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Trade Policy Review Body

TRADE POLICY REVIEW

TURKEY

Report by the Secretariat

This report, prepared for the third Trade Policy Review of Turkey, has been drawn up by the WTO Secretariat on its own responsibility. The Secretariat has, as required by the Agreement establishing the Trade Policy Review Mechanism (Annex 3 of the Marrakesh Agreement Establishing the World Trade Organization), sought clarification from the Government of Turkey on its trade policies and practices.

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Document WT/TPR/G/125 contains the policy statement submitted by the Government of Turkey.

CONTENTS

Page

Page

CHARTS

TABLES

Page

APPENDIX TABLES

SUMMARY OBSERVATIONS

(1) THE ECONOMIC ENVIRONMENT

1. Since its second Trade Policy Review (TPR) in 1998, Turkey has implemented four economic stabilization programmes. Trade and investment reforms, with a focus on export promotion, have been major features of these programmes. The fourth programme, initiated in response to the 2001 economic crisis experienced by Turkey, has shown positive results. Real GNP growth improved from -9.5% in 2001 to 7.8% in 2002 (more than double the 3% initial target), and inflation declined from 68.5% to 29.7% (its lowest rate in two decades and well below the 35% official target).

2. As part of its economic adjustment strategy, Turkey adopted a floating exchange-rate regime in February 2001. After recording deficits of 0.7% and 4.9% of GNP in 1999 and 2000, respectively, the current account registered a surplus of 2.4% of GNP in 2001 (partly due to the reduction of traditional merchandise trade deficit following the real depreciation of the Turkish lira by 21.1%); in concert with Turkey's economic recovery, the current account recorded a deficit of 0.8% of GNP in 2002.

3. However, Turkey's economic situation remains fragile. Its public sector net debt burden is still high (79.4% of GNP in 2002): the public sector's primary surplus was 3.9% of GNP in 2002, against a target of 6.5%. Inflation remains high, and since 1998, economic growth has been largely a recovery from recession, with growth alternating with recession.

4. Turkey's vast potential for attracting investment remains largely untapped, in part because of economic instability, slow progress in the implementation of its privatization programme, and restrictions on foreign direct investment (FDI) in sectors such as broadcasting, transport, and telecommunications. Over the period 1980-02, total FDI inflows into Turkey (about US$14.7 billion) were less than foreign investment in some emerging countries in a single year. The 2003 law on foreign investment is expected to pave the way for a surge in FDI inflows commensurate to Turkey's potential.

5. Turkey has a relatively diversified export base. In general, since 1998, the importance of manufactured goods has increased, while the share of primary products (mainly food, and to a lesser extent mining products) has declined. Machinery and transport equipment, clothing, textiles, food products, and iron and steel are the main exports. More than half of Turkey's exports go to the European Union (EU), with Germany the major market. Goods imports, dominated by machinery and transport equipment, chemicals, and fuels, largely originate in the EU (45.3% of total merchandise imports in 2002), led by Germany. Turkey continues to be a net exporter of services, albeit with a surplus that decreased from US$13.5 billion in 1998 to US$7.9 billion in 2002. Tourism accounts for more than half of total services receipts, while the major items on the debit account are transportation and travel services.

(2) INSTITUTIONAL FRAMEWORK

6. Since its previous Review, Turkey has maintained broadly unchanged its overall institutional framework regarding trade policy formulation. The Undersecretariat of the Prime Ministry for Foreign Trade (UFT) continues to formulate, administer, and coordinate Turkey's foreign trade policies. Depending on the nature of the issues, the UFT consults with relevant ministries and other institutions, which also take part directly or indirectly in foreign trade policy formulation and/or implementation. The views of the private sector, including NGOs, are customarily taken into consideration throughout the process.

7. Turkey has amended its domestic legislation on intellectual property rights and telecommunications, and enacted new legislation on, inter alia, customs, anti-

dumping and countervailing measures, standards and other technical regulations, banking, energy, and government procurement to comply with its obligations under the EU acquis communautaire and the WTO Agreements.

8. Turkey is an original Member of the WTO, an observer to the plurilateral agreements on Government Procurement and Trade in Civil Aircraft, and a party to the Information Technology Agreement (ITA). It grants at least MFN treatment to all its trading partners.

9. Turkey has a customs union agreement (mainly on industrial products) with the EU, and a free-trade agreement (also on industrial goods) with EFTA. It has signed 14 bilateral trade agreements (up from six in 1998) with a view to bringing its trade regime into line with its customs union with the EU. Negotiations continue with seven other countries. Turkey participates in the Euro-Mediterranean Partnership, the Economic Cooperation Organization (ECO), and the Black Sea Economic Cooperation (BSEC).

(3) TRADE POLICY INSTRUMENTS

10. The tariff is Turkey's main trade policy instrument. Recent reforms have led to a slight decline in average tariffs; the simple average MFN rate declined from 12.4% in 1998 to 11.8% in 2003. However, the tariff remains complex, still comprising ad valorem, specific, mixed, compound, and formula duties. Non-ad valorem duties apply mostly to agricultural goods. Imports of animal products carry the highest tariffs, with ad valorem rates ranging up to 227.5% on meat products and edible meat offal. In aggregate, the tariff displays mixed escalation, negative from first-stage processed products to semi-finished goods, and positive from semi-finished to fully processed products. This structure is influenced by the high tariffs on raw agricultural products, and to a lesser extent, by the tariff structure in certain industries.

11. Some 46.3% of Turkey's total tariff lines are bound; rates applied to certain products are well below the bound rates. This leaves Turkey margins for tariff increases. Some 1.5% of total lines carry non-ad valorem tariffs while they are bound at ad valorem rates, risking broken bindings. Extension of the scope of tariff binding commitments, and further tariff rationalization, through simplification of the structure and reduction of rates, should introduce more predictability and transparency in the tariff regime, reduce the need for concessions, and ensure the further integration of Turkey into the multilateral trading system.

12. Both to simplify and to harmonize its tax system with the EU's, Turkey has modified its excise duty legislation; introduced the Special Consumption Tax (SCT), which replaced various taxes and charges; and reduced the number of value-added tax (VAT) rates from five to three. However, the Mass Housing Fund (MHF) continues to apply to certain imports of fish and fishery products. With 33 anti-dumping actions out of 46 investigations over the period 1995-02, Turkey ranks eleventh among WTO Members in terms of initiation of anti-dumping investigations. It has not taken any countervailing measures or any action under Article XIX of the GATT.

13. In addition to duty and tax concessions, various incentives schemes are available to Turkish exporters in the form of finance, insurance, guarantee, promotion, and marketing assistance. The number of export credit programmes administered through the Turk Eximbank has increased from 14 to 20 since 1998, and KOSGEB, the public agency for the development of small and medium-size enterprises (SMEs), applies several schemes for improving exports by SMEs. The number of free zones has continued to rise alongside various financial benefits.

14. Turkey enacted two new laws on government procurement, where supplies of Turkish origin are eligible for up to a 15% price preference. In addition, in the automotive industry, foreign investors usually *accept a certain share of local content in their production, although this is not compulsory. In general, import licences are maintained on health, sanitary, phytosanitary, and environmental grounds, under international conventions to which Turkey is a signatory, or to administer tariff quotas set on MFN or preferential basis.*

15. The State exerts a direct and strong influence on the economy, mainly through its control of public enterprises. Some of these are sheltered from competition and some remain a severe drain on public revenue. Recognizing the need to increase efficiency and reduce the pressure on scarce resources, a reinvigorated privatization programme is in progress in many activities, including banking, transportation, energy and telecommunications. In addition to the Competition Authority, several regulatory bodies have been established to handle technical issues relating to competition in their respective areas. Nevertheless, price controls still apply to certain cereals, utilities, energy and sales of tobacco.

16. To improve protection of intellectual property rights (IPRs), Turkey has taken steps to further align its legislation on IPR on the TRIPS Agreement of the WTO and on the relevant EU legislation.

(4) Sectoral Policies

17. Agriculture is an important sector of the Turkish economy despite the decline in its contribution to GDP (to about 12%); it employs over 34% of the population. So far excluded from Turkey's bilateral trade agreements, agriculture remains the most tariff-protected sector, with an average MFN rate of 25%. Tariff protection and State support have insulated the sector from competition and world market price signals. Turkey is in the process of implementing a wide-ranging five-year programme (2001-05) to restructure the sector. Some of the measures that potentially have the most production distorting effects (e.g. administered prices, production subsidies) are being phased out and replaced by a less distortionary direct support system. Turkey also aims to reduce its direct involvement in production, processing and marketing of agricultural goods. However, because of relatively high tariff protection, export subsidies are still granted on certain agricultural products.

18. The mining, quarrying and energy sector is being developed; Turkey is among the fastest growing energy markets in the world. Several public enterprises continue to dominate mining and energy activities in Turkey, and firms and consumers face very high electricity and natural gas prices. With the general objective of improving the functioning of the sector and reducing costly government transfers, the energy sector has a certain priority in Turkey's privatization programme. Under recently enacted laws, the energy sector, the electricity and natural gas markets in particular, is being liberalized, with a view to improving efficiency.

19. Manufacturing contributes around one fifth to real GDP and about 80% to the total value of merchandise exports. Public enterprises have significant shares in industries such as iron and steel, chemicals, tobacco, and beverages. Further, a complex system of state aids to manufacturers remains in place. High tariff protection applies to some processed food products, with tariffs ranging up to 227.5%. In general, in the absence of incentives, the mixed structure of the tariff does not encourage investment in industries producing semi-finished goods.

20. Services is the most important sector in terms of contribution to GDP (about 65%). Turkey has taken measures to address some of the structural problems in certain services activities, notably banking and telecommunications, where independent regulators have been appointed and the scope of the liberalization and privatization process has been extended. Nevertheless, public companies (e.g. Turk Telekom, Halk Bank, Ziraat Bank, and Turkish Airlines) continue to dominate services activities, and still operate under monopoly, or hold exclusive rights in *several branches of the sector. Liberalization of services should improve the efficiency of other economic activities and the competitiveness of Turkey's exports, especially by reducing costs related to telecommunications and transport. Under the General Agreement on Trade in Services (GATS), Turkey maintains some MFN exemptions; it has made commitments in several services categories.*

(5) TRADE POLICY AND TRADING PARTNERS

21. Turkey participates actively in the multilateral trading system and in various preferential arrangements to benefit from increased market access. Its membership in several regional and bilateral trade agreements, particularly the customs union with the EU, has contributed to improving competition in the economy but has also made its trade regime more complex. Future trade agreements could further complicate its regime and might detract from multilateral efforts, given the increased demand on limited administrative and negotiating resources, but delays in alignment of its preferential trade regime to that of the EU's may lead to trade diversion to the detriment of Turkey's exports. Further multilateral trade liberalizations could help address this situation.

22. Because of structural difficulties, high external indebtedness and political instability, Turkey's stabilization programmes are yet to show full and sustained effects. Exclusion of agriculture from areas covered by preferential trade agreements has limited further exposure of the sector to competition. The high level of tariff protection for agricultural products makes it difficult for them to be exported or to be used as inputs in the production of export goods without support, including subsidies. This, together with delays in privatization, further drains resources needed for debt payment.

23. Continued structural reforms, including privatization, and further tariff rationalization would contribute to better resource allocation, and improve Turkey's ability to attract investment. Improvement of Turkey's multilateral commitments, both on goods and services, would increase the predictability of its trade regime and render its reforms more credible. In the meantime, trading partners could help by ensuring that their markets are fully open to Turkey's exports.