

EXECUTIVE SUMMARY

i. **Turkey’s economic development has global significance, given its size, role as a regional power, and strategic location, bridging East and West.** Turkey is a member of the Organization for Economic Co-operation and Development (OECD), and the prospect of European Union (EU) accession remains a key anchor of political and economic reforms. Turkey, with a population of 70.6 million, is one of the large middle-income partners of the World Bank Group (WBG).¹

ii. **Turkey has one of the world’s 20 largest economies.** Gross Domestic Product (GDP) reached US\$400 billion, and GDP per capita reached around US\$5,500 in 2006, following a spectacular recovery from a deep economic crisis in 2001.² Turkey has succeeded in reducing poverty, from about 28 percent of the population in 2003, to about 18 percent in 2006, pulling more than 7 million people out of poverty.³ Fewer than 10,000 people, or less than 0.01 percent of the population, are extremely poor, living on US\$1 or less a day. At the same time, some social indicators lag behind those of countries with similar incomes.

iii. **Turkey’s vision for development, set out in its Ninth Development Plan 2007-2013, is “a country with an information society, growing in stability, sharing more equitably, globally competitive and fully completed her coherence with the European Union.”**⁴ In achieving this goal, Turkey can build on a track record of six years of stabilization, rapid economic growth, and declining poverty.

iv. **The goal of the new Bank Group Country Partnership Strategy (CPS) for FY08-11 is for the Bank Group to be a partner with Turkey in realizing her development vision—to achieve fast and sustained growth with equity—through full integration into the Government’s formulated development strategy.** Accordingly, the CPS is shaped directly by Turkey’s Ninth Development Plan and by the Government’s Program and aims at contributing to three main development pillars: (i) improved competitiveness and employment, (ii) equitable human and social development, and (iii) efficient provision of high-quality public services.

v. **Pillar I: Improved Competitiveness and Employment Opportunities.** Government goals and outcomes to which the WBG program will contribute to under this pillar include (i) sound macro-policies leading to sound public debt and external position, (ii) increased private investment through improved export competitiveness and deeper and broader financial markets, (iii) increased employment, and (iv) reliable and efficient energy supply. Accordingly, analytic and advisory services (AAA)—including economic and sector work, dialogue, workshops, panels, and expert groups—is planned, inter alia, on selected

¹ Turkey is the largest borrower in the Europe and Central Asia Region and it has been the third largest World Bank borrower in terms of new commitments of over US\$1.5 billion during the last three years. Turkey is currently IFC’s fifth largest exposure after Russia, India, China and Brazil. As of September 2007, IFC’s committed portfolio totaled US\$1.6 billion.

² The Turkish authorities are completing work to update the data series for Turkey’s GDP to account for the structural evolution of Turkey’s economy. The update, which is expected to revise GDP upwards and to be released in the coming months, may affect key macroeconomic indicators.

³ National poverty data, TurkStat, end 2006.

⁴ Turkey’s Ninth Development Plan 2007-2013, Page 11, para.1.

growth issues (e.g., employment, informality), Turkey's investment climate, its energy strategy, female labor force participation, financial sector aspects, and public private partnerships. WBG financing under this pillar is planned in the same thematic focus areas—with specific operations and investments expected in the areas of competitiveness, access to export and small and medium enterprise (SME) finance, employment, and private-public financing of skill training and social inclusion as they relate to employment. The CPS also envisages substantial Bank Group financing in the energy sector, which reflects the importance of energy security and energy efficiency for the economy, as well as the priority the Government places on the energy sector and on continued substantial Bank Group engagement. Infrastructure, especially energy and transport, is expected to be a priority area for IFC financing, while Bank support for the railway sector is expected to continue.

vi. **Pillar II: Equitable Human and Social Development.** Government goals and outcomes to which the WBG program will contribute to under this pillar include (i) increased effectiveness of the social security system and improved income distribution as well as improved social inclusion and the fight against poverty, (ii) making the health system more effective, and (iii) enhancing the educational system and increasing the sensitivity of education to labor demand. The CPS envisages continued extensive Bank engagement—including analysis, advice, and financing—as Turkey's partner in the implementation of social security reform as well as social inclusion and welfare policy. Parametric and institutional changes in the pension and health insurance systems, supported by the Bank, are expected to improve the long-term financial sustainability and equity of the social security system and dramatically increase access to health services for the most vulnerable groups of the population, through the introduction of fiscally sustainable universal health insurance. In view of the critical importance of skills to improve competitiveness and employment, and its role in reducing inequalities, education will remain a priority area for the WBG program. Following the completion of the Bank-supported primary education project, ongoing and planned future Bank and IFC financing is expected to focus on secondary and tertiary education as well as technical and vocational skill training, both public and private.

vii. **Pillar III: Efficient Provision of High Quality Public Services.** Government goals and outcomes to which the WBG program will contribute to under this pillar include (i) a better structured public expenditure system, (ii) strengthened public sector governance, and (iii) improved local service delivery and disaster preparedness. The planned WBG program will include analysis, advice and dialogue on public expenditure and finance, public debt management, regional development and municipal finance, and natural disaster risk assessment. Planned IBRD financing includes continued programmatic policy-based lending in support of strengthened public administration and governance and improved public service delivery, in addition to social security reform, as well as financing for investments to strengthen Turkey's cadastre and judiciary systems, municipal infrastructure and services, irrigation, and natural disaster preparedness. IFC financing is expected to focus on private sector participation in urban transport as well as water, wastewater and waste management sectors, as and when further private sector participation occurs in these sectors. The CPS also envisages further exploration of the possible use of the joint WB-IFC Sub-national Financing Facility, which provides financing to sub-sovereign public entities without sovereign guarantees.

viii. **Flexibility is a guiding characteristic of the CPS.** The CPS is demand driven and is designed and will be implemented flexibly, so as to respond to evolving priorities, with an

appropriate mix of instruments. The Government's priorities will drive the program, and the WBG will seek to mobilize the best available technical expertise and international experience and, working together with the authorities, find, develop, and support integrated development solutions. The two main reasons for flexibility in the composition and phasing of WBG financing, reflecting the Turkish authorities' preference, are the intrinsic and persistent uncertainties and volatility in global financial markets and the rapid evolution of the Turkish economy. Such flexibility is also consistent with the implementation of the Bank Group's MIC Strategy.⁵

ix. **The WBG offers Turkey its full range of analytic, advisory, and financing instruments.** The CPS envisages IBRD engagement through free-standing and programmatic economic and sector work, just-in-time TA and advice, WBI capacity building, investment and policy lending at the project, program, sector, local, and country level, contingent financing tools (such as for catastrophic risks), as well as banking advisory services. Development policy lending is expected to account, on average, for around fifty percent of IBRD financing. This substantial share of development policy lending reflects the authorities' strong interest in DPLs to accompany and support Turkey's ongoing reform agenda, primarily because of the Bank's comparative advantage in policy advice and support linked to flexible budget financing. IFC also expects to provide a wide variety of products and services in Turkey—including loans, equity, quasi equity, and syndicated loans. MIGA guarantees are available as well.

x. **The CPS envisages Bank financing equivalent to new commitments up to US\$6.2 billion.** The phasing of Bank financing and the mix of DPLs and investment financing will be flexible. Thus, Bank financing may be front-loaded, back-loaded, or evenly phased, and the share of DPLs may exceed or fall short of the expected fifty percent average in any one year and over the 4-year CPS period—depending on the economic circumstances in Turkey and the substantive content and pace of implementation of the Turkish authorities' economic reform and investment programs. The levels of actual Bank financing will also depend substantially on the availability and terms of other financing, such as from domestic and international financial markets, the EIB, EU, and other development partners.

xi. **The design of the CPS and the Bank Group program reflects lessons learned, which have emerged from close collaboration with the authorities, the Completion Report for the FY03-07 CAS, and the Independent Evaluation Group (IEG's) Country Assistance Evaluation (CAE) , which covered the 1993-2004 period. Three main lessons** are that (i) the programmatic approach to development policy lending has proven useful; (ii) high quality analytical work has been critical as a basis for the in-country policy dialogue on key development challenges; and (iii) ownership and flexibility will be essential for the effectiveness of the new CPS—specifically, reliance on the leadership of the authorities in defining the program, and increased flexibility in terms of lending levels and instruments, content to respond to emerging priorities, and portfolio implementation.

⁵ Strengthening the World Bank's engagement with IBRD partner countries (DC2006-0014), September 7, 2006 and Strengthening the World Bank's engagement with IBRD partner Countries (DC2007-0022), October 9, 2007

xii. **The Bank Group will continue collaborating closely with Turkey's development partners.** Among these partners, the EU is particularly important, because of the process of Turkey's EU membership accession and the significant volume of EU financial assistance on grant terms as well as through EIB. The Bank has become more fully engaged with the members of the United Nations (UN) system, especially in the social sectors and in poverty alleviation and local development/participation. Turkey also receives significant development support from the Islamic Development Bank, the Montreal Protocol, the OPEC Fund, and bilateral ODA from a number of countries. Collaboration with the IMF will continue to focus on public sector and financial sector reforms, along with macroeconomic monitoring.

xiii. **Turkey's economic program and its Bank Group support continues to entail non-negligible risks.** The main risks factors include: (i) political economy risks—where the most important remaining political risks (after resolution of the political uncertainties before and after the 2007 elections) relate to the process of constitutional reform and the border tensions with Iraq, with the EU accession anchor expected to remain a major unifying force behind political and economic reforms and to continue mitigating risks; (ii) external vulnerabilities—where investors will observe the development of Turkey's large current account deficit and reliance on capital inflows, and where maintaining satisfactory macroeconomic performance and continuation of structural reforms will be the key to mitigating external financing risks; (iii) risk of natural disasters—where Turkey is one of the most vulnerable countries to natural disaster but continues to invest substantially in preparedness and mitigation; and (iv) reform implementation risks—where social consensus on the reform program and sufficient institutional capacity are needed for the implementation of the CPS, and which itself includes a host of planned activities that help promote such consensus and help build the requisite capacity.

xiv. **As of January 2008, Turkey enjoys a combination of political and economic stability, with a single-party government with broad public support and a clear mandate, an overall still favorable global economic environment, prospects of EU accession, and favorable long-term population dynamics. These circumstances provide Turkey with an historic opportunity, by continuing its strong economic policies and programs, to achieve sustained high income growth and better lives for the Turkish people and, over the medium term, approach the levels of income and development in other OECD countries and in the EU. This CPS aims for the WBG to be a partner with Turkey in realizing this opportunity.**