

OPINION



The start of EU-Turkey membership negotiations in 2005 was seen as one of the most important achievements of the AKP government [Reuters]

THE AKP DECADE AN ECONOMIC SUCCESS STORY?

Turkey's ruling party came to power more than 10 years ago, and has since secured some significant economic victories. But the country still needs a few radical reforms to deal with its growing challenges.





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More than a decade ago, Turkey’s November 2002 elections saw the Justice and Development Party (AKP) rise to power. It won 35 percent of the vote, but as only two parties (the AKP and the Republican People’s Party) were able to beat the very high electoral threshold of 10 percent, the AKP won the majority of seats in parliament. In the two elections that followed - in July 2007 and June 2011 - the AKP consolidated its one-party government through sizable increases in its electorate, reaching 50 percent of the vote in the last polls.



How was this quite singular political success in the history of democracy made possible? Various factors, economic as well as political, played a part. For example, the complete defeat of the traditional centre-right in November 2002 - which was held responsible for the mess of the 1990s - three economic crises accompanied by political instability, as well as liberals supporting the AKP in its fight against military tutelage, certainly played some role in this success. However, the decisive factor of the success has been economic performance.



The AKP came to power while Turkey was struggling to exit its worst-ever economic crisis. In 2001, the International Monetary Fund (IMF) Stand-By Arrangement, based on exchange rate targeting, was malfunctioning; the Turkish lira was depreciated by 100 percent; inflation reached triple digits; half the banks failed and, finally, gross domestic product (GDP) contracted by more than five percent. The three-party coalition was literally failing, and Kemal Dervis, the World Bank vice president, was nominated for the post of economic minister. He took charge of the realisation of radical economic reforms, with the support of the Turkish economic bureaucracy and IMF staff. In the second half of 2001, a new stand-by agreement was signed with the IMF, implementing a new economic regime based on floating exchange rates, an independent central bank, restructuring of the banking system and a severe fiscal discipline programme requiring a primary surplus (budgetary balance without interest payments) at 6.5 percent of the GDP.





The critical choice to be made by the newly elected AKP government was whether or not to continue with the IMF programme. It chose to continue, and succeeded in applying strict budgetary discipline to an extent that had not been seen since the 1970s. The primary surplus targets were almost achieved until the international economic crisis began in 2008. Nowadays, abusive austerity programmes in Europe are blamed for worsening an already severe recession. But this was not the case in Turkey. Fiscal discipline did not turn into austerity since public expenditures were not obliged to be cut. High primary surpluses have been achieved thanks to increasing tax revenues originating from high growth and improvements in tax collection. Indeed, fiscal discipline slowly but surely increased the confidence among economic actors. Inflation fell below 10 percent in 2006, as did real interest rates that were evolving above 20 percent. A real consumption and investment boom followed, pushing GDP growth to a six or seven percent level. And this high growth allowed increases in tax revenues. Needless to say that the per capita income increased significantly - in dollar terms, it almost doubled, which amounts to more than 50 percent in real terms.

However, we have to note that the domestic-led growth, accompanied by an appreciation of the Turkish lira, increased the current account deficit (CAD). But the deficit was easily financed by the abundance of international liquidity, as well as by a booming foreign direct investment following the start of the EU-Turkey membership negotiations in October 2005 - one of the most important achievements of the AKP government. So it was not surprising that the AKP increased its voter support in July 2007 up to 46 percent, thus consolidating its power.

Economic recovery

When the global financial crisis struck, Turkey's GDP growth was already decelerating due to domestic demand being out of breath (since it increased too rapidly during the preceding years). The Turkish economy went into a recession in the last quarter of 2008 following the international financial crisis. The recession lasted a year, causing a rather strong contraction of the Turkish economy and taking the unemployment rate up from 10 percent to 14 percent. Nevertheless, the recovery has been rapid and muscular. During 2010 and 2011 the GDP grew by more than nine and eight percent respectively, making Turkey the second best growth performer in the world, after China. This high growth allowed unemployment to decrease to its pre-crisis level. The AKP's success in the elections of June 2011 can thus be easily explained.




However, this high growth episode attained its limits rather quickly since it was exclusively based on domestic demand. By 2011, the current account deficit reached its historical peak at 10 percent, breaking a world record. Admittedly this was not a sustainable situation, given the fact that the Turkish lira was appreciating dangerously under the pressure of excess capital inflows. A sudden stop of capital inflows, that would cause an exchange rate shock, could have occurred at any moment. The Turkish economy truck was going full speed, heading towards a wall, and something had to be done. So, CBRT and the AKP government have decided on a cooling down operation called “rebalancing of the economy”.

‘Rebalancing’

The year 2012 was a year of “rebalancing”, or of correcting the country’s macroeconomic imbalances. CBRT’s task was not easy since there were multiple goals to achieve, like cooling loan expansion, depreciating the lira without losing control of inflation expectations, and switching growth from a domestic demand-led growth to an export-led growth to narrow the huge CAD. The central bank was obliged to develop a new monetary framework with new tools.

Central bank policies worked quite well. Domestic demand has come under control - maybe too much so - and growth has been based on net exports, with exports increasing more than imports. As predicted, the CAD began its decline along with the growth regime switch. The CAD ratio to GDP declined down to six percent from its peak of 10 percent. So far so good, but the cooling of domestic demand has been revealed to be rather excessive since it stagnated in 2012. The growth, based exclusively on net exports, declined to 2.2 percent. The government was expecting at least four percent that was targeted in the Medium Term Programme. This was insufficient growth for the fight against unemployment, and there were signs that the unemployment rate was rising.





From a social perspective, Turkey
has seen a decrease in income
inequality and in poverty

[Huseyin Narin/Al Jazeera]



Social changes

The macroeconomic performance of AKP rule during the last decade has certainly been successful despite the persistence of some unfixed structural problems, like low domestic savings and a lack of competitiveness. But from a social perspective, according to the Income and Living Conditions Surveys (SILC) of TurkStat published since 2006 and covering the period of 2005-2010 (the last available data), a decrease in income inequality as well as in poverty has been achieved.

Looking at two most popular measures of inequality, the Gini Coefficient (GC) and Relative Poverty Head Count Ratio (RP), it shows that between 2005 and 2010, GC decreased roughly from 43 percent to 40 percent, and the PR from 25 percent to 23 percent. Admittedly, those are modest improvements and income inequality still stands at high levels compared to European economies. However, it should be underlined that this decrease in income inequality has been realised parallel to a significant increase in the real income per capita. This means that welfare improvement has been stronger in the lower segments of society than in the upper segments. A direct measure of poverty, namely the state of material deprivation in Turkish society, also proves this welfare improvement. In a recent study (to be published in July) the Bahcesehir University Centre for Economic and Social Research (Betam), using the SILC data, computed the poverty rates according to three basic needs: the inability to eat meat, chicken or fish on every second day; the inability to properly warm one's home; and the inability to replace used clothes with new ones. The share of households unable to satisfy all those three needs was 25 percent in 2006, but declined to 19 percent in 2010.





The Turkish economy needs
balanced growth with more exports
and less imports [Huseyin Narin/Al Jazeera]



There have also been significant improvements in the supply of public services which are not considered in the computation of income inequality and poverty based on disposable income. For example, the share of education in the budget increased from 10 percent in 2002 to 15 percent in 2011, and the share of health expenditures went from 2.6 percent to 5.8 percent. Since, in the meantime, Turkish GDP increased in real terms by more than 50 percent, it should be underlined that the increase of education and health expenditures in real terms was well higher than the increase in shares.

Turkey's challenge

Undoubtedly the AKP decade has been globally positive for Turkey. Political stability has been secured, the economy became stronger and social welfare improved significantly. AKP rulers claim that Turkey emerged as a regional power during this decade. This claim is not yet fully confirmed since many political and economic problems remain unsolved. The main political challenge is deepening and stabilising the democratic regime. This requires a new constitution based on a consensus, and on solving the Kurdish issue by democratic means. Needless to say that these two issues are closely linked, one to the other. But at the moment, drafting a new constitution supported by a large consensus seems very difficult, if not impossible, and the peace process with the Kurdish PKK is underway, but success will depend on the implementation of radical democratic reforms.





So, the question becomes: What to do? The recipe is not very complicated but it is very difficult to implement. Radical reforms in the labour market, in the fiscal system, in various product markets and in all stages of education are needed in order to accelerate productivity increases, to cut production costs and to encourage domestic savings. At the same time, the state should spend more on research and development, more on education and more on infrastructure, without jeopardising the fiscal discipline.



At the moment, there is no willingness for those reforms in the AKP government. The party is more focused on establishing a presidential system that would make Prime Minister Recep Tayyip Erdogan a powerful president in the next decade than on a reform agenda. One can say that all urgent reforms are considered from the prism of this presidential ambition and from its eventual effects on the AKP's vote support in the coming elections (local elections will be held in March 2014, and Turkey will elect a president of the Republic by popular vote for the first time in July 2014).

But if political and economic reforms are not implemented, what will happen? It is a critical question. And most likely, Turkey would simply be trapped in a low growth regime under which the AKP will be faced with increasing problems, and a coming decade that will be even more challenging than the previous one.

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