than 2.5 million Syrian refugees in Turkey, and terrorist bombings in two main trade areas linking Turkish and Syrian economies. Similarly, the expanding power vacuum in Iraq is producing security threats that cross Turkish borders. Iraq is experiencing a surge in the number of violent non-state actors operating on its soil. Increasing their numbers and expanding their areas of control, these militant groups are one of the biggest impediments to the proper functioning of the Iraqi state, and of Turkish-Iraqi economic relations.

State capacity problems in Turkey's neighborhood largely invalidate previous assumptions regarding Turkey's role because the economy-driven integration theses, which relied on a functionalist logic of bilateral cooperation, took a certain level of stateness for granted. However, the new regional security structure has put Turkey's trade and investment performance in serious jeopardy by undermining the stability of

traditional trade routes. The decline in Turkey's trade with its regional partners is a clear indication of this trend. Turkey's total trade volume with MENA countries declined to \$55.8 billion in 2014; it had hovered around \$63.8 billion in 2012. Economic relations are expected to worsen further after 2015. For instance, the import volume from January to November 2015 decreased 34 percent in comparison to the same period in 2014. Similarly, the export volume decreased 10.4 percent. Members of the self-proclaimed Islamic State group in Iraq demand that Turkish truck drivers pay arbitrary tributes, which poses insurmountable challenges for more than 2,000 Turkish firms operating in the region.³ Turkish trucks cannot now transfer their products through Iraq, the main transport route for Turkish exporters to reach out the Middle Eastern and Gulf countries.

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Worsening ties with key regional countries such as Egypt have also had devastating consequences for Turkey's economic interests. After the collapse of Syria and Iraq, the only remaining viable trade route to the MENA region, via Egypt, also became dysfunctional. Turkey signed the Ro-Ro transit transport agreement with Egypt during the Morsi government to bypass conflict-ridden lands, but this agreement was cancelled by the Sisi administration in retaliation for what it saw as Turkey's harsh political stance. In a similar vein, Libya's internationally recognized government "decided to exclude Turkish firms from operating in

² Aryn Baker, "Syria's Economy Will Take at Least 30 Years to Recover, Says the U.N.," *Time*, April 3, 2014.

³ Ceyhun Kuburlu, "İhracat İçin İŞİD Haracı" ["ISIS Tribute for Exports"], *Hürriyet*, August 8, 2014.

Libya.⁴ Turkish construction firms are estimated to have lost more than \$15 billion, with no serious prospect of compensation. The recent tug-of-war between Russia and Turkey is also likely to disturb expanding bilateral economic relations.

Back to Square One: European Markets, Again

The deterioration of Turkey's economic relations with its neighbors has re-emphasized the importance of the European markets. However, the crisis in the euro area and sluggish growth rates both make Turkish firms less competitive in Europe. Furthermore, the developmental level that Turkey has reached necessitates new policies to counter newly emerging economic challenges and to remain competitive in European markets.

In this context, the second dimension of state capacity that concerns Turkey's domestic economic transformation comes to the fore. States with high capacity have the infrastructural power to organize domestic industrial relations in a way that ensure high value-added production to sustain export performance. Following the 2001 economic crisis, Turkey developed a robust regulatory state, thanks to which the banking system was placed under the strict supervision of independent regulatory institutions. The previously bloated public finance was also put in order. In a benign regional security environment, the government's commitment to a regulatory state paradigm ensured robust economic growth, which in turn constituted the backbone of an economy-led regional integration strategy. At its current level of development, however, the Turkish economy has reached a new milestone: the middle-income trap.

The middle-income trap is defined as the slow-down tendency in rapidly growing economies after their per capita income has reached a certain threshold. Once countries have reached the middle-income plateau,

moving to high-income levels becomes a daunting task. World Bank research estimates that of the 101 middle-income countries in 1960, only 13 reached high-income status by 2008.⁵ There is now a quasi-consensus among analysts that Turkey is approaching this middle-income trap. This trap dictates paradigm change in three interrelated realms. First, Turkey needs a comprehensive industrial strategy to upgrade its production and trade composition because the share of high value-added products relative to Turkey's manufactured exports is now less than 2 percent. Research and development spending is around 1 percent of GDP. Both are comparative very low figures. Second, the education system needs to be reformed so as to encourage creative thinking and mitigate supply/demand mismatch in the Turkish labor market. The average duration of an individual's schooling in Turkey is now 7.5 years, a figure well below the OECD average. Third, the consolidation of the legal system under a pluralistic and inclusive institutional order that guarantees political accountability and transparency will inform the contours of new economic reforms.

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Conclusion

There is a strong correlation between Turkey's economic performance and the success of foreign-policy proactivism. From 2002 to 2007, its economy grew at an annual rate of 6.8 percent, which coincided with Turkey's rising profile as a benign regional power. Economic growth performance declined 3.2 percent annually between 2008 and 2014 for domestic and international reasons. This period similarly coincided

4 "Libyan Gov't to Exclude Turkish Companies from Contracts," *Hurriyet Daily News*, February 23, 2015.

5 World Bank, *China 2030: Building a Modern, Harmonious, and Creative High-income Society*, Washington, March 23, 2013, p. 13.

with ample difficulties in Turkish foreign policy. These challenges have seemingly catapulted Turkish trading state toward a crossroads. The regional security environment has dramatically changed over the last few years. Dealing with failed states and imminent stateness problems, rather than economy-driven integration, are likely to be the main paradigm in the post-Arab upheavals. At the same time, the importance of European markets is likely to make a comeback in Turkey's foreign economic relations. At this point, however, Turkey also has domestic state capacity problems. This suggests that a shift in Turkey's foreign economic policy is in order. Otherwise it might be the case that the Turkish trading state has reached its limits.

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About the Author

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