CHATHAM HOUSE

briefing paper

After the Boom: Risks to the Turkish Economy

Fadi Hakura

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Summary points

- After a strong post-crisis recovery, Turkish growth slowed sharply to 2.2 per cent in 2012. The success of Prime Minister Erdoğan's government has been rooted in economic prosperity, which will remain a central issue for his popularity.
- Turkey's economy has been boosted by the rise of socially conservative, export-oriented entrepreneurs known as the 'Anatolian Tigers', nurtured by business networking through Islamic social networks, return migration from Germany, free-market economic policies, and institution-building by the previous secular-inclined establishment.
- Other strengths of the Turkish economy include successful strategies for the movement of labour from low- to higher-productivity sectors and poverty reduction.
- The sources of 'easy' economic growth from macroeconomic stability and fiscal discipline have been largely exhausted, however. Turkey's consumer-driven economic model cannot sustain consistently high growth rates and is being undermined by low investment and savings rates, limited export sophistication, pervasive gender inequality and inefficient use of its 'demographic dividend'.
- Turkey's growth potential will be constrained unless it implements productivity-enhancing reforms before the problems of an ageing population start to be noticeable around 2025. To avoid reform 'fatigue', it should focus on tackling the main bottlenecks to economic growth: the quality of human capital, and incomplete reform of governance and institutions.

Introduction

The Turkish economy, once a by-word for hyperinflation and budgetary imprudence, was until recently apparently in the midst of a renaissance. As chilling winds swept through much of the Western world, Turkey was basking in the warmth of 8–9 per cent growth rates, manageable inflation and fiscal probity.

The statistics reveal the extent of this startling economic turnaround. Over the last decade, the world's 16th largest economy grew by $383 billion, exports rose from $63 billion to $135 billion and per capita incomes doubled (in current US dollars) against a backdrop of central government debt shrinkage from three-figure levels to 46 per cent of gross domestic product (GDP).[1]

This turnaround was regarded as all the more remarkable considering the identity of its steward: the Islamist-rooted Justice and Development Party (JDP). Turkey demonstrated – at least on the surface – that Islam, democratic governance and prosperity were perfectly compatible. That was, undoubtedly, a powerful message to the new Islamist governments in Egypt, Morocco, Tunisia and other post-Arab Spring countries.

Recent protests in Istanbul have revealed the polarization within Turkey over Prime Minister Recep Tayyip Erdoğan's social policies and political leadership style. But his electoral success has been rooted in Turkey's economic prosperity, and the sustainability of high growth rates will remain a central issue for the endurance of his popularity. It is therefore important to consider whether Turkey has the wherewithal to maintain recent growth rates given the status of its overall policy reforms, the quality of its institutions and current global dynamics.

This paper seeks to contribute to the debate, first by outlining the major shifts in Turkey's economy and then by assessing whether its economic experience provides an adequate foundation for high future growth rates.

Steady economy

Turkey is a prime case study demonstrating how the effects of a precipitous economic collapse can be reversed. As the liberalization of the 1980s went unsupported by sound macroeconomic policies and institutional reforms, the economy suffered repeated crises in the following decade: in 1991, 1994, 1998, 1999 and, worst of all, 2001. Lack of fiscal discipline and heavy reliance on monetary financing led to high inflation and real interest rates.

An inadequate regulatory and supervisory framework for the banking system encouraged financial institutions to funnel short-term borrowing from depositors into loans of dubious quality and government securities. Inefficient state enterprises dominated several economic sectors. Policy durability was undermined by a succession of short-lived coalition governments that implemented populist measures.

Then, under the aegis of former Economy Minister Kemal Derviş, Turkey recovered swiftly from the 2001 collapse. He concluded a stand-by agreement with the International Monetary Fund (IMF), liquidated insolvent banks, privatized state-owned enterprises, liberalized the energy and telecommunication markets, introduced a free-floating Turkish lira (TL), created an autonomous central bank, and set up independent financial and market regulatory bodies. Turkey's European Union accession process and policy continuity under the subsequent single-party JDP government accelerated the recovery.[2]

Erdoğan's leadership had brought more efficiency and predictability to economic policy-making since 2002. Turkey's central bank had earned plaudits from financial markets for bringing inflation under control.[3] Credibility became a cornerstone of Turkish economic, fiscal and monetary policies, enabling the domestic business community and foreign investors to engage in long-term planning within a more stable political environment.

1 Organisation for Economic Co-operation and Development, http://www.oecd-ilibrary.org/economics/country-statistical-profile-turkey_20752288-table-tur. World Bank, http://data.worldbank.org/country/turkey.

2 Mihai Macovei, 'Growth and Economic Crises in Europe: Leaving behind a Turbulent Past', European Commission (Economic and Financial Affairs Directorate-General), Economic 386, October 2009, http://ec.europa.eu/economy_finance/publications/publication16004_en.pdf.

3 Emre Alper and Ozan Hatipoğlu, 'The Conduct of Monetary Policy in Turkey in the Pre- and Post-crisis Period of 2001 in Comparative Perspective: a Case for Central Bank Independence', Munich Personal RePEc Archive, MPRA Paper No. 18426, January 2009, http://mpra.ub.uni-muenchen.de/18426/1/MPRA_paper_18426.pdf.

The 'Anatolian Tigers'

Turkey has witnessed a conspicuous phenomenon in the Muslim world: the rise of socially conservative, market-embracing and export-oriented business elites combining capitalism with piety. A new class of entrepreneurs, leading mostly family-owned small and medium-sized enterprises (SMEs), unleashed an industrial renaissance in various Anatolian cities in the country's Asian heartland, notably in Balıkesir, Denizli, Gaziantep, Kayseri and Konya. They are challenging the once-unassailable export and investment dominance of Istanbul, the economic powerhouse of Turkey.

'Turkey has witnessed a conspicuous phenomenon in the Muslim world: the rise of socially conservative, market-embracing and export-oriented business elites combining capitalism with piety'

Boydak Holding, a Kayseri-headquartered furniture producer, epitomizes the growth of this modern-day rags-to-riches Islamic capitalism. Founded in 1957, Boydak has catapulted itself from being a small workshop in Kayseri to a multi-billion-dollar industrial conglomerate spanning a bank, a transport company, a trading arm and Turkey's largest cable factory.[4] It now exports to over 100 countries.

Kayseri's 'economic miracle' did not spring out of a vacuum. Islamic social networks facilitated an environment in which budding entrepreneurs could mingle, network and negotiate deals.[5] In the words of one writer: 'They grew up in praying and mosque-going households, and many got to know one another – and still network – in Nurcu circles [a pro-business Islamic social network].'[6]

Three other decisive factors fuelled the success of the 'Anatolian Tigers'. One is return migration: Anatolians returning from Germany replicated business ideas and ventures in their home towns.[7] Secondly, free-market reforms initiated in the 1980s and consolidated under the JDP fostered entrepreneurship, a widening availability of commercial loans and aggressive export promotion in foreign markets.[8] A third, but a commonly ignored, factor was the importation by the previous secular-leaning establishment of European political, economic and social institutions. Turkey stood out for decades as one of the few countries in the region that enjoyed a semblance of democratic pluralism, the rule of law, a modern education system and a viable manufacturing sector.

Structural change

Turkey's economy has been moving resources, predominantly labour, from low-productivity activities, such as traditional agriculture and informality, to higher-productivity, modern industries and the tradable sector. In 2000, manufacturing absorbed a quarter of total public and private investments; by 2008, the figure was 50 per cent. Similarly, the composition of exports has reflected this change.

This diversification of investments and exports into the tradable sector raised the added value of Turkey's productive capacities, its ability to compete in global markets and the private return on invested capital. It is noteworthy that the post-2000 growth rates according to three different

4 European Stability Initiative, 'Islamic Calvinist: Change and Conservatism in Central Anatolia', European Stability Initiative, 19 September 2005, http://www.esiweb.org/index.php?lang=en&id=156&document_ID=69.

5 Pelin Turgut, 'Anatolian tigers: regions prove plentiful', *Financial Times*, 20 November 2006.

6 Vali Nasr, 'Turkey's supreme irony: Kayseri's business globalists', *The Globalist*, 8 June 2010, http://www.theglobalist.com/printStoryId.aspx?StoryId=8292.

7 Deniz Karcı Korfalı, Ayşen Üstübici and Helene De Clerck, 'Turkey: Country and Research Reports', EUMAGINE, 28 September 2010, http://www.imi.ox.ac.uk/pdfs/research-projects-pdfs/eumagine-pdfs/eumagine-project-paper-5-turkey-country-and-research-areas-report.

8 Nicholas Birch, 'Turkey: "Muslim Calvinists" in Anatolia Show How Piety Can Blend with Modernity', Eurasia.org, 23 July 2008, http://www.eurasianet.org/departments/insight/articles/eav072408a.shtml. Simon Cameron-Moore, '"Anatolian Tigers" go where Turkey's diplomacy leads', Reuters, 13 July 2010, http://www.reuters.com/article/2010/07/13/us-turkey-tigers-idUSTRE66C2Q320100713.

measures of productivity – GDP per worker, GDP per capita and manufacturing value added per worker – exceed those in all previous periods.[9]

Poverty reduction

Turkey's growth performance not only created a new middle class – which enjoyed the largest gains of household after-tax income[10] – but also, according to the Organisation for Economic Co-operation and Development (OECD), 'reduced income inequality considerably'.[11] Turkey's Gini coefficient (where 0 and 1 correspond to complete income equality and inequality respectively) decreased from 0.403 in 2006 to 0.38 in 2010.

Furthermore, while the income of the richest 10 per cent in Turkey was about 18 times that of the poorest 10 per cent in 2005, this ratio had narrowed to 14 times by 2009.[12] Similarly, the proportion of Turks below the poverty line fell during this period from 20.5 per cent in 2005 to 18.1 per cent in 2009[13] and the rate of child poverty declined from one-third of children in 2006 to one-quarter in 2010.[14] Poverty and equality indicators have, however, stagnated since 2010.

There are three main causes of this uptick between 2006 and 2010: a three per cent yearly increase in non-agricultural employment; a reduction in interest on debt payments from 22 per cent to 16 per cent of the national budget, allowing for increased social transfers to the poor; and a rise in the minimum wage and in the lowest public-sector earnings by, respectively, 16 per cent and 28 per cent in real terms (i.e. omitting inflation).

'Objective 2023'

Erdoğan's 2011 general election slogan, 'Hedef 2023' ('Objective 2023'), set the ambitious target of tripling the size of the economy, increasing exports to $500 billion and joining the world's top ten economies by 2023, the centenary of the Turkish republic. Average per capita income would, he predicted optimistically, be $25,000 a year, not far below that of Spain today.[15]

> 'Erdoğan's 2011 general election slogan set the ambitious target of tripling the size of the economy, increasing exports to $500 billion and joining the world's top ten economies by 2023'

Turkey would need annual growth of nine per cent to satisfy the prime minister's expectations, of which 3–4 per cent is 'guaranteed' growth assuming a two per cent US dollar inflation and 1–2 per cent yearly appreciation of the Turkish lira. This means that during the next decade Turkey needs at least an annual average GDP growth rate of five per cent, grounded on exports rather than domestic demand.[16]

It has been argued that few countries manage to achieve growth rates of eight per cent on a durable basis. As reported by a commission of 19 political leaders and

9 Dani Rodrik, 'The Turkish Economy After the Crisis', Harvard University, 24 November 2009, http://www.hks.harvard.edu/fs/drodrik/Research%20papers/Turkish%20economy%20after%20the%20crisis.pdf.

10 Emre Deliveli, 'Social Implications of Turkish Reforms', *Hürriyet Daily News*, 15 April 2013, http://www.hurriyetdailynews.com/social-implications-of-turkish-reforms.aspx?pageID=449&nID=44893&NewsCatID=430.

11 'Divided We Stand: Why Inequality Keeps Rising', OECD, December 2011, http://www.oecd.org/document/51/0,3746,en_2649_33933_49147827_1_1_1_1,00.html.

12 Turkish Statistical Institute, http://www.turkstat.gov.tr/PreTablo.do?alt_id=1011.

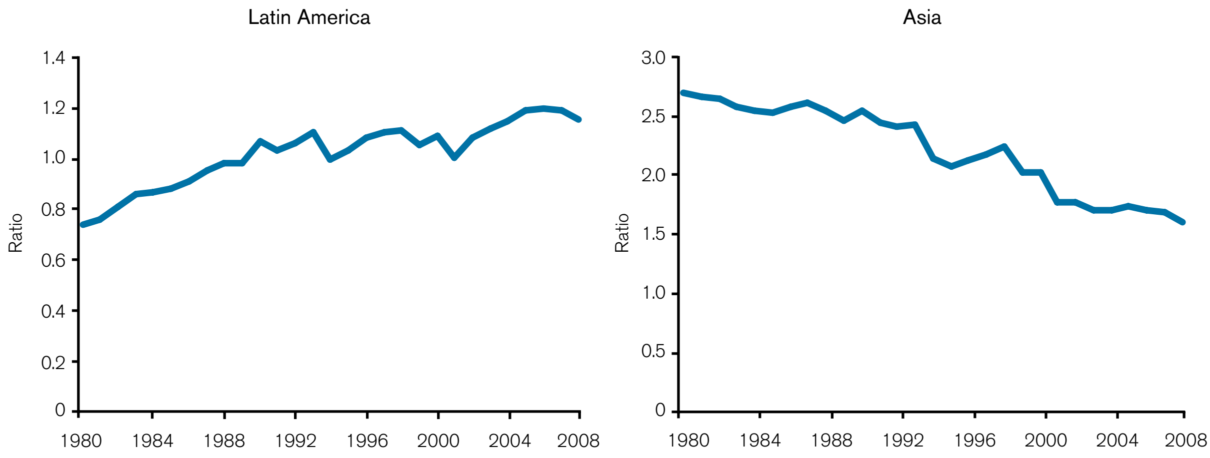
13 World Bank, http://data.worldbank.org/country/turkey.

14 Seyfettin Gürsel, 'Material deprivation among children', *Today's Zaman*, 22 April 2013, http://www.todayszaman.com/columnist-313393-material-deprivation-among-children.html.

15 Gwynne Dyer, 'Will Turkey grant Erdogan's dreams?', *Winnipeg Free Press*, 11 June 2011, http://www.winnipegfreepress.com/opinion/westview/will-turkey-grant-erdogans-dreams-123678784.html?viewAllComments=y.

16 Seyfettin Gürsel, 'AK Party's 2023 vision', *Today's Zaman*, 4 October 2012, http://www.todayszaman.com/columnist-294315-ak-partys-2023-vision.html.

Figure 1: Ratio of GDP growth per capita in Turkey to growth in Latin America and Asia, 1980–2008



Source: Dani Rodrik, 'Turkey's Growth Story', presentation at the conference on 'Turkey's Experience with Neo-Liberal Economic Reforms', London School of Economics, 28 October 2011.

Notes: 1.0 on the scale represents equal growth.

Asia includes Hong Kong, Malaysia, the Philippines, Singapore, South Korea, Taiwan and Thailand.

Latin America includes Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Mexico, Peru and Venezuela.

academics from around the world tasked with identifying important insights on policy levers to help countries achieve high, sustainable and inclusive growth, economies confined to a model based on private consumption rarely witness consistently high growth rates.[17] Turkey, where private consumption accounts for 70 per cent of national income, typifies such an economy.

Turkey is categorized as an 'upper-middle-income' country by the World Bank (defined as having per capita income between $3,976 and $12,275).[18] Its GDP per capita growth rate was between that of Latin America and that of Asia until recently (see Figure 1). In 2012, its growth was 2.2 per cent.[19]

In the case of Turkey, the risks of restrained growth rates are real and substantial. It needed 55 years to escape its low-income status,[20] which is comparatively much easier than achieving the transition from middle-income to high-income status. Turkey has so far experienced only the 'easy' growth derived from macroeconomic stabilization[21] and can no longer simply rely on low-cost labour resources and the easy adoption of new technology as sources of growth.

Figure 2 indicates that during the last decade Turkey's economy has experienced two episodes of sharp recession followed by a booming recovery and a subsequent period of prolonged deceleration: in 2002–07 and 2008–12. These exemplify an economy hovering between stagnation and a solid growth cycle, where domestic demand cannot sustain growth and employment indefinitely.[22]

17 Commission on Growth and Development, 'The Growth Report: Strategies for Sustained Growth and Inclusive Development', World Bank, 2008, http://siteresources.worldbank.org/EXTPREMNET/Resources/489960-1338997241035/Growth_Commission_Final_Report.pdf.

18 World Bank, http://data.worldbank.org/about/country-classifications/country-and-lending-groups#Upper_middle_income.

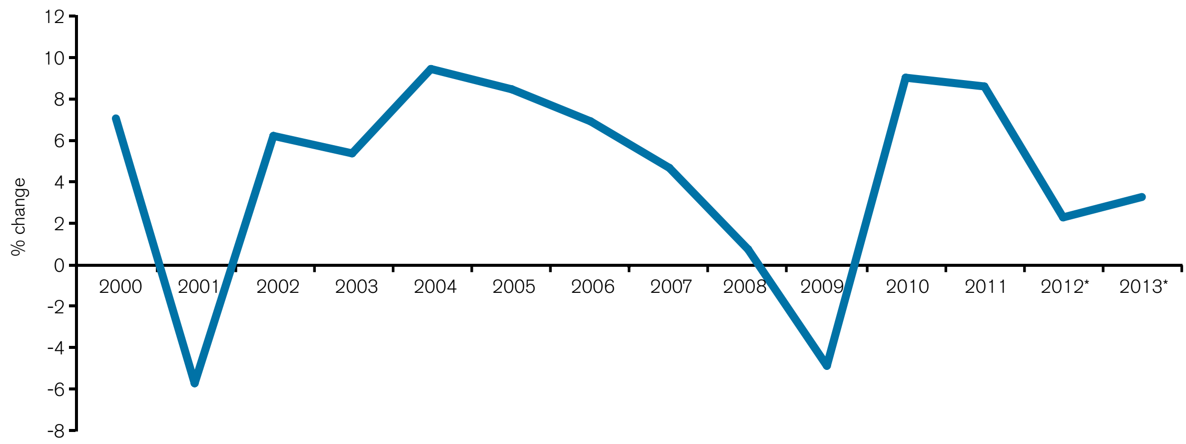
19 http://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG.

20 Hakan Taşçi, 'The real challenge for the Turkish economy', *Today's Zaman*, 22 May 2012, http://www.todayszaman.com/columnist-281105-the-real-challenge-for-the-turkish-economy.html.

21 Willem H. Buiter, 'It's a long way to Copenhagen', CEPS Policy Briefs, 1 March 2006, http://www.ceps.eu/book/its-long-way-copenhagen.

22 Cevdet Akçay and Murat Üçer, 'A Narrative on the Turkish Current Account', *International Journal of Trade and Diplomacy*, Vol. 2, Winter 2008, https://www.simmons.edu/academics/undergraduate/east-asian/docs/Ogus_Binatli_and_Sohrabji-JITD_paper.pdf.

Figure 2: Turkey's GDP 2000–13, constant prices



Source: IMF, *2012 World Economic Outlook.*
*Projected.

Turkey's consumption-based economic paradigm has several characteristics that undermine growth: low investment and savings rates, limited sophistication of exports, pervasive gender inequality and inefficient use of its 'demographic dividend'. Each of these features will be elaborated in turn below.

Domestic investments and savings

Generally, sustainable growth requires national investment rates of 25 per cent of GDP or above, counting both public and private expenditure. Between 2000 and 2010 Turkey's rate fluctuated between 15 per cent and 22 per cent of GDP, and in only four years of these years did it exceed 20 per cent.[23]

In addition, the quality of its insufficient investment rates is wanting. Turkey misallocated investment expenditures from manufacturing towards residential uses and other non-productive sectors in the post-1980s period; and this was accompanied by the fact that public and private investment no longer complemented each other.[24] Istanbul's skyline testifies to this dash for concrete, which triggered the recent protests over redevelopment plans for Gezi Park adjoining Taksim Square, one of few remaining green spaces in Istanbul; TL 7.5 billion ($4.6 billion) had been earmarked for urban renewal projects in the city for 2012 alone.[25]

High-growth economies need to set aside a considerable share of their income as savings, with a national savings rate of at least 20–25 per cent of GDP, to fund domestic investment needs. Turkey's savings rate, on the other hand, decreased from over 23 per cent in the 1990s to 12.7 per cent in 2010, the lowest rate since 1980.[26] The main culprit is plummeting household savings, which more than offset the increase in savings that would normally be associated with rising incomes. This is due to post-crisis credit growth, falling interest rates, rising

23 World Bank, http://data.worldbank.org/indicator/NE.GDI.TOTL.ZS.
24 Sumru Altuğ and Ünal Zenginobuz, 'What has been the Role of Investment in Turkey's Growth Performance?', Boğaziçi University, February 2009, http://www.econ.boun.edu.tr/public_html/RePEc/pdf/200902.pdf.
25 Constanze Letsch, 'Istanbul sees history razed in the name of regeneration', *Guardian*, 1 March 2012, http://www.guardian.co.uk/world/2012/mar/01/istanbul-city-urban-renewal.
26 World Bank and Turkey's Ministry of Development, 'Sustaining High Growth: The Role of Domestic Saving', Turkey Country Economic Memorandum, Synthesis Report (Conference Edition), 14 March 2012, http://siteresources.worldbank.org/TURKEYEXTN/Resources/361711-1331638027014/CEM_DomesticSavings_fulltext.pdf.

house prices, pent-up consumption and the increase in the middle classes' share of consumption.[27] As the economy recovered, this reduced the need for 'precautionary savings' (i.e. money saved to guard against the uncertainty of future income).[28]

Unsurprisingly, the ratio of household liabilities to disposable income has grown from 4.7 per cent in 2002 to 50.6 per cent in 2012.[29] This may indicate the increasing likelihood of a financial crisis in the near future that will be exacerbated by the steady rise in the share of consumer credit in the budgets for the lower- and middle-income households and by declining rates of home ownership for the median group of households which constitute the backbone of the labour force.[30] At 51 per cent of GDP, Turkey's net external debt is among the highest for emerging markets, driven mainly by a surge of private-sector borrowing.[31] The average debt-to-equity ratio of the largest 500 firms in Turkey was 120 per cent in 2010 and 141 per cent in 2011, compared with roughly 50 per cent in the United States and 70 per cent in Europe in 2011.[32]

Turkey's current account deficit (CAD), where national investments exceed national savings,[33] reached an unsustainable 10 per cent of GDP in 2011 and is expected to shrink only gradually in the next few years.[34] Turkey is in a vicious circle: economic growth drives investment needs that cannot be satisfied by domestic savings,[35] which causes addiction to fickle and footloose speculative financial flows ('hot money') to finance its CAD.[36] Owing to the 'sudden stop' of foreign capital inflows in the 2008–09 global financial crisis, Turkey suffered one of the sharpest subsequent recessions among emerging markets.[37]

Turkey's persistent CAD is driven primarily by structural, as opposed to cyclical, factors: a low savings rate, trade composition, and a heavy dependency on imports of energy, intermediate and capital goods in relation to Turkish exports and manufacturing industry.[38] Reliance on an overvalued lira to control inflation, the inflation differential relative to other currencies and the excessive importance of intermediate imports mean economic growth hurts the supply of exports and trade balances.[39] Turkey's imports of goods and services as a proportion of GDP rose from 26.2 per cent to 32.7 per cent between 2004 and 2011, while its exports of goods and services rose only from 23.6 per cent to 23.8 per cent in the same period.[40]

27 Murat Üçer and Caroline Van Rijckeghem, 'The Evolution and Determinants of the Turkish Private Saving Rate: What Lessons for Policy?', ERF Research Report Series No. 09-01, February 2009, http://eaf.ku.edu.tr/sites/eaf.ku.edu.tr/files/rr09-02.pdf; Cevdet Akçay and Murat Can Aşlak, 'One Man's Happiness is Another's Agony? Not Necessarily', Yapı Kredi Bank, Macro Brief, 20 November 2008, http://www.yapikredi.com.tr/enUS/macroeconomic_research/pdf/macro_briefs/2008-11-20.pdf.

28 Emre Deliveli, 'Saving private savings II', *Hurriyet Daily News*, 19 March 2012, http://www.hurriyetdailynews.com/saving-private-savings-ii.aspx?pageID=449&nID=16304&NewsCatID=430.

29 Emre Deliveli, 'Marcroeconomics 101 for journalists confused by Finance Ministers', *Hurriyet Daily News*, 24 June 2013, http://www.hurriyetdailynews.com/macroeconomics-101-for-journalists-confused-by-finance-ministers.aspx?pageID=449&nID=49321&NewsCatID=430.

30 Alper Duman, 'Household Debt in Turkey: The Critical Threshold for the Next Crisis', Izmir University of Economics, Prepared for ECOMOD 2013, April 2013, http://www.ecomod.net/system/files/HouseholdDebtinTurkeyAlperDuman.pdf.

31 Benjamin Harvey and Taylan Bilgiç, 'Erdogan's IMF Triumph Masks Surge in Private Debt: Turkey Credit', Bloomberg, 14 May 2013, http://www.bloomberg.com/news/2013-05-13/erdogan-s-imf-triumph-masks-surge-in-private-debt-turkey-credit.html

32 Vefa Tarhan, @Vefa_Tarhan, 20 June 2013, http://www.twitlonger.com/show/n_1rku9vq.

33 An alternative definition of current account deficit is the sum of imports of goods and services plus net returns on investments exceed the value of goods and services.

34 'Turkey posts record current account deficit', *Hurriyet Daily News*, 14 February 2012, http://www.hurriyetdailynews.com/turkey-posts-record-current-account-deficit.aspx?pageID=238&nID=13690&NewsCatID=344.

35 Fazıl Kayıkçı, 'Discussion on Sustainability of Current Account Deficits in Turkey', *International Research Journal of Finance and Economics*, Issue 74, 2011, http://www.eurojournals.com/IRJFE_74_08.pdf.

36 'Istanbuls and bears', *The Economist*, 7 April 2012, http://www.economist.com/node/21552216.

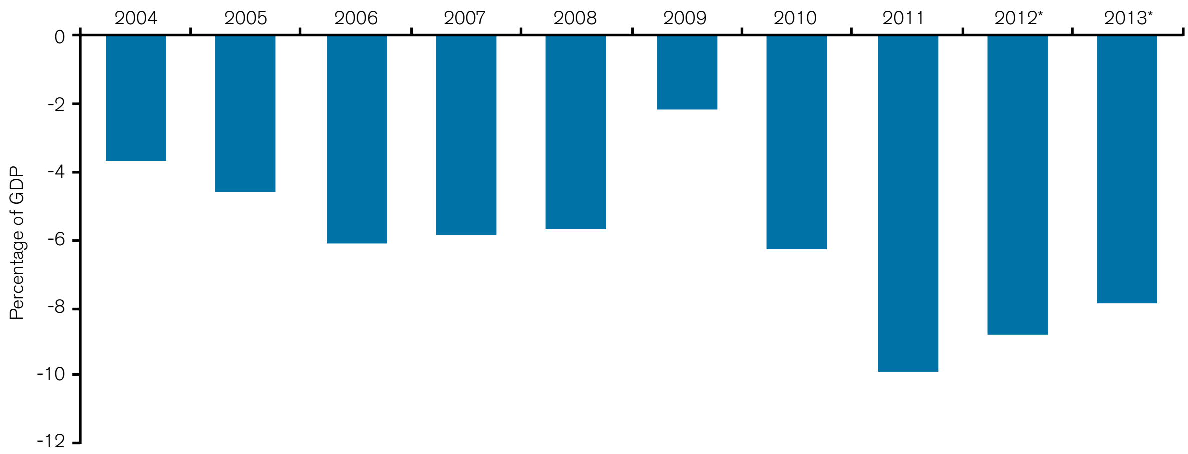
37 Rodrik, 'The Turkish Economy After the Crisis'.

38 Mary Stokes and David Rogovic, 'Mind the (Current Account) Gap in Turkey', *Forbes*, 25 August 2010, http://www.forbes.com/2010/08/25/turkey-deficit-economy-opinions-columnists-doctor-doom.html.

39 Ayla Oğuş Binatli and Niloufer Sohrabji, 'Elasticities of Turkish Trade', Izmir University of Economics, Working Paper 0906, 2009, http://www.simmons.edu/undergraduate/academics/ departments/economics/docs/Turkish_trade_elasticities.pdf; Yaşar Vural and Mahmut Zortuk, 'Foreign Direct Investment as a Determining Factor in Turkey's Export Performance', *Eurasian Journal of Business and Economics*, Vol. 4, No. 7, 2011, http://www.ejbe.org/EJBE2011Vol04No07p13VURAL-ZORTUK.pdf.

40 OECD, http://www.oecd-ilibrary.org/economics/country-statistical-profile-turkey_20752288-table-tur.

Figure 3: Turkey's current account balance, 2001–13 (as % of GDP)



Source: IMF, *2012 World Economic Outlook.*
*Projected.

Since Turkey's export and import growth tend to move concomitantly, the CAD cannot be effectively dealt with by depreciation of the lira alone. Thus the foreign trade and current account deficits are not necessarily 'sustainable' (i.e. at a level that prevents a permanent increase in a country's external debt-to-GDP ratio) without slower economic growth and a contraction of domestic consumption, as happened in 2009 (see Figure 3), which would reduce the CAD to a more manageable five per cent of GDP, thereby leaving it less vulnerable to the vagaries of international financial flows.[41]

This mismatch between global purchasing power and domestic productive capacity cannot continue to grow indefinitely. One can measure the former by average purchasing power (dark blue line in Figure 4) in US dollars and the latter by average productivity (light blue line in Figure 4). According to one study, this implies that Turkey's 'average dollar-based income – per capita as well as per worker, currently running at around $10,000 and $30,000, respectively – is simply too high, compared to [its] average productivity levels'.[42] As a result, Turkey's per capita incomes increased by only 31 per cent (in constant 2005 US dollars) after stripping out inflation and exchange-rate effects,[43] rather than the oft-quoted 300 per cent in nominal terms.

The government has not delivered an adequate policy response so far. It has opted for tax incentives to encourage indigenous production of intermediate goods and reduce its import needs – a form of import substitution – while also increasing government contributions to and tax breaks for private pensions. The tax incentives are expected to have only a limited impact on the national savings rate[44] and several economists have questioned the efficacy of the latter as a highly complex scheme that does not tackle the root

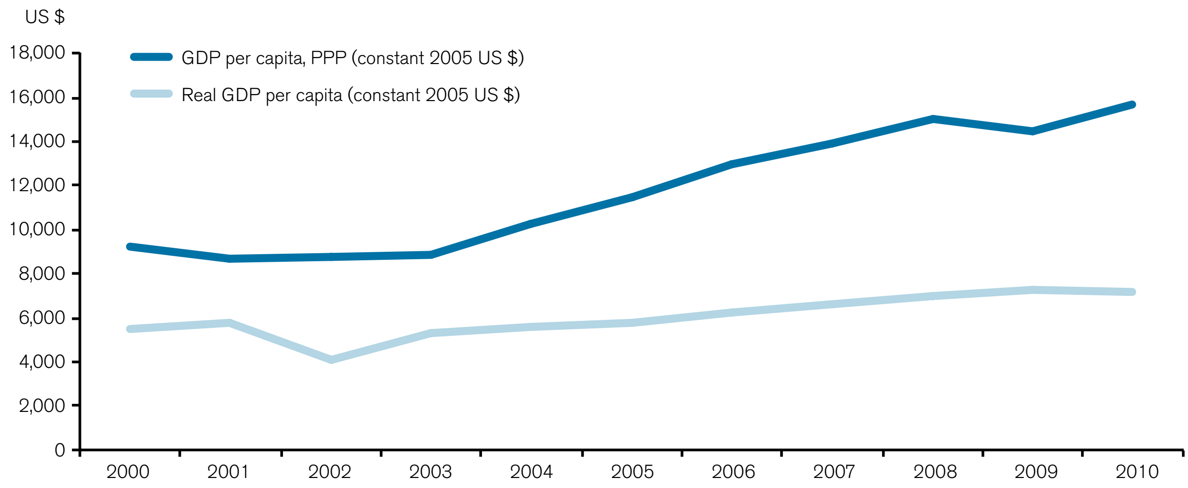
41 Aysu İnsel and Fazıl Kayıkçı, 'Evaluation of Sustainability of Current Account Deficits in Turkey', *Modern Economy*, Vol. 3, No. 1, January 2012, http://www.scirp.org/Journal/PaperInformation.aspx?paperID=16805.

42 Murat Üçer, 'How Should We Read Turkey's Current Account Deficit?', Centre for Economics and Foreign Policy Studies (EDAM), Autumn 2011, http://edam.org.tr/document/Newsletter%202011-Fall.pdf.

43 World Bank, http://data.worldbank.org/indicator/NY.GDP.PCAP.PP.KD?page=1.

44 Caroline Van Rijckeghem and Murat Üçer, 'The Evolution and Determinants of the Turkish Private Saving Rate: What Lessons for Policy?', Powerpoint presentation, 11 June 2008, at the TÜSIAD-Koç University Economic Research Forum Conference on Micro-Macro Perspectives on Private Savings in Turkey, http://eaf.ku.edu.tr/sites/eaf.ku.edu.tr/files/cvr.pdf.

Figure 4: Turkey's global purchasing power versus domestic productive capacity



Sources: World Bank and US Department of Agriculture.

causes of the CAD.[45] Instead, considering the argument that sustainable high economic growth precedes higher savings, government policy needs to focus on removing impediments to growth and reducing the vulnerability resulting from low savings during the transition period.[46]

Limited sophistication of exports

A recent IMF paper constructed indices for countries' 'sophistication of exports', as measured by the average income and productivity level associated with all their exports. This demonstrates that increasing the sophistication of exports of goods and services can be an important contributor to overall economic growth. More sophisticated sectors not only create more value-added activities but also act as 'engines of growth', as they generate spillover effects for the whole economy.[47]

Turkey is in the middle of the spectrum of export sophistication; it has not yet been able to increase its export sophistication as China and India have done.[48] It has specialized in stagnant sectors whose share of global trade has been declining and is generally more competitive in goods with lower relative prices, where minimizing costs is the strategic issue.[49] High-tech exports – products with high research and development intensity, such as in aerospace, computers, pharmaceuticals, scientific instruments and electrical machinery – have accounted for just two per cent of total manufactured goods exports on a consistent basis since 2002.[50]

45 See, for example, Oxford Business Group, 'Turkey: a Cautious Approach', 9 May 2012, http://www.oxfordbusinessgroup.com/economic_updates/turkey-cautious-approach; Emre Deliveli, 'Turkey: Industrial Policy, New Investment Incentives Scheme and the Current Account', Emre Deliveli's Blog, 26 May 2012, http://www.economonitor.com/emredeliveli/2012/05/26/turkey-industrial-policy-new-investment-incentives-scheme-and-the-current-account/; and Ozan Acarı and Esen Çağlar, 'An Assessment on the New Incentive Package', TEPAV Note, April 2012, http://www.tepav.org.tr/upload/files/1336653759-4.An_Assessment_on_the_New_Investment_Incentive_Package.pdf.

46 Eser Pirgan Matur, Ali Sabuncu and Sema Bahçeci, 'Determinants of Private Savings and Interaction Between Public and Private Savings in Turkey', *Topics in Middle Eastern and African Economies*, Vol. 14, September 2012, http://www.luc.edu/orgs/meea/volume14/PDFS/Saving%20study_V_eas7_1.pdf.

47 Rahul Anand, Saurabh Mishra and Nikola Spatafora, 'Structural Transformation and the Sophistication of Production', IMF Working Paper, WP/12/59, February 2012, http://www.imf.org/external/pubs/ft/wp/2012/wp1259.pdf.

48 Ibid.

49 Erol Taymaz, Ebru Voyvoda and Kamil Yılmaz, 'Uluslararası Üretim Zincirlerinde Dönüşüm ve Türkiye'nin Konumu' ['The Transformation of International Production Linkages and Turkey'], Koç University – TÜSİAD Economic Research Forum, Yayın No. EAF-RP/11–01, December 2011, http://eaf.ku.edu.tr/sites/eaf.ku.edu.tr/files/eaf_rp_1101.pdf.

50 World Bank, http://data.worldbank.org/indicator/TX.VAL.TECH.MF.ZS?page=1.

Pervasive gender inequality

Female emancipation is a critical driver of economic growth, robust democratic pluralism, and a state's security and stability.[51] Given the status of women in Turkey, therefore, the probability of maximizing economic affluence is more challenging. Indeed, the position of women is a prominent obstacle to the further development and growth of the 'Anatolian Tigers'.[52]

> 'Female emancipation is a critical driver of economic growth … Given the status of women in Turkey, therefore, the probability of maximizing economic affluence is more challenging'

Turkish women live in a socially conservative society in which they face significant restrictions. According to the United Nations Development Programme (UNDP) and the World Economic Forum (WEF), respectively, Turkey is positioned 101st out of 109 countries for gender empowerment[53] and 122nd out of 135 for gender equality.[54] At 31.2 per cent, its female labour force participation rate – the proportion of working-age women in employment – is less than half the average of 60 per cent for the OECD.[55] Social conservatism acts as one of the chief barriers to female employment, together with the lack of job opportunities for women in urban environments, the decline in agricultural employment, poor education of women, lack of childcare services and inadequate working conditions.[56]

Excluding women from the labour force is costly. Assuming a 50 per cent female labour force participation rate achieving the average level of productivity ($30,000 value added per worker per annum), Turkey's annual economic loss amounts to $419 billion. This is greater than the economy's GDP gains over the last ten years.[57]

Inefficient use of demographic dividend

Turkey's youthful population – the median age is 29.2 years[58] – has been a source of vitality for the economy. The country is going through the 'demographic window of opportunity', where the proportion of the working-age population (those between 15 and 64 years) is bulging, while the proportion of the 'inactive' youth (below 15 years) and the elderly (65 years and above) is shrinking.

51 *The Economist*, 'A Guide to Womenomics: the Future of the World Economy Lies Increasingly in Female Hands', 12 April 2006, http://www.economist.com/node/6802551; Ronald Inglehart and Pippa Norris, 'The True Clash of Civilizations', Foreign Policy, April 2003, http://www.hks.harvard.edu/fs/pnorris/Articles/Articles%20published%20in%20journals_files/The_True_Clash_Inglehart_Norris_Foreign_Policy_2003.pdf; Sabri Ciftci, 'Modernization, Islam, or Social Capital: What Explains Attitudes Toward Democracy in the Muslim World?', *Comparative Political Studies*, Vol. 43, No. 11, November 2010; Valerie M. Hudson, 'What Sex Means for World Peace', *Foreign Policy*, 24 April 2012, http://www.foreignpolicy.com/articles/2012/04/24/what_sex_means_for_world_peace.

52 European Stability Initiative, 'Islamic Calvinist: Change and Conservatism in Central Anatolia', 19 September 2005, http://www.esiweb.org/index.php?lang=en&id=156&document_ID=69.

53 UNDP, 'New Horizons: UNDP Turkish Monthly Newsletter', Issue 47, November 2009, http://www.undp.org.tr/Gozlem2.aspx?WebSayfaNo=2196.

54 Ricardo Hausmann, Laura D. Tyson and Saadia Zahidi, 'The Global Gender Gap 2011: Rankings and Scores', World Economic Forum, 2011, http://www3.weforum.org/docs/GGGR11/GGGR11_Rankings-Scores.pdf.

55 Gökçe Uysal, 'More Women are Working', BETAM, Research Brief 12/134, 26 July 2012, http://betam.bahcesehir.edu.tr/en/wp-content/uploads/2012/07/ResearchBrief137.pdf; 'More women execs recruited as overall female labor lags behind', *Hurriyet Daily News*, 8 March 2012, http://www.hurriyetdailynews.com/more-women-execs-recruited-as-overall-female-labor-lags-behind.aspx?pageID=238&nID=15503&NewsCatID=345.

56 Ersin Kalaycıoğlu and Binnaz Toprak, 'İş Yaşamı, Üst Yönetim ve Siyasette Kadın' ['Women in the Work Force, Top Administration and Politics'], TESEV Yayınları, Istanbul, 2004; İdil Göksel, 'The Reasons of Decreasing Trend of Female Labour Force Participation in Turkey: The Role of Conservatism', Izmir University of Economics, April 2011, http://www.siecon.org/online/wp-content/uploads/2011/04/Goksel1.pdfs; World Bank and State Planning Organization, 'Female Labor Force Participation: Trends, Determinants and Policy Framework', Report No. 48508-TR, 23 November 2009, http://siteresources.worldbank.org/TURKEYEXTN/Resources/361711-1268839345767/Female_LFP-en.pdf.

57 Esen Çağlar made the calculation based on a female labour force participation of 24 per cent. 'The annual cost of keeping women at home is $574 billion', TEPAV Articles, 2 April 2012, http://www.tepav.org.tr/en/kose-yazisi-tepav/s/3165.

58 CIA, *World Factbook*, 2013, https://www.cia.gov/library/publications/the-world-factbook/geos/tu.html.

This translates into reductions of expenditure on education and social security, and rising tax revenues.[59]

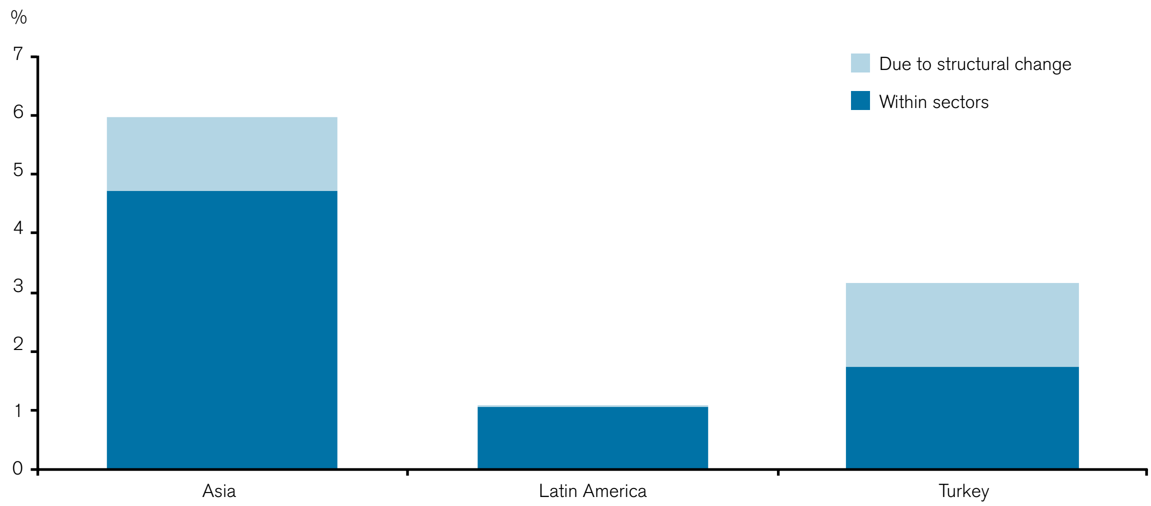
Turkey is heavily dependent, therefore, on favourable demographics and structural change – the transfer of workers from low- to higher-productivity sectors – for labour productivity growth. These factors accounted for 45 per cent of total growth for the period 1990–2005, with the remainder due to productivity increases within each economic sector.[60] In that respect, Turkey's performance lies between that of Asia and that of Latin America (see Figure 5).

Yet Turkey cannot rely indefinitely on the demographic dividend, which normally happens only once and lasts around 50 years. Moreover, its benefits can be frittered away without proper education and employment policies.[61] Based on UN estimates, Turkey's demographic window of opportunity will begin to close in 2025.[62] Figure 6 illustrates the precipitous fall in the Turkish fertility rate between 1962 and 2010. At 2.09 in 2010, the rate was just below the replacement level of 2.1 necessary to keep population numbers steady.

After about 2025, Turkey's dependency ratio – i.e. between those in the labour force and those outside it – is expected to rise again as the population starts ageing. This will incur an intergenerational transition of resources from education to social security, healthcare and pension provision for the elderly.

Erdoğan views the drop in fertility as a threat to national security. He has exhorted women to have three children, and condemned Caesarean births and abortions.[63] He is particularly apprehensive that the Kurdish community could be a majority in Turkey in 2038 since the average birth rate for Kurdish women is more than double the national rate for Turkish mothers.[64]

Figure 5: Decomposition of labour productivity growth, 1990–2005



Source: Dani Rodrik, 'Turkey's Growth Story', presentation at the conference on 'Turkey's Experience with Neo-Liberal Economic Reforms', London School of Economics, 28 October 2011.

59 'Turkey's Population Young and Rapidly Expanding', *Euromonitor International*, 24 January 2012, http://blog.euromonitor.com/2012/01/turkeys-population-young-and-rapidly-expanding.html.

60 Sumru Altuğ, Alpay Filiztekin and Şevket Pamuk offered a figure of 33 per cent as the contribution of structural change to Turkey's productivity growth. 'Sources of Long-Term Economic Growth for Turkey, 1880–2005', Centre for Economic Policy Research, 6 October 2006, http://www.cepr.org/meets/wkcn/1/1658/papers/Altug.pdf.

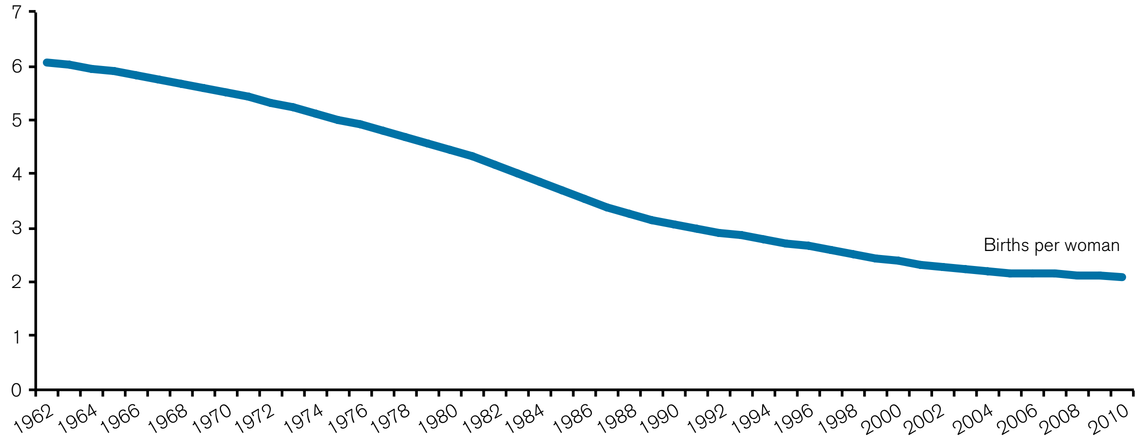
61 John Ross, 'Understanding the Demographic Dividend', Policy Project, September 2004, http://www.policyproject.com/pubs/generalreport/Demo_Div.pdf.

62 United Nations Children's Fund (UNICEF), 'Children in the Population', http://www.unicef.org.tr/en/content/detail/53/children-in-the-population.html.

63 James D. Zirin, 'Erdogan's Turkish Spring: Crosscurrents in the Bosphorus', *Forbes*, 4 June 2012, http://www.forbes.com/sites/jameszirin/2012/06/04/erdogans-turkish-spring-crosscurrents-in-the-bosphorus/.

64 Palash R. Ghosh, 'Turkey: high Kurdish birth rate raises questions about future', *International Business Times*, 16 May 2012, http://www.ibtimes.com/articles/341685/20120516/turkey-kurds-demographics-birth-rate-erdogan-babies.htm?page=all.

Figure 6: Turkey's fertility rate, 1962–2010



Source: World Bank.

Demographers question the accuracy of Erdoğan's forecast but concede that on current trends, the 'balance of power [between Kurds and Turks] could start shifting' within 40 or 50 years.[65] Since both communities prefer endogamy (i.e. marriage within the same ethnic group), the current evidence suggests the demographic differential between them will continue to increase.[66]

Nevertheless, Erdoğan's focus of concern seems misguided. The central risk is that procrastination on economic and social reforms is coinciding with the fast-approaching demographic reversal, due in less than a generation. According to a 2012 study by the Turkish Statistical Institute, the share of the population made up of children aged up to 17 years had dropped from 41.8 per cent in 1990 to 30 per cent by 2012 and is set tumble further to 25.7 per cent by 2023, 19.1 per cent by 2050 and 17.6 per cent by 2075.[67] Turkey cannot rely forever on the power of demography to propel productivity and economic growth.

Prioritization of reforms

This paper has identified low investment and savings rates, low value-added exports, gender inequality and inefficient use of its demographic dividend as features of Turkey's economic growth model. Does this mean Turkey has to tackle all these features simultaneously? Arguably, the short answer is 'no' since they may be symptomatic of deeper issues influencing the trajectory of the economy.

Turkey is normally prescribed a laundry list of economic reforms to advance its economy beyond middle-income status. This list looks daunting and endless, thereby generating anxiety and reform 'fatigue' in the government. Prioritizing the reform agenda is probably a more constructive approach. This means tackling the two main bottlenecks to growth: quality of human capital and incomplete reform of governance and institutions.

Human capital

The quality of human capital (i.e. education and training) remains a major constraint on growth and innovation in

65 Yigal Schleifer, 'Turkey: What's behind the AKP's New Anti-Abortion Agenda?', Eurasianet.org, 4 June 2012, http://www.eurasianet.org/node/65490.

66 İsmet Koç and Mehmet Ali Eryürt, 'Demographic integration through intermarriage of Turks and Kurds in Turkey', Presentation to European Population Conference 2010, 1–4 September 2010, http://epc2010.princeton.edu/abstractViewer.aspx?submissionId=100371.

67 Turkish Statistical Institute (TÜİK), 'Statistics on Child, 2012', http://www.turkstat.gov.tr/PreHaberBultenleri.do?id=13488.

Turkey.[68] The sophistication of exports has been linked with productivity, and productivity with human capital.[69] Ultimately, high educational quality is a fundamental plank of a competitive economy.[70]

Every three years, the OECD ranks the mathematical, scientific and reading skills of 15-year-old students in 40 countries. Turkey secured the greatest score improvements in this assessment between 2003 and 2009, albeit from a very low base.[71] This improvement is attributable to higher education budgets, rising school enrolment, more classrooms and modernization of the curriculum. Overall, however, Turkey stands 32nd among 34 OECD members and 40 per cent of Turkish 15-year-old students do not achieve a basic level of competence in mathematical literacy.[72]

Turkey is also ranked 90th out of 187 countries by the UNDP in terms of average duration of education for 25-year-olds.[73] In addition, the WEF ranked Turkey respectively 63rd, 74th, and 124th out of 144 countries in terms of primary education and healthcare, higher education and training, and labour market efficiency.[74]

Moreover, Turkey's past accomplishments may unravel under the recently enacted sweeping education reforms[75] that reflect Erdoğan's desire to nurture a more 'religious youth'.[76] These changes have lowered the age at which parents can send their children to Islamic schools – *imam hatips* – and other vocational schools. More religious courses have been added to the school curriculum and home-schooling for female students has been allowed.[77]

Turkish schools are already criticized for fostering conformity, insularity, rote learning and deference to authority as opposed to critical thinking and individual initiative.[78] So reinforcing these traits will hardly equip future generations with the requisite skills to succeed in an increasingly complex global economic environment.

> 'Turkey stands 32nd among 34 OECD members and 40 per cent of Turkish 15-year-old students do not achieve a basic level of competence in mathematical literacy'

According to a recent survey of 10,174 young people aged 15–29 across Turkey, most respondents did not speak a foreign language; only one in ten had travelled abroad; one-third did not read newspapers; the most popular activity was watching television, and ultra-nationalist soap operas received top ratings.[79]

68 İzak Atiyas and Ozan Bakış, 'Türkiye'de Büyümenin Kısıtları: Bir Önceliklendirme Çalışması' ['Constraints on Growth in Turkey: A Prioritization Study'], TÜSİAD Yayın No -T/2011/11/519, November 2011, http://www.tusiad.org.tr/__rsc/shared/file/Rapor-TRdeBuyumeninKisitlari.pdf.

69 İzak Atiyas, 'Uluslararası Üretim Zincilerinde Dönşüm ve Türkiye'nin Konumu' ['The Transformation of International Production Linkages and Turkey'], Koç University – TÜSİAD Economic Research Forum, Discussant Paper, Sabancı University, 2 March 2012, http://ref.sabanciuniv.edu/sites/ref.sabanciuniv.edu/files/2012-03-02_izak_atiyas.pdf.

70 Ozan Acar, 'PISA Sonuçları Işığında Türkiye'nin Rekabet Gücünün Değerlendirilmesi' ['Competitiveness Assessment of PISA results for Turkey'], TEPAV, 19 February 2008, http://www.tepav.org.tr/upload/files/1271251457r2163.PISA_Sonuclari_Isiginda_Turkiye___nin_Rekabet_Gucunun_Degerlendirilmesi.pdf.

71 Bengisu Özenç and Selin Arslanhan, 'An Evaluation of the PISA 2009 Results', TEPAV Evaluation Notice, December 2010, http://www.tepav.org.tr/upload/files/1292317950-2.An_Evaluation_of_the_PISA_2009_Results.pdf.

72 OECD, http://www.oecd.org/pisa/pisaproducts/pisa2009keyfindings.htm.

73 UNDP, 'Human Development Report 2012', http://http://hdrstats.undp.org/en/indicators/103006.html.

74 World Economic Forum, *Global Competitiveness Report 2012–2013*, 2012, http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2012-13.pdf.

75 Gökçe Uysal-Kolaşin and Duygu Güner, 'Eğitimin Kalitesinde Sınırlı İyileşme' ['The modest improvement in the quality of education'], BETAM, Araştırma Notu 10/102, 17 December 2010, http://betam.bahcesehir.edu.tr/tr/wp-content/uploads/2010/12/ArastirmaNotu102.pdf.

76 'Erdoğan resurrects debates of Islamization', *Al-Arabiya News*, 9 February 2012, http://english.alarabiya.net/articles/2012/02/09/193621.html.

77 Daniel Dombey, 'Education reforms divide Turkey', *Financial Times*, 14 March 2012, http://www.ft.com/cms/s/0/5c60ca4c-6a0c-11e1-b54f-00144feabdc0.html#axzz1xgg8Llsh.

78 Jenny White, 'Turkish Education: Authority or Critical Thinking, Assertive Masculinity or Consensus', Jenny White's Blog, 28 March 2008, http://kamilpasha.com/?p=203.

79 Burak Bekdil, 'The Turkish ideal, too, is youth', *Hurriyet Daily News*, 14 March 2012, http://www.hurriyetdailynews.com/the-turkish-ideal-too-is-youth.aspx?pageID=238&nID=15943&NewsCatID=398.

Education issues further affect Turkey's economic prospects indirectly through their impact on 'interpersonal trust' – the willingness of one party to rely on the actions of another party – throughout the country's human capital. Turkey's levels of interpersonal trust are considerably lower than OECD averages (see Table 1). University-educated educated Turks, especially, are less than one-quarter as trusting of others as their peers in other countries. Turkey stands out among the 20 countries in the survey as the only one where higher educational attainment correlates with lower feelings of trust.[80]

Table 1: Proportion of adults expressing interpersonal trust, by level of education, 2010

	Below upper secondary (%)	Upper secondary (%)	Tertiary (%)
OECD average	34	42	53
Turkey	16	12	12

Source: OECD, *Education at a Glance 2010.*

Such levels of mistrust are deeply damaging to Turkey's 'social capital' (the patterns and qualities of relationships in a community) and human capital and, by extension, its economic growth.[81] Communities with high levels of human capital are typically also characterized by high levels of social capital in its various forms, and the reverse effect is also valid.[82]

Turkey's low social capital is not conducive to the promotion of innovation and wealth creation.[83] The European Commission has concluded that Turkey is the least innovative economy in Europe.[84] It had the sixth lowest labour productivity among OECD countries in 2011 as measured in terms of GDP per hour worked. This is the most important contributor to the income gap between Turkey and the EU.[85]

Governance and institutions

Another major obstacle to sustainable growth is the weakness of governance and institutions. Turkish society is seen as tolerant of unequal distributions of power and inclined to low levels of individual rights.[86] These features are normally associated with countries where growth rates are volatile, current account deficits are persistent and the momentum for reform is rarely robust even in the presence of positive macroeconomic indicators. In Turkey, the concentration of political power in the hands of a few individuals tends to undermine state institutions and does not encourage an enduring stable political environment for reform. In August 2011, for example, the government abruptly curtailed much of the independence of the public procurement regulator and eight other market regulatory bodies.[87] Unsurprisingly, Turkey is ranked only 64th out of 144 countries in terms of the efficiency and transparency of its public institutions, according to the WEF.[88]

Throughout Erdoğan's 11-year single-party government, the EU accession process has been the principal driver for reforms. These flourished at the height of that process but ebbed dramatically when it stalled, even though the prime minister secured an overwhelming second-term election victory in 2007. This paralysis of reforms has been

80 'Learning not to trust? The OECD on Turkish education', Istanbul Notes, 28 September 2010, http://istanbulnotes.wordpress.com/2010/09/28/learning-not-to-trust-the-oecd-on-turkish-education.

81 I. Semih Akçomak and Bas ter Weel, 'Social Capital, Innovation and Growth: Evidence from Europe', IZA Discussion Papers, No. 3341, http://www.econstor.eu/dspace/bitstream/10419/35000/1/560201257.pdf.

82 Robert D. Putnam, 'Education, Diversity, Social Cohesion and "Social Capital"', OECD, Note for Discussion, 2004, http://www.oecd.org/general/meetingofoecdeducationministers-raisingthequalityoflearningforall-chairssummary.htm.

83 Francesco Sarracino, 'Economic Growth and Social Capital: Happily Together Ever After', CEPS/INSTEAD, Working Paper No. 2011–52, October 2011, http://www.statistiques.public.lu/catalogue-publications/working-papers-CEPS/2011/52-2011.pdf.

84 European Commission (Enterprise and Industry Directorate-General), 'Innovation Union Scoreboard 2011', 2012, http://ec.europa.eu/enterprise/policies/innovation/files/ius-2011_en.pdf.

85 World Bank, 'Turkey Investment Climate Assessment. Vol. II', 8 November 2007, http://www.yoikk.gov.tr/dosya/up/eng/ICA%20Volume_II.pdf.

86 Geert Hofstede, Gert Jan Hofstede and Michael Minkov, *Culture and Organizations: Software of the Mind* (McGraw Hill, 3rd edn, 2010).

87 Cengiz Aktar, 'Development at any cost', *Today's Zaman*, 13 June 2012, http://www.todayszaman.com/columnist-283463-development--at-any-cost.html.

88 World Economic Forum, *Global Competitiveness Report 2012–2013.*

reinforced by an uncompromising style of leadership as laid bare by Erdoğan's reaction to the recent protests in Istanbul's Taksim Square, by his determination to introduce a centralized presidency, for which he hopes to run in 2014, and by the local and general elections scheduled respectively for 2014 and 2015. Naturally, the fruits of long-term reform initiatives, such as upgrading the rule of law or transforming the education system and vocational training programmes, require focused government attention and do not conform to the short timelines of electoral politics; but they are, nevertheless, essential to propel the Turkish economy forward.

Conclusion

Erdoğan has ruled, until recently, with a steady hand amid what was a blossoming economy. Turkey has become a regional force to be reckoned with and for a long time a darling of financial markets. National self-confidence, political ambitions and economic prowess go hand in hand.

The prime minister needs to beware, however, of overconfidence and triumphalism. Past performance based on 'easy' growth released by lower inflation and fiscal discipline is no guarantee of future success.[89] Turkey's growth strategy suffers from a serious flaw in its excessive reliance on domestic demand-led growth, putting at risk the sustainability of a fast-paced economy. Given current institutional and policy constraints, it might struggle to achieve even modest growth rates of 2–5 per cent and will be vulnerable to foreign investor sentiments unless it bases growth more on productivity gains.

Time is of the essence. After about 2025, it is anticipated that Turkey's 'demographic window of opportunity' will start closing, population ageing will be in full swing and its middling prospects for prosperity may well become the norm.

89 Daniel Kahneman, *Thinking, Fast and Slow* (London: Penguin), 10 May 2012.

Fadi Hakura is the Manager of the Turkey Project and an Associate Fellow of the Europe Programme at Chatham House.

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