TÜSİAD 40

TURKISH INDUSTRY & BUSINESS ASSOCIATION

THE SPIRIT OF ENTERPRISE
U.S. CHAMBER OF COMMERCE

U.S.-TURKISH ECONOMIC RELATIONS IN A NEW ERA: ANALYSIS AND RECOMMENDATIONS FOR A STRONGER STRATEGIC PARTNERSHIP

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Thomas J. Donohue

The U.S. Chamber of Commerce is committed to expanding the United States' commercial relations with Turkey. When I was in Istanbul in late 2011, I saw firsthand that Turkey is a highly important regional economic player with a strategic location and a growing and well-trained labor force that has great opportunities for American companies. Those tremendous advantages along with our joint memberships in the G20, World Trade Organization, and Organization for Economic Cooperation and Development mean the U.S. and Turkey need to step up our dialogue not only about how we manage our economies but also on key global economic, financial, and trade issues. We have come far, but given the size of the two markets, there is a lot more we can do together to achieve the full potential of the economic and commercial relationship.

The U.S. Chamber through its Turkey Working Group is playing a central role in keeping the U.S. business community focused on the growing opportunities that exist in the Turkish market. As this report illustrates, establishing joint ventures between our companies is one important way to build business relationships and is a method to expand trade. The report also recommends that the 1985 U.S.-Turkey Bilateral Investment Treaty should be brought up-to-date to create a more secure and predictable climate for our firms. An additional recommendation is for enhanced cooperation between the U.S. and Turkey in the G20 context, including our common interests in creating economic growth, fighting protectionism, and ensuring efficient financial markets. We believe that these recommendations can be a very good start to a new phase of the U.S.'s commercial relationship with Turkey.

As two global leaders, the United States and Turkey must seize the opportunity to further deepen our commercial ties. We must work to lower trade barriers, increase investment, and act together to fulfill our global economic and commercial responsibilities. The U.S. Chamber of Commerce looks forward to being a partner in that endeavor and further strengthening America's bilateral ties and global engagement with Turkey.

Sincerely,

Thomas J. Donohue
President & CEO
U.S. Chamber of Commerce

Ümit Boyner

For a long time, bilateral relations between the United States and Turkey have been primarily dominated by military/strategic considerations. The economic component of this partnership has been virtually absent from the strategic framework, making it vulnerable to political fluctuations and considerations in both countries.

However, after President Obama's visit to Turkey in April 2009, a new era in bilateral relations has hopefully started. The two governments have launched "U.S.-Turkey Strategic Framework of Economic and Commercial Cooperation" in an attempt to improve trade and investment ties with a more structured private sector involvement by the establishment of a U.S.-Turkish Business Council. TUSIAD supports this initiative and believes that it will have a positive impact on both nations.

As the voice of Turkish business, TUSIAD has had strong relations with American business circles and public institutions since opening a representative office in Washington, D.C. in 1998, regularly communicating and collaborating with the U.S. Congress, the U.S. administration, business circles, think tanks, media, as well as international and Turkish-American organizations.

In 2010, TUSIAD International, the strategic business development unit of TUSIAD, established a U.S. Working Group with the purpose of fostering and revitalizing trade and investment relations between Turkey and the U.S., reaching a higher level of partnership between private industries of both countries, supporting interaction between government bodies of both countries, and achieving concrete, result-oriented and knowledge-based initiatives and activities.

TUSIAD efforts for the further development of Turkey-U.S. economic relations gained a new momentum with the signing of a memorandum of understanding (MoU) with the U.S. Chamber of Commerce, our counterpart organization in the U.S., in October 2011. The MoU aims to improve bilateral economic relations between the two countries through joint activities and projects and to explore new areas of cooperation.

TUSIAD and the U.S. Chamber of Commerce, both members of B20, the business representatives of G20 countries, represent respectively Turkish and U.S. business communities. B20 offers yet another platform for TUSIAD and the U.S. Chamber of Commerce to collaborate on bilateral economic issues as well as global and regional ones.

This study "U.S.-Turkish Economic Relations in a New Era: Analysis and Recommendations for a Stronger Strategic Partnership" is commissioned jointly by TUSIAD and the U.S. Chamber of Commerce as a first step of their common initiatives. TUSIAD strongly believes that this study will be a guide and platform for both U.S. and Turkish business people for innovative as well as abundant discussion in the upcoming period.

Ümit BOYNER
President of TUSIAD

EXECUTIVE SUMMARY

During his visit to Turkey in April 2009, President Obama expressed his desire to see a more diversified and deepened U.S.-Turkey relations in the context of a novel "model partnership." This signified the willingness to add new dimensions to bilateral ties, which have long been dictated by security concerns and interests. Strengthening economic ties beyond trade dominated by military merchandise has been a cardinal objective of the new mode of bilateral strategic engagement expressed in terms of the model partnership. In this context, the two governments launched the U.S.-Turkey Framework for Strategic Economic and Commercial Cooperation (FSECC), which entailed a new cabinet-level initiative to tackle challenges to enhanced economic relations with a more structured private sector involvement through a Business Council composed of representatives from both countries. Although late in coming, this shift of focus of bilateral relations to the economic domain is a significant and necessary action if one takes into account the recent developments and trends in the global political economy. The looming recession in Europe and the recent turmoil in the Middle East and North Africa have made the United States even more important as far as Turkey's efforts to diversify its trade ties are concerned.

Turkish-American economic integration over the last 10 years has decreased as the U.S. market has been oriented toward other emerging economies thanks to changing international supply and global value chains. The lion's share of the expansion of North-South trade went to East Asia, as China became a global manufacturing hub. Today, industrial production of the surplus economies in Asia is largely driven by U.S. demand. In contrast, while Turkey has succeeded in gaining access for its products to the European supply chains, it has failed to do so in the U.S. market. When President Bill Clinton visited Turkey in November 1999, the United States' share of Turkish foreign trade was 8.2%. In 2010, this had fallen to less than 5.5%. Likewise, U.S. foreign direct investment in Turkey has remained far below potential.

In this context, U.S.-Turkish economic relations risk further marginalization in the near future if public and private stakeholders in both countries do not take concrete and innovative steps. This study examines the current state of trade and investment between the United States and Turkey, as well as the legal frameworks governing it and barriers/issues of concern, and looks at the global and multilateral context in which strengthening economic ties can be explored. It offers case studies of sectoral and individual firms' success, from joint ventures to export promotion strategies. Finally, it offers recommendations by which trade and investment can be increased. Among these are:

- Rewriting the bilateral trade and investment framework
- Better aligning the two countries' export promotion strategies
- Setting up new forums of dialogue and consultation for the U.S. and Turkish business communities
- Utilizing the forum of the G20 to produce mutually satisfactory solutions to economic issues of concern

Successful improvements in trade and investment between Turkey and the United States cannot be realized without the active participation of institutional and private-sector actors in both countries. The goal of this report is to provide one modest step in that direction, identifying challenges to and opportunities for the enhanced economic relations that would underpin a model partnership.

CONTENTS

List of Abbreviations

AGOA	African Growth And Opportunity Act
BIT	Bilateral Investment Treaty
CAGR	Compound Annual Growth Rate
DEIP	Dairy Export Incentive Programme
EFTA	European Free Trade Area
EEX	European Energy Exchange
Ex-Im Bank	Export Import Bank Of The United States
EU	European Union
FDI	Foreign Direct Investment
FSECC	U.S.-Turkey Framework For Strategic Economic And Commercial Cooperation
FTA	Free Trade Agreement
GDP	Gross Domestic Product
GMP	Good Manufacturing Practices
GSP	Generalized System Of Preferences
GTA	Global Trade Alert Database
ICT	Information And Communication Technologies
IIAT	International Investors Association Of Turkey
IMF	International Monetary Fund
JV	Joint Venture
ISPAT	Turkish Investment Support And Promotion Agency
MFN	Most Favored Nation
NAFTA	North American Free Trade Agreement
NEI	National Export Initiative
OECD	Organisation For Economic Cooperation And Development
OPIC	Overseas Private Investment Corporation
R&D	Research And Development
TAIK	Turkish-American Business Council
TEI	Tusas Engine Industries
TIFA	Trade And Investment Framework Agreement
TDZ	Technology Development Zones
USTR	United States Trade Representative
WTO	World Trade Organization

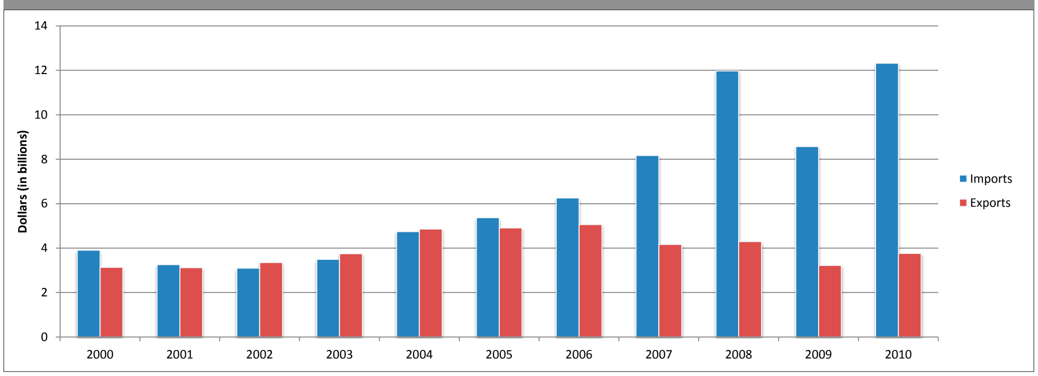
1. STAGNATING ECONOMIC TIES

Trade: Increasing in the U.S.'s favor

There is an upward trend in bilateral trade between Turkey and the United States. According to the data provided by the Turkish Ministry of Economy, bilateral trade volume in goods reached $16 billion in 2010, with $3.8 billion exported by Turkey and $12.3 billion exported by the United States. This growth was largely driven by the steady increase in Turkish imports from the United States over the past decade, thanks to high economic growth and rising domestic demand. Turkey also saw overall exports growth earlier in the decade, but Turkish exports to the U.S. are now back down to the levels seen at the beginning of the decade. Although both countries have overall trade deficits, the bilateral trade deficit is shouldered by the Turkish side and is steadily increasing. Turkey's traditional export and import partners are in Europe, and its trade with other neighboring countries has been increasing thanks to dedicated effort. Growth of trade with the United States, meanwhile, has lagged behind (see graphs below).

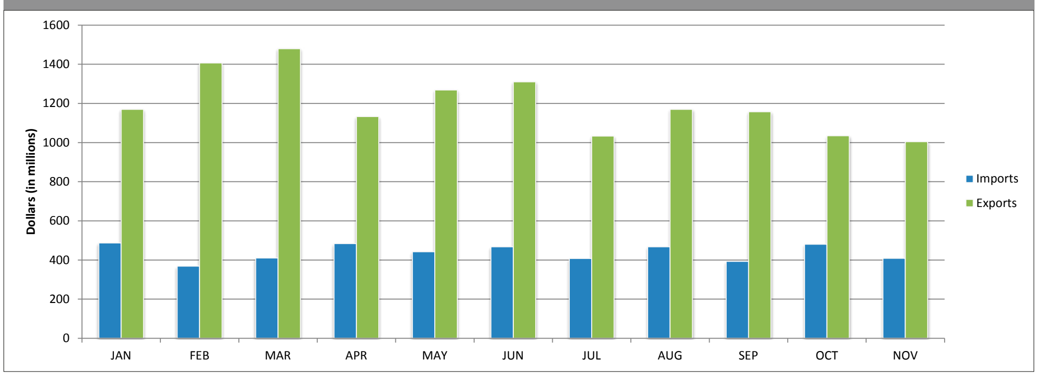
Turkish exports to the United States have been concentrated in labor- and capital-intensive products. Leading export categories are textiles and clothing articles; iron and steel products; machinery; vehicles; stones, plaster and cement (travertine and marble); processed fruit and vegetables; and tobacco and snack foods. U.S. exports to Turkey have been concentrated in capital- and research-intensive goods; leading categories include aircraft, iron and steel, and machinery, although raw-material-intensive goods from the agriculture sector (cotton yarn and fabric, oil, soybeans, tree nuts, and rice) are also key exports.[1]

TURKEY - UNITED STATES BILATERAL TRADE



Source: Turkish Ministry of Economy

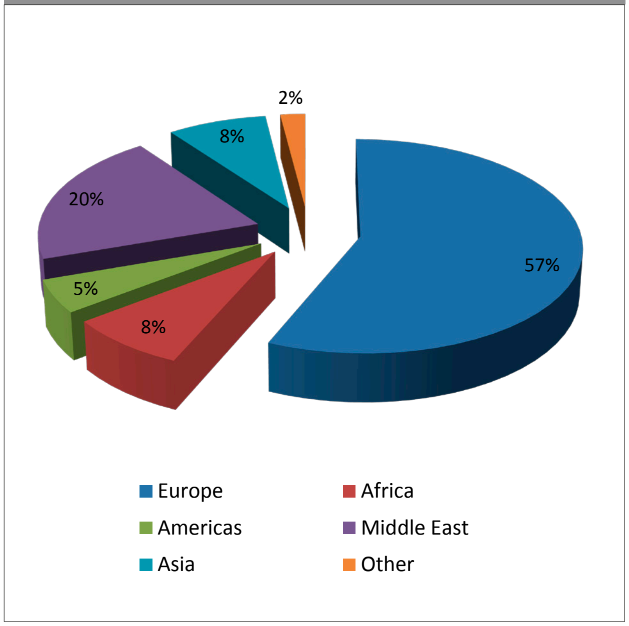
TURKEY - UNITED STATES BILATERAL TRADE (2011)



Source: United States International Trade Commission

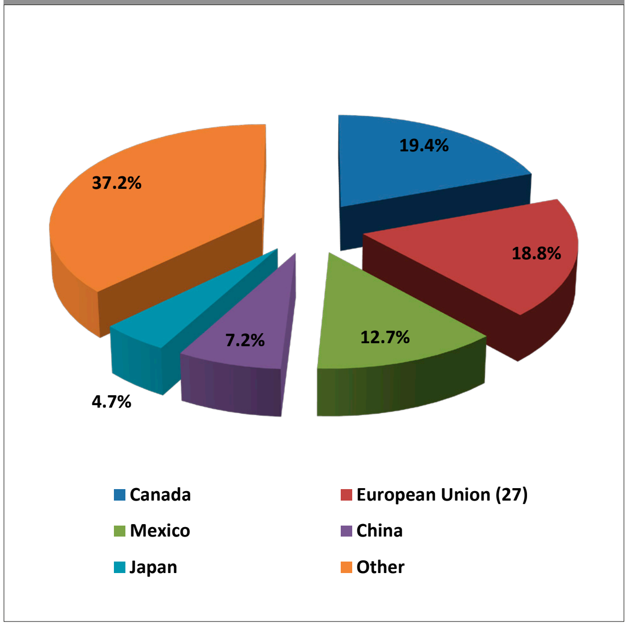
[1] See November 2011 TUSIAD Report *Constraints on Growth in Turkey: A Prioritization Study* for a detailed analysis on the sources of trade imbalance between the US and Turkey

TURKISH EXPORTS BY REGION



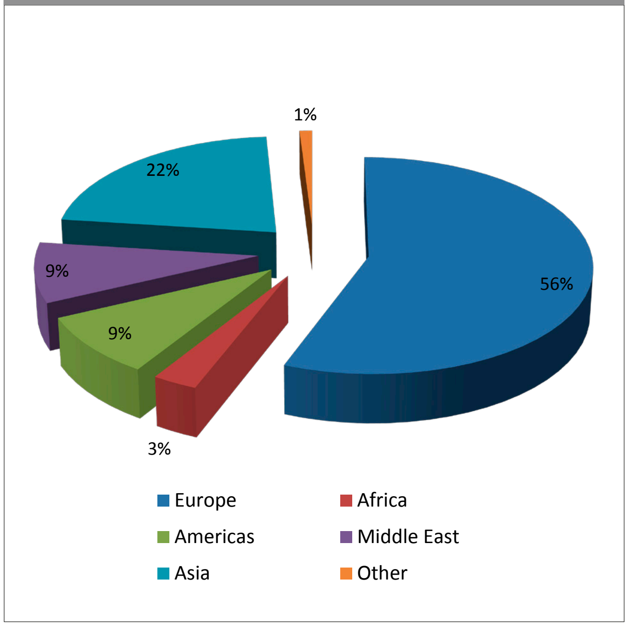
Source: Turkish Ministry of Economy

US EXPORTS BY MAIN DESTINATION



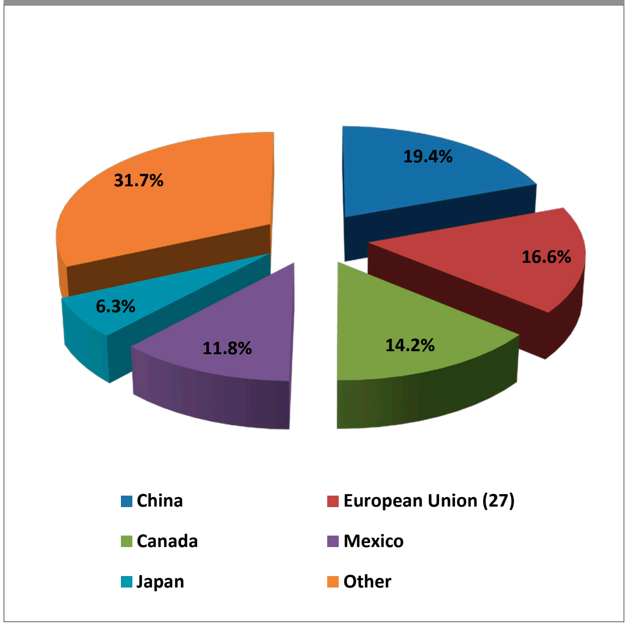
Source: World Trade Organization

TURKISH IMPORTS BY REGION



Source: Turkish Ministry of Economy

US IMPORTS BY MAIN ORIGIN



Source: World Trade Organization

TURKEY'S EXPORTS TO THE U.S.	2010 IN MILLIONS OF DOLLARS
Industrial Supplies And Materials	1,582
Consumer Goods (Nonfood), Except Automotive	1,111
Capital Goods, Except Automotive	850
Automotive Vehicles, Parts And Engines	416
Foods, Feeds, And Beverages	348

Source: US International Trade Commission

U.S. EXPORTS TO TURKEY	2010 IN MILLIONS OF DOLLARS
Industrial Supplies And Materials	4,824
Capital Goods, Except Automotive	3,331
Foods, Feeds, And Beverages	963
Military Type Goods	738
Consumer Goods (Nonfood), Except Automotive	428
Exports, N.E.C., And Reexports	139
Automotive Vehicles, Parts And Engines	124

Source: US International Trade Commission

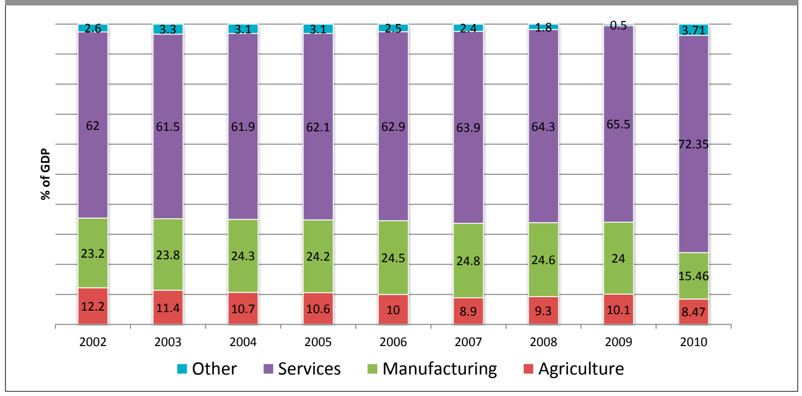
TRADE IN SERVICES: THE NEGLECTED LINK IN BILATERAL TIES

Satisfactory data are not available from either country or international institutions on the amount and full nature of bilateral trade in commercial services, but it is clear that the services sectors offer great potential as a means by which to improve bilateral economic relations. Both Turkey and the United States need to devote more resources to quantifying this very significant but thus far neglected domain. We do know that both parties run overall surpluses in commercial services trade. Turkey's share in global trade in services is increasing as the services sector's proportion of total domestic production is on the rise, from 62% of GDP to 72% between 2002 and 2010. According to the WTO, in 2010 Turkey ranked the 16th biggest exporter in the world and the 24th largest importer. (In the same year, the United States ranked second both as an exporter and importer, following the European Union.) [2]

In contrast to its trade deficit in goods, Turkey's trade in services recorded a surplus of $14.5 billion for 2010, with approximately $33 billion in exports and $18 billion in imports. Two-thirds of Turkey's services exports are accounted for by travel services — i.e., tourism. The country drew nearly 30 million visitors in 2010, generating more than $20 billion in income. According to a recent WTO report, Turkey has also developed significant exports capacity in other commercial services, such as transportation, construction, communications, and insurance. As will be discussed in detail below, these sectors provide lucrative opportunities for U.S. companies both in terms of investments in Turkey and to reach out to growing markets in the Middle East, North Africa, the Caucasus, Central Asia, and the Balkans. The WTO reports that in 2008, Turkey was the fourth-largest exporter of personal, cultural and recreational services (including health and education services), following the European Union, United States, and Canada, with exports totaling $1.22 billion.

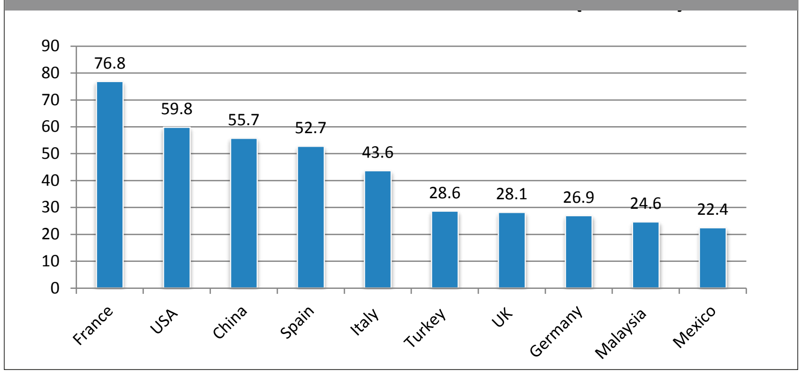
Turkey also developed export capacity in insurance services reaching an amount of $752 million in exports in 2008. Financial services at large remain more import-focused. However, financial investments by U.S. companies in Turkey are particularly important as they create externalities by catalyzing economic flows by financing trade and investment in other sectors. Furthermore, the Turkish government's objective of turning Istanbul into an international financial center would create new opportunities for U.S. and other foreign investors. On the other hand, in construction, Turkish firms undertook international projects generating more than $100 billion between 2003 and 2009, and several Turkish companies were included in the top 100 of Engineering News-Record's most recent ranking of international contractors by revenue [3], including Renaissance Construction, GAMA, and Enka Construction & Industry.

TURKEY GDP BREAKDOWN



Source: Turkish Statistical Institute

INTERNATIONAL TOURIST ARRIVALS 2010 (MILLION)

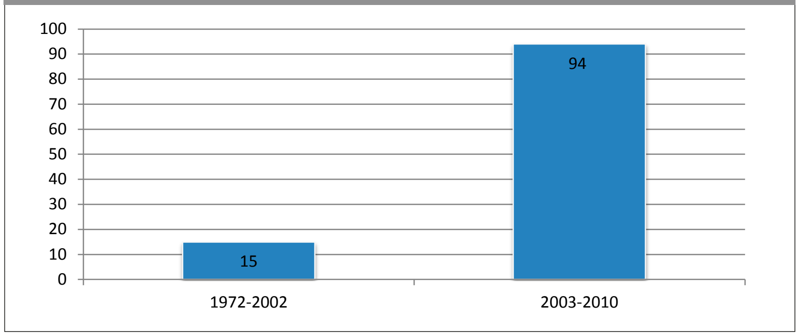


Source: Turkish Statistical Institute

TURKISH TRANSPORTATION AND LOGISTICS INDUSTRY Turkey's transportation and logistics sector grew at an average compound annual growth rate (CAGR) of 6.2% between 2003 and 2007, with globally generated revenue of $3.4 billion in 2007. The forecast for 2012 is $4.5 billion, growing at a 5.4% CAGR. The sector is estimated to represent approximately 8–12% of Turkish GDP, making the sector worth roughly $60 billion. It is a strong growth industry, having tripled in value since 2002. Average growth over the last five years has been 20%, and forecasts indicate the value of the industry could be as large as $120 billion by 2015. The influence of the transportation sector is expected to increase further in the future, as a huge number of highway, rail, and other transport-related projects are either already underway or expected in the coming years to accommodate an increasingly industrialized country. Turkey's current transportation network is below EU-27 standards, mainly due to a lack of density of highways and railroads. To this end, new transport hubs are planned in a number of villages. Large-scale privatization projects are on a continuous rise as well, with even the two major Bosphorus bridges likely to be taken from government control in the next few years. Topographical features make harbor construction and involvement in maritime trade a challenging, and therefore lucrative, industry.

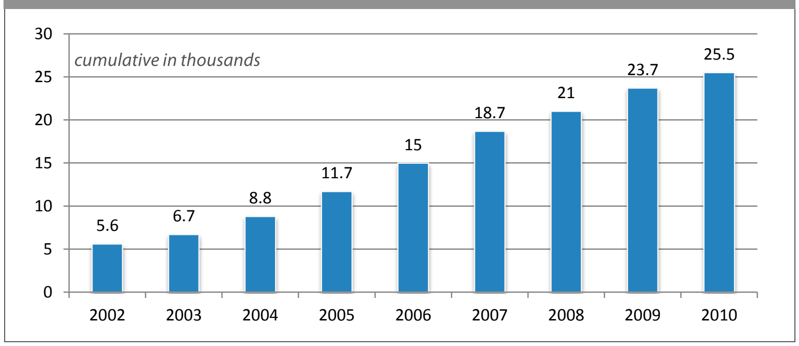
[2] For detailed figures see Appendix Table 2: Turkey's Exports and Imports of Commercial Services in Years and Categories.
[3] Engineering News-Record Top 225 International Contractors Ranking http://enr.construction.com/toplists/InternationalContractors/001-100.asp

FDI INFLOWS (USD BILLION)



Source: Central Bank of the Republic of Turkey, Turkish Undersecretariat for Treasury

NUMBER OF COMPANIES WITH FOREIGN CAPITAL



Source: Turkish Undersecretariat for Treasury

CARLYLE-BAHCESEHIR US-based private equity firm Carlyle Group ventured into the Turkish education sector by acquiring a 48% stake in Bahcesehir K-12 Schools in October 2011. Carlyle Group previously acquired 40 percent of Medical Park in Turkey, a healthcare company operating a hospital chain. The group's recent acquisitions and its listing of Turkey as a priority market for its $500 million fund designed for the region underline the growing interest in American companies in Turkey's services sector.

PHARMACEUTICALS The innovative pharmaceutical industry spends roughly $65 billion on R&D each year, a large percentage of which is on pre-clinical research and clinical trials (Source: PhRMA). Turkey currently receives only a small fraction of this investment owing to a number of factors, including product registration requirements, reimbursement and pricing systems, the intellectual property framework, and the new Good Manufacturing Practices (GMP) policy. However, several factors have also created opportunities to increase pharmaceutical investment in Turkey: the country's human capital, its ability to serve as a geographic hub, and its efforts to expand its healthcare system. Attracting investment to the biopharmaceutical sector will help strengthen Turkey's effort to diversify its economy into knowledge-intensive industries. This is also important in the context of the country's focus on becoming a center for medical tourism. With the right policy and regulatory environment, Turkey can substantially increase its percentage of biopharmaceutical R&D investment, particularly in pre-clinical and clinical trials. The country is also well positioned to be a manufacturing and logistics hub for the industry with the right policy environment. Ireland, Singapore, and, in the United States, the greater Boston area serve as excellent models in this regard.

FOREIGN DIRECT INVESTMENT FLOWS: FAR BELOW POTENTIAL

Turkey has become one of the rising markets for foreign direct investment in the past decade. The most significant factor in this rise has been political and economic stability due to a single-party government, progress toward EU accession, and energy dedicated to structural reforms after the market crash of 2001. Thanks to a new FDI law and increased privatization, along with other strategies of the ruling Justice and Development Party (AKP) government, FDI inflows to Turkey registered a total amount of $94 billion between 2003 and 2010. This is a significant change, given that FDI stocks over the past three decades totaled only $15 billion. Turkey attracted $13.42 billion in foreign direct investment in 2011. The number of foreign companies invested in Turkey in the last eight years increased from 5,600 to 25,500. On a bilateral level, U.S. FDI stock in Turkey was $6.3 billion in 2009, according to the U.S. Commerce Department, while Turkey's FDI in the United States was $218 million in 2007.

A listing of the major source countries for FDI inflows to Turkey demonstrates the fact that European companies have been more interested than their American counterparts in Turkey as a destination for production outsourcing. According to the International Investors Association of Turkey (IIAT), the share of European capital in total FDI inflows between 2005 and 2009 (the most recent data available) was around 65%, whereas the American share stood at just 9.4%. In 2008, there were 929 U.S. companies active in Turkey, but that number represented only 4.4% of overall international companies there. Around half of U.S. FDI in Turkey went to the finance sector, followed by retail and wholesale, logistics and utilities, and automotive manufacturing. Among others, notable U.S. investments included Texas Pacific Group's $350 million purchase of Mey Icki in 2006 and Citigroup's $3.2 billion investment in Akbank in 2007.

An overall sectoral breakdown of FDI inflows shows the significance of services sectors for foreign direct investors, including U.S. companies, since they have been interested in Turkey's service industries more than in manufacturing and agriculture. IIAT reports that 74.1% of FDI inflows between 2005 and 2009 were to services, particularly financial intermediation (44.2%), whereas industrial sectors received 25.7%. The country's privatization program was a significant factor in attracting FDI; according to the Turkey Privatization Administration, privatization between 1985 and 2010 generated $42 billion, $32 billion of that between 2005 and 2010.

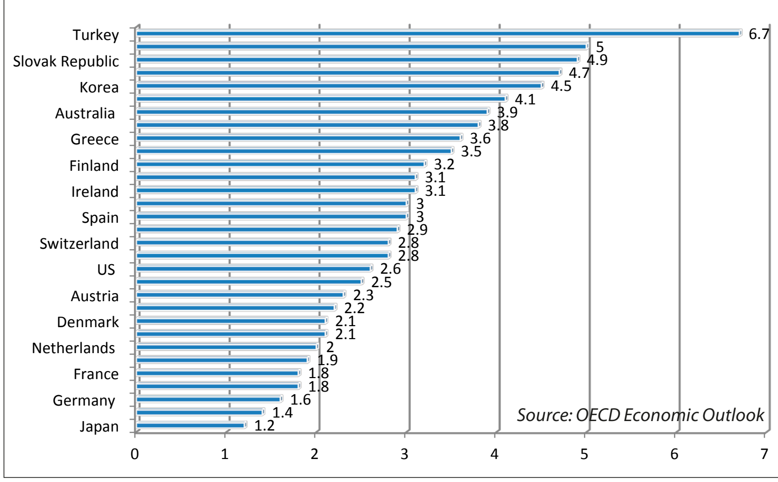
2. TURKEY: A GROWING MARKET FOR U.S. EXPORTS AND INVESTMENTS

Turkey recorded a sustainable growth rate until the global economic downturn, with a stable inflation rate in the single digits (although there has been a sharp increase in inflation in 2011 and overheating has become a significant issue) and a debt-to-GDP ratio that remains lower than that of its European neighbors. It was the fastest growing economy in Europe in 2010, with an annual GDP growth of 8.9%, and is expected to grow faster than the OECD countries and most emerging economies in the coming years. Interest rates have fallen sharply in recent years, while per capita income and purchasing power have been increasing. Turkey also benefits from a young, skilled, and highly productive workforce.

While still not investment grade, Turkey's credit rating has been upgraded by the major credit agencies in the last couple of years, underlining a growing confidence. After its upgrade of the foreign currency and local credit ratings to BB and BB+, respectively, in February 2010, Standard & Poor's raised the local currency rating by two notches to BBB- in September 2011. Fitch raised Turkey's long-term foreign currency rating by two notches, to BB+ from BB-, in December 2009, while Moody's upgraded Turkey's sovereign credit rating from Ba3 to Ba2 in December 2009 and upgraded the country's local and foreign currency ratings from stable to positive in October 2010.

However, Turkey's growing account deficit and its large external financing requirement have made the country extremely vulnerable amid the deteriorating global outlook. Turkey's 2011 current account deficit increased by 65 percent and reached $77.8 billion. It is important to note that total inflows through net errors and omissions in 2011 reached $12.5 billion, financing 16.2% of the current account deficit. Recognizing the increasing vulnerabilities, Fitch downgraded Turkey's outlook to stable from positive in November 2011, citing concerns about a balance of payments bottleneck, among other risks. With its current account deficit bordering on 10% of GDP, Turkey is the prime target for contagion from the troubled European banking system, and unless the country's current account deficit and credit growth can be controlled, further downgrades seem possible. The fact that Turkey's current account deficit is largely financed by short-term capital flows makes FDI inflows from the United States an important priority.

AVERAGE ANNUAL REAL GDP GROWTH (%) FORECAST IN OECD COUNTRIES (2011-2017)



ENERGY Over the past few years, the energy sector has become the focal point of new investments in the Turkish economy. Turkey has been actively pursuing policies that aim at diversifying energy sources and supply routes, liberalizing both the power and gas sectors and promoting the country's role as a major natural gas hub for Europe and the wider region.

Conventional hydrocarbons account for the biggest share of the energy mix in Turkey. Around 30% of the country's energy supply is met by coal, and gas and oil together are also close to 30%, followed by hydropower and renewables. Significant potential in renewable energy, particularly wind and solar, could offer new investment opportunities. Turkey's Ministry of Energy and Natural Resources is aiming, by 2023, to add 20,000 MW of installed wind power capacity and utilize all technically and economically usable hydroelectric capacity.

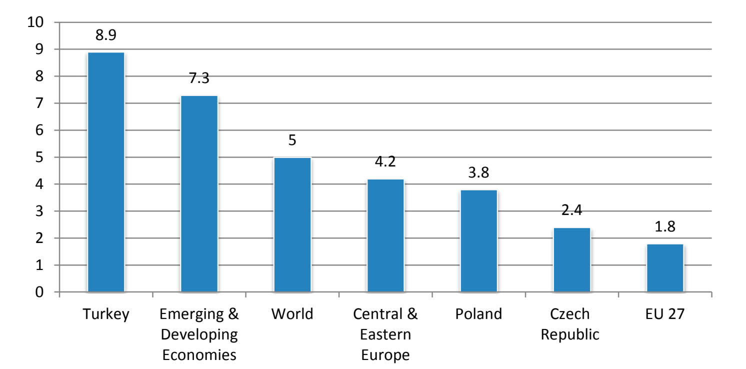
The country's domestic oil and gas production meets less than 3% of its energy needs. Foreign majors such as ExxonMobil and Chevron are involved in the exploration of the Turkish sector of the Black Sea. These explorations have not yet yielded economically feasible results, but Mediterranean seems to be a promising new area that will receive more attention in the coming years. Turkey's state-owned pipeline operator, BOTAS, previously owned all oil and natural gas pipelines. The Natural Gas Market Law, No. 4646 of 2001, stipulates the reduction of BOTAS's market share in gas imports to 20 % and transfer of gas import contracts to the private sector, while also aiming at the unbundling of BOTAS. So far, this initiative has seen mixed success, but the Turkish government did not seek an extension of the Western Line contract with Russia, preferring instead an import agreement through the private sector.

Turkey's electricity market is another fast-growing sector worth mentioning. There has been a wave of major privatizations of state-owned electricity distribution companies in the last couple of years, and this is expected to continue. Turkey signed a deal with Russia in 2010 to build Turkey's first nuclear power plant in the coastal town of Akkuyu, in Mersin. This was an attempt to diversify its energy sources, decrease current account deficit and attract FDI inflows. There are also ongoing talks with South Korea for a second nuclear power plant in Turkey's northern province of Sinop.

The country's transition to a competitive market structure and its strategic role as a connector between energy-rich countries to the east, such as Russia and the Central Asian republics, and demand centers in the West make the energy sector particularly appealing. This is particularly true for natural gas, and Turkey has been actively pursuing policies that would promote its role as a regional and major European gas hub. Turkey is involved as a transit country in several projects competing to carry Caspian natural gas to Europe. The country's status as a bridge between Europe and Asia, both geographically and politically, puts it in a position to continue to grow in importance as an energy hub. Turkey's increasing cooperation with Azerbaijan in the energy sector, including projects such as the Trans-Anatolian Pipeline, would further reinforce Turkey's role in the region.

Turkey's position as a major energy importer and its fast-growing consumption will require new investments in the sector. To meet demand, the country needs $130 billion of investment between now and 2023. Turkey's rising consumption in the framework of a liberalized gas market presents significant opportunities for American companies to supply gas to the Turkish market, especially as LNG. The planned introduction of an energy exchange, modeled after the European Energy Exchange (EEX), would also enable long-term price formation, allow for the start of derivative operations, and thus offer far greater visibility for investors.

ANNUAL REAL GDP GROWTH (%) 2010



Source: IMF World Economic Outlook, April 2011

THE FATIH PROJECT The ICT sector's interest in the Turkish education industry has increased tremendously with the introduction of the FATIH project, which envisions "smart classes" for primary education in Turkey, including plans for tablet computers for every student and electronic blackboards for classrooms. The $7.5 billion project entails providing tablet computers for 16 million students, as well as broadband Internet and smart blackboard technology for 40,000 schools and 620,000 classrooms in Turkey. The project is a priority for the government, and it was promoted by Prime Minister Recep Tayyip Erdogan in the run-up to the June 2011 elections. The pilot project will start at 51 schools in 12 provinces in February 2012. Bidding for the project is expected to start in 2012, with plans to move to an IT-intensive education model by the end of 2013. General Mobile has won the bidding for the pilot project.

Domestic demand in Turkey has seen a boom since the 2001 economic crisis, and it has remained high despite the global crisis as GDP growth resumed, the lira appreciated, and the increase in energy prices kept import growth rates high. Parallel to the integration of the Turkish economy into Europe's, there is an increasing demand for intermediary and capital goods to feed production both for domestic consumption and regional and global supply chains. In this context, two-thirds of Turkish imports have been in intermediary goods, followed by capital and consumption goods. The composition of the country's exports has been reshaped by the increasing pace of industrialization, especially after the establishment of the Customs Union agreement with the European Union in 1996. Thanks to the EU-driven economic transformation the share of total exports held by capital-intensive goods, such as machinery and transport equipment, has overtaken that of labor-intensive goods such as textiles and clothing, while knowledge- and technology-intensive value-added exports are also on the rise.

In this context, Turkish producers supply needed intermediary goods largely from the European market rather than American or other markets. According to the European Commission, around 45% of Turkish imports from the EU in 2010 were in machinery and transport equipment, followed by chemicals and related goods (17.6%), and other manufactured goods (15.1%). Similarly, the share of technology- and knowledge-intensive goods coming into Turkey from the United States is rising, although not to the same level of such imports from the EU. The share of such goods in the total EU export mix to Turkey, including aircraft and machinery as well as pharmaceuticals and organic chemicals, is increasing, whereas U.S. exports to Turkey are still dominated by capital- and raw-material-intensive products, with a high share of iron and steel and increasing share of farm products.

There is great potential for the diversification of U.S. agricultural exports to Turkey. Turkey is both an exporter and importer of farm products, and U.S. companies have already succeeded in increasing exports of cotton yarn and fabric, soybeans, tree nuts, and rice. As will be discussed in more detail later, livestock and meat could offer new opportunities to export to Turkey.

However, to achieve a sustainable enhancement in bilateral trade relations, one needs to analyze the ways U.S. producers can integrate with Turkish producers and exporters. Considering Turkey's continued economic

INFORMATION AND COMMUNICATION TECHNOLOGIES (ICT) In the wake of the 2001 financial crisis, Turkey experienced a surge in mobile and broadband Internet and technologies, with telecommunications covering nearly 73% of the total $29 billion Turkish ICT market, and the compound annual growth rate (CAGR) from 2005 to 2009 reaching 14%. While the IT sector—hardware, software and broadband—has grown significantly since 2001, its portion of the total market is significantly lower than in Western European and CEE countries, revealing considerable room for advancement. The relatively young Turkish population is eager to adopt new technologies; IT spending is expected to grow from $7.2 billion in 2009 to $10.5 billion in 2014 , and mobile network infrastructure already covers the entire country.

Additionally, the state has actively promoted liberalization and privatization of the telecommunications sector, selling 55% of the previously entirely state-owned fixed-line operator Turk Telekom to a private company, Oger Telecom, in 2005, and divesting further state-owned shares with an IPO in 2008. At present, the country's three licensed mobile operators, Turkcell, Avea, and Vodafone, count 62.8 million registered subscribers out of a population of 78.785 million. The market penetration rate is at 83.9%, but when compared to the 125% rate in EU countries, it is clear that the industry still has a lot of ground to cover. Investment and tax incentives are another set of measures introduced by the government for companies with local subsidiaries. Several foreign companies such as Dell, Siemens, Cisco, NCR, IBM and Hewlett-Packard have already benefited from these incentives. New Technology Development Zones (TDZs) founded across the country offer tax exemption for research- and development-based revenues of companies located on their territory. Business Monitor International recently named Turkey the fastest-growing IT market in the world for 2009–2014.

[4] Republic of Turkey Prime Ministry Investment Support and Promotion Agency of Turkey (ISPAT) August 2010 Report *Turkish Information and Communication Technologies Industry*

growth, increasing demand, and established industrial infrastructure, there is further potential for U.S. exporters to expand their market shares in both technology-intensive intermediary goods and consumer products. Increasing exports, especially of products such as chemicals, machinery, automobile parts, beverages, and cosmetics, could serve to improve the balance of trade in Turkey's favor and incorporate Turkish suppliers into supply chains dominated by U.S. multinationals. It should be noted that European companies, which have established shares and business contacts in Turkey, are the primary competitors of U.S. exporters. To succeed in the Turkish market, it is essential to develop similar relationships, identifying strong local partners with necessary market knowledge and contacts.

In addition, Turkey's geographical proximity to other markets in Europe, the Caucasus and Central Asia, and the Middle East and North Africa, and its preferential trade arrangements with the European Union and neighboring countries put the country in an advantageous position for American entrepreneurs seeking access to those markets. Over the past decade, Turkey has invested significant energies in increasing its ties with neighboring and surrounding economies and succeeded in expanding its markets with new business connections. U.S. exporters and investors can develop strategies to leverage established know-how and market shares through partnerships with local entrepreneurs, especially through joint ventures in the automotive, construction, and energy sectors, among others.

Turkey's ongoing privatization program likewise offers lucrative investment opportunities for American entrepreneurs. There are still 19 major entities waiting to be privatized, and the state has over a 50% share in 11 of those entities. Privatization from 2011 to 2013 is expected to generate around $50 billion in revenue. Sectors under the scope of privatization include banking, energy, transportation, telecommunications, and lotteries. Properties slated to be privatized include eight toll highways, three ports, the two bridges over the Bosphorus, various electricity generation and distribution companies, and gambling license rights.

Recent changes to the Turkish incentive system also provide opportunities for U.S. investors in selected industries. A new incentive regime was developed by the Turkish Investment Support and Promotion Agency (ISPAT) to accompany Turkey's industrialization and development strategies, which aim to enhance the country's export capacity and integrate Turkish producers into supply chains with a broader domestic value added, to encourage transfer of technology. The regime divides Turkey into four zones and includes incentives in the form of reduced corporate tax, social security premium contributions for employers, and interest support. Additional reforms, now underway, aim to create strategic clustering around industries and to restructure free zones. FDI in the following industries covered by the regime has the greatest potential to enhance bilateral economic ties by integrating domestic Turkish production with the U.S. economy:

- automotive
- chemicals and pharmaceuticals
- energy
- financial services
- medical devices
- aviation
- construction
- transportation and logistics

AUTOMOTIVE INDUSTRY Turkey's automotive industry has experienced substantial growth over the past two decades, owing mainly to the increasing purchasing power of its large population as a result of economic growth and the massive expansion of international trade following the Customs Union Agreement with the EU. The expansion has been so big that the automotive sector has become Turkey's leading export sector, exporting about $16.9 billion in 2009, equivalent to 17.4% of Turkey's export revenues. Turkey ranks 17th in automobile production in the world and seventh in Europe. Though the economic crises had a large effect on exports, which fell by nearly 31% in 2009, government incentive schemes helped the sector stem the tide relatively well overall, with growth rates through 2013 expected to be around 4.5 to 5%. Turkey's advantages are its skilled work force, mature and agile supplier industry, competitive labor costs, strategic location, and large internal market with a significant growth potential. On the downside, Turkish automotive exports are dependent to a large extent on demand in Europe.

Total production increased by a CAGR of 14.3% from 2002 to 2009. Foreign investment in the industry has increased substantially in recent years, with three of the four major car producers being Turkish-foreign partnerships (Ford- Otosan, Oyak-Renault, and Tofas-Fiat). Overall, Ford- Otosan is the biggest player in the Turkish market, followed by Oyak-Renault, Tofas (a joint venture between Koc Holding and Fiat), and Toyota.

3. THE U.S. MARKET AND OPPORTUNITIES TO INCREASE TURKISH EXPORTS

Turkish exports to the U.S. market do not reflect the overall transformation of domestic production and exports since the Customs Union with the European Union went into effect. Indeed the Customs Union paved the way for a dynamic reorganization of the Turkish economy with significant welfare creation and trade diversion owing to the adoption of the Common Commercial Policy of the European Union, opening of the Turkish market to intense international competition, and supportive structural reforms. As a consequence, Turkey's foreign trade both with the European Union and the world has reached historical highs since 1996, and the overall composition of the nation's imports and exports has reached a shift of comparative advantage from labor-intensive industries to more knowledge- and capital-intensive goods, with the automotive industry taking over the top spot in the export mix since 2004. The average annual rate of increase for all Turkish exports between 2002 and 2006 was around 24%; automotive products increased 38.5% in the same period, followed by electrical machinery, growing by 28.7%.

In contrast to this general trend in Turkey's trade with the world, the majority of Turkish exports to the United States continued to be of labor and capital-intensive goods — textiles and clothing, iron and steel products, and stones, plaster and cement. Labor-intensive products still constitute around 40% of Turkish exports in merchandise goods.

Thanks to comparative advantage gained over time, Turkey has successfully increased its exports to the United States in certain research- and capital-intensive goods, including automotive, iron and steel, cement and construction materials, electronics and manufactured metal goods. A close examination of the shifts in goods exported to the American market shows that capital-intensive exports such as ships, automotive products, iron and steel, and cement are increasing at a larger scale compared to other goods (See Table 3 in the Appendix). The auto industry is fifth in the world in the export of mass transit vehicles, though it took a hit in the 2008–2009 economic crisis. The shipbuilding industry saw rapid growth earlier in the 2000s, but again, the financial crisis hit hard, causing a drop of more than 50% in exports from 2008 to 2010. A continued focus in these industries might result in higher shares in the U.S. market, despite intense competition and limitations in domestic demand and growth prospects.

JOINT VENTURES Joint ventures are an excellent way of increasing exports to the United States, and there are already several good examples, including the success of Ford-Otosan and other automotive ventures and the Tusas Engine Industries (TEI) venture between General Electric and Turkish Aerospace Industries, which produces parts for commercial, military, and marine engines and ranks among the top Turkish exporters to the United States. Joint ventures are also a good way to export to third markets, as the Ford-Otosan example demonstrates.

Another key industry with potential for increased market share is cement and construction materials. Turkey is the second largest exporter of cement in the world and the third largest producer in Europe. Turkey also has 40% of the world's marble reserves, and exports of marble and other natural stones have grown rapidly over the past 10 years. The country ranks fifth in the world in the production of ceramic tiles and in 2008, ranked 11th in the world in the production of steel. It is also ranked in the top five worldwide exporters of glassware, gold jewellery, and precious stones.

Turkish companies have preferred exporting to Europe and the Middle East rather than the United States due to a number of market-oriented challenges. In the traditional labor-intensive products that still constitute around 40% of Turkish exports in merchandise goods, there is intense competition with Asian economies such as China, which have lower labor costs. Under such circumstances, Turkish textiles and clothing will struggle to increase their market shares, with the exception of companies such as Mavi Jeans that can appeal to higher-end consumers with their quality and marketing strategy.

FORD-OTOSAN JV The successful partnership between Ford and Otosan became a model for Turkish-foreign joint ventures, not only in the automotive sector but other sectors as well. Koc Holding and Ford Otosan both hold 41% ownership in the joint venture, the remaining being public. Following Ford's gradual increase of its ownership to 41% by 1997, the company quickly became one of the most successful business ventures in Turkey. Today, the company employs more than 10,000 people, and its net sales reached $4 billion in the first nine months of 2011. The company became the third biggest Turkish exporter in 2010 and exports cars manufactured in its Turkish plants to both Europe and North America. The company's Transit Connect vehicles are used as taxis in several U.S. cities, including New York, Washington, and Los Angeles. The company is the biggest player in the Turkish automotive industry and holds a market share of 15%.

Another significant disadvantage of Turkey is the lack of the kind of logistical infrastructure in the United States that other competitors have. Turkish exporters lack facilities such as logistics centers, export promotion showrooms, and storage houses, as well as the type of strategic governmental support provided by the Chinese or Brazilian governments to their exporters to build up networks of retailers and relationships.

Due to the large scale of the U.S. market, retail margins are low. Turkish exporters are not able to compete with companies already in the market due to high sale volumes needed to enter the market. This is particularly challenging for small and medium-sized Turkish companies, which lack the tools provided, for instance, by Brazil's APEX trade agency to support export diversification, integration into global and regional supply chains, and entry into the U.S. market.

Furthermore, success in the U.S. market depends upon the ability of exporters to meet the tastes and preferences of American consumers which, in some goods and services, deviate considerably from those in Turkey's traditional export markets. Turkish manufactured products do meet the quality standards demanded in the U.S. market, thanks to significant steps taken by the Turkish government toward standardization and private-sector investment. But the Turkish private sector has further succeeded in responding to the tastes and preferences of consumers in Europe, making significant investments to adjust their products' models, sizes, and designs to meet those preferences and adapting marketing and branding. For instance, the Turkish TV and home appliances industry has captured large shares in European markets by adapting production to higher technical standards through investments in assembly lines and research and development. According to the Turkish electronics producer Vestel, the success of the company in Europe largely depended on its R&D awareness, strong connections with universities and research centers, strategies to develop higher-quality products by conducting patent searches and an analysis of new technology and strategies of competing companies. However, similar strategies of long-term planning, investments in R&D and marketing, and adjustments to domestic production patterns have not been adopted by a majority of Turkish companies seeking access to the U.S. market.

A long-term strategy to gain a fair share in the U.S. market is an utmost necessity not only for companies but also governments. Most governments whose industries have succeeded in increasing their share in the U.S. market have developed sophisticated export promotion strategies to align the composition of their exports with that of U.S. imports through promotion of selected industries and products for which there is continued and increased demand. Fixing the mismatch between Turkey's exports composition to the United States and the U.S.'s import composition, dominated by research- and raw-material-intensive products, requires efforts of this kind. Suffice it to note that countries such as Spain, which have succeeded in enhancing their market share in the U.S. market, especially in the health and pharmaceutical sectors during the last decade or so, adopted product/industry targeting in their export promotion strategy to align the composition of their exports to the United States' research-oriented import composition. Turkish exporters in the same period lacked an export promotion strategy with U.S.-market-specific alignment focusing on high-value-added research-intensive goods. Successful export promotion strategies also include service industries, which have been out of the scope of Turkey's trade policy and strategies with the exception of the construction sector.

MARKETING AND BRANDING: RED BULL AND MAVI JEANS A more creative and aggressive export promotion strategy can be pursued both by the Turkish Ministry of Economy and the members of exporters' unions. This strategy might have a strong pillar of marketing and branding. Austria's Red Bull offers an excellent case study in developing a creative marketing strategy to enter the U.S. market. Only four years after going on sale in the United States in 1997, Red Bull had captured 65% of the U.S. energy drinks market. The company avoided traditional forms of marketing and adopted an "anti-branding/anti-marketing" strategy. It primarily targeted "Generation Y," people born after 1981, relying on certain buzzwords to draw attention, targeting university campuses and conducting grassroots "person-to-person" marketing that sought to label Red Bull as an "underground" drink. Similar potential for Turkish brands can be seen in the success story of Mavi Jeans, which entered the U.S. market in 1996 with a high-fashion focus and retailing through showrooms in New York and Los Angeles. In an interview, Mavi Jeans's CEO noted that "Mavi's philosophy is to build a Mediterranean fashion brand around jeans which are both a perfect fit and epitomize the culture of blue jeans. We call this sexy, intimate, modern and inspiring world 'Maviterranean.' "

With regard to exports in commercial services to the U.S. market, construction, transportation, and travel services have the greatest potential for success. More details can be found on Turkish service industries such as construction, energy, transportation and logistics, information and telecommunication services throughout this report. It is worth noting here in particular the potential offered by the travel services category, in particular medical tourism. Turkey is rich in thermal resources, with more than 1,000 thermal springs putting the country in 7th place in the world. Turkish thermal treatment facilities developed a capacity to entertain approximately 1.5 million visitors from abroad. Turkey has also developed a comparative advantage in other medical services, including complex surgery, offering high quality at a lower price. According to the West Mediterranean Development Agency and TAIK, the cost of an angioplasty operation in Turkey is estimated to be around $3,500, in contrast to a total cost of around $100,000 (before insurance coverage) in the United States. Bypass surgery costs more than $200,000 in the United States, but only around $12,000 in Turkey. There is a similarly huge difference in the cost of cardiac valve, hip, and knee surgeries. This potential could not only be further leveraged with increased exports to the United States through medical tourism, but also through U.S. investments in Turkey, in particular in hospitals, spas, and thermal facilities.

4. TRADE POLICY ENVIRONMENT IN TURKEY

Compared to the U.S. system, in which Congress has strong authority on trade policymaking compared to the executive, the Turkish parliament is not an active player. Although parliament is able to change laws and make new laws on trade, the executive branch implements the laws and regulations, ensures Turkey's compliance with its international commitments, negotiates new agreements, and takes measures towards opening markets or protecting sectors from unfair competition. The Ministry of Economy, recently created to replace the Undersecretariat of Foreign Trade, has the primary responsibility for trade policy. Trade in services, which was a responsibility of the Treasury, has also been integrated into the ministry's mandate. The Ministry of Agriculture, meanwhile, retains the right to regulate domestic production through certain measures that might have an impact on trade. Because of the difference in the balance of power, business lobbying takes a different form in Turkey than it does in the United States. Since the government in power generally holds the majority in parliament, lobbying groups pressure the leading figures in the government and the ruling party, as well as the ministries responsible for regulations.

TURKEY'S FTAs Turkey has free trade agreements in force with the following countries: Albania, Bosnia and Herzegovina, Chile, Croatia, EFTA, Egypt, Georgia, Israel, Jordan, Macedonia, Montenegro, Morocco, Palestine, Serbia, Syria, and Tunisia. In addition, either negotiations are underway for FTAs or the agreements are in internal approval process with the following countries: Cameroon, Colombia, Democratic Republic of Congo Ecuador, Faeroe Islands, Gulf Cooperation Council, Lebanon, Libya, Malaysia, Mauritius, Mercosur, Moldova, Seychelles, South Korea and Ukraine.

Turkey's FTAs generally contain comprehensive provisions for tariff reductions in manufactured products and trade remedies; agriculture and services are generally outside the scope of those accords. In this regard, Turkish FTAs are far less comprehensive than "deep integration" accords, such as NAFTA or the Trans-Pacific Partnership currently being negotiated by the United States and Asia-Pacific countries. Deep integration deals are currently in force or being negotiated by many developed and developing countries, and include WTO-plus provisions on investment, competition, capital mobility as well as services, detailed rules of origins, and rules on tariff and non-tariff barriers. Deep FTAs create a behind-the-border regulatory framework that facilitates cross-border operation of companies along the supply chains. Turkey's FTAs fall short of creating a comprehensive regulatory framework, and the country's intentions to extend similar agreements to neighbors and surrounding countries are impaired by its obligations to the European Union. Turkey particularly wants to intensify economic cooperation with countries in its region and through regional bodies such as the Black Sea Economic Cooperation Organization. However, the Customs Union with the European Union does not allow Turkey to pursue independent preferential deals with third parties not considered for an FTA by the EU for various political and economic reasons.

Turkey has a market open to international trade, thanks to its membership in the World Trade Organization and the EU Customs Union. The Ministry of Economy has been working for a long time to develop a strategy to increase the value of exports to $500 billion by the 100th anniversary of the republic in 2023. In this context, since the early 2000s Turkey has successfully increased its trade with countries in its region through implementing the Trade Enhancement Strategy with Neighboring and Surrounding Countries, which was followed by another strategy developed for the African continent. In this context, Turkey opened new embassies and trade representative offices in African countries and elsewhere.

NEW TRADE MEASURES WITH POTENTIAL TO AFFECT U.S. EXPORTS

U.S. exporters are concerned about ongoing problems created by specific trade policies. The complex tariff schedule, uncertainties about the relationship between tariff bindings and applied most favored nation (MFN) tariff rates, and challenges created by Turkey's customs regime (regulations, procedures, and valuation methods) are prevailing challenges. At the same time, Turkey has launched a number of new protectionist measures since the beginning of the economic crisis. The Global Trade Alert (GTA) database, which went online in 2009 to monitor protectionist measures taken by G20 members, confirms this trend. Among others, two measures reported by the Global Trade Alert to have a direct negative impact on U.S. exports are (1) the increase of import tariffs on ethyl alcohol products in January 2010 [5] and (2) new antidumping duties put in force in June 2009 on imports of polyvinyl chloride suspension grade from certain countries, including the United States. The GTA database also lists other measures that have the potential to hurt U.S. exports to Turkey. These

[5] According to the Ministry of Economy there has not been any tariff increase on ethyl alcohol since January 2010.

include the initiation of a safeguard investigation and announcement of a future provisional duty on imports of woven fabrics in July 2011; the initiation of a safeguard investigation on imports of polyethylene terephthalate in June 2011; and recent changes to steel import tariffs. The World Bank's Temporary Trade Barriers Database, however, shows that such barriers put in force by Turkey mainly target developing countries, particularly China, rather than the United States.

Turkish farming has long been protected by high tariffs and other measures. Most agricultural products are not covered by the Customs Union agreement. Certain measures affecting imports of livestock, meat, fruits, and vegetables, implemented by the Ministry of Agriculture in the past for safety and health purposes, were criticized for being excessive or beyond WTO standards, Recently, however, the government took radical steps to reduce tariffs on wheat products, live animals, and meat, aiming to supplement insufficient domestic production by reducing the cost of imported products to Turkish consumers. This policy change might create a significant opportunity for U.S. exporters in the near future.

FOREIGN DIRECT INVESTMENT REGULATIONS

Foreign direct investment is regulated through legal measures put in force by Parliament and implemented by the Treasury and various ministries. The current government has registered significant progress toward improving the business environment and conditions for FDI. The biggest step was the 2003 FDI Law, which included provisions increasing the freedom to invest, simplifying procedures for investment, and shifting foreign investment policy from screening to monitoring. This critical law adopted the international standards by which a "foreign investor" is defined and emphasized the equal treatment principle for such investors, which now covers both real persons and foreign legal entities with the new definition. The government also established the Investment Support and Promotion Agency (ISPAT) to institutionalize a systematic approach to attract FDI. These steps were taken to supplement structural reforms accomplished since the banking crisis in 2001. Finally, in 2009 parliament adopted a new incentives regime for both domestic and foreign investors, including a mix of tax and non-tax incentives for investments and exports as well as special provisions on free trade zones, technology parks, research and development, and incentives for less developed regions. While some incentives are provided horizontally across the country, others are provided for companies investing in specific regional economic zones.

According to the OECD's FDI Regulatory Restrictiveness Index, Turkey has an open regime for most economic sectors. The index measures the restrictiveness of a country's FDI rules by examining four major categories of restrictions:

- Foreign equity limitations
- Screening or approval mechanisms
- Restrictions on the employment of foreigners as key personnel
- Operational restrictions, e.g. restrictions on branching, capital repatriation, or land ownership

Based upon existing limitations, the index rates restrictions in each sector from 0 to 1, the former indicating that there are no restrictions and the latter indicating that the sector is fully closed. The OECD index illustrates that overall, Turkey had a more open FDI regime than the United States in 2010 with a rate of restrictiveness of 0.082 versus 0.089. However, there are still restrictions on the maritime and air transport, radio and TV broadcasting, accounting and audit, and mining sectors (See the sectoral comparison of U.S. and Turkish restrictiveness indexes in the Appendix, Table 4). The U.S. government has concerns about ongoing barriers also in the financial services, telecommunications, and energy sectors. U.S. insurance companies operating in the Turkish market also are seeking the continuation of structural reforms in the field of insurance and pensions and the increase of government incentives for the private pension system.

The World Bank's Doing Business 2012 report ranks Turkey 71st out of 183 countries, up from 73rd in 2011. The tables on the next page show Turkey's ranking and comparison to other countries in its region on factors such as starting a business, dealing with construction permits, registering property, getting credit, protecting investors, paying taxes, trading across borders, enforcing contracts, and resolving insolvency.

According to a 2010 survey by the American Business Forum in Turkey (ABFT), American investors are particularly concerned with what they see as the unpredictability of the Turkish business environment and lack of transparency of regulations and procedures. Among others, the following issues were listed as major concerns:

- heavy government involvement in different areas of business life;

- the lack of transparency in decision-making, customs services, etc.;
- an opaque process of lawmaking;
- frequent and often retroactive changes in laws, regulations, and policies, especially concerning taxation;
- different interpretations of the rules and regulations by bureaucrats at different levels; and
- hidden taxes and additional fees charged by different authorities.

ABFT's 2011 Survey[6] on the Business and Investment Climate in Turkey also provides interesting insights. According to the survey, only 30% of American investors believe that the legal system is efficient, and only 39% believe that Turkish judges are impartial. An insufficient level of high school education is also an important issue cited by investors. However, despite these areas that need improvement, 69% of the investors surveyed recommended investing in Turkey, and 75% believe the country's market potential is considerable.

The legal system is considered problematic by American investors for a number of reasons, including the favoring of domestic investors over foreigners, delays in processes, and a lack of experts and judges with sufficient technical knowledge to deal with cases concerning technological issues and intellectual property rights (IPR). IPR law and its implementation is still seen as a problematic area, especially regarding the lax enforcement of trademarks, copyrights, and patent protection.

The U.S. pharmaceutical industry is especially concerned about the lack of sufficient legislative, judicial, and enforcement steps to protect drug patents and undisclosed test and other commercial data. The industry is also concerned about certain regulations having impact on their exports to the Turkish market. These include medicinal products registration processes, Good Manufacturing Practices (GMP) inspection requirements for imported pharmaceuticals, and pricing and reimbursement procedures. These regulations are in place either as part of national health policies that aim to ensure the provision of health services and products at a reasonable cost and quality, or with the motivation to discourage import of generic products and to make Turkey a production base in pharmaceutical sector. Although Turkey provides significant incentives for FDI in research and development for pharmaceuticals, foreign companies prefer to invest elsewhere. The total amount of FDI together with other chemical products was recorded as $60 million in 2010. To attract investment in the industry, the Turkish government might consider consultations with foreign and domestic producers and revising existing policies based upon those consultations.

TURKEY DOING BUSINESS RANKING SUMMARY AND DEVELOPMENT

	DB 2012 Rank	DB 2011 Rank
Starting a Business	61	63
Dealing with Construction Permits	155	153
Getting Electricity	72	73
Registering Property	44	39
Getting Credit	78	75
Protecting Investors	65	60
Paying Taxes	79	83
Trading Across Borders	80	79
Enforcing Contracts	51	51
Resolving Insolvency	120	122

Source: World Bank Doing Business Report 2012

	Doing Business 2012 Rank	**Doing Business 2011 Rank**
Georgia	16	17
Armenia	55	61
Bulgaria	59	57
TURKEY	**71**	**73**
Romania	72	65
Serbia	92	88
Greece	100	101
Russia	120	124
Syria	134	136
Iran	144	140
Iraq	164	159

Source: World Bank's Doing Business 2012 report

[6] American Business Forum in Turkey (ABFT) Business and Investment Climate in Turkey 2011
http://www.abft.net/PDF/ABFT_BusinessInvestmentClimateinTurkey_2011.pdf

5. TRADE POLICY ENVIRONMENT IN THE UNITED STATES

The United States' management of trade policies and foreign direct investment differs from that of Turkey because of the political system's checks and balances between the legislative and executive branches. The U.S. Congress takes a more active role in shaping trade policies than does the Turkish parliament, though it grants the executive branch the authority to negotiate and sign international agreements. Although the United States Trade Representative (USTR) is responsible for negotiations and for coordinating the implementation of trade policies, other executive bodies, such as the Departments of State and Commerce and the Food and Drug Administration, also take roles in policymaking and implementation. The system of checks and balances allows all stakeholders, including exporters and importers, to influence decision-making by lobbying both the legislative and executive branches.

Overall, the United States has an open market both for foreign investors and exporters. The U.S. has 17 free-trade agreements (FTAs) in force, including NAFTA with Canada and Mexico. Due to partisan differences over labor and environment standards, FTAs with Colombia, Panama and South Korea, which were negotiated under George W. Bush's presidency, long awaited congressional approval before they were finally passed in October. Meanwhile, the Obama administration has also pursued negotiations for a Trans-Pacific Partnership agreement with Australia, Brunei, Chile, Malaysia, New Zealand, Peru, Singapore, and Vietnam.

While average tariffs to access the U.S. market are lower than 3%, major challenge for foreign traders and investors rest in non-tariff barriers such as customs procedures and measures related to security and consumer protection, and behind-the-border regulatory restrictions that stem from diverging regulatory standards. Turkish exporters are particularly concerned with increasing measures at the borders, and delays and other problems on business visas due to security concerns since the terrorist attacks of September 11, 2001. Another concern is the duration of the safeguard and anti-dumping remedies of the U.S. regime, some of which are applied for a long period of time and arguably become punitive rather than remedial. Getting the necessary permits to start a business is particularly difficult for Turkish small and medium enterprises due to the high financial commitment requirements and other cumbersome regulations. Even getting a tourist visa can become a challenge for Turkish citizens, as the lack of a visa waiver program means travelers must submit several financial documents as well as detailed information about the trip in advance. Improved transportation links in the form of new direct flights between Istanbul and Washington and Los Angeles are likely to contribute positively to the trade and investment relationship, but bureaucratic hurdles continue to make it difficult for Turkish nationals to travel to the United States.

Although it is an open market, not all sectors are fully open to foreign competition. During the trade policy review of the United States at the WTO in 2010, the Turkish government complained about domestic regulations in the services sector. The OECD FDI Regulatory Restrictiveness Index confirms that there are ongoing restrictions against foreign investors in some U.S. sectors, including fishing, mining, electricity generation, radio and TV broadcasting, communications, air transportation, banking, and certain other financial services. There are discriminatory restrictions in the U.S. maritime services sector[7].

U.S. FREE TRADE AGREEMENTS The United States has FTAs in force with 17 countries: Australia, Bahrain, Canada, Chile, Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Israel, Jordan, Mexico, Morocco, Nicaragua, Oman, Peru, and Singapore. Congress approved long-stalled FTAs with South Korea, Colombia, and Panama on October 12, 2011.

Another sector that has definitely not been fully liberalized is the U.S. farming industry. The United States retains protections for its agriculture sector, especially in the form of export subsidies first put into effect by the 2002 farm bill. Products receiving government support include corn, cotton, soybean, wheat, tobacco, dairy, rice, and peanuts. Due to the U.S. government's ongoing budget problems, it is expected that some of these subsidies will be removed during congressional deliberations for a new farm bill in 2012. This being the case, the United States has recently taken further protectionist measures on dairy products. The Dairy Export Incentive Programme (DEIP), which operates by providing cash bonuses to U.S. exporters, was expanded in 2009. DEIP was first established in 1985 and subsequently reauthorized by farm bills in 1990, 1996, 2002, and 2008. Although the program has been less used in recent times, the United States announced in May 2009 that allocations would be stepped up to the maximum allowed under the Uruguay Round Agreement on Agriculture. The United States has been criticized for undermining the

[7] For instance, provisions of the Merchant Marine Act of 1920, also known as the Jones Act, restrict the carriage of passengers and goods between domestic ports to U.S.-built and -flagged vessels.

credibility of the WTO system by raising tariffs and export subsidies to the maximum allowed level, even if WTO rules are not actually breached. According to the GTA, expansion of the DEIP has coincided with requests from the National Milk Producers Federation, illustrating the power of the U.S. farming lobby. These subsidies, achieved and supported by the farming lobby, make it extremely difficult for foreign competitors, including Turkish exporters, to enter the U.S. market. Agricultural cooperation aimed at expanding trade in certain products should be part of the bilateral mechanisms and conversations between the two countries.

PROTECTIONIST PRESSURES AND THE TRADE AGENDA

The protectionist pressures on both Congress and the White House have increased since the beginning of the economic downturn, and are not limited to farming. A hot issue on the U.S. trade agenda over the last few years has been competition from China and its arguably unfair trade practices, such as currency manipulation. The Global Trade Alert reports that 18 measures were brought up in Congress that would potentially have a negative impact on exports of Turkish goods and services to the American market. Most of those measures were withdrawn or suspended, but Congress did act upon a couple of crucial measures important for Turkish exporters and investors.

For instance, the American Recovery and Reinvestment Act, the $787 billion stimulus bill passed in January 2009, included the so-called "Buy American" clause, the stipulation that all iron, steel and other manufactured goods used in stimulus-funded programs be produced in the United States. While imports of close trading partners and most industrialized nations were not affected by the "Buy American" clause, those of major players such as the BRIC countries (Brazil, Russia, India, and China), developing and transition economies as well as Turkey were. Another provision of the law (Section 604) took this further by requiring that funds allocated for Department of Homeland Security programs could not be used for the procurement of "certain covered items unless grown, reprocessed, reused or produced in the United States." Examples of items covered under this provision included clothing, bags, wool, and even any equipment used to produce the items that might contain foreign materials. The GTA reported that these measures were among those that have potentially negative effects for Turkish exporters.

On the other hand, the Obama administration launched the National Export Initiative (NEI) in January 2010. President Obama set the goal of doubling U.S. exports in the next five years (by the end of 2014) in order to create jobs for 2 million unemployed Americans. Turkey was designated as one of six "next tier" emerging markets for which a government-wide export strategy would be implemented.

Finally, a significant regulatory issue for Turkish exports concerns access to the U.S. market provided by the Generalized System of Preferences (GSP). Over the past four decades, GSP has been the largest preference program in force in the United States, offering duty-free trade preferences to thousands of products from almost 130 developing and least developed countries. However, in 2010 Congress could not agree on the terms of an extension of the system, and the program expired on December 31, 2010. The program was reintroduced months later following an intense debate in Congress.

Regardless of its status, GSP has not provided stable access for Turkish products, although it covered almost 20% of all Turkish exports to the United States. It has long been proposed that countries above a certain income level, including Turkey as well as Brazil, India, and others, should be completely graduated from the program. Moreover, the system of program extensions for limited periods of time, and the influence of domestic lobbies on Congress's decisions about coverage and eligibility of the products, mean that GSP is unpredictable. Notably, the textiles and apparel lobbies have used their influence to exclude those products from many countries' GSP coverage. Jewelry was another item that was covered by the GSP for Turkey. However, gold products, with the exception of gold-chains were removed from the Turkish list in the second half of 2008. That resulted in a significant decline in Turkish exports that continued in 2009 and 2010.

NATIONAL EXPORT INITIATIVE (NEI) The strategy identifies eight priorities that would be implemented by different agencies comprising the Trade Promotion Coordinating Committee (TPCC), including the Departments of Commerce and Transportation and the U.S. Export-Import Bank. These priorities cover exports by small and medium-sized enterprises, federal export assistance, trade missions, commercial advocacy, increasing export credit, macroeconomic rebalancing, and reducing barriers to trade. In addition, the initiative prioritizes "export promotion of services" as a crucial area completely missed in Turkey's exports strategies over the past decades. The strategy entails stronger inter-agency coordination to support U.S. exporters especially through programs of the U.S. Export-Import Bank (Ex-Im Bank) and Overseas Private Investment Corporation (OPIC). The Ex-Im Bank is the principal government agency responsible for aiding U.S. exports through a variety of loan, guarantee, and insurance programs. Its programs support American export firms of any size, including a focus on small businesses through the Export Credit Insurance and Working Capital Guarantee programs, among others. Turkey is one of the nine priority countries in the world for the US Ex-Im Bank. OPIC was established in 1971 to help U.S. businesses invest overseas and to promote economic development in new and emerging markets. Its programs provide project finance and political risk insurance against the risks of inconvertibility, political violence, or expropriation. The agency also provides financing through direct loans and loan guarantees. One of eight priorities of the president's National Export Initiative is the provision of export credit and other forms of financing for small and medium enterprises that export through Small Business Administration (SBA), Ex-Im Bank and OPIC programs.

[7] Such protectionism did not initially go down well either inside or outside the United States, resulting in an amendment specifying, somewhat vaguely, that the provisions "shall be applied in a manner consistent with U.S. obligations under international agreements." This meant that the United States could differentiate among trading partners on the basis of previously signed deals, such as the WTO's Government Procurement Agreement (GPA), the Caribbean Basin Initiative (CBI), or other reciprocal agreements with trading partners. Since Turkey is not a party to the GPA, "Buy American" applied to its imports.

6. BILATERAL LEGAL AND INSTITUTIONAL FRAMEWORK FOR TRADE AND INVESTMENT

Two bilateral agreements govern the flows of trade and investment between Turkey and the United States. A Bilateral Investment Treaty (BIT) has been in force since 1990, followed by a Double Taxation Avoidance Agreement in effect since 1997. Additionally, the two counties signed a Trade and Investment Framework Agreement (TIFA) in 1999, which constituted the basis for annual Trade and Investment Council meetings where the two parties consult on issues related to trade and investment. Since neither of these agreements is comprehensive enough to provide preferential access or commercially meaningful discriminatory treatment to the other party, they fall short of ensuring economic integration between the two countries, especially along international supply chains that could bring together U.S. and Turkish producers of goods and services.

It is essential for the two parties to consider a more modern legal and institutional framework given the fact that the United States is negotiating new preferential trade agreements with a number of Asia-Pacific countries, and other major competitors of Turkey already enjoy preferential access to the U.S. market either through bilateral agreements or through unilateral programs. For example, South Africa is a major beneficiary of the African Growth and Opportunity Act (AGOA). AGOA is legislation approved by the U.S. Congress in May 2000 in order to assist the development of the economies of sub-Saharan African and to increase trade between the United States and the region. It expanded the benefits under the GSP program by providing additional quota and duty-free access into the United States for products from 41 countries. While the program has helped many low-income African countries to increase their exports in a number of products including textiles and especially oil, it proved crucial to a regional power, South Africa, by allowing preferential, duty-free access for its automotive products—exports that now amount to $2 billion a year.

Because of Turkey's membership in its Customs Union with the European Union, it is not at liberty to negotiate an FTA with the United States until the EU signs its own FTA with the United States. Toward this end, at the November 2011 U.S.-EU summit, Washington and Brussels agreed to launch a High-Level Working Group on Jobs and Growth to explore options for deeper transatlantic economic integration, including negotiations which could lead to a U.S.-EU FTA. While it is too soon for the United States and Turkey to launch their own bilateral trade talks, the EU could decide to associate Turkey closely with the work of the U.S.-EU High-Level Working Group to facilitate early progress on a Turkey-U.S. FTA.

Turkey and the United States might consider revising existing accords to strike a more comprehensive and modern framework that would help build a better business

TURKEY-EU CUSTOMS UNION AND FTAs The European Union (EU) has preferential trade agreements with several countries mainly in the form of FTAs. Its Customs Union (CU) extends to a couple of small economies in Europe, such as Andorra and San Marino, in addition to Turkey. All other recently acceded countries to the EU had signed FTAs before they joined, whereas Turkey concluded a Customs Union before full membership. Similarly, non-member European countries such as Switzerland, Norway and Iceland, which have formed a trade bloc under the European Free Trade Area (EFTA), have a preferential trade agreement with the EU called the European Economic Area.

The legal premise of the Customs Union between Turkey and the EU is based upon the Ankara Agreement of 1963, which had envisioned a three-step transition process for the accession of Turkey to the European Economic Community (then a Customs Union itself). The three-step process was completed with the formation of the EU-Turkey CU in 1995 before Turkey's full membership to the Union, which had in the meantime evolved into a single market and then an economic union.

The major difference between a CU and FTA rests in the formation of a common commercial policy and adoption of common external customs tariffs in the case of CU in addition to the elimination of a substantial part of trade barriers bilaterally. For instance, Mexico, which is party to NAFTA, is relatively independent in determining its tariffs and trade policies vis-à-vis third parties, while it is bound to eliminate trade barriers against other NAFTA countries. However, Turkey is bound by the EU Common External Tariff and the Common Commercial Policy, determined by 27 EU member states and the European Commission in Brussels. In this regard, Turkey is allowed to negotiate and sign preferential trade agreements only with third parties with which the EU engages in preferential deals.

environment for the private stakeholders of the two countries. For instance, as part of such a new framework (which could be called a Strategic Economic Partnership Agreement) the two countries could revise the existing U.S.-Turkey BIT by renegotiating it in order to insert comprehensive provisions that would at the very least lock in significant reforms that Turkey has already undertaken unilaterally. The Turkey-U.S. BIT is somewhat outdated. Since it was signed in 1985, Turkey has negotiated BITs with more than 80 other countries to encourage FDI inflows, increase transfer of technology and know-how, and provide protection to foreign investors from expropriation. On the U.S. side, BITs signed with more than 50 countries have evolved over time to cover sophisticated measures for investment and investors' protection, and investment liberalization has also been part of recent U.S. FTAs.

A more comprehensive BIT might help improve the predictability of the business environment for U.S. investors and ensure transparency of domestic investment provisions in Turkey. The parties could elaborate extensive provisions for "prior comment" that would allow the two sides to have an opportunity to file comments on potential regulatory changes beforehand. Through building national inquiry points and publishing regulations as required, the new BIT would also contribute to the transparency of the business environment in Turkey, a major issue for American investors. BITs are designed to provide certain discriminatory benefits for the signatories. The parties should be aware of the fact that the EU will soon negotiate and sign a new BIT with Turkey and other countries that have an agreement with member states, owing to the Treaty of Lisbon amendments to the acquis communautaire, which empower the European Commission to negotiate investment agreements on behalf of all 27 EU member states. The new BIT between Turkey and the EU might provide certain privileges for European investors, depending on its content and scope. In this regard, before Turkey extends certain benefits to other parties, the United States and Turkey might consider extending those benefits to each other through a revision of the existing BIT. Finally, in both alternatives, the U.S. and Turkish governments might consider revising the Double Taxation Avoidance Agreement to encourage joint investment, for instance through eliminating the tax-sparing provision in the Treaty.

As other elements of such a "second best" alternative, the parties might also consider a new unilateral preferential trade scheme for Turkish exporters with benefits similar to AGOA's for South Africa. In this regard, the parties could consider unconditional access to the U.S. market for selected Turkish products such as automobiles, TV sets, and other electronics. A Strategic Economic Partnership Agreement might also contain other elements such as provisions on technology transfer and/or "WTO-plus" rules (on intellectual property rights and/or other areas) to make it attractive to stakeholders in both countries. The elements of the bilateral deal including the BIT could help build a better regulatory framework for supply chains in the joint production of more research-intensive goods and services.

MODERN BITs The most comprehensive investment agreement thus far is Chapter 11 of NAFTA, which provides rights for investors that include a settlement mechanism for disputes against the governments that are party to NAFTA. The contemporary BITs signed by the United States follow a standard, updated "2004" model, developed by USTR and the State Department through consultations with other government agencies. The 2004 model contains certain minimum provisions for nondiscriminatory liberalization of capital movements, as well as investment and investor protection. BITs and investment chapters in existing FTAs throughout the world also include extensive provisions, but the U.S. model still provides the most comprehensive of these. There are 17 investment-related provisions covered in modern agreements. These include:

- Establishment
- Acquisition
- Post-establishment operations
- Resale
- Most favored nation treatment
- National treatment
- Nationality of management and board of directors
- Performance requirements
- Prior comment opportunity
- Duty to publish
- National inquiry point
- Denial of benefits
- Minimum standard of treatment
- Treatment in case of conflict
- Expropriation and compensation
- Transfers restrictions
- Investor-state disputes

7. PROSPECTS FOR COOPERATION IN THE CONTEXT OF THE G20

The Group of Twenty (G20) was established in 1999 following the 1997 Asian crisis to bring together major developed and emerging economies to discuss and coordinate efforts to stabilize the global financial system. The platform was reinvigorated after the outbreak of the global financial crisis in 2008 with a series of meetings of finance ministers, central bank governors and heads of states and governments in order to coordinate measures to restore financial stability and to provide sustainable economic growth and development. Since the beginning of the financial and economic crisis, leaders of G20 countries have gathered at summits held in Washington in 2008, London and Pittsburgh in 2009, in Toronto and Seoul in 2010, and in Cannes in 2011. The agenda of the G20 has expanded from financial regulation and the reform of the Bretton Woods institutions to issues such as job creation, economic growth, global imbalances, poverty eradication and development, commodity and price volatility, and food security. At the end of the Cannes summit, G20 leaders made decisions on a number of issues, including adopting an ambitious action plan for growth and jobs, taking a new approach to the WTO Doha negotiations in 2012, acknowledging the significance of food security and agriculture, implementing and strengthening financial reform, discussing a possible global financial transaction tax, and agreeing to increase the IMF's resources when needed "for the benefit of the entire membership."

To offer a joint business input to intergovernmental negotiations, business organizations and companies from G20 countries have also come together since the G20 summit in London in March 2009 under the umbrella of the Business 20 (B20). The main objective of the B20 is to develop recommendations and issue commitments from the business bodies to deal with the G20 issues. The G20 is organized around 12 issues that are considered to be priorities for the business community, including economic policy, financial regulations, trade and investment, energy, and anti-corruption. Recommendations produced from 12 B20 working groups are presented to G20 leaders. Both TUSIAD and the U.S. Chamber of Commerce participate in the B20 and take an active part in business consultations in order to form a collective position.

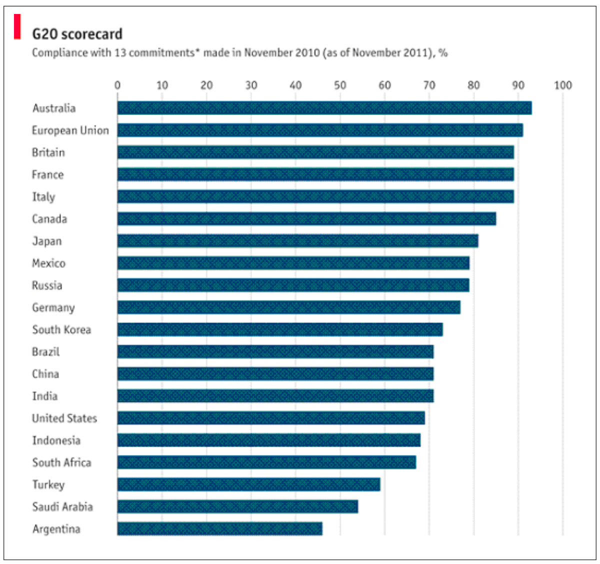
Turkey is a founding member of the G20. According to the IMF, it is the 16th largest economy in the world, and sixth in Europe, in terms of GDP at purchasing power parity. Some analysts put emphasis on Turkey's role within the G20 as a "middle power," as it plays an active and constructive role as a bridge between developed countries and emerging economies, as well as between Europe and Asia[9]. By definition, middle powers act as active members of the international system through international institutions, or regional or issue-based coalitions. Indeed, Turkey has demonstrated enhanced activism in its region and on certain global foreign policy issues, thanks largely to a spectacular economic performance and domestic political stability over the past decade. However, its activism at the G20 has so far been limited, especially compared to its proactive attitude regionally or as a non-permanent member of the UN Security Council, which lasted until the end of 2010.

Even though Turkey has a stake in most global issues, the G20 has not yet been perceived as a platform to pursue foreign economic policy objectives, while the inefficiencies within domestic inter-agency mechanisms and processes hinder Turkey's ability to act as an "agenda-setter." Inter-agency coordination of G20 issues is carried out by the Undersecretariat of the Treasury. When the issue at hand is not a traditional economic policy matter, interagency coordination becomes more burdensome and problematic for the Undersecretariat. There is a growing interest from the Turkish private sector in the deliberations of the G20, and an emerging domestic constituency to feed into inter-agency mechanisms and processes. As those issues grow from the financial domain to ones that have broader political implications, it would not be surprising to see a more active Turkish involvement in G20 agenda-setting in the near future, at least as visible as South Korea, particularly when Turkey assumes the presidency of the group in 2015.

So far, Turkey has played a reactive and constructive role rather than a proactive one on the issues brought to the agenda by other members. On some issues, Turkey took a position closer to G7 countries, while on others it adopted an attitude closer to other emerging economies. Among others, the reform of the Bretton Woods institutions—especially quota reform—has been a priority for Turkey. As a country that undertook serious structural reforms to modernize its banking system and financial markets following the financial crisis in 2000 and 2001,

[9] See for instance Hüseyin Bagci, "The Role of Turkey as a New Player in the G20 System" in Wilhelm Hofmeister and Susanna Vogt, G20 - Perceptions and Perspectives for Global Governance, e-book, Singapore, Oct. 19, 2011 and Dries Lesage and Yusuf Kacar "Turkey's Profile in the G20: Emerging Economy, Middle Power and Bridge-Builder," Studia Diplomatica, Vol LXIII, 2010, No2.

Turkey actively engaged in the G20 discussions on financial regulations. Parallel to Germany and France, Turkey has favored a G20 agenda against tax havens and tax evasion. On the other hand, parallel to its recent proactive approach to sub-Saharan Africa, poverty alleviation, food security and other development issues, Turkey supported South Korea's initiative to launch a Multi-Year Action Plan on Development under the G20 at the Seoul Summit in 2010.



Source: The Economist, adopted and revised from the overview of the G20 Research Group, based at the University of Toronto's Munk School of Global Affairs

Turkey naturally signed G20 communiques outlining commitments of essentially non-binding nature. To date, G20 members have committed to enhancing international cooperation, fighting corruption, strengthening regulation of financial institutions and instruments, implementing more market-oriented exchange rate policies, ending fossil-fuel subsidies, and not adopting new protectionist measures. Developed countries also committed to implement credible fiscal consolidation policies. As is seen in the scorecard above, overall Australia and the European G20 members performed better than the United States and most emerging economies in implementing the commitments. Turkey ranked 18th of the 20 constituencies, while the United States was 15th.

Turkey's bridging role as a middle power can help both it and the United States to accomplish common objectives within the G20 context on a variety of issues. Both countries are concerned about the ongoing eurozone crisis, and can work together to further leverage the G20 to mobilize IMF and other resources to intervene in the crisis. Turkey and the United States have shared interests in achieving a sustained and well-balanced global recovery. Addressing global trade imbalances in a more effective way, especially through steps to be taken by G20 members with persistent current account surpluses such as China, is also of interest of both the United States and Turkey. Exchange rate stability and the prevention of currency manipulation are likewise priorities.

Turkey and the United States can also further cooperate to expand the G20's trade agenda. Fighting protectionism and strengthening the multilateral trading system are areas to which both countries attach high importance. Turkey's position, especially on the nonagricultural market access negotiations chapter of the Doha Round, is close to that of advanced economies since Turkey has an open market in manufactured products owing to the Customs Union with the EU. Turkey can also play a more constructive role compared to other emerging economies on the expansion of the WTO agenda to new trade issues, such as investment and competition, if this is brought to the G20.

8. RECOMMENDATIONS TO IMPROVE ECONOMIC TIES

The race among emerging economies continues on an intensified scale thanks to the global economic downturn, which has seriously hampered growth prospects in advanced economies that suffer from budget and public debt problems while the demand for consumption and imports is in decline. In particular, Asia-Pacific countries are working hard to increase economic ties to the United States through investing in global value chains and embarking upon new trade deals. U.S.-Turkish economic relations, meanwhile, suffer from a number of market-based and regulatory barriers that deserve attention and require concrete steps from stakeholders in both countries to change. These challenges exist alongside economic opportunities that would benefit both parties and bilateral relations if they can be taken advantage of. Officials and the business community should aim to come together around a new economic agenda that benefits from a strategic vision and political will. The following recommendations offer a road map for this agenda.

GOVERNMENTS SHOULD CREATE A NEW BILATERAL LEGAL FRAMEWORK TO ENHANCE TRADE AND ENCOURAGE INVESTMENT

To create a more enabling environment for businesses and to better integrate the two economies, the U.S. and Turkish governments should create a modern legal framework going beyond the existing patchwork of agreements and protocols. Such a framework can be developed as a "U.S.-Turkey Strategic Economic Partnership Agreement," including elements of unilateral preferential access for Turkish goods into the U.S. market and a revised BIT. Unilateral preferential access by leveraging the existing GSP or a newly formed preference program should target better access opportunities for Turkish research- and capital-intensive sectors such as automotives rather than labor-intensive sectors like textiles. The renegotiated and revised BIT should at least lock in the unilateral reforms in Turkey with provisions designed along new business-friendly regulations. It could contain other preferential provisions discussed above to enhance predictability and transparency for U.S. businesses operating/investing in Turkey. The Strategic Economic Partnership Agreement could also contain provisions covering WTO-plus issue areas such as intellectual property and public procurement. Finally, in both alternatives the U.S. and Turkish governments should consider revising the Double Taxation Avoidance Agreement to encourage joint investments especially through eliminating the tax sparing provision in the Agreement.

TURKISH AND U.S. EXPORT PROMOTION STRATEGIES SHOULD BE ALIGNED TO ACCOMPLISH MUTUALLY SET GOALS

As discussed, both the Turkish and U.S. governments have developed strategies to expand their exports with different timelines and policy tools. Both the National Export Initiative of the United States and Turkey's 2023 Strategy contain elements to expand trade between the two countries. They can work together to accomplish the overarching goal of improving bilateral economic relations through investment and trade by aligning their strategies and supportive policies. U.S. and Turkish exports and investment promotion agencies (the Turkish Ministry of Economy, ISPAT, USTR, U.S. Department of Commerce, U.S. Ex-Im Bank etc.) can come together to discuss how to align the two strategies in order to use their resources more efficiently and cooperatively, as well as setting a new timeline and targets to achieve certain mutually set benchmarks and goals.

TURKEY SHOULD DEVELOP A NEW EXPORT PROMOTION STRATEGY TARGETING THE UNITED STATES

The Turkish Ministry of Economy should adopt a new export promotion strategy that is capable of succeeding to increase and diversify trade with the United States. Such a strategy should identify key industries and products that can not only best help Turkey's economic and technological development and enable the integration of domestic production into regional and global supply chains but also have potential to succeed in the U.S. market. As discussed above, it is essential to respond to the import composition of the United States and the nature of demand in the American market. Therefore, such a strategy should distinguish itself from earlier strategies by targeting goods and services with potential to succeed in the U.S. market and outline policies to support exporters. In order to ensure the most beneficial integration of Turkish producers to global value chains, such a strategy should be aligned with the nation's investment promotion strategy. The new strategy should be empowered by policies helping Turkish businesses overcome challenges in logistical infrastructure and retail networks, and access to market information. To this end, the Ministry of Economy should support the establishment of joint logistics and business information centers in major U.S. ports and cities. The strategy should further help businesses access to market information through opening new economic and commercial counselors' offices in the United States, integrating the work of those offices with each other, and investing further in the analysis of the U.S. market for selected Turkish goods and services. It is essential to expand Turkey's export promotion strategies to commercial services in order to reap benefits in the U.S. market for expanding Turkish industries such as construction, transportation, health tourism, and software development.

CREATE NEW PLATFORMS FOR BUSINESS DIALOGUE AND COOPERATION

In both Turkey and the United States, there are a number of business bodies working to improve bilateral economic ties. On the American side are the U.S. Chamber of Commerce and the two Turkey-based American Chambers of Commerce (TABA and ABFT), as well as the American Turkish Council. In Turkey, there are TUSIAD (the industry federation), TOBB (the chamber of commerce) and its affiliate U.S. section TAIK, and TUSKON, among others. All these organizations and the annual meetings organized by ATC, TAIK and others as well as the official Business Council set up by the U.S. – Turkey Framework for Strategic Economic and Commercial Cooperations (FSECC), play an important role in business advocacy according to their resources, constituencies, and issue focus.The FSECC launched a new cabinet-level initiative to tackle challenges to enchanced economic relations with a more structured private sector involvement through a Business Council composed of representatives from both countries. This shift of focus of bilateral relations to the economic domain is a significant action and should be pursued with other initiatives. Enhancing economic activities requires U.S. and Turkish companies to come together for joint ventures, investments, and trade between the two countries. This can be best achieved by creating new platforms for enhanced business dialogue and cooperation. Bringing businesses together is especially crucial for small and medium-sized exporters in order to help them to identify strong local partners with necessary market knowledge and contacts. It is equally important to provide forums for U.S. multinationals to meet with Turkish suppliers through specifically designed programs in both countries. Both governments and companies should consider new channels to bring together exporters with importers and investors with suppliers in nontraditional sectors, going beyond military/security and energy. An annual conference for executives from all economic sectors, and companies of different scales can be coupled with other conferences and periodic dialogues organized for specific sectors such as electronics, automotives, medical services, chemicals etc.

TURKISH BUSINESSES SHOULD TAKE SERIOUS STEPS TO ENTER/ACCESS U.S. MARKET

As outlined in the report, Turkish exports face significant market-based challenges to gain share in the American market, including stiff competition, large scale and low profit margins, and logistical disadvantages. In order to overcome those challenges, Turkish companies and business associations can build joint logistics and business information centers in major U.S. ports and cities. These joint endeavors can best be operationalized by the Turkish Exporters Associations. Secondly, Turkish companies in sectors having potential in the U.S. market, such as electronics or medical services, should invest in creative marketing and branding. These investments can be done jointly or individually. Thirdly, companies seeking access to the U.S. market need to invest in "adding value" to products with potential. It is especially essential to enhance the quality of the products and adjust their size, taste, and models to respond to U.S. consumers with investments in R&D, market analysis, marketing, and branding.

USE TURKEY AND THE U.S. AS A BRIDGE TO ACCESS THIRD MARKETS ESPECIALLY THROUGH JOINT VENTURES

In their marketing strategies, American and Turkish companies should consider each other as hubs to export and invest in other markets in Europe, the Middle East and North Africa, the Caucasus and Central Asia, and Latin America. For instance, Turkish and American companies should work together through joint ventures in sectors such as construction, energy and health services to supply products to those regions. Construction and energy supply needs in Turkey and the Middle East can be provided by Turkish-American JVs. Companies could also consider building a healthcare zone in Turkey in which JVs would produce medical equipment, offering a convenient logistical route to Middle Eastern markets. Exports and investment promotion agencies can encourage their companies to work with Turkish/American companies to operate in third markets through Ex-Im Bank and OPIC programs supporting joint ventures in specific markets. The two governments should also consider the establishment of joint industrial zones between the United States, Turkey and Iraq by providing incentives to companies in selected sectors.

UTILIZE LUCRATIVE OPPORTUNITIES IN TURKEY TO ENHANCE EXPORTS/ INVESTMENTS IN KEY SECTORS

As discussed in the report, if U.S. exports and investments targeting Turkish markets can be channeled to certain non-traditional sectors and products, this would help building stronger economic ties through supply channels. Taking into account of the economic transformation of the Turkish economy from a labor-intensive supplier to a capital- and research-intensive supplier, U.S. companies should focus on exploiting exports, imports, and investment opportunities in a number of products and sectors, including services and farming, discussed in this report. U.S. companies should also develop investment strategies to benefit from lucrative opportunities in the ongoing privatization program and new incentives regime.

BUSINESSES AND GOVERNMENTS SHOULD ENHANCE DIALOGUE AND CONSULTATIONS TO DEVELOP A COMMON POSITION ON A SET OF (POTENTIAL) ISSUES ON THE G20 AGENDA

Although Turkey has not become an "agenda-setter" within the G20, it plays a constructive, bridge-builder role which is crucial for the United States to strike deals on certain politically contentious issues. Turkey might play a more proactive role in the G20 as the agenda expands from the financial domain to issues with further political implications, depending upon a better organized inter-agency process, larger participation from different economic sectors, and the strengthening of domestic constituencies. The U.S. and Turkish business dialogue should be expanded to cover specific G20 issues in the near future. U.S. business actors with stakes in the G20 agenda should work with their counterparts to create stronger domestic pressures for more active Turkish participation at the G20. The two countries should enhance dialogue to build collective positions on issues in which both countries have a stake, including the G20's role and support for the eurozone crisis, the G20's growth and rebalancing agenda, exchange rate stability, fighting protectionism, and expanding the trade agenda of the G20 to post-Doha issues. Such cooperation on global economic issues should in turn have a positive effect on the U.S.-Turkish bilateral commercial relationship.

BOTH GOVERNMENTS SHOULD ENCOURAGE OPPORTUNITIES FOR BUSINESSES TO DEVELOP NEW AVENUES TO RAISE ISSUES OF MUTUAL CONCERN

There is a need for increased consultations which would allow business representatives to meet with high-level government figures to discuss issues, challenges, and suggestions. In addition to broad-based discussions, governments and business associations could also organize sectoral meetings geared to representatives of relevant agencies and companies. For instance, a consultation mechanism could be developed to discuss problems of the pharmaceutical sector among representatives of the Turkish Ministries of Health and Economy and U.S. and Turkish pharmaceutical industry representatives.

APPENDIX

Table 1. Turkey-U.S. Trade (in thousands of dollars)

YEAR	IMPORTS-CIF	% CHANGE IN IMPORTS	EXPORTS-FOB	% CHANGE IN EXPORTS	VOLUME	BALANCE
2000	3.911.022	27,0	3.135.163	28,7	7.046.185	-775.86
2001	3.261.298	-16,6	3.125.771	-0,3	6.387.069	-135.527
2002	3.099.099	-5,0	3.356.126	7,4	6.455.225	257.026
2003	3.495.770	12,8	3.751.552	11,8	7.247.322	255.781
2004	4.745.195	35,7	4.860.041	29,5	9.605.235	114.846
2005	5.375.548	13,3	4.910.715	1,0	10.286.263	-464.832
2006	6.260.873	16,5	5.060.854	3,1	11.321.727	-1.200.019
2007	8.166.068	30,4	4.170.688	-17,6	12.336.756	-3.995.380
2008	11.975.929	46,7	4.299.941	3,1	16.275.870	-7.675.988
2009	8.575.737	-28,4	3.222.821	-25,0	11.798.558	-5.352.916
2010	12.318.394	43,6	3.769.260	17,0	16.087.654	-8.549.134

Source: Ministry of Economy, Turkey

APPENDIX

Table 2: Turkey's Exports and Imports of Commercial Services in Years and Categories

Flow	Indicator	Partner	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Exports (million usd)	Commercial services (excluding government services)	World	15084	13979	17909	22665	26439	25246	28586	34396	32626	32750
	Transportation	World	2854	2795	2184	3261	4917	4962	6532	7761	7549	8264
	Travel	World	8090	8479	13203	15860	18145	16838	18462	21862	21165	20723
	Other commercial services (travel and transport)	World	4140	2705	2522	3545	3377	3447	3591	4773	3913	3762
Imports (million usd)	Commercial services (excluding government services)	World	5633	5528	6690	9171	10307	10729	14528	16569	15544	18210
	Transportation	World	2021	1934	2707	4323	4859	4597	6896	7895	6519	8278
	Travel	World	1738	1880	2113	2519	2871	2741	3256	3492	4130	4807
	Other commercial services (travel and transport)	World	1874	1714	1870	2329	2577	3392	4376	5183	4895	5125

Source: OECD

Table 3: Turkish Export Growth

			2000 - 2008 Compounded Annual Growth Rate (CAGR)		
Product Line	**Total Turkish Exports 2008 ($ Billion)**	**Turkey - US Exports 2008 ($ Million)**	**Total Turkish Exports**	**Total Turkish Exports to US**	**Total US Imports**
Ships	2.6	46.6	47	37.8	4.5
Petrol & Gas	7.4	422.5	47.9	29.6	17.6
Automotive	18	78.7	36.2	18.4	2.1
Iron & Steel	16.8	757.8	31.7	16.7	13
Cement/Construction Materials	2.1	319.8	24.3	15.2	6
Fruits & Vegetables	5.3	181.7	14.3	12.5	9.5
Machinery	8.6	480.1	27.2	12.4	6.5
Manufactured Metal Goods	4.8	124.6	28.9	11.7	8
Electronics	7.4	52	25.2	10.3	0.5
Other	32.1	822.9		3.3	6.7
Television/Telephone	2.2	9.4	11.3	-1	8.3
Jewelry	1.7	191.8	19.9	-1.7	5.1
Textiles & Apparel	23	812.1	10.6	-7.4	3

Source: Turkish Statistical Institute

APPENDIX

Table: U.S. Exports and Imports of Commercial Services in Years and Categories

Flow	Indicator	Partner	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Exports (million USD)	Commercial services (excluding government services)	World	262494	269397	278866	322723	352557	393405	462529	510474	475979	421004
	Transportation	World	42202	42431	42002	48346	52674	57538	65961	75118	61829	70610
	Travel	World	88778	84753	83317	94108	102069	106905	119586	134970	121130	13479
	Other commercial services (excluding travel and transport)	World	131514	142213	153547	180269	197814	228962	276982	300386	293020	336915
Imports (million USD)	Commercial services (excluding government services)	World	200275	205677	217815	252266	270629	305000	334624	365013	334310	366822
	Transportation	World	57112	54655	61163	72470	78624	80967	81950	86265	67566	78079
	Travel	World	62977	61890	61103	70047	73830	77534	82118	86080	80102	82653
	Other commercial services (excluding travel and transport)	World	80186	89132	95549	109749	118175	146499	170556	192668	186642	206090

Source: OECD Stats (2001 through 2009), United Nations Service Trade Statistics Database (2010)

Table 4: OECD FDI RR INDEX 2010 *updated 12 September 2011*

PART 1

		TURKEY Total by sector	UNITED STATES Total by sector
Agriculture and forestry		0.000	0.000
	Agriculture	0.000	0.000
	Forestry	0.000	0.000
Fishing		0.000	0.625
Mining (including oil extraction)		0.050	0.100
Manufacturing		0.000	0.000
	Food and other	0.000	0.000
	Oil refining and chemicals	0.000	0.000
	Metals, machinery and other minerals	0.000	0.000
	Electrical, electronics and other instruments	0.000	0.000
	Transport equipment	0.000	0.000
Electricity		0.000	0.197
	Electricity generation	0.000	0.393
	Electricity distribution	0.000	0.000
Construction		0.000	0.000
Distribution		0.000	0.000
	Wholesale	0.000	0.000
	Retail	0.000	0.000

Source: OECD

Note: 1.000 is fully closed, 0.000 is fully open.

The FDI Regulatory Restrictiveness Index (FDI Index) measures statutory restrictions on foreign direct investment in 49 countries, including all OECD and G20 countries, and covers 22 sectors.

APPENDIX

Table 4: OECD FDI RR INDEX 2010 *updated 12 September 2011*

PART 2

		TURKEY Total by sector	UNITED STATES Total by sector
Transport		0.383	0.550
	Surface	0.000	0.000
	Maritime	0.575	1.000
	Air	0.575	0.650
Hotels and restaurants		0.000	0.000
Media		0.250	0.250
	Radio and TV broadcasting	0.500	0.500
	Other media	0.000	0.000
Communications		0.000	0.110
	Fixed telecoms	0.000	0.020
	Mobile telecoms	0.000	0.200
Financial services		0.000	0.042
	Banking	0.000	0.100
	Insurance	0.000	0.000
	Other finance	0.000	0.025
Business services		0.125	0.000
	Legal	0.000	0.000
	Accounting and audit	0.500	0.000
	Architectural	0.000	0.000
	Engineering	0.000	0.000
Real estate investment		1.000	0.000
Total FDI Index		0.082	0.089

Source: OECD

Note: 1.000 is fully closed, 0.000 is fully open.

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