

# Getting Back on Track with Turkey

European countries and the United States face a delicate set of challenges in dealing with Turkey. Most have long-standing relationships with Ankara and important interests at stake in the country's future. Yet the arrangements that have historically anchored each of their strategically important ties – the prospect of Turkey's eventual EU accession and its decades-long military alliance with the United States and other NATO members – are being challenged by divisions within Turkish society and government actions that have raised questions about Turkey's role within Western structures.

In the EU, voices calling for suspension of Turkey's membership negotiations are growing louder. Talks on upgrading the partial EU-Turkey Customs Union have stalled. In the United States, more voices are arguing for a fundamental review of the US-Turkey alliance. This summer, Washington triggered a run on the Turkish lira after slapping sanctions on the Turkish government over an American pastor, Andrew Brunson, who is being held in Turkey on terrorism charges.

Turkey's economic crisis had been building even before the dustup with Washington. The Turkish lira has plunged 40% this year, inflation this month hit a 15-year high of almost 18%, and growth has slowed dramatically. In response, the central bank startled the markets by raising its key interest rate to 24%. The country may need to seek a rescue loan from the IMF.

Although relations with Ankara are strained, neither the EU nor the US has an interest in a weak or unpredictable Turkish ally. There are signs that a deal releasing Pastor Brunson may be secured by the US midterm elections in November. If true, that gesture could afford all sides an opportunity to get their relations back on track. In the economic realm, that means pushing forward with a modernized EU-Turkey Customs Union and a US-Turkey Jobs and Growth Initiative.

More than two decades ago Turkey and its European neighbors experienced a similar spate of recriminations over challenging issues. Instead of letting their relations deteriorate further, the two parties agreed to a partial Customs Union. EU conditionality tied to the Customs Union was instrumental in helping Turkey move ahead with important reforms. The result was a boom in the Turkish economy and a significant expansion of Turkish-EU commercial ties. The economic growth and accompanying reforms that resulted to some extent from the partial Customs Union also transformed Turkey from being a country of emigration to one of immigration. Countries aspiring to transition to democracy and a market economy could look to Turkey's own development for orientation, thus burnishing the EU's transformative soft power in its neighborhood.<sup>1</sup>

The partial Customs Union has brought undeniable benefits to Turkey and to its Western partners. However, the 1995 accord was only 'partial' because it was limited to industrial goods and processed agricultural goods traded between the EU and Turkey. Coal, steel, agricultural products, services and public contracts remain excluded. In May 2015, the EU and Turkey agreed to modernize and extend the Customs Union to include agriculture, services, and government procurement. The negotiations have been difficult. Rather than succumbing yet again to a complete breakdown in relations, Brussels and Ankara should view Customs Union modernization and expansion as an opportunity to once again harness the virtuous dynamic generated by the partial Customs Union two decades ago.

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<sup>1</sup> See K. Kirişçi, O. Büyüklül: The EU and Turkey need each other. Could upgrading the customs union be the key?, Brookings Institution, 29 August 2017.

A modernized Customs Union is unlikely, of course, unless Turkey is also prepared to advance key political and economic reforms. Given current strains, a new deal may not be immediately feasible. But it should not be dismissed. In fact, additional elements should be considered, such as sanitary and phytosanitary measures, investment, dispute settlement and sustainable development.

An updated Customs Union could also leverage Turkish economic interests so as to address political challenges. Procurement, for example, has the potential to challenge Turkey's informal system of political patronage. Similarly, Turkish authorities and businesses are frustrated that Turkey currently has no say on the conclusion of trade agreements between the EU and third parties. A modernized Customs Union could provide mechanisms by which any easing of tariff and non-tariff barriers for EU firms negotiated by the EU, with the US for instance, would also apply to Turkish firms.

These considerations underscore the need for Turkey and the United States to consider upgrading their own commercial ties. The two countries have been NATO allies for more than six decades. Yet relations have been heavily skewed to the bilateral military alliance and become overly dependent on the ups and downs of those contacts. US-Turkish economic relations, in contrast, have been underdeveloped. Complementing the defense relationship with more robust economic ties would offer both partners greater stability and reassurance.

Turkey has been integrated increasingly into transatlantic value chains. More than 1,700 US firms are actively operating in the Turkish market in wholesale retail, information and communications technology, construction, real estate and manufacturing sectors. US companies use Turkey as a base to expand their operations across the Mediterranean, the Caucasus and the broader Middle East. Nonetheless, US-Turkish intra-industry trade and value chains are not as developed as with the EU, except for trade in iron, steel, vehicles and auto parts. Right now, a US-Turkey bilateral free trade agreement would be difficult. As long as Turkey continues to be in the Customs Union with the EU, Ankara does not have independent trade policy authority. In addition, current bilateral frictions, Congressional attitudes towards the Turkish government and policies, and the Trump administration's trade policies also render a bilateral free trade agreement implausible as an option for the foreseeable future.

Instead, the two sides might consider an alternative: a Jobs and Growth Initiative that affirms basic conditions for an expansion of bilateral commercial ties, including mutual commitment to the sanctity of democratically established and transparent domestic laws. If framed properly, such an initiative could reinforce momentum toward domestic reforms that could be generated from an upgraded EU-Turkey Customs Union as well as from the Turkish business community and other civil society actors within Turkey.

A Jobs and Growth Initiative could complement US-Turkish security ties by giving officials and stakeholders an additional institutional framework for policy deliberation and economic engagement. It could include a business advisory network. Both sides could prioritize efforts that could promote jobs and growth, for instance improved trade in services and investments that build Turkey as a regional managerial, production and R&D hub in its broader neighborhood. The two sides could work more effectively on workforce development, help small and medium-sized enterprises that are the source of most jobs, boost innovation economies and take advantage of the transatlantic digital economy. Finding some common ground on issues such as intellectual property rights and state-owned enterprises would be useful.

An upgraded Customs Union with the EU and a bilateral Jobs and Growth Initiative with the United States could provide Turkey with important Western economic lifelines at a time when it faces serious economic challenges, while giving Brussels and Washington tools to prod Ankara to undertake needed economic reforms. That would be a win-win for the EU, the United States, Turkey and Turkey's troubled neighborhood.

**Daniel S. Hamilton**, Johns Hopkins University, School of Advanced International Studies, Washington, D.C., USA.