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# Turkish economy: domestic demand still waning but exports fuelled by the lira's depreciation

- **Stagflation becoming a reality, exports are a key-source of revenues for economy, especially in the automotive sector**
- **Exporters are flexible; government support is vital for exporters to gain new market shares**

**Slower domestic demand, higher borrowing costs and the lira's depreciation have slowed industry momentum**

Turkey is experiencing a severe economic slowdown coupled with a jump in inflation as a result of the sharp depreciation of the lira during 2018, which hit the country's production and consumption dynamics. Last June, Coface downgraded Turkey's country risk assessment to high (C) and the 3rd quarter was marked by a wave of sector downgrades.

Government measures have helped to counter any further rise in inflation and temporarily support some sectors, although a full recovery will take time.

On the industrial production side, the pace of growth fell to 1.6% in 2018 from around 9% in 2017 and businesses continue to suffer from slower domestic demand. In September 2018, the annual increase in producer prices rose by a record 46%, while consumer prices jumped 24%. Domestic demand-driven sectors, such as construction, retail and information and communication technologies (ICT), are among the most-affected ones. But in 2019, inflation is expected to decelerate thanks to the base effect and slower pass-through from the weaker lira.

**Despite many challenges, exports are an important source of revenue for the economy**

The worsening of the economic circumstances fostered exports, which have become an important source of revenue for the Turkish economy. In 2018, exports rose by 7% YY to USD 168 billion, with key-performances in chemicals (17%), motor vehicles (12%) and paper (11%), followed by textile and clothing (5%) and food (4%).

The automotive sector represented the biggest export product in 2018, accounting for 17% of total exports. It particularly benefited from the economic growth in European countries (final destination of 50.3% of exports) and from several Government incentives.

Turkey enjoys a high degree of comparative advantage in textile, clothing, metals and plastics. This excellence helped the country to reach a threshold in sector specialisation and possibly record additional sophistication and market share in the future. This is in line with the government's new

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2019-2020 economic programme based on rebalancing the economy with higher exports. Pharmaceuticals, chemicals, petrochemicals, energy, machinery and software sectors are considered priority in terms of investment.

Technology continues to be a less favourable sector due to its limited capabilities.

A low level of technology and limited competitiveness are restraining factors for further expansion of Turkish exports. Turkey is highly integrated in the global value chains with a close relationship with industrial production in Europe, particularly in Germany (Turkey's biggest export market). Export revenues will therefore depend on the resilience of European growth, especially in automotive and textile-clothing.

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