

HOW TO PROMOTE MORE TRADE AND INVESTMENT FLOWS THROUGH A PRO-ACTIVE ECONOMIC DIPLOMACY? (1)

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The need for a comprehensive reform agenda has become extremely pressing in Turkey. At the international level, the key element is Turkey's drive towards EU membership, which will require a huge overhaul of its regime, practices and governance (inextricably linked with the pressing need for a new political architecture and a redefinition of tangible national interests in foreign affairs strategy). Domestically, the deepening economic crisis has accelerated needed reforms and brought an unprecedented sense of urgency. The post-crisis Turkey may well rebound and recover quickly on a solid basis, as was the case in the aftermath of the 1997 Asian crisis for Thailand and Korea. We see the novel economic diplomacy strategy as an essential part of Turkey's wide range of policy and institutional reform agenda, designed to put Turkey on a sound footing in the new international system.

More Economics and Less Geopolitics

During the Cold War, the Turkish diplomacy, like that of other NATO nations, was more focused on security, regional stability, and managing the balance of power between two superpowers and two competing models of governance. The business interests often took a back seat to these concerns. Business understood this—but it was frustrating. Today, we live in a different world, where competition among nations increasingly takes place in the economic arena, although for Turkey situated in a difficult neighborhood, the security issues still top the national agenda and foreign affairs. Yet, advancing Turkey's economic interests abroad will not only create valuable new business opportunities for Turkish firms, but this effort will also enhance Turkey's pursuit of more traditional foreign policy and security objectives by creating interdependencies and mutual interests that cannot be readily sacrificed.

Economics and geopolitics cannot be treated in isolation from one another. Without a sound economic base and technological leadership no nation can pursue realistic geopolitical goals. It is the US's number one economy position (not only its military might) that allows Washington to act effectively as the sole superpower in the world geopolitical contest. It is the exhausted, rusty economy that brought down the Soviet superpower in the early 1990s, giving birth to 15 independent states in its former geography. Russia that succeeded the USSR is today trying hard to regain that status – but in vain, unless it transforms itself into a world-class economic and technological might, comparable with the US.

Perhaps it is a bad timing to call today for less geopolitics in view of what's happening in the post-11 September era on the security front. Talks of a new configuration of the political balance in the greater Middle East region are rampant. Strategists, particularly in the US, speculate about the need to draw new maps and are brainstorming on the list of the "rogue" nations that should be ousted, beginning with Iraq. Geopolitical considerations matter a great deal nowadays. However, all these developments also coincide with serious concerns about the global economic

prospects, with the US, the EU and Japan moving from the slow-down toward the recession. So, there is a need to strike the right balance between geopolitics and economics, which have always been firmly linked to one another.

Turkey is currently high in the international agenda due to both its fragile economic situation and the growing geopolitical value. The events of September 11 have highlighted Turkey's status as the only Muslim country, combining modern capitalism and democracy with a moderate brand of Islam. It is also portrayed as the only Muslim country prepared to offer troops to the US-led military alliance against terrorism. On the economic front, the International Monetary Fund (IMF) has spent much of the last year struggling to manage the Turkish financial crisis and the structural reform recipes. The IMF has, in large measure, abandoned Argentina, a country having tried and failed to break out of a vicious circle of rising debt burden, higher interest rates, lower growth and weak government tax revenues. This situation has prompted the debate on whether or not Turkey's strategic significance played a role in IMF's strong support to Turkey under instruction from the US Administration.

Cyprus is another recent case in point, where efforts are today focused more on the geopolitics (i.e., maintaining the existing balance of power in the eastern Mediterranean), with little attention being paid to the economic aspects of the problem. As Cypriot leader Glafcos Clerides and Turkish Cypriot leader Rauf Denktash returned to the negotiating table, they have been discussing more than whether a unified Cyprus government will have a "federal" or "confederal" structure. The dire economic situation in the north and the growing income disparity between the two communities are among the major issues to be addressed. Although Turkish Cypriots yearn for EU membership, their weakened economic condition has made them feel more vulnerable. They worry that the freedoms of employment and property will enable wealthier Greek Cypriots to buy out their businesses and land, and ultimately drive them off the island. Greater economic equalization between Greek and Turkish Cypriots may eventually lead to a comprehensive settlement, thus serving the political interests of all the parties concerned.

Turkey has initiated a comprehensive socio-economic development scheme, called the "**South East Anatolia Project or GAP**". The project area includes the watersheds of the lower Euphrates and Tigris Rivers and the upper Mesopotamian plains. The construction of 22 dams and 19 hydroelectric plants will make the region an "export center" for agriculture and agriculture-based industrial goods. The Middle East, North Africa and the Asia-Pacific regions are the most likely profitable markets for agricultural surplus that will follow the completion of GAP. However, this project has also become the source of an ongoing diplomatic issue between Turkey, Syria and Iraq.

Since the late 1960's Ankara has been arguing for a joint study of land as well as agricultural and irrigational methods, in relation with the region's two transboundary rivers. Syria and Iraq adamantly refuse to discuss water allocation issue on this platform and they, instead, insist on the sharing of Euphrates and Tigris rivers' water flow on the basis of a mathematical division. When the GAP approaches completion, it is expected to revolutionize the economy of the region to such a degree that the ensuing social and economic changes will make it increasingly difficult for the governments of Syria and Iraq to resist indigenous pressures to co-ordinate their economies on a bilateral or multilateral basis with Turkey. Hopefully, the water diplomacy will be the cornerstone of a future regional economic co-operation between these three countries, rather than a source of confrontation.

Turkey is a natural transition point for hydrocarbon supplies from Russia, Iran, Iraq and, more recently, the Caspian

region. It is therefore not surprising that Turkey figures prominently in some of the major pipeline projects from the region, both as a consumer and as a transit point for exports beyond its territory into Europe. The race for a pipeline out of the region towards international markets has turned into yet another Great Game replayed. In the complex Caspian equation, energy security and competition for regional sphere of influence have to be balanced against economic feasibility. Too many routes out of the Caspian would mean smaller economies of scale — and greater expenses — for each project. Into this balance one also must add political realities. Though oil companies may have little enthusiasm for political considerations, they have to deal with them every day. In this process, Turkey, an active player as an energy importer and transit country, can dramatically influence the decisions and the course of events.

In terms of its policies toward Caspian energy, Turkey already has a good model to follow: the approach it has taken thus far toward the question of natural gas. Given the great significance of new gas supplies to the Turkish economy, policymakers recognized early that they could not afford to politicize the issue. The same approach should now be adopted for Caspian oil. Turkey has done all it can to support the Baku–Ceyhan project, and its efforts have given the project a very solid chance at viability despite a number of geographic, geological and economic obstacles. Now the focus is where it should be: on the daunting commercial challenges that are inherent in the financing and construction of an expensive, trans–border pipeline infrastructure. The end–users are more interested in less expensive electricity and gas than the zero–sum geopolitical games.

Strong Potential for Regional Economic Diplomacy

Turkey is the largest economy in its surrounding region and its potential is vast. Turkish society is young and dynamic. It is extremely energetic and adaptable — a society, which has come a long way, is still moving fast, and confident about its future. Today's Turkey is an increasingly diverse society in terms of policy perceptions and outlooks. Overall, this diversity and the sheer dynamism are pointing in the direction of a more modern Turkey, which is capable of having its own vibrant debate about its capacities, constraints and opportunities.

Despite persistent fiscal problems, inflation and budget deficits, and a growth slow–down this year, Turkish economy signifies many of the characteristics of a dynamic emerging economy: growth, a large and fast–growing population, openness to global economic forces, entrepreneurial class, and vast underdeveloped markets ripe for expansion. Turkey is no longer predominantly a rural and agricultural society, but increasingly an urban and industrial one. Income levels in the 'metropolitan' areas and their hinterlands are comparable to those of anywhere else in Europe. Istanbul, a city of around 12 million people, is a European industrial power in its own right and incidentally the largest European city.

The structural changes of the past two decades including the latest IMF–supported program are likely to sustain long–term economic performance. Measured in terms of purchasing power, Turkey ranks as the 17th largest economy in the world with a total GNP of about \$400 billion dollars. The size of its underground economy is estimated as big as the official one. It is by far the largest economy in the Balkans or the Middle East.

At first sight, Turkey has all the assets to function as an economic gateway between regions with sizeable markets and purchasing power from China to Europe, from Russia to the Middle East. The two strongest attractions are its

large domestic market and its skilled and cost-effective labour. The strength and competitiveness of domestically owned companies are another important positive element. Locally owned companies in Turkey, much more than in other countries, function as high-quality suppliers to multinationals. The country's physical infrastructure (i.e. transportation, communications, and energy), though still in need of further expansion and modernization, is one of the most modern and developed in the region.

Despite all its remarkable assets and advantages, Turkey has regrettably been "a miracle in the waiting" for too long largely because of the excessive governance problems. It is difficult to understand how a country as unique and resourceful in many respects as Turkey could not achieve its take-off while many other countries which started the development process later than Turkey have fared much better in raising the living standards of their citizens and enhancing the competitiveness of their national economies in the global marketplace.

"Big Emerging Market" and Growth Sectors

Turkey's prospective market growth and vast potential led to its designation a few years ago by the US Department of Commerce as one of the world's ten "Big Emerging Markets". The value of U.S. exports to Turkey exceeded total American sales to such markets as Russia, Sweden, India, and all of Eastern Europe. The value of total Turkish import demand is on par with markets like Brazil and Indonesia and is significantly higher than Argentina, Poland and South Africa. Increased spending on infrastructure projects and private sector investment is expected to generate strong demand for a wide range of capital goods. Recent export growth underscores the agility of Turkish entrepreneurs and the geographic advantage Turkey enjoys for sales into the European Union, Russia, Central Asia, and Middle Eastern markets.

Turkey's locomotive sectors include: tourism, clothing and knit-wear, ceramics, glass, processed food, construction, leather products, non-electrical machinery, tires, petro-chemicals, iron and steel, and defense industries while sectors with high growth potential include non-ferrous metals, shipbuilding, motor vehicles, mining products, chemicals and electronics. The country's top-five sectors -- namely textile, food, iron-steel and earth products -- provide 83 percent of Turkey's total exports and 66 percent of total employment, followed by agricultural products with 12 percent and mining and minerals with 2 percent.

Tourism is a major source of foreign exchange earnings and job creation. The potential for developing tourism is enormous: 7,000 km of beaches on the Black Sea and Mediterranean coasts, sites of ancient civilizations, both on the coast and inland, snow-covered mountains and a choice of climate (temperate or sub-tropical). Defense industry also shows a rising trend. The Turkish military foresees spending over \$30 billion on arms in the next eight years and up to \$150 billion by 2030. Among the big-ticket items to be contracted over the next decade are 1,000 main battle tanks, 145 attack helicopters, and four airborne early warning aircraft.

Turkey's rapidly growing economy needs new sources of energy. Electrical energy demand in Turkey is growing by approximately eight percent a year. Many possibilities have been identified, be they the Russia-Turkey, Turkmenistan-Turkey-Europe, Turkey-Egypt natural gas projects, or the Baku-Tbilisi-Ceyhan pipeline. The energy sector promises to be one of the lucrative areas for foreign investors. By 2020, Turkey's annual energy demand will

likely increase to 565 kWh. The gap in Turkey's energy needs and its energy supply will be filled by an ambitious plan of energy investments for which the participation of foreign and local private capital has been encouraged by the government. 340 power plants with a total capacity around 87,000 megawatts will be installed by 2020.

There are major investment opportunities concerning infrastructure projects that are essential to supporting Turkey's economic growth. Impressive road and rail projects have been designed in order to connect Pan-European transport corridors to Central Asia. There are plans for new container ports on Northern Marmara and North Aegean locations, in Mersin and Iskenderun. Privatization in telecommunications is on the drawing board. By 2002, Turkey aims to increase its subscriber line capacity to 20 million from 12.7 million in 1993, and increase the telephone line density to 25 per 100 persons. The system is expected to be 80 percent digital by that point. Huge infrastructure projects are not the only opportunities for foreign businesses. From fashion to foodstuffs, Turkey is also producing large quantities of goods that can be exported throughout the world.

Yet, A Timid Player in Economic Diplomacy

The Ozal period witnessed a successful play of the "economics over geopolitics" strategy through the 1980s. He used to take with him hundreds of businessmen to official state visits abroad and lobby for their contracts and trade/investment deals. There were serious allegations of abuse and favoritism during this period. But all these efforts were in large measure based on individual initiatives; an institutionalized approach could not take root. Turkey has lacked an integrated, systematic and consistent framework for economic diplomacy initiatives and their management. After Ozal's departure, economic diplomacy was again relegated to secondary importance. This deficiency has badly reflected on the efforts to maintain and advance the nation's commercial interests abroad. From what we have observed in the international economic fora over the past decade, Turkey seems to have failed to fully grasp the importance of economic diplomacy and the need to employ economics for its political advantages. Attempts to place a comparable emphasis on economic issues as opposed to the oft-mentioned "high politics" are not coherent, well orchestrated and effectively translated from the glossy political statements to actual deeds. As a result, vital economic interests have been compromised.

For example, the Turkish public interest in the EU Customs Union negotiations was mostly related to the ultimate goal of whether Turkey would be included in the list of accession candidates, rather than how such a trade pact will affect Turkey's industrial competitiveness in the Euroland, whether agricultural products and the services sector could also be fitted into the deal, and what sort of additional compensations could have been extracted (2). Despite its obvious benefits to the Turkish economy, the widespread belief is that a better customs union deal could have been concluded if the Turkish negotiators fought their way as hard-nosed and well-prepared as their European counterparts.

Another example that springs to mind is the smooth acceptance by Turkey of China's WTO accession. It is not that we suggest that Ankara could have blocked it; but just like Mexico did as the last country to negotiate its bilateral deal with China on WTO accession terms, Turkey could have used some of its bargaining chips in favor of its textile, clothing and iron-steel industries, which now suffer from the floods of cheap Chinese imports. Another frustration

occurred in Central Asia and Caucasus, where high political and economic expectations were raised without any consideration to Turkey's ability to deliver. A strong government guidance and result-oriented support could have made a big difference. Similar stories can be cited for Turkey's less than successful economic diplomacy initiatives with the US, Russia, Japan and others.

It would, however, be unfair to discount the hard and diligent work performed by many Turkish diplomats in support of economic diplomacy initiatives; but the root problem has been that their efforts are not part of a well-defined and institutionalized strategy that strives to achieve synergies with other governmental departments and the private sector under strong political leadership.

It is true that, whichever way one looks at it, the geography of Turkey is unique. Turkey is the eastern frontier of Europe and the western frontier of Asia. It is at the same time a part of the Balkans, the Caucasus and the Middle East. The Balkans is its access to Western Europe. The Black Sea is a bond between Turkey, Russia and the Ukraine. The Caucasus is its opening to China over the Central Asian republics. And finally, the Middle East and the Mediterranean link it with the Arab peninsula and Africa. However, there is little evidence of the effective use that Turkey has made of such a wide international exposure, particularly for establishing or consolidating its market presence in these regions. In most of the foreign trade and investment statistics of South East Europe, Central Asia, Russia, Ukraine and Caucasus, Turkey trails behind many OECD countries.

Membership in Free Trade Arrangements

In addition to the 1996 customs union, which commits Turkey to adopt the EU's common external tariff and a commercial policy "substantially similar" to that of the EU, including adoption of the EU's preferential trade regime with third countries, Turkey has already signed Free Trade Agreements with the EFTA member countries and is in the process of finalizing agreements with the other EU applicant countries.

There is certainly room for a wider, imaginative economic diplomacy in these regions (which have close historical, cultural and trade ties to Turkey). Turkey is a founding member of the Black Sea Economic Cooperation (BSEC) in which the governments of Albania, Armenia, Azerbaijan, Bulgaria, Georgia, Greece, Moldova, Romania, Russia, Turkey and the Ukraine are nurturing multilateral co-operation on a number of issues including trade. Turkey, along with Pakistan and Iran, is a founding member of the Economic Cooperation Organization (ECO). ECO, whose membership beyond the founders includes Afghanistan, Azerbaijan, Turkmenistan, Uzbekistan, Kyrgyzstan, Tajikistan and Kazakhstan has had limited success in improving trade cooperation. Turkey is a founding member of the Southern Europe Cooperative Initiative (SECI) (3). One can add to this list other less than successful initiatives such as the D-8 group or the Turkic Summit process.

Most of these initiatives were announced with great fanfare, but have not (so far) progressed much due to the lack of clear leadership and vigorous follow-up of their agenda. The need has been strongly felt for Turkey to reconsider the relative importance and perceived benefits of the multiplication of such initiatives that Ankara launched or joined, and come up with a sober assessment of its priorities believed to serve the foremost economic (and foreign policy) interests.

There should be a clear vision of how all these elements can be transformed into Turkey's economic and trade interests in concrete terms, who should be in charge of their implementation and what would be the benchmarks to judge their performance. Otherwise, the rhetoric will continue to prevail. Turkish policy makers have learned that increased economic activities will inevitably lead to increased interdependence and reduced regional political problems, and that they cannot treat domestic issues in isolation of international economic environment and realities.

Openness to Foreign Investment

On paper Turkey has one of the most liberal investment regimes of the OECD. Almost all areas open to the Turkish private sector are also fully open to foreign participation and investment. While Turkey's policies do not discriminate against foreign investment, as is the case in many nations, all companies – regardless of ownership – are subject to the political uncertainties, excessive bureaucracy, and sometimes unclear legal environment that prevail in Turkey, although the recent reforms will reduce the severity of the problems. For instance, although the government strongly supports new foreign investment in Turkey's energy sector, successive court rulings have delayed many projects for years. As a result, aggregate foreign direct investment in Turkey as of 2001 is estimated by governmental sources to be only slightly more than \$13 billion.

According to Turkish Treasury data, as of March 2001, 5,456 foreign firms invested and are operating in Turkey (4) Total authorized foreign capital since 1980 was \$ 29.2 billion, and aggregate actual inflows reached \$ 14.2 billion. In 2000, EU countries accounted for 60.2 percent of authorized new foreign investment, OECD countries accounted for 88.6 percent, and Islamic countries for 2.3 percent. Over the past two decades, France (18.5 percent) has been the top source of foreign investment, followed by the Netherlands (13.6 percent), Germany (12.7 percent) and the U.S. (11.5 percent).

In 2000, about 61.4 percent of foreign investment were in services, 36.4 percent in manufacturing, and about 2.2 percent in mining and agriculture combined. The sub-sectors with the greatest amount of authorized foreign investment include banking (13.9 percent); trade (8.1 percent); food, beverage and tobacco processing (6.5 percent); chemicals (6 percent); and electronics and electrical machinery (3.5 percent). Between 1980 and March 2001, 42.6 percent of actual capital inflows were invested in services, 54.9 percent in manufacturing, 1.5 percent in agriculture, and 0.9 percent in mining.

Corruption remains as a significant barrier to direct foreign investment. Turkey's Minister of Energy was forced to resign in May 2001, in connection with a series of corruption investigations into his ministry. At that time, various investigative bodies were engaged in at least nineteen different high profile corruption investigations. The public has strongly supported these and other investigations and has clearly expressed its preference for greater transparency and accountability by both public and private officials. Turkey has a wide variety of laws, regulations and penalties banning corruption, but enforcement is uneven. Turkey has signed, but not yet ratified, the OECD anti-bribery convention.

Dynamic Private Sector: A New Actor in Foreign Affairs

Many Turks are increasingly uncomfortable with the traditional, dominant role of state institutions. The state still remains a leading actor in the Turkish economy and society as a whole. But the balance is steadily changing, with several important implications for Turkey's economic and political diplomacy. Despite large deficits, high inflation, lack of structural reform, half-hearted privatization efforts, and the deepening problem of the illegal sector, the economic dimension of Turkey's external relations has grown enormously in importance over the past decade. Economic and "geo-economic" issues such as energy investment, Caspian oil routes, water-sharing, environmental standards, Balkan reconstruction, corruption, and co-operation on international crime, are acquiring greater importance.

The Turkish private sector is dominated by a number of large holding companies, whose upper management is controlled by prominent families. They wield considerable political influence. Most large businesses continue to float publicly only a minority portion of company shares in order to limit outside interference in company management. Private-sector organizations, notably the Turkish Industrialists' and Businessmen's Association (TUSIAD), representing a constellation of the most prominent Turkish holding companies, but also TOBB and DEIK, have begun to articulate policy interests in an institutionalized manner. At the same time, these organizations are emerging as more important and influential interlocutors on strategic issues ranging from Russia to EU accession. Turkish entrepreneurs (such as Sarik Tara of ENKA Holding) have played a leading role in the burgeoning economic relationship between Turkey and Russia, now one of Ankara's leading trade partners.

In the Arab Middle East, where Turkey's official relationships have often been difficult, the private sector has been an active player. Turkish influence in the Caucasus and Central Asia has been advanced considerably by the role of Turkish companies and foundations. In the Balkans, where economic reconstruction is high on the international agenda, and closely linked to regional security, the Turkish private sector is involved. It is worth noting that leading actors (such as Rahmi Koc of KOC) on the Turkish commercial scene have been among the most active in attempts to improve Turkish-Greek relations, including joint ventures in the Balkans and elsewhere. The private sector is thus likely to have a considerable influence on the future shape of Turkey's economic and political diplomacy.

No Doubt, Turkey's Economic Future Lies with EU and US

One does not need to be a genius to figure out where Turkey must set its sights for increased trade, investment, finance and technology exchanges. Between 1992 and 2000, U.S. GDP grew from \$7.3 trillion to \$10 trillion in 2000 prices, and the EU from a combined GDP of \$7.6 trillion to \$9.1 trillion. All the nations of the world are vying to sell to these two markets.

Turkey's trade volume totalled \$82.3 billion (\$27.8 bn exports and \$54.4 billion imports) in 2000. Its 10 top export markets and their share are Germany (%18), USA (%10), Italy (%8), UK (%7.2), France (%6.2), Spain (%3.2), The Netherlands (%2.9), Russia (%2.8), Israel (%2) and Belgium (%2). The combined share of Azerbaijan, Kazakhstan, Uzbekistan, Kyrgyzstan and Turkmenistan in Turkey's foreign trade is less than %2. In terms of foreign investors, The Netherlands leads the league, followed by Germany, USA, Italy, UK, Japan and Korea. The Turkish government's efforts to diversify its outreach to Latin America, Asia and Africa have not resulted in any meaningful shift and all initiatives aimed at opening new markets will remain complementary to the primary US and EU markets.

The European Union's Helsinki summit decision of 10 December 1999 declaring that Turkey "is destined to join the EU on the basis of the same criteria as applied to the other candidate States" has profound, somehow painful, consequences for the future evolution of Turkey, that of the European Union and Turkey's relations with the United States. Even if this "historic move" was made for the sake of realpolitik, it still represents a major leap forward in the European strategic thinking. No doubt many Europeans will continue to oppose Turkey's membership on cultural and religious grounds—indeed, such opposition may intensify if Turkish membership becomes a more imminent reality. However, a Turkey economically sound, competitive and solidly anchored to European markets will be relatively easy to adhere to the EU on an equal footing and after the negotiations on EU's common agricultural policy, cohesion/regional funds and free movement of people – areas, which require highly talented and well-trained Turkish trade diplomatists.

Turkey and the United States are engaged in a strategic partnership whose agenda encompasses such critical issues as energy, trade, finance, investment, defense, regional issues and democracy. Relations have entered a new stage after the bipolar world ended and the Soviet Union dissipated. Many political observers thought that Turkey's security value for the Western countries had been considerably diminished; but, as a world power, the U.S. saw the facts earlier than most European countries that on the contrary the geopolitical importance of Turkey has increased more in international politics and economics.

The bilateral trade volume has more than tripled since 1980 – indeed, from \$1.6 billion in 1985 to \$6.4 billion in 1999 — due to the growing awareness of American businesses of the economic opportunities in the Turkish market. However, current trade and investment trends between the two countries clearly disfavor Turkey. The U.S. has gained a significant foothold in almost every sector of the Turkish economy, while Turkish investors and traders' penetration in the world's largest export market remains very limited. Turkey is one of the few countries with which the U.S. has a favorable trade balance: the imports to exports ratio is 2 to 1.

Russia and Turkey are partners as well as rivals. The Ottoman Empire and the Russian Empire, predecessor states to today's Turkish Republic and Russian Federation, fought more than a dozen wars from the late seventeenth century until the First World War. The Turkish–Russian relationship of today is far more relaxed than it has been for decades. Common, sometimes clashing, geopolitical interests assure their interdependence. Substantial Russian–Turkish economic interests are strong enough to overcome the political misperceptions that now mar bilateral relations. Turkey purchases major quantities of natural gas from Russia. There are 30,000 Turkish workers and some \$6 billion invested by the Turkish construction sector in Russia. There is also considerable tourism in both directions.

Middle East and Israel. The increasing sophistication of the Turkish economy gradually reduced the importance of Arab markets in Turkey's overall trade profile — currently a small fraction of its total trade volume. Turkey also signed an agreement with Israel on 14 March 1996, during former President Demirel's state visit to Tel Aviv, which created a free trade area between the two countries, calling for the lifting of all customs tariffs by 2000, and opening the way for joint action in the markets of the US, EU, and the Turkic republics.

The economic component of Israeli–Turkish relations has achieved considerable importance for Ankara. Turkish

exports to Israel have increased thirteen-fold since 1989, from \$30 million that year to \$390 million in 1997. Overall trade volume has grown seven-fold during this period, from \$90 million to \$620 million. In 1989, Israel was merely Turkey's thirteenth largest market in the Middle East and North Africa. By 1997, it was second largest, and, in the first six months of 1998, Israel (\$220 million) had virtually pulled even with Saudi Arabia (\$230 million) as Turkey's leading Middle East/North Africa market. The Islamic Middle East has declined in economic importance for Turkey; once consuming some 45 percent of Turkish exports in the early 1980s, it now buys just 10 percent.

Turkey and China, both situated at the opposing ends of Asia, but linked by the Eurasian landmass, strive for a powerful role, commensurate with their rapidly growing economic and political influence, in their respective geographies. Turkish policy toward China has thus far been driven primarily by a preoccupation with economic concerns. While economic and trade ties remain in the vital interest of Turkey, it is imperative to look beyond these issues to the emerging situations in political, social, and cultural change, with special consideration given to the role of China in Eurasia and the Middle East and potential co-operation areas. Both Turkey and China cannot, and should not, restrict themselves to a single level of political and economic interaction with other nations. Forging an effective and long-term Turkish-Chinese strategic partnership has become an urgent task.

Such a partnership, based on solid and mutually beneficial interests, should not be viewed as coming at the expense of their existing set of relations. Bear in mind that Turkey's traditional allies and partners such as the United States, the EU countries and Japan also strive to forge similar partnership with the "Middle Kingdom".

The Way Ahead

Clearly, the winds of globalization have fundamentally changed the parameters of Turkey's current standing and future prospects in the world geopolitics and economy. If the new trends are not well assessed, the chances are that Turkey could miss some valuable opportunities.

Although the country still has a difficult road to travel before consolidating a fuller democracy and a developed, knowledge-based, world-class competitive economy, few would disagree that Turkey has a potentially critical role in shaping the future of a region of great international importance in economic, security and foreign policy terms. But, to play that role most constructively and to maximum benefit of its national interests, it is widely accepted that Turkey must first address its chronic domestic political and economic problems, and build the necessary capacities in terms of human capital and institutional development.

Current governance and political structures are largely inadequate and ineffective in meeting the challenges of the 21st century and unleashing the vast potential that the country has. They must be reconstructed and modified to respond to new realities and requirements. The reforms that have thus far been proposed, and much less frequently implemented, are usually ad hoc adaptations. To remedy these disconnects in a more fundamental way, Turkey needs a new economic and political paradigm.

The implementation of Ataturk's modernizing program is still in progress and, in our opinion, requires four major rethinking and adjustments (5):

- Achieving domestic stability and peace by ensuring greater freedom and rights, easing the religious polarization, addressing the income disparity and the regional imbalance, as well as restoring the public confidence in the justice system;
- Preparing the ground for, and negotiating its way to, its accession to the European Union in the next decade;
- Greater engagement with the global system, long overdue adjustment in foreign relations, and redefinition of its national interests in light of its domestic circumstances and international winds of change; and
- Building an internationally competitive economy through greater injection of funds to human capital development, by focusing on its emergent strategic sectors and high technologies, as well as through pursuit of a vigorous economic and trade diplomacy.

To do so, Turkey does not need to reinvent the wheel: just look around at the successful examples, such as the UK, France, Singapore, Thailand and Hong Kong, which put the economic diplomacy at the center of their foreign policies. The most effective diplomacy is the one that is well-designed and –orchestrated with key government and private sector actors on board, and it should combine the elements of various types of diplomacy, i.e. political, public, military, trade, energy, environment, water, and culture to achieve synergies.

We all know that those countries that fuse their strategic goals with information, communication and technology and those that convince their people to adopt these targets will lead the 21st century. The Turkey of 2010 and 2015 will be considerably different from the Turkey of today; therefore, we should take a longer-term perspective to achieve synergies between the goals of Turkey's integration with the European Union and its strategic relationship with the United States, without neglecting the dynamic Eurasian and Latin America dimensions. I strongly believe that economics will prevail over geopolitics in the medium to longer term.

1. This paper is the revised version of the author's presentation to the conference on "LA TURQUIE DANS LES POLITIQUES EUROPEENNE ET AMERICAINE, Convergences, divergences et interactions", organized by CERI, Paris, 10–11 December 2001. The views expressed do not necessarily reflect those of any organization he is associated with.

2. The main characteristics of the Customs Union are that goods move freely between the EU and Turkey without being subject to customs duties or quantitative restrictions. In line with the customs union, Turkey has eliminated all customs duties and quantitative restrictions of industrial products of EU origin. The Customs Union covers only industrial and processed agricultural products. Traditional agricultural products are outside the scope of the Customs Union. Concerning processed agricultural products, the parties have agreed on the establishment of a system in which Turkey would differentiate between agricultural and industrial components of the duties applied on these products, similar to the model applied in the European Community. For products imported into Turkey from third countries, Turkey applies duty rates specified in the Community's common customs tariff, except for those products classified as sensitive.

3. A regional association aimed at encouraging cooperation on a variety of issues including customs, transportation and anti-crime efforts. SECI member states include Albania, Bosnia & Herzegovina, Bulgaria, Croatia, Greece, Hungary, the Former Yugoslav Republic of Macedonia, Moldova, Romania, Slovenia and Turkey.

4. Turkey's largest foreign investors include Telecom Italia, Renault, Toyota, Fiat, Castrol, Enron Power, Citibank, Pirelli Tire, Unilever, RJR Nabisco, Philip Morris, United Defense, Honda, Hyundai, Bosch, Siemens, DaimlerChrysler, Chase Manhattan, AEG, Bridgestone–Firestone, Cargill, Novartis, Coca Cola, Colgate–Palmolive, General Electric, General Motors–Opel, ITT, Ford Motor Co., Lockheed Martin, Gillette, Goodyear, Hilton International, Aventis, McDonald's, Nestle, Mobil, Pepsi, Pfizer, Procter and Gamble, InterGen and Shell.
5. Detailed recommendations are made in the author's strategy report "Towards a New Economic Diplomacy Strategy for Turkey" published by TUSIAD in October 1998.

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