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Modernisation of the EU–Turkey Customs Union

The German Debate on Modernisation of the Customs Union Considering Economic Interests, Prospects of Cooperation and Political Obstacles

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The project

The future of the EU's Customs Union with Turkey

Still a candidate for membership in the European Union, Turkey has outgrown the status of one-sided dependency on the EU. Ankara developed a more independent foreign policy that entails both areas for cooperation with Brussels but also for conflicts with the EU and its member states. Cases in point are the cooperation on migration on the one hand side and tensions with Greece and Cyprus in the eastern Mediterranean on the other. The EU needs working channels for communication and cooperation with Turkey. However, membership negotiations stall, talk on visa liberalization stuck, and the European Council blocks the opening of talks to re-negotiate the Customs Union.

To look for ways to overcome the deadlock, CATS and think tanks from five EU member-states are looking into the respective nation debates on the economic and political pros and cons of re-negotiating the Customs Union. We find an overall interest in the deepening of economic cooperation and a variety of political issues to be addressed once working relations with Turkey are established.

This report is part of this joint endeavour in which the Centre for Applied Turkey Studies (CATS) cooperates with Institut français des relations internationales (IFRI), Paris; Elcano Royal Institute (Elcano), Madrid; The Polish Institute of International Affairs (PISM), Warsaw; Istituto Affari Internazionali (IAI), Rome and Hellenic Foundation for European and Foreign Policy (ELIAMEP), Athens.

Modernizing and deepening the EU-Turkey Customs would be mutually beneficial for Germany and Turkey

However, due to political differences no progress has been made in this issue since 2014. For Turkey, the most important region in terms of trade is still Europe. More than half of all Turkish exports by value are delivered to European countries, while only a quarter are sold to Asian countries. The importance of other regions such as Asia-Pacific and North Africa is on the increase. However, the trade with Russia and China e.g. is highly asymmetrical at the expense of Turkey and Turkish exports to these countries seem not to be expandable in the short and medium term. This illustrates the importance of the European market for Turkish industry. Current economic slowdown in Turkey may enhance Berlin's and Brussels' leverage on Ankara to advance the issue.

Therefore, it is essential to rationalise and de-emotionalise the German debate on the EU-Turkey Customs Union and to align the German debate to the discussion on the matter in other EU member states.

Introduction

Turkey is still officially a candidate for full membership in the European Union (EU), although the negotiations between Ankara and Brussels have been in a deadlock since 2016. As of 1995 Turkey is, via the Customs Union (CU), a part of the European economy and European as well as German value chains. After 25 years, both sides today recognise that the EU–Turkey CU requires updating to rectify design deficiencies that undermine the operational effectiveness of the bilateral trade agreement. Turkey demands a stronger voice in EU trade policy formulation and wants to be involved in future EU free trade agreements.¹

Turkey is not permitted to have a seat and say at the free trade negotiations of the EU with third countries because it is not a member state of the EU. Third countries with which the EU concludes free trade agreements sometimes refuse to conclude the agreement with Turkey. Consequently, Turkish firms do not receive automatic reciprocal access to the markets of those countries, while imports from them can enter Turkey duty-free by way of the trade deflection via the EU.²

Besides involvement in free trade negotiations of the EU with third countries, Ankara is also looking for deepening of the agreement and extending the scope of the CU to services and unmanufactured agricultural goods. Turkey further demands the simplification of the procedures for Turkish export goods as well as transportation conditions for Turkish vehicles transiting between EU states. A 2014 World Bank report also shows that “road transport permits should be liberalized at least for those goods covered by the CU”.³

On the European side, the *European Commission* has proposed updating the trade agreement, expanding the scope of the EU–Turkey-CU to the service sector, and rights of establishment, public procurement and agriculture.⁴ However, Turkey’s bilateral political disputes⁵ with individual EU member states – such as Germany, Austria, the Netherlands, Greece, Cyprus, Belgium et al. – as well as domestic developments such as growing authoritarianism,⁶ the undermining of democracy, the rule of law, and the separation of

¹ For Turkey’s concerns regarding the CU see Türkiye Cumhuriyeti Ticaret Bakanlığı (Republic of Turkey Ministry of Commerce), “Gümrük Birliği Neden Güncelleniyor?” [Why Is the Customs Union Updating?], 9.1.2019, <https://bit.ly/2BRBCgU>.

² World Bank, *Evaluation of the EU-Turkey Customs Union*, report no. 85830-TR (March 28, 2014), p. ii.

³ *Ibid.*, p. 85.

⁴ See European Commission, “Meeting of Heads of State or Government with Turkey – EU-Turkey Statement”, 29.11.2015, https://ec.europa.eu/commission/presscorner/detail/en/STATEMENT_15_6194; European Commission, “Commission proposes to Modernize the Customs Union with Turkey”, 2.12.2016, <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1609>.

⁵ See for example Celal Özcan, “Merkel Conveys Germany’s Veto on Customs Union Update with Turkey to Juncker”, *Hurriyet Daily News*, 31.8.2017, <https://www.hurriyetdailynews.com/merkel-conveys-germanys-veto-on-customs-union-update-with-turkey-to-juncker-117422>; *Deutsche Welle*, “Kein Ausbau der EU-Türkei-Zollunion”, 27.6.2018, <https://www.dw.com/de/kein-ausbau-der-eu-tuerkei-zollunion/a-44414110>.

⁶ Current *Transformation Index BTI* of German Bertelsmann Stiftung identifies Turkey as ‘among the countries that have fallen the most’ in terms of democracy: ‘As of January 2019, Turkey’s three major problems are the worsening economic situation, rising authoritarianism, and a deep polarization of society’. See *BTI 2020 Country Report Turkey*, <https://www.bti-project.org/content/en/downloads/reports/country-report-2020-TUR.pdf>.

powers especially as of 2016 after the coup attempt, have hindered the prospects for an update of the Customs Union. Additionally, there is resistance on the same grounds from the European Parliament.⁷

Among experts and decision-makers, the modernisation of the CU with Turkey has been and is still being discussed controversially. While some scholars and experts argue in favour of an upgrading of the EU–Turkey CU to keep Turkey close to Europe, others refuse the modernisation of the agreement because this would appease Turkish President Recep Tayyip Erdogan.⁸ Supporters mainly argue in terms of power politics and geostrategy, while opponents justify their position normatively.

In consideration of all these issues and controversies, some experts and decision-makers advocate an alternative, more gradual and open-ended strategy to move the process forward. Given the resistance of decision-makers, media and both left- and right-wing political parties, there is neither an elaborated concept nor a roadmap for negotiations over the modernisation of the CU.

How to deal with and how to overcome this deadlock constellation? To contribute to answering this question, a twofold analysis is required: analysis of economic relations between key EU member states and Turkey; as well as a review of the arguments, attitudes and positionings of decision-makers, economic and other relevant actors on the EU–Turkey CU and its modernisation.

Following this logic, this policy paper deals with Germany–Turkey economic relations and is divided into three parts. It begins with an analysis of the economic relations and interdependencies between Germany and Turkey. Then, the focus shifts to the German debate on modernisation of the EU–Turkey CU: primary lines of argumentation, attitudes and positioning of relevant actors and the media. The study concludes with implications for German decision-makers.

⁷ See European Parliament, 'Parliament Wants to Suspend EU Accession Negotiations with Turkey', Press release (13.3.2019), <https://www.europarl.europa.eu/news/en/press-room/20190307IPR30746/parliament-wants-to-suspend-eu-accession-negotiations-with-turkey>.

⁸ See for example Mehmet Uğur, 'Why EU Should Not Upgrade the Customs Union with Turkey', *Social Europe* (8.2.2018), <https://www.socialeurope.eu/eu-not-upgrade-customs-union-turkey>; Kadri Taştan, 'Customs Union an Anchor for Turkey–EU Relations', *The German Marshal Fund of the United States (On Turkey)*, August 2017.

Germany–Turkey Economic Relations

Economic relations between Germany and Turkey encompass areas including trade and commerce, foreign direct investments, commercial partnerships and tourism. The previous integration of Turkish industry into the European economy via the CU has led to a steady intensification of bilateral economic relations and interdependencies. Especially as of 2002, Turkish industry has increasingly been integrated into European and German value chains and production networks. High levels of trade and foreign direct investments are demonstrative of this. The EU is by far Turkey's most important trading partner and, conversely, Turkey is the EU's sixth largest trading partner.⁹

Bilateral Trade

Volume and key sectors

Both Turkey and Germany have export-oriented economies. In 2019 Turkey exported products worth 171.1 billion US dollars around the globe. That figure represents roughly 0.9 percent of overall global exports, which were estimated at 19.285 trillion US dollars in 2018. The most important region in terms of trade is still Europe, although the importance of other areas is growing. Fifty-six percent of Turkish exports by value are delivered to European countries, while 25.9 percent are sold to Asian countries. 9.3 percent of Turkey's exports go to Africa and 5.6 percent to North America. A much smaller percentage, 1.6 percent of Turkish exports, go to Latin America (excluding Mexico but including the Caribbean).¹⁰

From a continental perspective, Europe is the top destination for Turkish exports, and from a national perspective, Germany is the most important country for Turkish exports. Exports worth 15.4 billion US dollars were shipped to Germany in 2018, which represents 9 percent of total Turkish exports.¹¹ In terms of imports to Turkey, Germany ranks third among source countries.

From the side of Germany, Turkey ranks 18th among Germany's most important trading partners in exports and 16th in terms of imports. Exports to Turkey represent 1.5 percent of all German exports. For 2018, there was a positive trade balance of 5 billion US dollars in favour of Germany.¹²

⁹ Wirtschaftliche Dienste, 'Die Zollunion zwischen der EU und der Türkei', in *Dokumentation der Wissenschaftlichen Dienste des Deutschen Bundestages* (WD 5 – 3000 – 107/16), 2017.

¹⁰ Daniel Workman, 'Turkey's Top Trading Partners', in *World's Top Export*, 1.2.2019, <http://www.worldstopexports.com/turkeys-top-import-partners/>.

¹¹ Ibid.

¹² See *Trading Economics*, 'Germany Exports by Country', <https://de.tradingeconomics.com/germany/exports-by-country>.

Table 1: Turkey's top 10 trading partners (2018)

	Country	Export \$	%		Country	Imports, \$	%
1.	Germany	15.4 billion	9	1.	Russia	21.99 billion	11
2.	UK	10.9 billion	6.3	2.	China	20.72 billion	9.9
3.	Italy	9.3 billion	5.4	3.	Germany	20.41 billion	9.8
4.	Iraq	9 billion	5.2	4.	USA	12.38 billion	5.9
5.	USA	8 billion	4.7	5.	Italy	10.15 billion	4.9
6.	France	7.6 billion	4.5	6.	India	7.54 billion	3.6
7.	Spain	7.6 billion	4.5	7.	UK	7.45 billion	3.6
8.	Netherlands	5.4 billion	3.2	8.	France	7.41 billion	3.5
9.	Israel	4.4 billion	2.5	9.	Iran	6.93 billion	3.3
10.	Russia	3.9 billion	2.3	10.	South Korea	6.34 billion	3.0

Source: <http://www.worldstopexports.com/turkeys-top-import-partners/>

Source: <https://tradingeconomics.com/turkey/imports-by-country>

In contrast to trade with the EU and Europe – despite the trade deficit – trade with Russia and China has a very asymmetrical characteristic to the disadvantage of Turkey. While exports from Turkey to Russia in 2018 total 3.8 billion US dollars, conversely, Russian exports to Turkey total 22.3 billion. Turkey exports to China goods worth 2.9 billion US dollars; whereas Chinese exports to Turkey amount to 20.71 billion.¹³ Due to the economic structure of these countries, Turkish exports to Russia and China seem not to be significantly expandable in the short and medium term, which once again shows the importance of the European market.

In macroeconomic terms, Turkey's total exported goods represent 7.3 percent of its overall Gross Domestic Product in Purchasing Power Parity (PPP) for 2019, valued at 2.347 trillion US dollars. In 2014, Turkey's exports made up of 9.4 percent related to the overall GDP per PPP, while in 2018, the share of exports in the GDP in PPP declined to 7.3 percent. This indicates a relatively strong reliance on products sold on international markets for Turkey's total economic performance, which is comparable with Germany with its likewise strong reliance on international markets. It is interesting to note that Turkey also provided 48.8 billion US dollars worth of exports-related services to global customers for an additional 2.1 percent of GDP in PPP.¹⁴

The following export product groups represented the highest dollar value in Turkish global export during 2018. Table 2 below also shows the percentage share each export category represents in terms of overall global exports from Turkey. Turkey's top export products are vehicles (cars, trucks and other automobiles), machinery, iron/steel, clothing, electrical machinery, precious metals, etc.

¹³ See Website of Turkish Foreign Ministry, 'Türkiye-Çin Halk Cumhuriyeti Ekonomik İlişkileri', <http://www.mfa.gov.tr/turkiye-cin-halk-cumhuriyeti-ekonomik-iliskileri.tr.mfa>; Turkish Foreign Ministry, 'Rusya Federasyonu'nun Ekonomisi', <http://www.mfa.gov.tr/rusya-ekonomisi.tr.mfa>.

¹⁴ Daniel Workman, 'Turkey's Top 10 Exports', in *World's Top Exports*, 4.2.2020, <http://www.worldstopexports.com/turkeys-top-10-exports/>.

Table 2: Turkey's top 10 exports - product groups (2019)

	Product group	Value in \$	% of total exports
1.	Vehicles	26.2 billion	15.3
2.	Machinery including computers	16.5 billion	9.6
3.	Iron, steel	9.9 billion	5.8
4.	Knit or crochet clothing...	9.1 billion	5.3
5.	Electrical machinery, equipment	8.7 billion	5.1
6.	Gems, precious metals	7.3 billion	4.3
7.	Mineral fuels including oil	7.3 billion	4.3
8.	Articles of iron or steel	6.5 billion	3.8
9.	Clothing, accessories	6.5 billion	3.8
10.	Plastics, plastic articles	6.3 billion	3.8

Source: <http://www.worldstopexports.com/turkeys-top-10-exports/>

The following Table 3 displays top product groups exported from Turkey to Germany.

Table 3: Top product groups in Turkey's trade with Germany (2015, in 000 USD)

Product groups	Export	Import
Motor land vehicles and their parts	2,012,382	5,706,054
Machinery, broilers, mechanical equipment	2,084,352	4,540,674
Iron, steel and copper, and their products	1,084,841	1,317,706
Knitwear apparel and accessories	1,887,251	12,158
Electrical machinery and tools	898,692	1,644,564
Plastic and rubber products	782,289	1,663,138
Unwoven clothing and accessories	798,854	17,078
Vegetable and fruit products	686,825	19,299
Vegetable and fruits	528,335	16,059
Pharmaceuticals	48,446	794,253
Air and space craft and their parts	99,621	580,145
Total export and import with Germany	13,421,376	21,351,983
Total Turkish export and import	143,882,631	200,199,144

Source: Compiled from data provided by TÜİK; Kemal İnat, "Economic Relations between Turkey and Germany", *Insight Turkey* 18, no. 1 (2016): 21–34 (30).

The most important export goods from Turkey to Germany are: 1. textiles and clothing (25.5 percent of total exports to Germany), 2. motor vehicles and motor vehicle parts (17.3 percent), 3. machines (13.1 percent), 4. food (7.5 percent), 5. electro-technical (5.3 percent), 6. metal products (5.3 percent), 7. rubber products (3.2 percent), 8. chemical products (3.0 percent), non-ferrous metals (2.2 percent) and 10. furniture (2.1 percent).¹⁵ Going the other direction, the most important export goods from Germany to Turkey are: 1. machines (23.2 percent), 2. motor vehicles and motor vehicle parts (17.9 percent), 3. chemical products (17.4 percent), 4. electro-technical (6.9 percent), 5. measuring and control technology (4.3 percent), 6. metal products (3.3 percent) and 7. iron and steel (2.5 percent).¹⁶

¹⁵ GTAI – Germany Trade & Invest, "Türkei – Wirtschaftsdaten Kompakt", November 2019, p. 4.

¹⁶ *Ibid.*, p. 5.

Arms industry

Following the US arms embargo after Turkey's occupation of north Cyprus in 1974 and the embargo in the 1990s by European countries due to the armed conflict with the PKK, Turkey has made military-industrial independence to a top priority. The rapid growth of Turkey's arms industry and the ambitious developments of indigenous weapon systems are a consequence of this focus. Today, Turkey is the world's 18th arms exporting country. Turkish companies active in the arms industry are interested in cooperation with European and German companies due to their need for technology and know-how. Turkey was ranked in 2015 as 15th in global military spending, at 15,275 million US dollars. At the top of the list was the United States with spending of 596,024 million while China ranked second (214,787), Saudi Arabia (87,186) ranked third and Germany ranked ninth (39,393).¹⁷

In the 1990s, when waging a devastating war against the PKK in the south-east part of the country, Turkey was the world's largest arms importer (see Table 4 below). This included huge amounts of military equipment aided by NATO allies downsizing their own inventories. Tanks and armoured vehicles were imported from Germany, Italy and the US, as well as fighter aircraft from the Netherlands.

From 2001 to 2010 – internally a rather quiet period – Turkey received markedly fewer weapons from abroad and was only the ninth largest global arms importer. At this time, large purchases included a range of naval deals, such as four submarines (556 million USD), six minehunters (625 million USD) and six fast attack craft (FAC) from Germany, all of them partly assembled in Turkey.¹⁸

Table 4: Turkey as a leading arms importer (1991 -2015)

1991–2000		2001–2010		2011–2015	
Turkey	17,425	China	23,907	India	20,107
Taiwan	16,936	India	20,058	Saudi Arabia	9,932
Saudi Arabia	15,594	South Korea	11,050	China	6,680
Japan	14,791	Greece	10,073	UAE	6,552
South Korea	13,355	UAE	9,330	Australia	5,204
India	11,793	Pakistan	7,900	Turkey	4,926
China	10,815	Australia	7,759	Pakistan	4,723
Egypt	10,718	US	7,148	Vietnam	4,114
Greece	10,095	Turkey	6,311	US	4,109
Israel	7,399	Egypt	6,134	South Korea	3,761

Figures are SIPRI Trend Indicator Values (TIVs) expressed in USD million at constant (1990) prices. SIPRI Arms Transfers Database, generated 11 November 2016; for more information, see <http://www.sipri.org/databases/armstransfers/background>. Source: Quoted by Slijper (2017), p. 17.

Against the backdrop of the 'Arab Spring' and political instability in the region, especially the civil war in Syria, Turkey has stepped up its arms purchases in recent years, as reflected above for the 2011–2015 period, according to SIPRI (see Table 4 above). In 2011, Germany's ThyssenKrupp Marine Systems (TKMS) signed a EUR 2 billion contract to sell six Type-214 submarines being built in Turkey in the Gölcük Naval Shipyard. The delivery of these submarines was scheduled for 2019–2024.¹⁹ Table 5 below sums up Turkey's leading arms suppliers during the past decade. The United States is by far the largest, followed by Germany, which has mostly been the case since Turkey joined NATO in 1952. Other NATO allies, mainly Italy and the Netherlands,

¹⁷ Frank Slijper, *Power Projection. Turkey's Military Build-Up: Arms Transfers and an Emerging Military Industry* (Utrecht, 2017), p. 14.

¹⁸ *Ibid.*, p. 18.

¹⁹ *Ibid.*, p. 19.

have also been consistent suppliers over the years. However, trade relations with the NATO partners are under pressure, with Turkey diversifying its supplier base and developing military-industrial relations with for example South Korea, Israel and China.²⁰ In 2019, Turkey bought from Russia the S-400 anti-missile system and is further reconsidering also buying fighter jets from Russia.

Table 5: Turkish arms imports, top 10 suppliers and total imports (in million USD)

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	total
US	5	25	49	21	11	331	1,009	355	1,116	308	3,228
Germany	330	404	287	172	126	40	28	4	54	14	1,459
South Korea	104	104	173	173	181	206	198	53	6	6	1,202
Israel	6	99	97	320	69	22	9		17	15	654
Spain								135	229	73	437
Italy	30		30	5	5	8	170	35	72	32	387
China	28	35	35	35	35	35	35				238
Netherlands	13		13	13	13	42	38	50	55		238
UK	14	26	26	26	25						117
S. Arabia						62					62
Total	531	692	710	780	484	770	1,503	650	1,556	448	8,123

Source: Frank Slijper, *Power Projection. Turkey's Military Build-Up: Arms Transfers and an Emerging Military Industry* (Utrecht, Pax, 2017), p. 21; <http://www.sipri.org/databases/armstransfers/background>

President Erdogan has declared his full support for Turkey's military-industrial growth and his plan to supply Turkish armed forces with domestically produced tanks, ships, helicopters, satellites and warplanes.²¹ In recent years, Turkey has demonstrated that it can make major strides towards expanding and diversifying its arms industry with or without foreign assistance.²² A good example is the Teknopark Istanbul, which is intended as Turkey's Silicon Valley for the arms industry.²³ The strength and dynamism of the Turkish arms industry is also reflected by the fact that among the hundred largest arms-producing companies in the world, two of them are Turkish: the military electronics company Aselsan and Turkish Aerospace Industries. These two companies are described in greater detail below. There are also several state-controlled and private companies producing or assembling products such as grenades, missiles, military vehicles, aircraft and warships.²⁴

a) *Military electronics – ASELSAN*: At 1 billion US dollars in military revenues and employing nearly 5,000 people, Aselsan is Turkey's biggest arms company, ranked 58th (Defense News) or 69th (SIPRI) in the world. Established in 1975 to produce communications equipment, it delivered in 1980 its first 'manpack and tank wireless radios' to the Turkish army, followed in 1983 by the first export order. Applications for F-16 fighter jets and Stinger missiles soon followed; radar and electro-optical systems became part of the product range in the early 1990s. As of the turn of the millennium, Aselsan products were integrated into nearly every major weapon system acquired by the Turkish armed forces.²⁵ One of Aselsan's main international partners is Thales; its French

²⁰ Ibid., p. 21.

²¹ See Jonny Hog and Can Sezer, "Erdogan Aims to Turn Turkey into Major Defense Industry Power", *Reuters*,

²² 5.2.2015. In this comment, Erdogan is quoted as saying: 'Our goal is to completely rid our defense industry of foreign dependency by 2023'. <https://www.reuters.com/article/us-turkey-election-defence/erdogan-aims-to-turn-turkey-into-major-defense-industry-power-idUSKBN00C0FT20150527>.

²³ See also Yvonne-Stefania Efstathiou, "Turkish Defence Exports to 2023: Grand Ambitions", *ISS – International Institute for Strategic Studies*, 10.4.2019, <https://www.iiss.org/blogs/military-balance/2019/04/turkish-defence-exports>.

²⁴ For more information see <https://www.teknoparkistanbul.com.tr/en/what-is-a-teknopark>

²⁵ Slijper, *Power Projection*, p. 24.

²⁶ For more information see <https://www.aselsan.com.tr/en/innovation>.

and Dutch branches have worked closely with Aselsan for years. Thales and Aselsan are also cooperating to develop 'a family of launchers to integrate Thales Lightweight Multirole Missile (LMM) on Aselsan turrets together with the Aselsan Fire Control System, STAMP'.²⁶

b) *Aerospace – TUSAŞ*: Turkish Aircraft Industries Corporations (TUSAŞ) was established in 1973 under the auspices of the Turkish Ministry of Industry and Technology to reduce foreign dependency. In 1984, Turkish Aerospace Industries (TAI) was established by Turkish and US partners for a period of 25 years to realise the manufacture, systems integration and flight tests of F-16 fighter jets.²⁷

It has been reported that TAI assembled more than 200 of the fighter jets for the Turkish air force plus another 46 for Egypt. Located in Ankara, TAI is the world's 72nd biggest arms producer, according to Defense News (78th according to SIPRI), with 887 million USD, or 86 percent of its total revenues, coming from military sales.²⁸

As a result of its steps towards building an arms industry, today Turkey ranks according to SIPRI as the world's 18th arms exporting country for the period 2010–2015, with a clear upward trend visible for every year since 2011. According to a Reuters report, total arms exports rose by 18 percent to a substantial 1.65 billion USD in 2014, though that figure may also include civil aerospace sales.

Data provided by Defense Industry Manufacturers Association SaSaD (Savunma Sanayii İmalatçılar Derneği), Turkey's defence and aerospace manufacturers' association, show that the defence turnover more than doubled between the late 1990s and 2010, from an average of USD 1 billion to USD 2.7 billion, while exports increased from an average of USD 100 million to USD 634 million in 2010. There is an export-oriented drive, and indicators show a clear upward trend. In March 2016, the Turkish Exporters Assembly quoted a 30 percent rise in defence exports compared to the previous year, with the United States being the main destination with 34 percent of all exports, followed by Germany and the United Arab Emirates. According to the Turkey Exporters Assembly, in 2018 the Turkish arms industry exported to Germany goods worth 226 million USD, and in 2019 goods worth 256 million USD.²⁹ The Turkish daily *Sözcü* reported for the time period January–September 2019 exports of defence industry products worth of 184 million USD from Turkey to Germany. This puts Germany in second place after the USA (595 million USD) and ahead of Oman (180 million USD).³⁰

Aselsan's director recently stated: 'We're making products better than most in the West. We're cheaper... We're ready to share technology. The Turkish defence industry can be a valid alternative for the West'.³¹

To conclude, the national armaments industry is increasingly becoming an important driving force of the Turkish economy. Turkey's increasing ability to equip the armed forces with domestic weapons systems and military technologies raises the country's military clout and underscores its status as a regional power. This has been most recently observed in Syria and Libya. As Turkey becomes more and more a 'self-sufficient' country in military matters, dependence on arms deliveries from the USA and the EU (and therefore also from Germany) is decreasing. This means relative gains in power for Ankara vis-à-vis the EU and Germany, which is also going to affect negotiations to

²⁶ Slijper, *Power Projection*, p. 25.

²⁷ See the company website: <https://www.tusas.com/en/corporate/about-us>.

²⁸ Slijper, *Power Projection*, p. 25.

²⁹ See "2019-12-ülkelere-gore-sektorel-ihracat-rakamlari", <https://tim.org.tr/tr/ihracat-rakamlari>.

³⁰ "Savunma sanayi ihracati rekor kirdi", *Sözcü*, 5.10.2019,

<https://www.sozcu.com.tr/2019/ekonomi/savunma-sanayi-ihracati-rekor-kirdi-5371940/>.

³¹ Slijper, *Power Projection*, p. 36.

modernise the CU, if they indeed start. It has to be assumed that Ankara is going to continue its policy of autonomy vis-à-vis the EU.

Table 6: Turkish arms exports (2006-2015, top five destinations and all exports)

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	total
Saudi Arabia	8	20	26	26	33	44	39	44	39	52	309
Turkmenistan						20	20	40	60	91	231
UAE	7	7	7		3		10	20	20	80	154
Pakistan		19	26	7		22	22	22		24	142
Iraq	66										66
All exports	82	58	97	63	72	86	143	156	179	291	1,228

Source: Figures are SIPRI Trend Indicator Values (TIVs) expressed in USD million at constant (1990) prices. Figures may not add up due to the conventions of rounding. Source: SIPRI Arms Transfers Database, generated 9 November 2016; for more information see: <http://www.sipri.org/databases/armstransfers/background>

Automobile and supplier industry

Turkey has a dynamic, high-growth and export-oriented economy with internationally competitive industries. One relevant, if not the most important, sector in the Turkish economy is the automotive and supplier industry. This industry has become not only the locomotive for growth but also for technological and organisational innovation. Turkish automobile and supplier firms are among the leaders in Europe, especially in the production of buses where they rank highest Europe-wide.³²

Turkey is already a vital workbench in Europe and the world. Fourteen international car manufacturers – including Toyota, Honda, Ford, MAN and Renault – produced around 1.5 million cars in Turkey in 2019, of which around 80 percent were exported. The Turkish automobile and supplier industry ranks first in EU bus production, third in the production of vans and seventh in the production of passenger cars. As of 2018, Turkey is in 15th place in global automobile production with 1.55 million automobiles. For comparison: Germany is in fourth place with 5.12 million automobiles, France is 10th with 2.269 million automobiles and the United Kingdom is 13th with 1.583 million.³³

Turkey exported over a million automobiles to the EU (for comparison: Japan with just under 600 thousand is in second place). With its economic size, growing middle class and young population, Turkey is also a lucrative sales market for European automobile brands. In fact, 60 percent of the automobiles sold in Turkey are imported, mostly from Europe. In 2018, 169,964 German automobiles were sold in Turkey which makes up 27 percent of total automobile sales in Turkey (620,937). On the top was Volkswagen (66,834 automobiles), followed by Mercedes-Benz (22,438).³⁴

Besides, Turkey is also a central springboard for European companies to Africa, the Middle East and Central Asia. A case in point is the German Krone which produces truck trailers for Turkish and African markets.³⁵ Another case in point is Mercedes-Benz Türk A.Ş., a subsidiary of DaimlerChrysler AG in Turkey. In two plants based in the central Anatolian city Aksaray and in Hoşdere, a suburb of Istanbul, Mercedes-Benz Türk

³² Taysad, “Turkey: The European Automotive Hub”, unpublished presentation of Taysad.

³³ Ibid.

³⁴ Ibid.

³⁵ See Krone, <https://www.krone-trailer.com/english/company/locations-and-sales/tire-turkey/>.

produces trucks and buses for export to western and Eastern Europe, Asia and Africa.³⁶ Turkey's trade with Africa has quadrupled in the past two decades.³⁷ The increasing development of African sales markets by Turkish companies has enormous potential for German and European export industries. This in turn speaks for the intensification of European and German–Turkish economic relations and cooperation, for which a deeper customs union could form a good basis. More than 200,000 people are employed in Turkish car and supplier firms. A large number of the companies are members of the Turkish car manufacturers and suppliers association TAYSAD, which has 438 member companies. The association TAYSAD, founded in 1978, represents 65 percent of supplier products and 70 percent of exports. Eighty percent of its members are active in the Marmara region, 12 percent in the Aegean region and 8 percent in other parts of Turkey. Twenty-five percent of its member companies have foreign shareholders. As another association, OIB (Uludag Automotive Industry Exporters Association), represents the exporting automobile and supplier companies. The association, which was founded in Bursa in 1991 with 246 members and an export volume of USD 163 million, now has 5,800 active members, whose exports last year amounted to USD 31.6 billion. A good example of how the Turkish automobile and supplier industry is part of European production and value chains is the Turkish company Takosan from Kocaeli, which was awarded second place in the innovation competition hosted by the Association of European Automobile Suppliers (CLEPA). The company has been producing electronic automotive parts such as on-board computers, tachometers, electrical measuring devices and automatic door systems since 1979. Customers include the heavyweights Ford, Toyota, Renault, Fiat and more.³⁸ Coşkunöz Holding is one of the many Turkish know-how-based companies in the Turkish automotive industry. It exports 80 percent of its products – around 2,000 different auto parts – to Europe and elsewhere. The production hall in Bursa employs 1,200 people and operates 37 press lines that produce 120 million tons of sheet metal parts for automobile manufacturers. Its customers include BMW, Audi, Renault and VW.³⁹ Germany became the second-largest sales market for the Turkish automotive and supplier industry in June 2019, at 318 million US dollars. The main exports were cars, buses and minibuses. Exports to Germany were worth 2.2 billion US dollars in the first half of 2019.

Current account balance and tourism

The dilemma of the Turkish economy as an underdeveloped national economy is that foreign inputs such as intermediate goods and high-tech products must be imported in order to produce goods for export. Thus, increasing exports lead automatically to increased imports. The negative trade balance will not be relieved, as long as the proportion of high-tech production accounts for just 3.7 percent of total exports as was the case in 2016, and high-tech exports do not increase.⁴⁰ As we can see below, in times of economic slowdown and recession, the deficit in the balance of trade and current account balance decreases or approaches equilibrium. This was the case in 2009 as the Turkish

³⁶ <https://bit.ly/38EOVxu>.

³⁷ See 'DEİK: Turkey's Trade Volume with African Countries Increased by 4 Times' [DEİK: Türkiye'nin Afrika ülkeleriyle ticaret hacmi 4 kat arttı], *Dünya* (online), 12 May 2020, <https://www.dunya.com/ekonomi/deik-turkiyenin-afrika-ulkeleriyle-ticaret-hacmi-4-kat-artti-haberi-470152>.

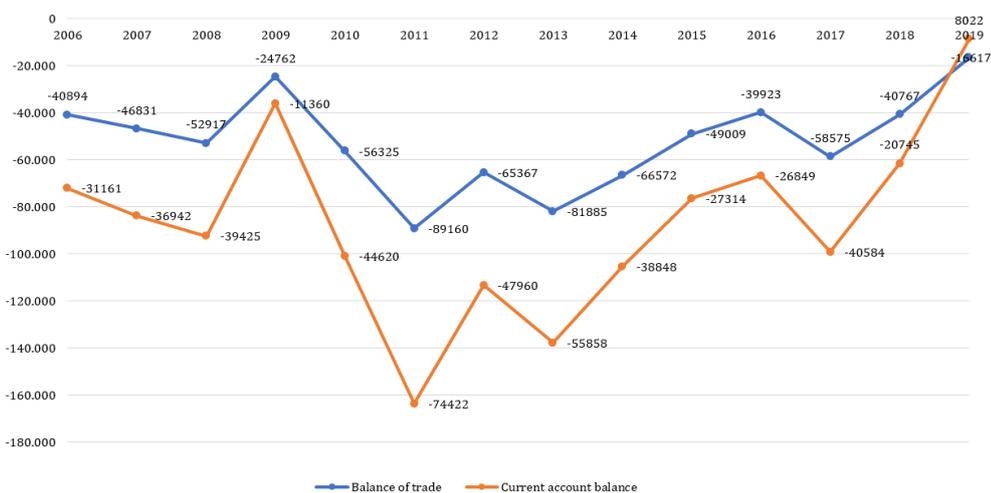
³⁸ <https://takosan.com.tr/?lang=en>.

³⁹ <http://www.coskunozholding.com.tr/en>.

⁴⁰ Deutscher Bundestag, 'Die Zollunion zwischen der EU und der Türkei', in *Wissenschaftliche Dienste des Deutschen Bundestages* (WD 5 – 3000 – 107/16), 10.

economy decreased and again in 2018 when the Turkish economy went into a currency crisis which was then followed by a recession in 2019. In 2019, Turkey had, first the time for decades, a positive current account balance. Responsible for the deficit in the balance of trade is the import of energy (oil and natural gas) as well as the dependence of the Turkish industry on intermediary goods and high-tech products from abroad. Meanwhile, tourism plays an essential role in closing the deficit of current account balance.

Trade and current account balance (in million USD)



Source: Türkiye Cumhuriyeti Merkez Bankası (Turkish Central Bank), <https://bit.ly/2ZSqcBx>

This has three consequences for EU–Turkey economic relations: First, it shows the reliance of the Turkish export industry on the European single domestic market in order to close the chronic trade deficit. The European common domestic market contains enormous sales potential for products from Turkey. This, secondly, increases the incentive for Turkey to negotiate with the EU to deepen the Customs Union, especially since this would send out an important signal to entrepreneurs in both Europe and Turkey. Even the prospect of modernisation of the CU would increase the attractiveness of Turkey as a field of investment (for FDIs) and of Turkish companies as partners in cooperation. Thirdly, against this background, the expansion of the Customs Union to include unprocessed agricultural products is of great importance, as from Turkey's perspective this would be another opportunity to increase exports to Europe and close the trade balance deficit.

Tourism is an important driving force of the Turkish economy. According to a comprehensive study by the World Travel & Tourism Council, it is one of the main pillars of economic dynamism in Turkey. The Turkish tourism industry recorded the most vigorous growth so far in 2018 with 15 percent. The contribution to the national economic performance was 96 billion US dollars. The tourism sector's share of gross domestic product in 2018 was 12.1 percent. It is the second largest sector after the construction industry (GDP contribution: 19.6 percent) and before agriculture (GDP contribution: 10.2 percent) and financial services (GDP contribution: 7.8 percent). The employment

contribution from travel and tourism was 7.7 percent in 2018, which is higher than financial services (3.3 percent) and banking (2 percent).⁴¹

The number of tourists in Turkey has been rising again since 2016, after a decline in 2015 due to domestic conflicts such as the escalation of the armed conflict with the PKK and IS terrorism as well as the instability in the Middle East region. In 2018, 38,951,902 foreign citizens came to Turkey, breaking the previous record set in 2014 (35,850,286). If we include the Turkish citizens living abroad who visited their country in 2018, there were 45.6 million visitors.

The tourism industry brought Turkey 24 billion US dollars in revenue in 2018. That is an increase of 4 and 8 billion US dollars respectively compared to 2017 (20.22 billion) and 2016 (15.99 billion). The share of tourism revenue in the export volume (just under 168 billion US dollars) was 17.5 percent (29.51 billion) in 2018, and the share of tourism in GDP was 3.8 percent. It can thus be seen that revenues from tourism contribute enormously, closing the deficit in the current account balance.

In 2019, 51,860,042 tourists came to Turkey,⁴² an increase of 12.2 percent over 2018. Of these, 45.1 million were foreigners and 6.1 million were Turkish citizens with permanent residence abroad. As the country of origin for tourists to Turkey, Russia comes first with 7 million and a share of 13.5 percent. Germany is in second place with 5.0 million and a share of 9.7 percent, followed by Bulgaria with 2.7 million (5.2 percent), England with 2.6 million (5 percent) and Iran with 2.1 million (4 percent).⁴³ The data suggest that Turkey's popularity as a travel destination is growing in Germany: in 2017, 1.7 million tourists from Germany came to Turkey in the first seven months of the year. In 2018 the number rose to 2.3 million. Considering that the bilateral tensions between Turkey and Germany are now in the past and that decision-makers from both countries are trying to reconcile, it is likely that the number of visitors from Germany will continue to increase.

Health tourism is one of the rapidly expanding sectors worldwide. Health tourism spending per capita is 6,500 US dollars, and experts estimate the global market in this area to be 100 billion US dollars. Turkey ranks fifth in health tourism worldwide – after the USA, Germany, Thailand and India. In 2018, Turkey attracted 551,748 health tourists, who spent an average of 2,013 US dollars per capita. Total health tourism revenue was 2 billion US dollars, and the country is on an upward trend: Turkey's share of global health tourism has grown by 25 percent annually in recent years. Health tourism revenue is expected to grow five-fold to 10 billion US dollars.⁴⁴

Human mobility between two countries – around five million persons from Germany visited Turkey in 2018 – contains business potential for travel agencies in Turkey and Germany. Extension of the CU to services would open up business opportunities and profits for German companies in tourism and transportation in Turkey.

⁴¹ World Travel & Tourism Council, <https://www.wttc.org/about/media-centre/press-releases/press-releases/2019/benchmarking-turkey/> (accessed 5 April 2020). See also Andreas Förster, 'Tourismus treibt die Weltwirtschaft an', in: *Reise vor 9*, 1.3.2019 (<https://www.reisevor9.de/inside/tourismus-treibt-die-weltwirtschaft-an>).

⁴² TÜİK, <http://www.tuik.gov.tr/PreHaberBultenleri.do?id=33669> (accessed 5.4.2020).

⁴³ TC Kültür Bakanlığı, 'Turizm İstatistikleri – Genel Değerlendirme 2019', <https://yigm.ktb.gov.tr/Eklenti/69320.turizmistatistikleri2019-4pdf.pdf?0> (accessed 5.4.2020).

⁴⁴ Zeynep Kahveci, 'Sağlık turistinin harcaması 2 bin doların üzerinde', *Anadolu Ajansı*, 13.8.2019, <https://www.aa.com.tr/tr/ekonomi/saglik-turistinin-harcamasi-2-bin-dolarin-uzerinde/1555756> (accessed 5.4.2020).

German Investments in Turkey

Volume of direct investments

Germany is, in the long term, one of the most important investors in Turkey (see Table 8). Between 1954 and 2014 Turkey hosted more than six thousand companies with German capital which made up of 14.4 percent of all companies with foreign capital in Turkey. Germany was followed – at a distance – by companies from the United Kingdom.

Table 7: International capital in Turkey 1954 -2014 (by countries)

Countries/ Years & numbers	2010	2011	2012	2013	2014	1954– 2014
Germany	454	592	484	417	380	6,070
UK	152	184	173	163	138	2,781
Netherlands	174	183	172	158	139	2,453
USA	101	160	114	104	92	1,512
Italy	91	112	107	101	98	1,222
Total	3,254	4,336	4,265	3,781	4,691	42,150

Source: Turkish Ministry of Economy, International Direct Investments 2014 Annual Report, cited by Kemal İnat, "Economic Relations between Turkey and Germany", *Insight Turkey* 18, no. 10 (2016), p. 27.

Between 2002 and 2015, the share of German foreign direct investments in Turkey amounted to 6.2 percent. In the years between 2010 and 2015, German FDIs made a significant contribution of 4,705 million US dollars, with the lowest yearly total being 384 million in 2015 and the highest being 1,968 million in 2013. In terms of FDI Germany is among the top six contributors; the others are all European countries with the exception of the U.S.

Table 8: Foreign direct investments in Turkey in Million USD (by countries)

Countries/ Years	2010	2011	2012	2013	2014	2015	2002-2015, total	Share, %
Netherlands	486	1,424	1,381	918	2,016	1,126	20,996	16,0
USA	323	1,401	439	326	334	1,566	10,755	8,2
Austria	1,584	2,419	1,519	657	31	45	9,348	7,2
Luxembourg	311	562	1,186	278	528	1,242	8,629	6,5
UK	245	906	2,044	300	1,051	596	8,599	6,5
Germany	597	664	491	1,968	601	384	8,442	6,2
Europe								
Total FDI in Turkey	6,256	16,136	10,759	9,878	8,576	11,778	132,165	100

Source: Turkish Ministry of Economy, International Direct Investments Statistics, cited by Kemal İnat, "Economic Relations between Turkey and Germany", *Insight Turkey* 18, no. 10 (2016), p. 27.

Between 2005 and 2015, Germany's share in FDI contributed by residents abroad is 6.2 percent, and by residents in Turkey 5.7 percent.

Table 9: German foreign direct investments in Turkey (in million USD)

	Germany's share in foreign direct investments in Turkey (by persons residing out of Turkey)			Germany's share in foreign direct investments by residents in Turkey		
	Total FDIs	Germany sourced investments in Turkey	Germany's share, %	Total investments	Investments in Germany	Germany's share, %
2005	8,535	391	4.6	1,065	158	14.8
2006	17,639	357	2.0	1,677	512	30.5
2007	19,137	954	5.0	2,275	42	1.8
2008	14,748	1,237	8.4	2,604	143	5.5
2009	6,266	497	8.0	2,040	82	4.0
2010	6,256	597	9.5	1,823	68	3.7
2011	16,136	664	4.1	2,542	90	3.5
2012	10,759	491	4.5	4,334	61	1.4
2013	9,878	1,968	19.9	3,226	253	7.8
2014	8,576	601	7.0	5,234	178	3.4
2015	11,858	387	3.2	5,240	250	4.7
2005–15	129,788	8,144	6.2	32,060	1,837	5.7

Source: Compiled from data provided by the Central Bank of Turkey, <http://evds.tcmb.gov.tr/>; Kemal İnat: "Economic Relations between Turkey and Germany", *Insight Turkey* 18, no. 10 (2016): 21–34 (30).

Due to the structural weaknesses and the low savings rate, Turkey continues to rely heavily on capital imports to finance its development programmes. However, more direct investments require political stability as well as reliable and transparent framework conditions. A good integration into the European economic and financial market is beneficial to attract investors. Strong domestic tensions and social, cultural and political polarisation worsen the business and investment climate in Turkey.

Total foreign direct investment increased by 32.4 percent to 16.6 billion US dollars in 2015 compared to 2014, according to Ministry of Economy reports, including foreign property investment of just under 4.2 billion. Excluding the real estate sector, 58 percent of EU inflows came from the Netherlands, followed by the UK and Germany. Less than 35 percent went into the processing industry and 30 percent into the financial sector.⁴⁵

Key sectors of German FDIs

The graphic below shows the sectors in which Turkish FDIs in Germany as well as German FDIs in Turkey take place. However, the investments are quantified not in terms of value, but in terms of the number of the projects in different branches (see Table 10).⁴⁶ Tables 10 and 11 show that a significant part of German direct investments concentrate in manufacturing industries – both in terms of the number of projects as well as in terms of turnover.

⁴⁵ Wirtschaftliche Dienste, 'Die Zollunion zwischen der EU und der Türkei', in *Dokumentation der Wissenschaftlichen Dienste des Deutschen Bundestages* (WD 5 – 3000 – 107/16), 2017, p. 10.

⁴⁶ GTAI – Germany Trade & Invest, 'Deutschland und Türkei – Partner in schwierigen Zeiten', 2018, p. 8.

Table 10: German-Turkish investments

Turkish investments in Germany		German investments in Turkey	
Number of projects by branches, 2003–2007		Number of projects by branches, 2003–2007	
Clothing and textiles	42	Automobile and parts	46
Consumer goods	24	Renewable energies	17
Transportation and logistics	10	Consumer goods	15
Communication	7	Real estate	8
Ceramics and glass	3	Energy (conventional)	5
Others	125	Others	228
Total projects	211	Total projects	319

Source: GTAI – Germany Trade & Invest, “Deutschland und Türkei – Partner in schwierigen Zeiten” (March 2018).

a) Automobile and Supplier Sector:

The automotive industry is the largest export sector in Turkey besides the clothing industry. Turkey also hosts German companies that produce commercial vehicles only in Turkey. The Daimler subsidiary Mercedes-Benz Türk operates a modern bus plant west of Istanbul and has a truck factory in Aksaray. This is currently being expanded for more than 100 million euros, so that capacities should double to 34,000 vehicles per year. In May 2017, the second Research & Development Centre of Mercedes-Benz Türk was established within the Aksaray Truck Plant with an additional investment of 8.4 million euros.⁴⁷ Mercedes-Benz Türk has another Research & Development Centre in Istanbul.

Table 11: Automobiles and suppliers with German capital

Company	Employees	Turnover in million \$
Mercedes Benz Türk	6,106	3,286
Bosch Sanayi ve Ticaret	7,985	1,302
MAN Türkiye	1,936	373
Aunde Teknik Tekstil	2,316	194
Bosch Rexroth Otomasyon Sanayii	1,000	152

Source: GTAI – Germany Trade & Invest, “Deutschland und Türkei – Partner in schwierigen Zeiten”, March 2018.

The commercial vehicle manufacturer MAN has been producing buses in Turkey since 1966. MAN, Türkiye was the first production site outside Germany and is the company's largest bus production centre. The German Bosch Group has a total of five subsidiaries in Turkey and employs around 17,500 people nationwide. The automotive supplier manufactures parts and components for over 30 car brands in Bursa. The product range includes gasoline and diesel injection units, filter systems, braking systems and service equipment. The trailer manufacturer Krone is currently expanding its annual capacity at the Izmir site from 10,000 trailers. Krone has also been producing the chassis itself in Izmir since 2017.⁴⁸

In 2018 Bosch Turkey reached a turnover of 20.9 billion Turkish Lira (almost 3 billion in US dollars). Sales in the Middle East region (excluding Turkey) amounted to 1.6 billion Turkish Lira. Five percent of the turnover of Bosch Groups has been earned by Bosch Turkey.⁴⁹

b) Energy and Electric Sector

Turkey is located at the crossroads of Europe, the region with the highest demand for energy worldwide, and the regions of the Near East, Caucasus and Central Asia, which own

⁴⁷ <https://www.daimler.com/career/about-us/locations/location-detail-page-5067.html>.

⁴⁸ See the subchapter on Automobile and Supplier Industry on p. 13.

⁴⁹ Unpublished PowerPoint Presentation, ‘Bosch Turkey and Middle East’.

the most abundant fossil energy resources. Primarily due to its withdrawal from the nuclear energy programme and coal extraction, Germany's need for fossil energy such as oil and natural gas has been gradually on the rise. Therefore, Germany is interested in binding (integrating) Turkey into the European Energy Community, while Turkey is interested, due to its increasing demand for energy, in minimising its dependency on Russia and Iran. Potentials in regenerative (renewable) energy sources make Turkey important for the German energy sector. There is a broad space for German companies for investment, for example, in helping Turkey to expand its renewable energy facilities. The energy sector is one of the industries in which Turkey is currently investing the most. Turkey is interested in reducing its import dependency on fossil fuels and is promoting renewable energies. About 40 percent of Germany's direct investment flowed into the energy sector between 2003 and 2017, including renewable energies.⁵⁰ In 2017, a consortium led by Siemens received a major order for the construction of wind turbines to produce 1,000 megawatts with a total value of 900 million euros. E.ON from Düsseldorf has been present in Turkey since 2012, in the form of a 50 percent stake in Enerjisa Enerji. Together with the joint venture partner Sabanci, a major Turkish industrial conglomerate, it serves nearly 20 million consumers of electricity nationwide. EWE Turkey Holding, a subsidiary of the German utility EWE, operates the natural gas distribution networks of the major cities Bursa and Kayseri.

Table 12: Electronics industry

Company	Employees	Turnover in million \$
BSH household appliances	7,113	1,540
Schneider electric	1,988	416
Bosch thermo-technical industry	1,200	379
Iron casting	1,213	222

Source: fDi Intelligence der Financial Times, quoted by: GTAI – Germany Trade & Invest, “Deutschland und Türkei – Partner in schwierigen Zeiten” (March 2018).

c) Transport and logistics

The increase in the exchange of goods between the European Union and Turkey requires investments in transport infrastructure. Turkey is expanding its seaports and airports, as well as the rail network, and is building more and more organised commercial areas. This increases the demand for logistics distribution centres. The German logistics provider DHL Express is currently building a new air freight centre for 60 million euros at the third Istanbul airport, which opened in October 2018. In addition, the DHL Supply Chain Türkiye in Istanbul and Gebze will set up three new warehouses by 2019 for the equivalent of just under 12 million EUR.

SunExpress – founded in 1989 by Lufthansa and Turkish Airlines as a joint venture – carries almost 10 million passengers annually. The airline expects continued growth and plans to establish a maintenance facility for aircraft in Antalya. The million-dollar project is scheduled to go into operation by 2022 at the latest. The German-Turkish airline flies 84 aircraft to 90 airports in 30 countries.⁵¹ In these sectors, the extension of the CU to services would be profitable for companies both in Germany and in Turkey.

d) Clothing

Turkey is among the world's most important textile and apparel manufacturing countries: it is the sixth largest clothing supplier in the world, and the third largest supplier to the EU

⁵⁰ GTAI – Germany Trade & Invest, ‘Deutschland und Türkei – Partner in schwierigen Zeiten’, 2018, p. 6.

⁵¹ Tuba Şahin, ‘SunExpress to Open 1st Hangar in Antalya, Turkish Coast’, *Anadolu Ajansı*, 11.7.2019, <http://bit.ly/2MuweV0>.

which absorbs 9.4 percent of Turkey's total exports. Turkey exports not only ready-made garments but also fabrics, worldwide. Countries of the EU, including among others Italy, Russia, Germany, Romania and Bulgaria, are the most important market for Turkey's fabric exports.

For many German entrepreneurs, Turkey is an important manufacturing location. German clothing manufacturers such as S. Oliver, Esprit or Hugo Boss produce in Turkey. Hugo Boss Textile has 3,945 employees and earns 160 million US dollars.⁵² In recent years the Turkish textile manufacturing industry has been facing challenges: the country has to compete with China. According to Hadi Karasu, Chairman of the Turkish Clothing Manufacturer's Association (TGSD), 'China's "One Belt, One Road" project is a threat for the Turkish apparel industry. Primarily, China carries its apparel industry to Western China where cheap labor is intense'. Due to its easier access to the EU market, the Chinese textile industry poses serious competition to the Turkish textile sector. The Turkish textile sector is also negatively affected by the free trade agreement between the EU and South Korea.⁵³

Furthermore, Turkey is an important market for German manufacturers of textile machinery. In 2017, Germany exported textile machinery worth 403 million euro.⁵⁴

⁵² See GTAI – Germany Trade & Invest, 'Deutschland und Türkei – Partner in schwierigen Zeiten', March 2018, p. 7.

⁵³ Akhi Akter and Mir Abdullah Al Mahfuz, 'An Overview of Turkish Textiles and Clothing Industry', *Textile Today*, 30.7.2018, <https://www.textiletoday.com.bd/overview-turkish-textiles-clothing-industry/>.

⁵⁴ Sherif Rohayem, 'Türkei bleibt wichtiger Markt für deutsche Textilmaschinen', *GTAI*, 11.2.2019, <https://www.gtai.de/gtai-de/trade/branchen/branchenbericht/tuerkei/tuerkei-bleibt-wichtiger-markt-fuer-deutsche-textilmaschinen-22022>.

Actors, Positionings and Arguments

Reasons for the Modernisation of the Customs Union

a) Expert discourses

Data presented in the previous part shows that due to the EU–Turkey CU since 1995, trade integration has been increased dramatically over the last two decades. Today, a significant number of Turkish companies, especially in the automobile and textile sectors, are an integral part of German value and production chains. The CU brought many benefits to Turkey as well as to the countries of the European CU. However, the current trade arrangement between the EU and Turkey is considered to require revision for organisational, economic and political reasons.

b) Organisational deficits and design errors

The need to rectify the EU–Turkey CU arrangement stems first of all from its deficits and design errors. To begin with, Turkey is excluded from free trade negotiations between the EU and third countries. However, it should be mentioned that this design flaw goes back to the fact that the CU was originally conceived as a transitory solution, a sort of preliminary stage to the EU membership of Turkey. Therefore, it became a true obstacle as the accession negotiations stalled and the prospect of EU accession has faded into the distance. In consequence, in the case of an EU free trade agreement with a third country, Turkey must open its markets to this country, while at the same time, improved access for Turkish exports into the country is denied. Due to this asymmetry in the decision-making structure of the European CU, cooperation between Brussels and Ankara is impaired. Furthermore, business circles refer to trade disputes, which, according to a BDI report, have ‘skyrocketed over the past few years’. Despite such design flaws, the Customs Union still does not contain any efficient and binding dispute settlement mechanisms.⁵⁵

c) Welfare gains through modernisation

The CU brought to Turkey and to CU countries significant growth and welfare gains. According to estimates and scientific projections, an extension of the EU–Turkey Customs Union arrangement to unprocessed agricultural goods and services would have further strong positive welfare effects on the Turkish economy. It is estimated that the gross national product could experience an additional growth of 1.84 percent. Turkish exports to the EU could increase by almost 70 percent.⁵⁶

According to a study by Bertelsmann Stiftung, ‘deepening of the customs agreement could lead to per capita income growth of USD 171’.⁵⁷ A deepening of the EU–Turkey CU and the conclusion of simple free trade agreements between Turkey and the EU’s new trading partners could result in a welfare gain of 2.13 percent for Turkey. In Turkey, per capita

⁵⁵ BDI – Bundesverband der Deutschen Industrie, *Modernisierung der Zollunion der EU-Türkei*, Berlin, 2017.

⁵⁶ Erdal Yalcin, Rahel Aichele, and Gabriel Felbermayr, *Turkey’s EU Integration at a Crossroads* (Gütersloh, 2016), p. 7 and p. 51.

⁵⁷ *Ibid.* p. 7.

income could increase by almost 200 US dollars. However, an extension of the CU to unprocessed agricultural goods and services would also bring welfare gains for Germany and the countries of the European CU. In contrast, repatriation of the CU agreement would have adverse welfare effects for Germany, for other countries of the European CU, and for Turkey.⁵⁸

Public debate

The German public debate over modernisation of the EU–Turkey CU is highly polarised. A repeated argument behind the refusal to modernise the Customs Union is that such a decision would be beneficial for the Turkish President Erdogan. A revision of the current agreement would strengthen the Turkish economy, stabilise the Turkish government and enforce the political position of Erdogan. Mehmet Ugur gets to the point perfectly when he suggests that ‘upgrading the customs union until positive evidence of commitment to the rule of law in Turkey’ would jeopardise ‘Europe’s own post-war value system’.⁵⁹ Those, on the other hand, who argue in favour of modernisation of the EU–Turkey CU base their position on arguments regarding security policy and geopolitics. A repeated argument for the modernisation of the Customs Union is that a confrontation course on this issue would drive Turkey into the arms of Russia.⁶⁰ Other pro attitudes refer to the Turkish civil society, Turkish oppositional actors as well as to the pro-Europe parts of the population. Such pro and contra arguments can also be found among politicians.

Roadmap for modernisation

Prior to negotiations to modernise the EU–Turkey CU, a World Bank report proposes a number of measures or recommendations to be taken by the contract parties. The first to be mentioned is resolving the ‘imbalances in formulating the common commercial policy through the development of formalized structures for appropriate consultations with Turkey’. A second step suggested by the report is liberalising road transport permits, especially for transit and at least for those goods covered by the CU. A third recommendation is establishing a specific business visa category for pre-qualified Turkish professionals travelling to the EU on business and with long-term and multiple entries, as well as simplified documentary requirements. The fourth step would be creating a well-designed dispute settlement mechanism and a dialogue to reduce the notification deficit. In terms of eventual modernisation, the World Bank report recommends widening the CU to the area of services as well as a greater trade integration in agriculture.⁶¹

⁵⁸ Ibid.

⁵⁹ See Mehmet Ugur, ‘Why EU Should Not Upgrade the Customs Union with Turkey’, *Social Europe*, 8.2.2018, <https://www.socialeurope.eu/eu-not-upgrade-customs-union-turkey>; Kadri Tastan, ‘Customs Union an Anchor for Turkey–EU Relations’, in *The German Marshall Fund of the United States (On Turkey)*, August 2017.

⁶⁰ Die Zollunion ist der entscheidendere Hebel’, interview with Michael Hüther, in *Institut der Deutschen Wirtschaft* (online) 25.7.2017, <https://www.iwkoeln.de/presse/interviews/beitrag/michael-huether-im-deutschlandfunk-tuerkeipolitik-die-zollunion-ist-der-entscheidendere-hebel-355182.html> (accessed 20.3.2020).

⁶¹ World Bank, *Evaluation of the EU-Turkey Customs Union* (report no. 85830-TR), 28.3.2014.

Positioning and Arguments of Political Actors

Federal government and foreign ministry

Despite favourable prospects for Turkey and countries of the European Union, many governments are reluctant to open negotiations with Turkey. Germany has become a visible and influential veto player in the formation of EU–Turkey dialogue and is currently blocking the negotiations with Turkey, although it has not given up the goal of modernisation of the EU–Turkey CU completely. As of December 1999, when the Helsinki European Council granted Turkey candidate country status with strong support provided by the German Gerhard Schröder government, German–Turkish relations took a positive turn in political and economic terms that lasted until 2013. In early 2013, Germany adopted, parallel to France after Sarkozy was voted out, a more positive attitude towards the acceleration of Turkey's EU accession process. However, in early June 2013 following the Gezi Park protests and Germany's subsequent official criticism of their handling by the Turkish government, Berlin decided to veto the opening of new negotiation chapters in Turkey's accession talks with the EU.

In late 2015 due to the irregular migration crisis, a sudden yet temporary rapprochement took place between Berlin and Ankara. Chancellor Merkel unanticipatedly supported the revitalisation of the Turkish accession process in exchange for Turkey's enhanced cooperation with the EU. In mid-2016, an extensive period of conflict and estrangement between Germany and Turkey opened as a result of various incidents including the adoption of a resolution by the German Bundestag recognising the mass killing of Armenians in 1915 as a 'genocide', Ankara's consequent ban on German parliamentary delegations visiting the Incirlik military base that hosted roughly 250 German troops as part of the anti-IS coalition, and Berlin's palpable criticism of post-coup developments in Turkey.

After a two-year phase of heightened estrangement and conflict, from early 2018 on German and Turkish leaders started avoiding accusations against each other. Some steps towards reconciliation have been taken by both governments since late summer 2018 in consideration of mutual strategic interests and converging preferences in both economic and political terms. After the Turkish currency decline in August 2018, German decision-makers stressed the importance of a stable Turkey in economic, political and geo-strategic terms. There were many other signs of relaxation in the bilateral relations between the two countries, which gave rise to the expectation that Germany and Turkey would now be moving closer together again. Indeed, several points of contention have been overcome since then.

However, a quick and complete recovery from turmoil appears still to be unlikely. Lasting authoritarian style of governance in Turkey, as well as a remarkably Turkey-sceptic German public opinion, make it hard to overcome the estrangement between Berlin and Ankara. Today, Germany is a visible and influential veto player in the formation of EU–Turkey dialogue and in the modernisation of the Customs Union: Berlin justifies this stance against the negotiations with Ankara by reference to the authoritarian turn in Turkey as of 2016.⁶² In the coalition agreement between the CDU, CSU and SPD (12.3.2018), for example, it is stated that no chapters are to be closed and no new chapters

⁶² See 'Breitseite gegen Erdogan: Merkel will Ausweitung der Zollunion auf Türkei verhindern', *Focus-Online*, 30.8.2017, https://www.focus.de/finanzen/news/konjunktur/bundesregierung-macht-ernst-breitseite-gegen-erdogan-merkel-will-ausweitung-der-zollunion-auf-tuerkei-verhindern_id_7530558.html.

opened in Turkey's EU accession process. Modernising the EU–Turkey CU or negotiations with Turkey are not even mentioned.⁶³

In 2017, Foreign Minister Sigmar Gabriel (SPD) declared that negotiations on the expansion of customs union between Turkey and the EU could only continue when a 'reasonable relationship' with Turkey can be established and added: 'This also includes the release of those we believe are innocent',⁶⁴ The parliamentary group of The Left (Die Linke) addressed in her small written request (Kleine Schriftliche Anfrage) to the Federal Government (Bundesregierung) the question of whether it pursues modernising the EU–Turkey CU. Instead of a direct answer, the Federal Government referred to the World Bank study of that year.⁶⁵ This is interesting and important because the World Bank study concerned proposes modernising the Customs Union. To this question, the government replied with the statement that for systematic problems in the context of the EU–Turkey CU, there could be only solutions that would be beneficial for both sides.⁶⁶

Political parties

CDU/CSU

The CDU and CSU do not oppose the expansion and deepening of the customs union with Turkey. They pose only the condition that there is a departure from the authoritarian course in Turkey. They make the start of talks conditional on progress being made on democracy, the rule of law, separation of powers, and human rights. MP Renate Sommer (CDU), for instance, said about the plenary resolution of the European Parliament on EU–Turkey:

We therefore call for the official suspension of the accession negotiations and the establishment of a new partnership. (...) The relatively well-functioning customs union, which could be extended to agricultural products and services, would be a conceivable basis for future EU-Turkey relations. However, we also want to tie this economic cooperation to strict criteria: respect for human rights, democracy, and the rule of law are also essential for us in this context. In the same way, Turkey must finally help clarify the Cyprus issue, fulfill its legal obligations towards neighboring countries and recognize their territorial integrity.⁶⁷

SPD

Due to the diplomatic tensions between Germany and Turkey as of 2016, modernisation of the EU–Turkey CU is not on the agenda. *However, the need for a new arrangement is not neglected by the party leadership.* Nils Schmid, MP and foreign policy spokesman for the SPD parliamentary group in the Bundestag, advocates the modernisation of the EU–Turkey CU for this would above all create more legal security for German companies in Turkey. For example, Europe does not have a reasonable mechanism to resolve disputes related to customs union violations. 'If the customs union were extended to tender for

⁶³ See Bundesregierung, 'Ein neuer Aufbruch für Europa Eine neue Dynamik für Deutschland Ein neuer Zusammenhalt für unser Land', 12.3.2020, <https://www.bundesregierung.de/resource/blob/975226/847984/5b8bc23590d4cb2892b31c987ad672b7/2018-03-14-koalitionsvertrag-data.pdf?download=1>.

⁶⁴ Markus Becker, 'Ankaras wunder Punkt', *Spiegel-Online*, 19.10.2017, <https://www.spiegel.de/wirtschaft/soziales/zollunion-der-eu-und-der-tuerkei-ankaras-wunder-punkt-a-1173730.html>.

⁶⁵ See footnote no. p. 55.

⁶⁶ <http://dipbt.bundestag.de/dip21/btd/18/106/1810686.pdf>.

⁶⁷ 'EU-Türkei Partnerschaft statt Beitrittsverhandlungen', CDU/CSU-Gruppe in der Europäischen Volkspartei, <https://www.cducusu.eu/artikel/eu-tuerkei-partnerschaft-statt-beitrittsverhandlungen>.

public contracts, Turkey would be forced to be more transparent, especially concerning construction contracts. In the past, corruption and nepotism were often suspected here.’⁶⁸ In an interview, Nils Schmid stressed the importance of the CU between EU and Turkey in economic and political terms. According to him, the EU–Turkey CU is a central component of the cooperation between the EU and Turkey. Although he also stressed the importance of negotiations as a means and occasion to improve bilateral relations between Germany and Turkey, he does not see any possibility of starting negotiations for updating the CU. Schmid considers the decision not to conduct negotiations with Turkey, to be justified by the reduction in democracy, undermining the rule of law, the suspension of the division of powers, and violations of human rights in Turkey.⁶⁹

Recently, Nils Schmid published a comment in the German economic newspaper *Handelsblatt* in which he stressed once again the importance of the CU: ‘The customs union gives the EU the market potential of an 80 million country that serves as a hub to Asia. At the same time, Turkey should not endanger its integration into European value chains and the resulting growth potential through a lack of transparency and corruption’.⁷⁰

Given the deterioration of the human rights situation in Turkey, EU accession negotiations can only be resumed if the current or another government achieves significant improvements in the areas of human rights, the rule of law and freedoms. One possible way out of this muddled situation could be to modernise the CU. According to Schmid, a first step could be to remedy the shortcomings in the implementation of the existing regulatory framework of the CU, before extending it to services and agriculture.

The Greens

Once a strong supporter of opening an EU membership perspective for Turkey and accession talks, today the Greens have a rather sceptical attitude. In an interview for *Merkur.de*, the Green Leader in the European Parliament Ska Keller spoke out against talks about expanding and deepening the customs union with Turkey: ‘For example, I wonder whether the customs union with Turkey is still justifiable given the systematic dismantling of democracy and the rule of law. But the conservatives, in particular, want to expand the customs union because that is good for business. It does nothing for democracy and human rights’.⁷¹

In an application, the Greens' parliamentary group asked the Bundestag to condemn Turkey's military offensive in northern Syria as violating international law, and to draw clear consequences. The application advocates not resuming negotiations with Turkey until Ankara resumes democratisation and respects the rule of law. It also calls for discontinuation of the accession talks, which are in fact already on hold. However, the application warns not to abort the accession talks completely, which ‘would send the wrong signal to the pro-European and democratic forces in Turkey’.⁷²

⁶⁸ Stefan Kegel, ‘Nils Schmid für Erweiterung der Zollunion’, *Südwest Presse* (online), 27.9.2018, <https://www.swp.de/politik/inland/tuerkei-nils-schmid-spd-plaedierte-erweiterung-der-zollunion-28025736.html>.

⁶⁹ Interview with Nils Schmid, on 6.3.2020 in Berlin, interview conducted by the author.

⁷⁰ Nils Schmid, ‘Wir dürfen die Türkei nicht aufgeben’, *Handelsblatt*, 8.3.2020, <https://www.handelsblatt.com/meinung/gastbeitraege/gastkommentar-wir-duerfen-die-tuerkei-nicht-aufgeben/25621666.html?ticket=ST-635078-lidvj4p1uS3pDS5NeGxP-ap3>.

⁷¹ <https://www.merkur.de/politik/europawahl-2019-gruenen-chefin-ska-keller-ueber-tuerkei-und-fehler-union-12269813.html>.

⁷² Antrag der Fraktion Bündnis 90/Die Grünen, Drucksache 19/14094, <http://dip21.bundestag.de/dip21/btd/19/140/1914094.pdf>.

The Left

The Left party has a clear position regarding the expansion of EU–Turkey CU. It is not only against the expansion but also advocates breaking off accession talks between the EU and Turkey. According to a press release by MP Sevim Dagdelen, spokeswoman for international relations of the Die Linke parliamentary group, the federal government ‘must not approve the planned expansion of the customs union with Turkey’. She legitimises this demand with the argument that ‘not only Turkish companies would benefit economically from an expansion of the customs union’, but also ‘the Turkish President Erdogan’. She terms it dishonest to call ‘for the accession talks to be stopped now ... while at the same time pushing ahead with the enlargement of the customs union, aware that this will politically strengthen Erdogan’.⁷³ In another press release, Dagdelen stated that the ‘planned negotiations for an expansion of the customs union with Erdogan’s Turkey must also be put on hold’.⁷⁴ Die Linke is the party that is most critical of Turkey and the German foreign policy towards Turkey.⁷⁵

FDP

Following Turkey’s incursion into northern Syria in October 2019, Christian Lindner, chairman of the FDP, called for an arms embargo against Turkey to suspend accession talks and to stop economic cooperation. FDP foreign politician Alexander Graf Lambsdorff had previously asked the German government to freeze the deepening of the customs union or the visa liberalisation hoped for by Turkey until further notice.⁷⁶

Positioning and Arguments of Economic Actors

Ministry of Economy and Energy

Since 1985 the German economy has been represented in Turkey by a delegate office of the German Chamber of Commerce and Industry (DIHK) in Istanbul. According to the Auswärtiges Amt, DIHK Istanbul has around 1,000 members. In 2004 the Turkish-German Chamber of Commerce and Industry was founded in Cologne. The Chamber has had its headquarters in Berlin since 2012 and has a branch in Cologne. As of 1962 there existed an investment protection agreement between Germany and Turkey. In July 2001, the Turkish International Arbitration Law entered into force. The bilateral double taxation agreement of 1985 was terminated on 1 January 2011, and a new double taxation agreement was signed 19 September 2011 in Germany, which came into effect retroactively on 1 January 2011.

In November 2012, Germany and Turkey agreed to set up the ‘German-Turkish Energy Forum’ as a platform for dialogue between decision-makers and entrepreneurs in the energy sector of both countries. The first ministerial meeting took place in Ankara in April

⁷³ Sevim Dagdelen, ‘Keine Erweiterung der Zollunion mit der Türkei’, Press release (18.11.2016), <https://www.linksfraktion.de/presse/pressemitteilungen/detail/keine-erweiterung-der-zollunion-mit-der-tuerkei/>.

⁷⁴ Sevim Dagdelen, ‘Auch Zollunion mit der Türkei auf Eis legen’, Press release (24.11.2016), <https://www.linksfraktion.de/presse/pressemitteilungen/detail/auch-zollunion-mit-der-tuerkei-auf-eis-legen/>.

⁷⁵ For press releases on Turkey, see <https://www.die-linke.de/themen/international/themen/erdogan-und-das-verhaeltnis-zur-tuerkei/>.

⁷⁶ <https://www.liberales.de/content/fdp-fordert-stopp-der-beitritts-gespraechen-mit-erdogan>.

2013. In addition, the economy ministries of both countries agreed to establish an economic and trade commission, JETCO (Joint Economic and Trade Commission).⁷⁷ Nevertheless, the attitude of the Federal Ministry for Economic Affairs and Energy towards modernising the EU–Turkey CU can be described as restrained. A speaker from the Ministry stated in an interview that German entrepreneurs' interest in Turkey is declining. Fewer German entrepreneurs are taking part in events organised by the Ministry to open up new markets in Turkey. He stressed that Turkey is seen as a whole by the German middle class; economic aspects are not abstracted from political aspects. Many companies are concerned about the arrests of Turkish-born Germans, which they perceive as unjustified and arbitrary. According to him, from the perspective of German companies, the 'political and legal frameworks are not inviting'. Regarding the modernisation of the CU, he stressed that starting negotiations would require that the Turkish government abolish measures that contradict the functioning of the Customs Union. If the CU functioned well, that would be a good argument for its modernisation. He downplayed the potential of using negotiations on modernisation of the CU as leverage for political influence: 'Even then you can't manage to move family businesses to Turkey. Negotiating the modernisation of the Customs Union without touching the political framework does not work'.

BDI – The Federation of German Industries

Economic actors are highly critical towards Turkey due to the worsening of political conditions, human rights violations and dismantling of democracy. In a joint statement of DIHK (Deutscher Industrie- und Handelskammertag, or Association of German Chambers of Industry and Commerce), BDI (Bundesverband der Deutschen Industrie, or Federation of German Industries) and BdB (Bundesverband deutscher Banken, or Association of German Banks) on the occasion of the round table of these organisations with the Turkish President Recep Tayyip Erdogan as well as German and Turkish companies, a number of measures were requested by the Turkish government to restore trust in Turkey and 'encourage German companies to make new investments'. Demands of the three business associations on the Turkish government also include compliance with the existing regulations of the CU.⁷⁸

In a position paper by the BDI, it is stated that the functionality of the Customs Union is at risk because the number of trade disputes has been increased in recent years. Tariff and non-tariff trade barriers are increasingly making access to the Turkish market more difficult. As a consequence, more and more German industrial companies are complaining about these market barriers. The current agreement contains neither arbitration mechanisms nor efficient binding dispute settlement mechanisms. In an expert interview, BDI employees explained the complaints of German businesspeople concerning the EU–Turkey CU. German companies are concerned about additional bureaucratic duties as well as registration obligations and hurdles imposed by the Turkish government on the entry of pharmaceutical goods and medicines into the Turkish market.

Corinna Neumann, research officer on industrial and economic policy for BDI, considers talks on modernising the customs union to be unlikely, because of the lack of 'some positive signals from Turkey'. Confidence-building steps on the part of the Turkish government are needed, for her to have a sense that Turkey can be relied upon. According to her, the biggest obstacle, from the perspective of German business circles, to

⁷⁷ See Deutsche Vertretungen in der Türkei, 'Bilaterale Wirtschaftsbeziehungen', <https://tuerkei.diplo.de/tr-de/themen/wirtschaft/-/1673720>.

⁷⁸ https://bdi.eu/media/presse/presse/downloads/20180927_Pressemitteilung_BDI_DIHK_BdB_Tuerkei.pdf.

negotiations with Turkey on modernising the CU is the general situation. Due to the diplomatic tensions with Ankara, the disagreements about the existing CU and the political instability and legal uncertainties, the EU is unable and unwilling to negotiate with Turkey and modernise the Customs Union. In short, the EU is waiting for confidence-building measures from Turkey.

The BDI position paper further states that the EU–Turkey CU has been and still is ‘an essential part of economic integration’ between the EU and Turkey. Both the open market principle and incomplete adjustment of the legal framework have significantly promoted the bilateral trade in industrial goods, the formation of common value chains as well as direct investments in favour of both EU states and Turkey. However, the paper estimates that the functionality of the Customs Union is at risk. In view of the conceptual weaknesses of the current agreement, the BDI paper supports the proposal of the European Commission to modernise the EU–Turkey CU.⁷⁹ The BDI position paper concludes with a number of policy recommendations for decision-makers. First, it suggests that existing trade barriers be removed by the Turkish government as a confidence-building measure. Second, it recommends that the EU and Turkey agree on the necessity for modernisation of the CU. A new agreement has to include a modern, clear and binding set of rules that guarantee legal certainty as well as an effective binding dispute settlement mechanism. Third, an updated agreement has to meet the requirements of the Trade for All strategy and cover topics such as sustainability, energy, raw materials, services and public procurement. Fourth, the BDI position paper suggests better coordination between EU and Turkey on their trade policies, which could include more efficient consultations to ensure sustainable harmonisation of regulations.⁸⁰

⁷⁹ BDI – Bundesverband der Deutschen Industrie, ‘Modernisierung der Zollunion EU-Türkei: Notwendige Verbesserungen für den Warenhandel’, position paper, p. 36.

⁸⁰ *Ibid.*, p. 3.

Implications for Decision-Makers

Data on bilateral trade, German foreign direct investments in Turkey and human mobility (tourism) demonstrate the intensive interdependence between the two countries. A great part of Turkish companies, for instance automobile and automotive suppliers, textile and clothing industries, energy and electronic sectors as well as transport and logistics, are integrated into the German, and thus European, value and supplier chains.

For Turkey, the most important region in terms of trade is still Europe, although the importance of other regions such as Asia-Pacific and North Africa is on the increase as well. More than half of all Turkish exports by value are delivered to European countries, while a quarter are sold to Asian countries. Only a small part of Turkey's export goes to Africa, although trade with Africa is on the increase, and to North America which has been on the decrease for decades. Turkish exports to Latin America are practically insignificant, at 1.6 percent. Trade with Russia and China is highly asymmetrical at the expense of Turkey. Turkish exports to Russia and China seem not to be expandable in the short and medium term. This again illustrates the importance of the European market for Turkish industry.

The arms industry and automotive industries are the most innovative and dynamic sectors of the Turkish economy. Turkey ranked as the world's 18th arms-exporting country for the period 2010–2015. Both the Turkish automobile industry as well as its automotive supplier industry are among the leaders in Europe. Companies of both sectors are highly integrated into European value chains and are interested in cooperation with European companies. Both industries bear huge potential for the German arms and automobile industry; especially German automobile brands such as Mercedes and MAN produce in Turkey, and others such as VW, BMW and Audi source quality and inexpensive products from Turkey.

Germany is in the long term one of the most important investors in Turkey. Between 1954 and 2014 the country hosted more than six thousand companies with German capital, constituting 14.4 percent of all companies supplied with foreign capital in Turkey. The greatest share of FDIs are from Europe, which is a great incentive for Turkey to have a clear prospect for modernisation of its Customs Union with the EU.

In short, the German market and investments are of great importance for Turkey. Turkey, on the other side, is a lucrative sales market, field for investments and supplier of intermediate products for German companies. Therefore, it is of great importance for Germany to keep Turkey connected to the European economy. Germany is also interested in Turkey continuing to focus on Europe in terms of politics and security issues.

Consequently, modernising the EU–Turkey CU is mutually beneficial: the Turkish economy will grow faster if the CU is expanded to include agricultural products and services. Even the prospects for a modernised CU would contribute enormously to the further stabilisation of the Turkish economy. The opening of negotiations for modernisation of the CU would help to overcome the uncertainty among European

economic actors about Turkey's future connection to Europe. Currently, many companies hold back on investments in Turkey.

The coronavirus pandemic plunged the global economy into a deep crisis. To overcome this will take time and will not happen without socio-political tensions. There are indications that globalisation will lose speed and intensity, which will prove disadvantageous especially for the highly globalised German economy. Therefore, the modernisation of the EU–Turkey CU could help to revive bilateral trade and open up new prospects. In a world of increased regionalisation of economic activity, shortening supply chains and geopolitical uncertainty, close relationships between Turkey and the EU would mutually beneficial.

Although the modernisation of the EU–Turkey CU has been on the political agenda since 2014, no progress has been made on this issue. How can this standstill be overcome?

Implications for decision-makers are that they could better capitalise on benefits by taking the following considerations into account:

1. Construct an overall strategy to deal with Turkey

A lesson from diplomacy is: in the absence of an overall strategy, disruptive events can bring negotiations to a stop. In the EU there is neither a consensus on how to deal with Turkey nor an overall strategy. While some EU member states consider the modernisation of the EU–Turkey CU pragmatic, others – among them Germany – seem to connect transformative goals to it. Therefore, a clarification on this issue is necessary. Then, two further questions must be clarified: Will the modernisation of the EU–Turkey CU represent the final or an intermediate stage? If it is a sub-goal, to what overarching goal(s) should the modernisation of the CU be subsumed?

2. Capitalise on the opportunity opened by the economic slowdown

Current economic slowdown in Turkey gives Berlin and Brussels strong leverage to encourage Ankara to turn to democracy and rule of law. Therefore, it is essential to rationalise and de-emotionalise the debate on the EU–Turkey CU. A balanced perspective on Turkey could advance this process.

3. Balance between normative and geo-economic and geopolitical considerations

In the German debate on modernisation of the CU, not only economic, but also political considerations play a significant part. The main obstacle seems to be the authoritarian turn in Turkish domestic politics, with Turkey's political system sliding to an illiberal one-man-regime. Turkey's behaviour on the Greek border in early March 2020, encouraging Syrian refugees to cross into Greece, has pushed the prospect of negotiations further into the distance. However, it should also be taken into account that Turkey's military posture in the Eastern Mediterranean and gaining influence, for example in Libya and in the region more generally, could further shift the power relations in favour of Turkey and complicate negotiations.

4. Recognise the challenges Turkey faces and find solutions

Germany's 2020 EU Council presidency could offer a chance to bring the issue back on the political agenda of the EU. A first step – with confidence-building consequences – could be working for liberalising transport conditions for Turkish vehicles transiting between EU states. Binding this on the conditional of a democratic turn would enable Germany to stay loyal to democratic norms and values. In doing so, Berlin would be spared the criticism of appeasement and disappointing democrats and pro-Western civil society in Turkey.

5. Encourage Turkey to repeal existing trade barriers and institute reforms

Instead of waiting for democratic reforms, repealing existing trade barriers and trust-building steps by the Turkish government, the German federal government could use the prospect of negotiations on modernisation of the EU–Turkey CU as leverage to get Ankara to take these steps.

Abbreviations

Aselsan	Askerî Elektronik Sanayii A.Ş. (Military Electronic Industries)
BdB	Association of German Banks (Bundesverband deutscher Banken)
BDI	Federal Association of German Industry (Bundesverband der Deutschen Industrie)
CDU	Christian Democratic Union (Christlich-Demokratische Union)
CLEPA	European Automobile Suppliers
CSU	Christian Social Union (Christlich Soziale Union)
CU	Customs Union
DIHK	Association of German Chambers of Industry and Commerce (Deutscher Industrie- und Handelskammertag)
EU	European Union
FDI	Foreign Direct Investments
FDP	Liberal Democratic Party (Frei Demokratische Partei)
GDP	Gross Domestic Product
JETCO	Joint Economic and Trade Commission
LMM	Thales Lightweight Multirole Missile
NATO	North Atlantic Treaty Organization
OIB	Uludag Automotive Industry Exporters Association
PKK	Kurdistan Workers' Party
PPP	Purchasing Power Parity
SaSaD	Defense Industry Manufacturers Association (Savunma Sanayii İmalatçılar Derneği)
SIPRI	Stockholm International Peace Research Institute
SPD	Social Democratic Party of Germany (Sozialdemokratische Partei Deutschlands)
TAI	Turkish Aerospace Industries
TAYSAD	Association of Automotive Parts and Components Manufacturers
TGSD	Turkish Clothing Manufacturer's Association
TKMS	ThyssenKrupp Marine Systems
TÜİK	Türkiye İstatistik Kurumu (Turkish Statistical Institute)
TUSAŞ	Turkish Aircraft Industries Corporations

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