

# Evaluation of the EU-Turkey Customs Union



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# Motivation

- ▶ **The EU–Turkey Customs Union was pioneering and unique**
  - EU’s first substantial CU with a non–member
  - Early attempt by the EU to share its legal system with a non–member
  - Turkey is one of just 3 countries to enter into a CU with the EU before becoming a candidate country
- ▶ **CU has been a major instrument of integration for Turkey**
  - Significant trade liberalization & harmonization with the *acquis*
  - More than fourfold increase in bilateral trade since 1996
  - Deeply integrated production networks
  - EU accounts for over three–quarters of FDI inflows to Turkey
- ▶ **Changing global economy is exposing design flaws: more integration is needed**
  - Rise of emerging markets
  - Changing trading relationships makes FTAs a policy priority for both parties

# Objectives of the evaluation

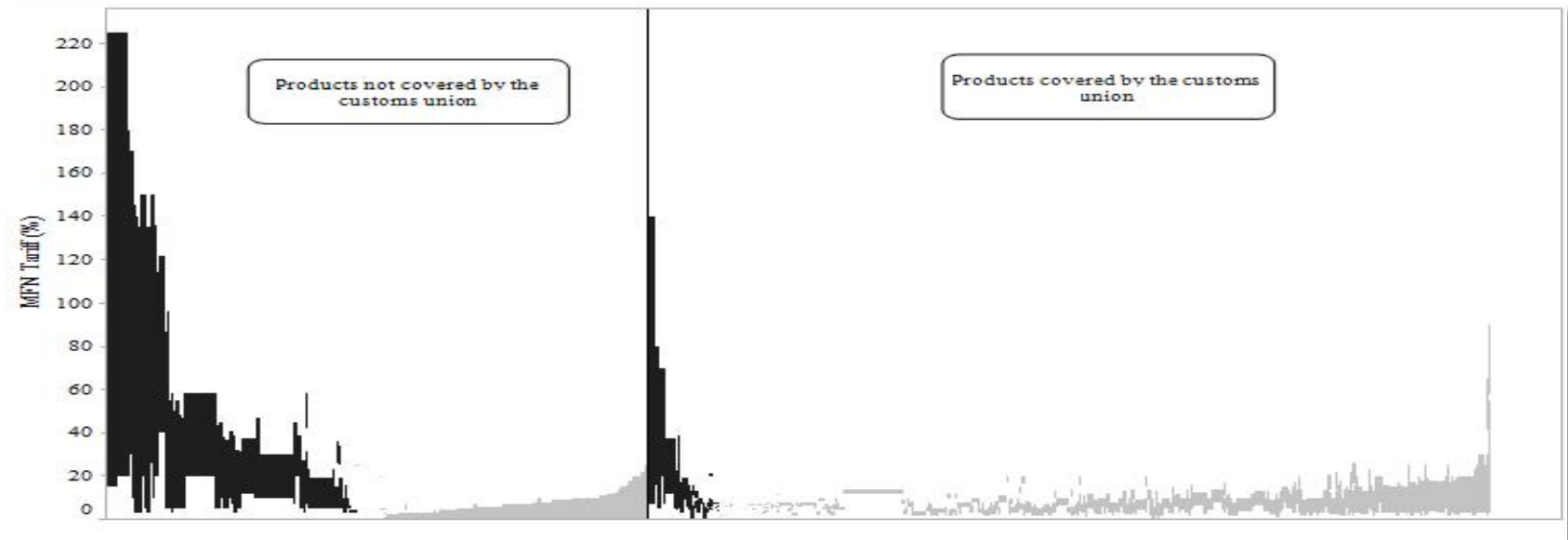
- 1) To assess the economic impacts of the CU
- 2) To make forward-looking, solution-orientated policy recommendations to improve the EU-Turkey trade relationship



## Key finding 1

# The CU has brought greater benefits than an FTA

- ▶ The common external tariff has anchored Turkey's import tariffs



\* *Dark bars show an increase in MFN tariff over 1993–2009 while light bars show a decrease.*

- ▶ Costly rules of origin are not needed
- ▶ Turkey's exports to EU 7% higher under a CU than an FTA
- ▶ EU exports to Turkey are 4% higher
- ▶ Most affected sectors: motor vehicles, televisions, clothing

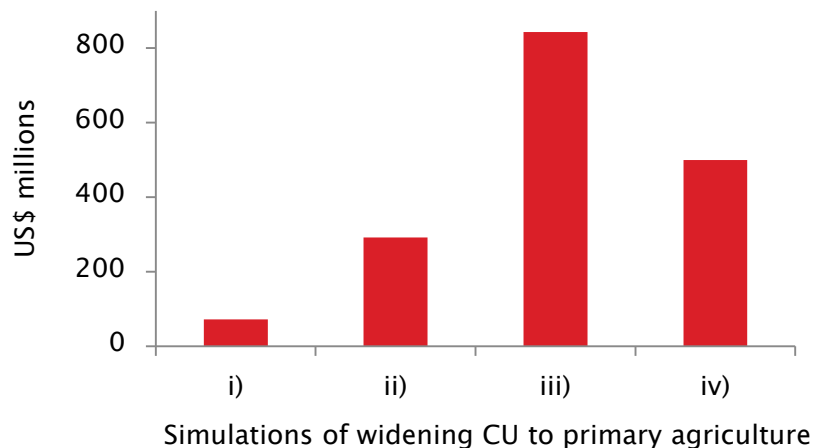
## *Key finding 2*

# Widening the agreement to primary agriculture would bring benefits to both parties

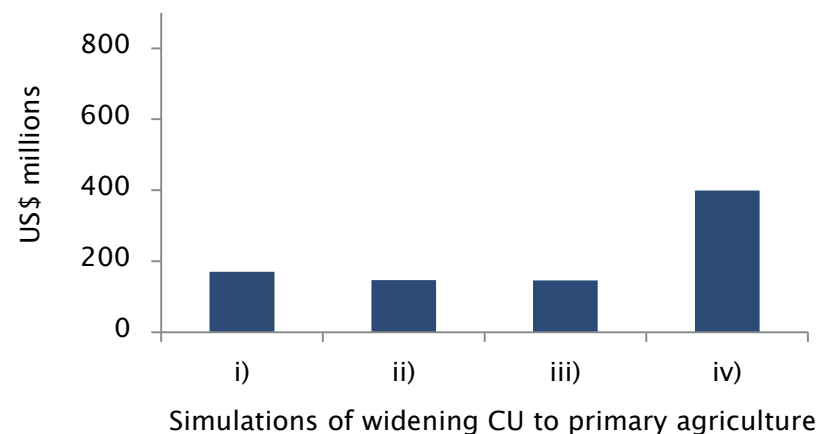
- Adopting the CET significantly decreases Turkey's import protection
  - ⇒ Lower prices for consumers but also lower farm employment in Turkey
- EU–Med countries face increased competition from oils and tomatoes
- EU animal product exports to Turkey increase
- Assumes Turkey can meet EU rules on food safety
  - ⇒ €2 billion required to modernize firms in dairy, meat, livestock & fish

# Simulated effects of deepening the EU–Turkey trade agreement in primary agriculture

a) Change in Turkish real income



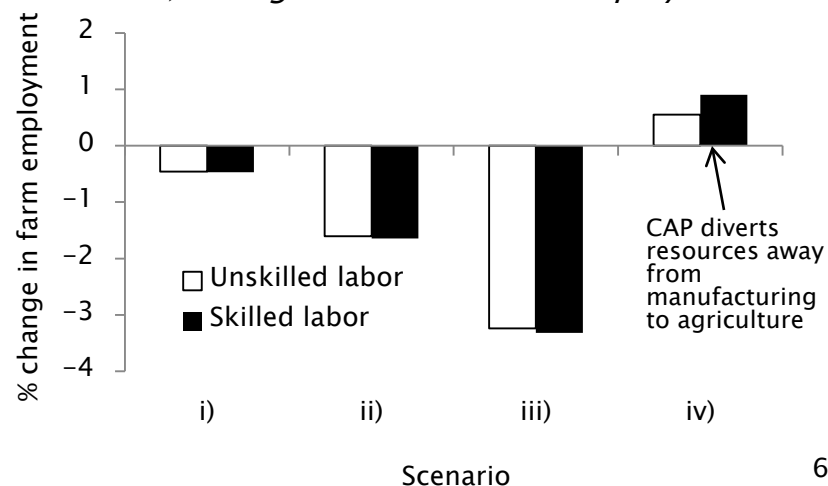
b) Change in EU real income



## 4 scenarios:

- i. EU–Turkey FTA in agriculture
- ii. FTA + EU’s common external tariff
- iii. CU in agriculture (common commercial policy)
- iv. Turkish adoption of the CAP

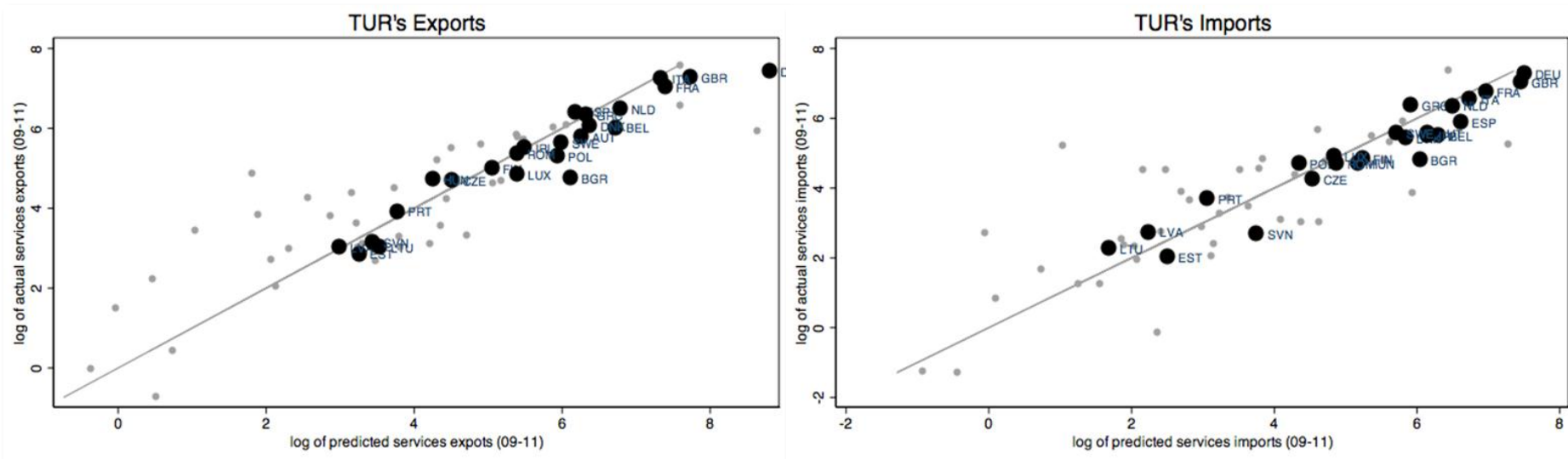
c) Change in Turkish farm employment



# Key finding 3

## Including services would boost trade

Gravity model of Turkey's services trade with the EU, 2009–11



- ▶ Model estimates suggest static gains of US\$1.1 billion for Turkey opening cross-border services trade
- ▶ Main differences in regulatory regimes are retail; transportation (EU more restrictive) & professional services; rail (Turkey more restrictive)

## *Key finding 4*

# Legal environment for public procurement in Turkey is open but implementation issues

- ▶ PP in Turkey accounts for 7% of GDP
- ▶ Since 2003, PP Law has been developed to align with the *acquis* in context of accession negotiations
- ▶ However some limits to foreign competition / potential EU contractors remain:
  - While most tenders are open, exclusions & exemptions are used (0.5% of GDP)
  - Foreign competition is also limited as a result of domestic price preferences
  - PP threshold is twice that of the EU



## *Key finding 5*

# Correct asymmetries to maximize gains

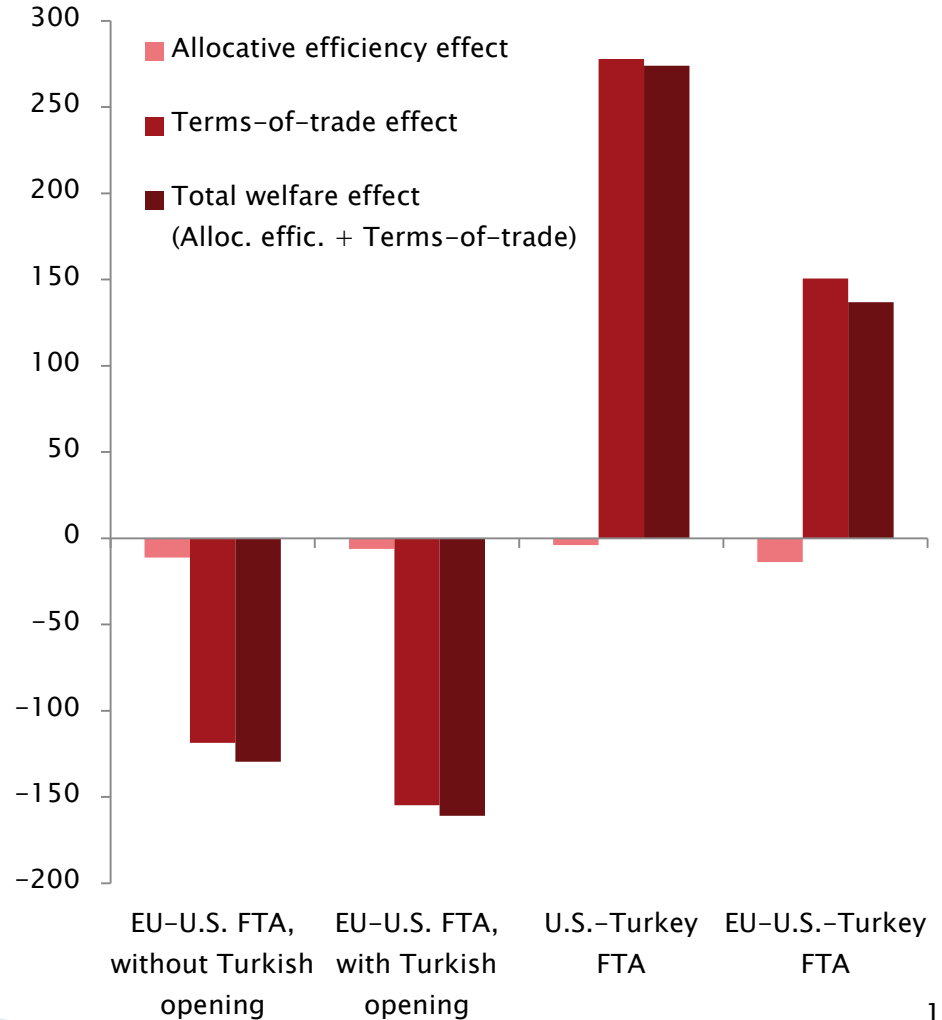
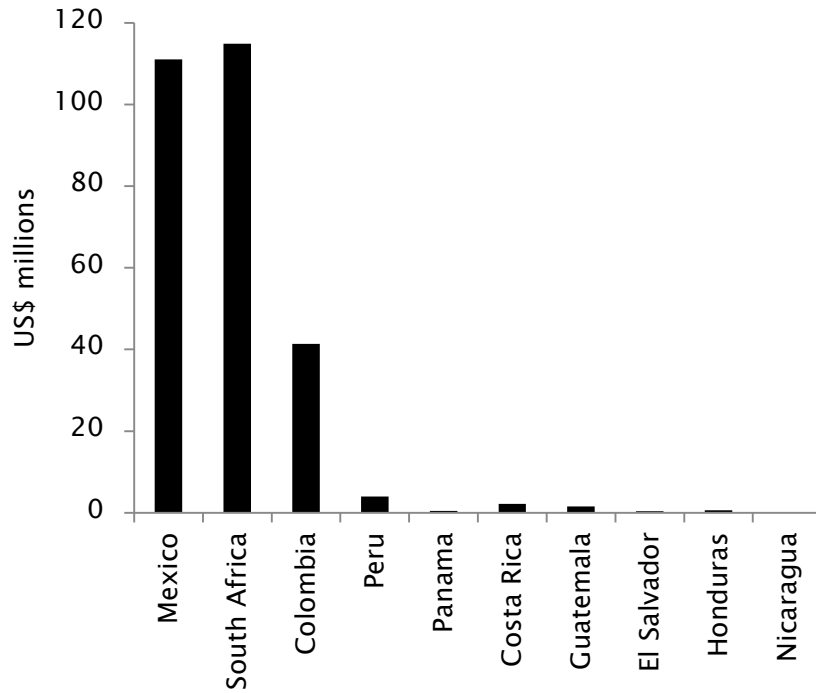
- ▶ Turkey has obligation to align with EU legislation but cannot participate in decision making in areas related to CU
- ▶ Provisions on institutional cooperation & decision shaping have not been properly implemented: increases risk of non-compliance
- ▶ First best solution would be to move forward with accession negotiations
- ▶ In the meantime improve information/consultation sharing mechanisms to reduce impact of asymmetries
  - E.g. establish 'Friends of Turkey' working groups; greater representation on comitology committees

## *Key finding 6*

### Formalize parallel negotiations for FTAs

- ▶ Some EU FTAs have not been concluded with Turkey (e.g. Algeria, RSA, Mexico)
- ▶ EU FTAs with US etc. risk larger potential losses for Turkey
  - Limits Turkish market access
  - Erodes Turkish preferences in the EU market
  - Creates trade deflection (that could necessitate ROOs)
- ▶ Parallel track negotiations mirroring the main EU negotiations that start & conclude at the same time could resolve the problem
- ▶ But Turkey must also be ready to negotiate to a standard of comprehensiveness e.g. services, agriculture, regulations

# Welfare effects of finalizing non-compliant FTAs for Turkey



## *Key finding 7*

# Formal mechanism needed to ensure transparency in Turkey's transposition of the *acquis*

- ▶ With some exceptions, Turkey has aligned to the *acquis* in areas covered by the CU
  - As of 2010, 85% according to the Turkish Ministry of EU Affairs
  - However the Commission has not been able to verify the transposition
- ▶ Important since exported products to the EU are assumed to comply with all technical regulations if the *acquis* has been adopted
- ▶ Lack of harmonization in select Old Approach directives & risks from continued harmonization
- ▶ Process of transposition is also outdated: last list issued in 1997
- ▶ Formal mechanism needed to keep track of stock of EU legislation & status of transposition to reduce the 'notification deficit'

## *Key finding 8*

# Implement functioning dispute settlement mechanism

- ▶ Existing DSM limited to disagreements on duration of safeguards
- ▶ Improved DSM would rebalance market access obligations and resolve various trade irritants
- ▶ A DSM where one party can bring a case on a broader range of disputes would be more effective
- ▶ To facilitate implementation, simultaneously reduce asymmetries in decision making

## *Key finding 9*

# Reduce trade costs for continued growth in trade

- ▶ Road transport permits—especially for transit—should be liberalized at least for goods covered by the CU
  - Commission could receive a mandate to negotiate: i) transport services; or ii) road transit agreement (Hungary and Romania); or iii) road transport agreement (Switzerland)
  - Transport Policy Chapter of the *acquis* could be opened
- ▶ Establish a “Green Lane” for pre-qualified business people traveling to the EU on business to obtain long-term, multiple entry visas with simplified documentary requirements
- ▶ Enhance dialogue before Trade Defense Instrument investigations are launched on EU–Turkey trade e.g. Early Warning System

# Summary

- ▶ CU has unfulfilled potential
- ▶ Widening preferential trade to primary agriculture and services would bring important gains to both parties
- ▶ Other recommendations can be taken up one-by-one or as a package:
  - Reducing asymmetries in the decision making process
  - Formalizing parallel negotiations for FTAs
  - Green lane for visas for pre-qualified Turkish professionals
  - Liberalizing road transport permits on trade covered by the CU
  - Better coordinating before TDI investigations launched
  - Strengthening dispute settlement
  - Increasing transparency in Turkey's transposition of the *acquis*