

## The Economic and Social Agenda in Turkey--A World Bank Perspective

### Slide 1. Title Slide

**Good evening. I would like to begin with thanking the Turkish American Association for inviting me to this session this evening—and for the opportunity to share with you today my views about Turkey and about the prospects and priorities for the country**

- Turkey's **strong record** of fiscal consolidation and structural reforms after the 2001 crisis has given it a **leading position in the world economy**.
- With sound macroeconomic policies and strong reforms, Turkey will continue to do well and continue to be a good investment—I am confident of that.
- Turkey's **challenge now is how to move to the next development stage**—that is, from \$10-15 thousand per capita income to, say, three times that.
- One **lesson from international experience** is that further significant gains in income per capita will become more difficult, and that such further gains will **require further strong reforms to improve the investment climate and increase productivity**—in addition to sound macroeconomic policies.

### Slide 2. Growth is back...

- On macroeconomic management, **Turkey is doing extraordinarily well in a difficult global environment**.
- Turkey has maintained sound macroeconomic policies and has achieved sustained stability since 2002—which itself has helped boost growth.
- This graph shows, in the red line, quarterly GDP growth (year-on-year). Turkey was among the 10 % hardest-hit countries in 2009; but it was also one of the quickest to bounce back. **Growth in 2010 is likely to have exceeded 8%**.
- Unemployment has come back down. It's 'only' about 1.0% higher than before the crisis.
- **Why did Turkey bounce back so fast?** The key reason is the **structural reforms** since 2002, in response to the **2001 crisis** in Turkey, which was a crisis “**made in Turkey**” (unlike the last one, which was “**made in America**”).

- **The financial system is now in good shape**, banks have enough capital to lend (Turkish banks are actually **among the best capitalized** in Europe, with capital ratios of about 20% of their lending, on average).
- Second, the government has built a **track record of reducing its debt** and managing the economy well. Between 2002 and now the national debt has **about halved**. **Investors** see Turkey as a **well-run economy** they are interested in putting their money into.
- Third, Turkey's **firms are also in good shape**. The financial crisis has in a sense **tested** Turkey's private sector and it **passed the test**.
  - Those debts overseas proved to be manageable; Turkish firms' balance sheets are actually quite healthy.

### Slide 3: External vulnerability

- **As growth has resumed, so has the current account deficit**, particularly as the oil price has bounced back.
- **So far the rising current account deficit to us looks financeable; indeed Turkey has recently been accumulating official reserves.**
- **One development to watch is the proportion of external financing that is short-term.** This graph shows that over half of external financing has recently been short term. A rapid unwinding of these positions could cause volatility. We have a good dialogue with the government on economic management, and we believe they have in place the correct framework to manage this.
- **Recent upgrades in outlook by the rating agencies support our overall positive view on Turkey's economic management and prospects.**
- **In the longer term, higher productivity, higher exports to more diverse markets and higher domestic saving are the keys to reducing Turkey's reliance on external finance.**

### Slide 3. How competitive is Turkey today?

- **The key development challenge for Turkey today, in a global economy with tough competition for investment flows, is to build *global* competitiveness.** Turkey is an OECD and G20 country and competes with Brazil, China, India, Mexico, Russia. This is where many challenges lie.

- **So, how competitive is Turkey, globally, for doing business?**
- **The World Bank Group's *Ease of Doing Business* report for 2011 ranks Turkey 65th among 183 countries.** This is down from 60th place last year.
- Turkey's 65th rank among 183 countries in the World Bank's Doing Business compares with its **61st rank (among 139 countries) in the Global Competitiveness Index (GCI) of the World Economic Forum.**
- By the way, **under the methodology of the Global Competitiveness Index, Turkey is considered to be in the efficiency-driven stage of development.**
  - At this stage, a country must begin to develop more efficient production processes and increase product quality because wages have risen and cannot be reflected in higher prices.
  - So competitiveness is then increasingly expected to be driven by higher education and training, efficient goods markets, well-functioning labor markets, developed financial markets, and the ability to harness the benefits of existing technologies.

#### **Slide 4. Constraints to growth**

- **In our continuing Investment Climate work with Turkey, we try to dig deeper into the possible constraints to productivity and growth.**
- This graphs shows some of the key findings from the most recent round of this Investment Climate work, over the last 12-18 months, which was based on a survey of 1,200 firms.
- **Let me highlight here two obstacles that firms mention that stand out: access to finance, and an educated, skilled workforce.** Firms also mention taxes and political stability—but they do so in many, if not most, countries.
- **Access to finance is a particular constraint for medium-sized firms,** which generate most jobs. 34 percent of medium-sized firms cited this as their single most important constraint.
- **As we are talking about small and medium firms ...**
- **... our Investment Climate work also found strong indications that SMEs are disproportionately burdened by business regulations.**
- The so-called “time tax”, that is the time management spends on government bureaucracy, is a major issue especially for small and medium firms—*if they are formal, or put differently, the time tax is one reason why firms*

**remain informal.** Other reasons of course include taxes, as you can see in this graph as well, and labor regulations, which we already talked about.

**Slide 5. Time tax**

- Now, our Investment Climate survey shows that **the time tax is a problem not just for small firms, but for all firms.**
- **This graph shows that, in Turkey, the top management in enterprises spends a strikingly high amount of time (27 percent) dealing with red tape.** That is, with a large number of rules, with highly complex rules, with differences between rules, with frequent changes in rules, or with a discretionary, unpredictable implementation of rules, be it for taxes, for licenses, for procurement, or other transactions.
- This time tax in Turkey – 27 percent—is much more than in comparator countries such as Brazil (19 percent), Hungary (13 percent), Poland (13 percent), Bulgaria (11 percent), Czech Republic (10 percent), Romania and Chile (both 9 percent).

## Slide 6. Education: Focus on Quality

- Now coming back to education and skills
- Good education and skills are essential for long-term productivity and competitiveness...
- Turkey now has almost universal *primary* school enrolment, and secondary school enrolment has grown significantly.
- Access to preschool and tertiary education are new priorities, and we are working on these with the Government.
- The Government plans to invest much more in preschool education, which is still low in Turkey, and in early childhood development more generally.
  - We enthusiastically support this preschool agenda ... just like we support a continued focus on the education of girls and women, which, over time, will help raise women's labor force participation.
  - There is overwhelming evidence that **such investments in preschool and early childhood development will have large positive effects for children's learning and success later in life.**
  - And in addition they will promote equal opportunities and a fair chance in life for *all* children.
- Now, beyond access to education, Turkey faces a major challenge to improve the quality and relevance of education.
  - **The average 15-year-old Turk lags 1-2 school years behind their OECD counterpart** in reading, science, and math—the graph on the left.
  - The graph on the right shows the regional variation and how far short of OECD standards Turkey's regions are falling.
  - **We are also working with the government on educational quality**, and our new study on the quality of education will come out shortly.

## Slide 7. Unemployment

- So what about jobs?
- This slide shows that **unemployment rates in Turkey have remained stubbornly high**, even during periods of high growth.
- Unemployment is still **high by international standards, and it is especially high among youth**—about double the general rate.
- To be sure, unemployment has come down from the crisis peaks. But if we correct for seasonal effects, total unemployment is still up about 1.5% on pre-crisis levels, more than 2% among the young.
- **Demography is one important reason** for Turkey's continuing high unemployment, including and especially among youth:
  - 700,000 young people join the working-age population every year.
  - **It is a huge challenge to keep creating jobs, good jobs, for so many young people, year after year!**
- **But demography is also a huge opportunity, a potential asset for economic growth:**
  - Generating jobs, indeed generating good jobs, for youth *now* is the key for capturing the large potential dividend of today's large youth cohort.
  - This demographic window of opportunity will close by 2020!
- **Turkey's young people face fundamental challenges when they enter the labor market:**
  - many do not have the skills that employers seek;
  - and **rigid labor markets** make it difficult for employers to hire them
- **So what to do?** The solution lies in addressing these fundamental structural challenges in education and in labor markets ... and the Government has recognized and prioritized this agenda.
- I will come back to these structural policy priorities, education and labor markets, shortly.

## Slide 8. Female Employment

- **Now, in addition to employing its young people, Turkey faces a particular challenge in increasing female employment.**
- Turkey's State Planning Organization and the World Bank jointly conducted a study of the participation of women in the labor force.
  - We found that **only about one quarter of Turkish women participate in the labor force**—less than half compared with the EU and the OECD, as you can see in this group.
  - Moreover, **the rate for women is only about one third of the rate for men!**
- Our joint SPO and World Bank study shows that **increasing the number of women who are actively employed in Turkey would increase national economic output and families' incomes.** It would also improve the lives not just of women, but also of men and children, and it would reduce poverty.

Now I would like to turn to some of the economic policy and reform priorities for Turkey that, we believe, over the medium term can make a difference for economic growth, incomes, and jobs ...

These policy and reform priorities have to do with Turkey's global competitiveness, with making it easier to do business and employ people, with increasing productivity, and with promoting innovation and better education.

## **Slide 9. Labor markets**

- I already mentioned Turkey's labor market regulations as a critical constraint. **Improving labor market flexibility will increase Turkey's competitiveness, promote growth, raise incomes—and also, and importantly, will help create jobs, especially for youth and women.**
- **The Turkish authorities did enact the *first* phase of a labor market reform in the summer of 2008, which is noteworthy and is helping.**
- **But employment protection remains highly restrictive in Turkey.** This slide shows one measure from the Bank's annual *Doing Business* survey: **Turkey's redundancy costs remain exceptionally high, at the equivalent of 95 weeks of salary.** Turkey scores in the lower third of countries on this measure. So focusing on labor regulations will be an important priority for Turkey.

○ **How to make labor markets more flexible while also protecting workers?**

The Government is working intensively on labor market reform, and we have a very productive technical dialogue. We see two important policy directions: (1) reducing **restrictions on flexible contracting**, in particular liberalizing short-term and part-time work; and (2) improving unemployment benefits while reducing **severance obligations**, to **protect workers, people, not jobs.**