

T.C.  
MARMARA ÜNİVERSİTESİ  
AVRUPA TOPLULUĞU ENSTİTÜSÜ  
AB İKTİSADI ANA BİLİM DALI

**THE EFFECTS OF CUSTOMS UNION  
WITH PARTICULAR REFERENCE TO  
SELECTED ASPECTS OF  
TURKISH ECONOMY**

(Yüksek Lisans Tezi)

BARAN ALTINEL

İstanbul - 2005

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Tez Danışmanı : Prof. Muzaffer DARTAN

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## **ABSTRACT**

The purpose of this thesis is to study the effects of EU-Turkey Customs Union on Turkish Economy in terms of selected parameters and to make a general evaluation on whether it is effective for Turkey or not. In the thesis, first, regional integrations and customs union theories are briefly examined, then the development of relations between EU-Turkey is detailed and finally the effects of customs union is discussed, with an additional part covering the effects of customs union on automobile and textile clothing sectors.

Customs union is often narrowed down to foreign trade. The effects of customs union is discussed under the headings of foreign trade, FDI, financial aids, competition and other parameters like effects on way to membership, technical barriers on trade, intellectual property rights and public income.

Turkey benefited from Customs union in terms of foreign trade. The trade deficit with the EU decreased, Turkey's export to EU increased and no trade diversion occurred with third countries.

FDI inflows to Turkey did not increased as expected after Customs union due to lack of necessary stable political and economic environment and lack of legal infrastructure.

Turkey did not receive enough financial aid after Customs union, yet resources allocated blocked due to political reasons rather than economic reasons. Competition environment in Turkey developed via the Customs union, which in turn increased both producer and consumer utility.

Turkey has not yet completed legal alignment on technical barriers to trade. IPRs consciousness is improving due to Customs union harmonization. Public income did not decrease because the decrease in tariff rate is compensated with the increase in total trade. All the adjustments that Turkey has been making since 1963 will ease the negotiation process in the related chapters.

There is no serious evidence under the light of parameters discussed that Customs union, most sophisticated economic and politic action taken by Turkish Republic throughout her history, hurt Turkish economy even though the existence of negative issues like absence of political willingness, no representation in the decision-making mechanisms, aid blockings based on political reasons. Consequently, it seems that economic benefits outweigh results raised from political issues and overall effect of customs union on Turkish economy is positive.

## ÖZET

Bu tezin yazılmasındaki amaç, AB-Türkiye Gümrük Birliği'nin Türkiye Ekonomisi üzerindeki etkilerini seçili parametrelerle incelemek ve Türkiye için etkili bir uygulama olup olmadığı hakkında genel bir değerlendirme yapmaktır. Tezde, önce bölgesel entegrasyonlar ve gümrük birliği teorilerine değinilmiş, devamında AB-Türkiye arasındaki ilişkilerin gelişimine yer verilmiş, son olarak Gümrük Birliği'nin etkileri ve hazır giyim ile otomotiv sektörlerinin nasıl etkilendiği incelenmiştir.

AB-Türkiye arasındaki Gümrük Birliği genellikle sadece dış ticarete indirgenmiştir. Bu tezde Gümrük Birliği'nin Türkiye Ekonomisi üzerindeki etkileri dış ticaret, mali yardımlar, doğrudan sermaye yatırımları, rekabet ve diğer (üyelik sürecinde, ticaretin önündeki teknik engellerin kaldırılmasında, fikri mülkiyet hakları üzerinde ve kamu gelirleri üzerinde etkileri) başlıkları altında incelendi.

Dış ticaret açısından Gümrük Birliği Türkiye için faydalı olmuştur. AB-Türkiye arasındaki dış ticaret açığı azalmış, AB'ye ihracatımız artmış, üçüncü ülkelerle yapılan ticarete bir sapma oluşmamıştır.

Gerekli politik, ekonomik istikrarın ve yasal altyapının oluşmaması nedeniyle doğrudan sermaye yatırımlarında Gümrük Birliği sonrası istenilen etki görülmemiştir.

Gümrük Birliği sonrasında ekonmik nedenlerden ziyade siyasi nedenlerle Türkiye'ye yeterli miktarda mali yardım ayrılmadığı ve ayrılan yardımların da kullanımının engellendiği belirlenmiştir.

Gümrük Birliđi uyum yasaları çerçevesinde rekabet ortamı gelişmiş, bu da hem üretici hem tüketici faydasını arttırmıştır.

Ticaretin önündeki teknik engellerin kaldırılmasında Türkiye, uyum çalışmalarını henüz tamamlamamıştır. Fikri mülkiyet hakları bilinci Gümrük Birliđi sayesinde Türkiye’de yerleşmektedir. Kamu gelirlerinin artan ticaret hacmi nedeniyle azalan gümrük oranlarından etkilenmediđi gözlemlenmiştir. Gümrük Birliđi uyumu çerçevesinde yapılan 1963’den beri yapılan tüm yasal altyapı deđişiklikleri Türkiye’nin müzakere döneminde ilgili alanlarda yapması gereken mevzuat uyumunu kolaylaştıracaktır.

Türkiye Cumhuriyeti tarihinin en kapsamlı siyasi ve ekonomik kararı olan Gümrük Birliđi’nin, siyasi irade eksikliđi, ilgili karar alma mekanizmalarında yer alınamaması, mali yardımların siyasi nedenlerle engellenmesi gibi negatif yönlerine rağmen, incelenen parametreler ışığında Türkiye ekonomisine zarar verdiđine dair bir bulguya rastlanmamıştır. Sonuç olarak, Gümrük Birliđi’nin Türkiye’ye siyasi yarardan çok ekonomik yarar sağladıđı ve ekonomiyi genel olarak olumlu etkilediđi belirtilebilir.

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## ABBREVIATIONS

ASEAN	Association of South East Asian Nations
CAP	Common Agricultural Policy
CCP	Common Commercial Policy
CCT	Common Customs Tariff
CE	Conformite European
CEE	Central and Eastern European
CEN	European Committee for Standardization
CENELEC	European Committee for Electrotechnical Standardization
DPT	State Planning Institute
EC	European Community
ECSC	European Coal and Steel Community
EEC	European Economic Community
EFTA	European Free Trade Area
EIB	European Investment Bank
EP	European Parliament
EU	European Union
EURATOM	European Atomic Agency Community
FDI	Foreign Direct Investment
FTAs	Free Trade Agreements
GATT	General Agreement on Trade and Tariffs
GNP	Gross National Product
GSP	Generalized System of Preferences
IEC	International Electrotechnical Commission
IIPA	International Intellectual Property Alliance
IMF	International Monetary Fund
IPRs	Intellectual Property Rights

ISO	International Standardization Organization
NAFTA	North American Free Trade Area
NATO	North Atlantic Alliance Organization
NPAA	National Program for the Adaptation of the Acquis
OECD	Organization for the Economic Cooperation and Development
OEEC	Organization of the European Economic Community
R&D	Research and Development
TBMM	Grand National Assembly of Turkey
TERRA	Turkey Earthquake Relief and Rehabilitation Aid
TRIPs	Trade Related Aspects of Intellectual Property Rights
TSE	Turkish Standards Institute
TSE mark	Certificate of Conformity
TSEK	Conformance Certificate
TÜRKAK	Turkish Accreditation Authority
USA	United States of America
USSR	Union of Soviet Socialist Republic
WIPO	World Intellectual Property Organization
WTO	World Trade Organization
WW	World War

## I. INTRODUCTION

In the beginning of 19<sup>th</sup> century, westernizing meant modernization and civilization for Turkey. Efforts to align with the west accelerated after proclamation of Turkish Republic. Turkey was either member or among the first members of organizations like North Atlantic Alliance Organization (NATO), Council of Europe and Organization for the Economic Cooperation and Development (OECD). Turkey (then the Ottoman Empire) was officially considered part of Europe since the Paris Agreement in 1856. This agreement mostly covered Turkey from facing up to questions whether Turkey is a part of Europe or not.

EU-Turkey relations have been officially continuing for 46 years. It all started with Turkey's application for membership to newly founded European Economic Community (EEC). The most important outcome of this relationship, putting aside the decision to start negotiations, was the completion of customs union. It took 32 years from 1963 to 1995 for EU and Turkey to construct the infrastructure. The customs union between EU and Turkey is a unique one among the similes because of two reasons. It is structurally different from a customs union in the classical sense that it is not only elimination of customs duties, quotas and application of common customs levels against third countries but also it includes the harmonization of all the measures that can affect trade directly or indirectly. The second distinction is, Turkey although has to fulfill necessary obligations, does not have the right to take part in decision-making mechanisms because she is not a full member. The customs union is the last phase of the three-stage integration model foreseen on the Ankara Agreement, which constitutes the legal basis of the partnership between EU and Turkey.

It has been 10 years since the Customs Union Decision was taken and more than 9 years since it entered into force. Several studies have been done by Turkish or foreign academicians. As it stressed above customs union between EU and Turkey differs from the others by its scope and unique structure. Because of this, it has an effect on a wide area, from foreign trade to environment. This makes difficult to measure all the parameters and giving a judgement on effects of customs union accurately.

The effects of customs union is chosen as the subject on the grounds of two reasons. First one is customs union between EU and Turkey is not evaluated as it is supposed to be. Customs union is often narrowed down to foreign trade, characterized as an expensive step taken on the way to Europe and costed Turkey more than it brought. This thesis will try to show that Turkey is benefiting from customs union contrary to the general belief, in terms of foreign trade, FDI, financial aids, competition and other parameters like effects on way to membership, technical barriers on trade, intellectual property rights and public income. As stated above, in EU-Turkey case, because there are various areas affected by customs union, only the parameters that are relatively more important and parameters with enough data are taken into consideration.

The second reason is that customs union is the most sophisticated economic and politic action taken by Turkish Republic throughout her history. Thirty-two out of forty-six years of EU-Turkey relations are spent on customs union. It is one of its kind and worth more academic studies and research.

Second section of the thesis is on economic integrations and customs union. In economic integrations part, a brief historical background is provided with the reasons why economic integrations are widespread. Some well-known definitions of economic integrations will be followed by types of economic integrations. Customs union part will start by general information, which includes definition and general rules for successful formation of customs union. This section will end by an explanation of customs union theories.

Third section of the thesis is on the history of EU-Turkey relations. Section will begin by a brief history of the EU. Second part of this section will analyze past and present of EU-Turkey relations decade by decade, starting from 1959. In this part, focus will be on milestones of EU-Turkey relations. Details and importance of each of them will be explained. Third part will give concise information about the future of EU-Turkey relations particularly with respect to opening of negotiations and customs union. Fourth and last part of the section is on the institutions of EU-Turkey association, which will detail each institution one by one.

Fourth section will include the effects of the customs union. First part will analyze foreign trade effects, explaining the change in figures and composition of foreign trade starting from 1960s to the end of 2004. The success of customs union is often linked to the performance of foreign trade in public opinions. Therefore, particularly this part is more detailed. Second part will explain foreign direct investment (FDI) effects. It will show the development of FDI after customs union and compare Turkey's performance with other countries. Third part will consist of financial aid effects. In this part EU-Turkey, financial relations will be detailed. Fourth part will focus on competition by explaining the arise for need to competition, Turkey's actions on competition and what may it brought to Turkey. Fifth part will analyze other effects with four sub-divisions. They are effects on the way to membership, effects on technical barriers to trade, effects on intellectual property rights (IPRs) and effects on public income. Final part of this section will detail effects of customs union on two selected sectors: automobile and textile-clothing sector. These two sectors are chosen because what they are expecting from customs union and what customs union brought to them is very different.

In the conclusion section, the overall effects of customs union on Turkish economy will be summarized.



## **II. ECONOMIC INTEGRATIONS AND CUSTOMS UNION**

Economic integration may be defined as the institutional combination of separate national economies into larger economic blocks or communities. Economic integration can also be integrated in two senses. In a dynamic sense, it is the process whereby economic frontiers between member states are gradually eliminated, national discrimination is abolished, with the formerly separate economic entities gradually merging into a larger whole. In a static sense, it is the situation in which national components of a larger economy are no longer separated by economic frontiers but function together as an entity. Economic integration is concerned with the promotion of efficiency in resource use on a regional basis. There are various definitions and types of economic integration. Customs union, which this thesis is particularly interested in, is a basic form of integration and the one with which orthodox theory is mainly concerned.

### **2.1. Economic Integrations**

#### **2.1.1. History of Economic Integration**

The main reason of the World War (WW) I was the dispute between the European countries on distribution of colonies. England, France and Russia, the winner countries,

continued their dominance on colonies until WW II. It was nothing but Germany's greed to get what it did not get in WW I started WW II in 1939<sup>1</sup>. Unlike the first one, WW II caused a new system alternative to capitalism to emerge. The flagship of new system was the Union of Soviet Socialist Republic (USSR).

The world witnessed competition in political, economical and social area between capitalist bloc, led by the United States of America (USA), and socialist bloc, led by the USSR. This polarization accelerated economic integration movements. Economic integration movements gained considerable importance after 80's by the help of increasing openness, economic and political interdependence among the participating countries. Although economic integrations are not new to the world economy, it gained considerable attraction.<sup>2</sup>

There are several reasons why the integration movements are so widespread.<sup>3</sup> First of all the integration movements leads trade barriers among the participating countries to disappear. Because of elimination of fiscal, technical and administrative barriers, the participating countries open their market to each other. This provides benefiting from a larger market and a rise in intra-regional trade. Lower transportation and transaction costs together with geographic proximity create more economic gains for participating countries. Secondly, the fear of being excluded from trade blocs and to be subject to the discriminatory trade practices may also be a driving force in the formation of the integrations and in the participation to such integrations. Thirdly, the inefficiency of the multilateral agreements -which has defects in providing cooperation among a large number of countries due to high transaction costs-,<sup>4</sup> may also be a factor for the formation of the integrations. Fourthly, political reasons are also an important determining factor for the formation of regional integrations. North American Free

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<sup>1</sup> Mustafa Çelen, Globalleşme Sürecinde Bölgesel Ekonomik Entegrasyonlar. İstanbul: Süreç Gümrük Birliği Özel Sayısı, 1995, P:29

<sup>2</sup> Sait Akman & Muzaffer Dartan, The Regionalism In The World Economy: Novel Expectations From An Old Habit. İstanbul, Marmara Journal Of European Studies, 1998, Volume:6 No:1, P:3

<sup>3</sup> Osman Küçükahmetoğlu, Lecture Notes. İstanbul:2002

<sup>4</sup> Sait Akman & Muzaffer Dartan, The Political Economy Of Regionalism In World Trade. İstanbul, Marmara Journal Of European Studies, 1997, Volume:5 No:1-2, P:45

Trade Area (NAFTA), Association of South East Asian Nations (ASEAN), European Union (EU) is most known examples of regional integration. There is a widespread belief that the EU constitutes the most advanced regional integration among currently existing ones and is also the largest common market in the world economy in terms of its scope and coverage of established institutions, timetables of integration, and a standardized process of decision-making.

The total number of notified preferential agreements in force is 206. In addition, around 30 agreements were signed between 2003 and 2004 and are awaiting entry into force and approximately 60 agreements are in the negotiations/proposal stage. More than third of global trade takes place between countries that have some reciprocal trade agreement.<sup>5</sup>

### **2.1.2. Definitions of Economic Integration**

In developed market economies, integration is taken to be a way of introducing the most profitable technologies, allocate them in the most efficient way and foster free and fair competition.

In the former socialist countries, integration meant the planning of the development of certain industrial activities.

In the developing countries, integration is one of the tools for economic development.

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<sup>5</sup> UN, World Economic Situation and Prospects 2005. New York:UN Publications, 2005, P:38

There are plenty of definitions given by economists. The well-known and widespread accepted definitions are listed below.<sup>6</sup>

### **2.1.2.a. Tinbergen's Definition**

Tinbergen gave one of the first definitions of integration in 1954. He splitted integration into two; positive integration and negative integration. According to Tinbergen, negative integration is the removal of discriminatory and restrictive institutions and the introduction of freedom for economic transactions. Removal of tariffs and quotas are examples to negative integration. Positive integration, on the other hand, is the adjustment of existing and the establishment of new polices and institutions. Introduction of common economic policies is an example of positive integration.<sup>7</sup>

### **2.1.2.b. Robson's Definition**

Robson, in 1998, argued that economic integration is concerned with the promotion of efficiency in resource use on a regional base. Necessary conditions for its full attainment included the elimination of all barriers to the free movement of goods and factors of production within the integrated area and discrimination based on nationality amongst the members of the group in that respect. Robson defines full integration as freedom of movement of goods and factors of production and an absence of discrimination. Freedom of movement for factors is not allowed for in some types of international economic integration hence this definition cannot be applied to all integrations.<sup>8</sup>

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<sup>6</sup> Osman Küçükahmetoğlu, Lecture Notes. İstanbul:2002

<sup>7</sup> Jan Tinbergen, International Economic Integration. Second, Revised Edition. Amsterdam: Elsevier Publishing Company, 1965, P:3

<sup>8</sup> Peter Robson, The Economics of International Integration. Third Edition. London: Routledge, 1998, P:2

### **2.1.2.c. Molle's Definition**

Molle, in 1997, argued that economic integration is gradual elimination of economic frontiers between independent states. As a result, the economies of these states end up functioning as one entity.<sup>9</sup>

### **2.1.2.d. Pelkman's Definition**

According to Pelkman, in 1997, economic integration is the elimination of economic frontiers between two or more economies. In turn, economic frontier is any demarcation over which actual and potential nobilities of goods, services and production factors.<sup>10</sup>

### **2.1.2.e. Balassa's Definition**

Ballassa, in 1973, argued that economic integration is a process and a state of affairs. As a process, integration means the removal of discrimination between different states, while as a state of affairs it means the absence of different forms of integration.<sup>11</sup>

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<sup>9</sup> William Molle, The Economics of European Integration. Third Edition. Aldershot: Ashgate, 1998, P:8

<sup>10</sup> Jacques Pelkmans, European Integration. New York: Longman, 1997, P:2

<sup>11</sup> Bela Balassa, The Theory of Economic Integration. Illinois: Homewood, 1961, P:1

### **2.1.2.f. El Agra's Definition**

El Agra, in 1999, claimed that regional integration is concerned with the discriminatory removal of all trade impediments between at least two participating nations and with the establishment of certain elements of cooperations and coordination.<sup>12</sup>

There is a wide consensus on three issues of the definition of economic integration. First one is, economic integration refers to division of labor. Second one is, economic integration involves mobility of goods or factors or both. Third one is, economic integration related to discriminatory or non-discrimination in the treatment of goods and factors.

### **2.1.3. Types of Economic Integration**

#### **2.1.3.a. Preferential Tariff Agreement**

The rates of tariffs on trade among participating countries are lower compared to rate of tariffs on trade charged with third countries.

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<sup>12</sup> Ali M. El-Agra, General Introduction, Ali M.El-Agra (ed.), European Union, Fifth Edition. London: Printice-Hall, 1998, P:1

### **2.1.3.b. Free Trade Areas**

It is an agreement among countries about the elimination of all tariff and quantitative restrictions on mutual trade. Every participating country retains its own tariff and other regulation of trade with third countries. The basis of this agreement is the rules of origin. These rules prevent trade deflection, which is import of goods from third countries into the area by a country that has a relatively lower external tariff than the partner country, in order to re-export the good to partner country. European Free Trade Area (EFTA) constitutes a good example of free trade areas.

### **2.1.3.c. Customs Union**

Participating countries not only remove tariff and quantitative restriction on their internal trade but also introduce a common external tariff on trade with third countries. There is coordination between the participating countries in international negotiations about trade and tariffs.

### **2.1.3.d. Common Market**

Apart from customs union, free mobility of factors of production exists. Common regulations and/or restrictions on the movement of factors with the third countries are introduced. That is common market consists of an internal market and common external regulation for both products and production factors. The European Community (EC) was an example for common market.

### **2.1.3.e. Monetary Union**

The currencies of the participating countries are linked through irrevocably fixed exchange rates and are convertible or one common currency circulates in all participating countries. Capital movements within the area are free. The EU is a typical example for monetary union.

### **2.1.3.f. Economic Union**

Economic union means a high degree coordination or even unification of the most important policy areas such as fiscal, monetary, industrial, regional, transport and other economic policies.

### **2.1.3.g. Total Economic Union**

It combines the characteristics of the economic and the monetary union. There is a single economic policy and supranational government with great economic authority.<sup>13</sup>

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<sup>13</sup> William Molle, The Economics of European Integration. Third Edition. Aldershot: Ashgate, 1998, P:12



**TABLE 1.1**  
**The Types of Economic Integration**

	Liberalization Of Trade	CCT	Liberalization Of Factors Of Production	Common Currency	Harmonization Of Economic Policies	Single Economic Policy
FTA	x					
CU	x	x				
Common Market	x	x	x			
Monetary Union	x	x	x	x		
Economic Union	x	x	x	x	x	
Full Eco. Union	x	x	x	x	x	x

Source: Osman Küçükahmetoğlu, Gümrük Birliği. İstanbul: N/A, 2000, P: 12

## 2.2. Customs Union

### 2.2.1. General Information on Customs Union

In practice there are three fundamental legal documents where in customs union is defined. These are General Agreement on Trade and Tariffs (GATT) Article 24, Treaty of Rome Article 9 and a verdict of La Hayes International Justice Court. Article 9 of the Rome Treaty, which constitutes basis of the EU's CU states that "the Community shall be based on a customs union which shall cover all trade in goods and which shall involve

the prohibition between member states of customs duties on imports and exports and of all charges having equivalent effect, and the adaptation of a common customs tariff in their relations with third countries”. Article 9 also defines the three prerequisite of customs union; the elimination of tariffs among member countries, the adaptation of common customs tariff to third countries and the distribution of customs revenue among member countries according to a formula.

Formation of customs union provides a movement towards free trade however, it does not provide a global free trade. Since, the free trade is kept among the member countries and common customs tariff (CCT) is applied there is a discrimination against the non-member countries.

The CCT differentiates customs union from free trade area. In free trade areas, member countries are free to adopt their own tariff levels where as in customs union member countries are forced to adopt a single tariff rate. Customs union increases trade among member countries and decreases their trade with third countries.<sup>14</sup>

First known customs union formation was in Germany in 1834. Today’s largest customs union is the EU.

According to traditional customs union theory, the formation of a customs union has a trade creation and trade diversion effect. Trade creation happens when domestic production is replaced by a lower price import from the partner country. Trade diversion on the other hand happens when low price import from third country is replaced by a high price import from the partner country. The balance between trade creation and trade diversion determines welfare gain or loss respectively.

Although there are, no rules set for successful formation, in the sense of trade creation, of customs union there are some generalizations.<sup>15</sup> First, having a larger customs union is better than having a smaller one. Because a large customs union may include most efficient producer of different goods, which decreases the possibility of trade diversion. Secondly having higher tariff rates in the home country and in the

<sup>14</sup> Keith Penkth, The Customs Union, in Frank McDonald and Stephen Dearden (eds.), European Economic Integration. Second Edition. London and New York: Longman, 1994, P:1

<sup>15</sup> Osman Küçükahmetoğlu, Gümrük Birliği. İstanbul: N/A, 2000, P:45-46

partner country in the initial situation and the smaller CCT after the formation of the customs union increases trade creation effects. Thirdly, the more competitive economies of member countries the more possibility of trade creation. It is because in competitive economies where the member countries produce the same commodity at similar cost levels, less efficient member country may tend to import, instead of producing domestically, which increases trade creation. Fourthly, when member countries are geographically close to each other, that is, they already trade with each other; the possibility of trade diversion is slight. Fifthly, if the demand for member countries' goods is greater than those of non-member countries' the possibility of trade creation increases.

### **2.2.2. Customs Union Theories**

#### **2.2.2.a. J. Viner**

Viner changed the belief that customs union is a step forward to free trade by saying that customs union may also be a step towards protectionism. He argued that a customs union amounts to free trade between the members and protectionism vis-à-vis the outside world. These two effects of a customs union are trade creation and trade diversion respectively, implying the impacts of the customs union on welfare. His analysis is based on some strict assumptions like perfect competition in the commodity and factor markets, full employment, and perfect factor mobility within individual countries but not among countries, foreign trade equilibrium and transport costs, which are not included since tariffs, are assumed the only trade restriction. In a country where there was no import from the other countries, before the formation of customs union, due to the high tariff rates and lower prices of the domestic products, there will be a shift in the supply source from a higher to a lower cost of supply after the formation of the

customs union. This is called trade creation effect of the customs union, which implies a reduction in the production of domestic product and a rise in the import from partner country. On the other hand, Viner assumed that there are some commodities, which one of the member countries newly exports it from other member country, although it imported them from the third country before the formation of the customs union. There is a shift from a low cost third country to a higher cost member country. This is called trade diversion effect of the customs union. Therefore, the trade creation and trade diversion effects of the customs union are the determining factor for the establishment of a customs union.<sup>16</sup> At this point, Viner's contribution to customs union theory appears. Viner by differentiating trade creation and trade diversion, challenged the common belief that preferential moves to free trade is necessarily welfare improving. A low average tariff rates, a greater potential scope for the division of labor, a larger economic area and a comparative advantage among the member countries, are the examples of advantages of customs union given by Viner.

### **2.2.2.b. R.G. Lipsey**

Lipsey criticized Viner's analysis and argued that a simple conclusion that trade creation is efficient and trade diversion is inefficient may not be valid and a country may gain welfare although it forms a customs union, which results from trade diversion effects. He said that *"...when consumption effects are allowed for, the simple conclusions that trade creation is 'good' and trade diversion is 'bad' are no longer valid. Although the distinction between trade creation and trade diversion is fundamental for classifying the changes in production consequent on the formation of a customs union, it is one on which welfare conclusions can be based."*<sup>17</sup> To explain Lipsey referred to two opposite effects of the trade-diverting customs union. On the one hand, in a trade-

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<sup>16</sup> Jacob Viner, The Customs Union Issue. New York: Carnegie Endowment for International Peace, 1950, P:44

<sup>17</sup> R.G. Lipsey, The Theory of Customs Union: Trade Diversion and Welfare , *Economica*, vol:24, 1957, P:40-46

diverted customs union, the country shifts its purchases from a lower to a higher cost source of supply and it becomes necessary to export a larger quantity of goods in order to obtain any given quantity of imports. Secondly, with the elimination of tariffs, the divergence between domestic and international prices is eliminated. It forces the consumers in the country to adjust their purchases to a domestic price ratio. It now becomes equal to the transformation rate at which export commodity is transformed into the import commodity by means of international trade. Lipsey concluded that the final welfare effect of the trade-diverted customs union must be the net effect of these two opposing tendencies the first working to lower the welfare and the second to raise it.

#### **2.2.2.c. C.A. Cooper-B.F. Massell**

Cooper and Massell argued that unilateral tariff reductions are better than the customs union, since this kind of policy lead to trade creation effects without any trade diversion. When a customs union is formed, the same commodities imported from a partner country, but at a higher cost will replace the commodities formerly imported from outside sources. The shift to higher cost source of supply tends to lower country's real income and consequently consumer welfare. According to Cooper and Massell developing countries still tends to choice forming/participating to customs union because if a given level of aggregate import competing industrialization were the objective, the cost of it to developing countries with small markets could be reduced but unions that permitted trade of industrial production among themselves while maintaining protection against the producers of developed countries.<sup>18</sup>

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<sup>18</sup> C. Cooper, B. Massell, A New Look at Customs Union Theory, The Economic Journal, vol:75, 1965, P:742-747

#### **2.2.2.d. J.E. Meade**

Meade generally accepted Viner's assumptions, yet he considered Viner's arguments inadequate. He tried to find out a balance between the economic losses resulted from the trade diversion and economic gains resulted from the trade creation. Meade argued that in the case of trade diversion, although the cheaper third country is left out, the people in one of the member country will want to buy more commodities from the partner country than they wanted to buy from the lower third country, due to lower prices, because of the removal of the tariffs. This would result in an additional consumption and demand, which must be taken into account when the welfare effect of a customs union is calculated. Meade also argued that the customs union might have trade creation effects. His example was, there is a country that produces its needs domestically, since it is the cheapest way. This means there was no trade before the formation of customs union. After the formation of customs union, with the removal of tariffs, the commodity, which is produced in the member country, becomes cheaper and the country may prefer to import it rather than to produce it at home. This may lead to trade creation.<sup>19</sup>

#### **2.2.2.e. M. C. Kemp-H. Y. Wan**

M.C. Kemp and H.Y. Wan contrary to Viner's approach argued that any group of countries could always form a customs union with a CCT and that had two desired properties; the non-member countries welfare would not change whereas the member countries welfare would improve. This theory lies on two assumptions. First, the CCT should be arranged in a way that it should not affect the amount of trade realized among these countries before the formation of the customs union. Second member countries of the customs union should apply countervailing duties as a whole, which enable the

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<sup>19</sup> J.E. Meade, The Theory of Customs Union, in P. Robson (ed.), International Economic Integration, Great Britain: Chaucer Press, 1971, P:49-57

member countries to continue trade relations with the non-member countries so the trade diversion effects disappear. According to M.C. Kemp and H.Y. Wan, the member countries of the customs union may increase their gains and benefits without deteriorating the welfare levels of the non-member countries. Since the customs union leads to a net welfare gain, it is possible to increase the scope of the customs union by covering the whole world. They said that “...let any subset of the countries form a customs union. Then there exists a common tariff vector and a system of lump-sum compensatory payments, involving only members of the union, such that there is an associated tariff-ridden competitive equilibrium in which each individual, whether a member of the union or not, is not worse off than before the formation of the union.”<sup>20</sup> There are some practical difficulties about the application of this theory, since it merely provides proof of the theoretical existence of such unions but do not provide any guidance as to the necessary and sufficient conditions that such unions needs to satisfy.

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<sup>20</sup> M.C. Kemp, H.Y. Wan, An Elementary Proposition Concerning the Formation of Customs Union, Journal of International Economics, vol:6, 1976, P:95-97

### **III. HISTORY OF TURKEY-EU RELATIONSHIP**

Turkey began "westernizing" its economic, political and social structures in the 19th century. Turkey chose Western Europe as a model following the First World War and the proclamation of the Republic in 1923. Turkey has ever since closely aligned itself with the West and has become a founding member of the United Nations, a member of North Atlantic Alliance Organization (NATO), the Council of Europe, the Organization for the Economic Cooperation and Developments (OECD) and an associate member of the Western European Union.

#### **3.1. The History of the EU**

Europe who escaped from the chaos of Middle Ages via mercantilism and enlightenment has established today's civilization infrastructure. The rose of the idea of nationalism and the idea of the United Nations of Europe are simultaneous. Philosophers and thinkers like Kant, Saint Simon, Victor Hugo has constituted basis of the idea. For instance Victor Hugo during one of his speeches in French Parliament said; "Like how the USA has crowned the new world, there shall be a time when United Nations of Europe will crown the old world. Accepted or denied the idea of unity will continue its maintenance as a thousand year dream of a continent continuously torn down." Throughout the history kings, politicians and religious men ran after this dream.



In the 20th century, the idea became necessary rather than a dream. After WW II, the old world was economically devastated. Furthermore, the world was dominated by two super-powers, the USA and the USSR. European countries were aware of the fact that none of them stands against these two super-power countries individually. Therefore, initiatives to unite Europe were more than ever. The list of movements is astonishing; United Europe, French Council to Unite Europe, Federalist European Union, Union of European Parliaments and etc.<sup>21</sup>

First successful examples on the road to unite were Organization of the European Economic Community (OEEC) and BENELUX, which were established by the Netherlands, Belgium and Luxembourg in 1948. OEEC's aim was to provide economic cooperation among the states of Europe to constitute a strong Europe. Important steps towards economic liberalization were taken during the time of OEEC. Later on, the USA, Canada, Spain and West Germany joined and the organization revised to Organization of Economic Cooperation and Development (OECD). OECD today with 30 members has a 76% share of world trade.<sup>22</sup>

On 09 May 1950, the then French Foreign Minister Robert Schuman, who has influenced from the then Head of French Planning Institute Jean Monnet, announced that the rich coal and iron mines in area of Ruhr are going to be operated with West Germany and added that any European country could join. This invitation was positively responded by Italy, Belgium, the Netherlands and Luxembourg. After a year of negotiations on 18 April 1951 six countries signed the treaty establishing European Coal and Steel Community (ECSC), which is also known as Paris Treaty. After successful implementation of Paris Treaty, two more initiatives were taken immediately. First one was European Defense Community in 1952, second one was European Political Union in 1953. Unfortunately, both of them ended with failure. These led to the fact that no political union can be constituted before the completion of economic union. The success of ECSC encouraged the signing countries to consider covering more economic area.

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<sup>21</sup> SÜREÇ, Gümrük Birliği Özel Sayısı. İstanbul: N/A, 1995, P:40-45

<sup>22</sup> OECD, Annual Report 2004. Paris: OECD, 2005, P:8

Consequently, European Economic Community (EEC) and European Atomic Agency Community (EURATOM) were established in Rome on 25 March 1957.

In 1969 ESCS, EURATOM and ECC were merged into European Communities and in 1993 because of Maastricht Treaty EC took the name European Union.

The first founding treaties of EU were signed by six countries. In 1973 England, Denmark and Ireland joined. Then in 1981 Greece, in 1985 Spain and Portugal and in 1995 Sweden, Austria and Finland joined. With the last wave of enlargement, 10 new countries (South Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia) joined and the EU has now 25 members. There are four candidate countries, which are Bulgaria, Romania (these 2 countries are expected to become member in 2007) Croatia and Turkey. The EU 25 has become a giant with 459 million population in 2004 and €1.800 billion intra trade in 2003.<sup>23</sup> The EU is going to start negotiations with Turkey negotiations on October 2005 simultaneously with screening process.

### **3.2. Past and Present of EU-Turkey Relations**

Turkey has been involved with EU more than 45 years. This is a lot of time to do many things. However, at the end of this 45-year relationship Turkey is still a candidate country who is not expected to become a member for another 10-15 years. From what aspect you look the ultimate fact will not change; the relationship is not where it was supposed to be. Each side has its own reasons, and it is not this paper's aim to dig into it. The milestones of the EU-Turkey relationship will be highlighted below decade by decade starting from 1959 to end of 2004.

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<sup>23</sup> The European Commission, Portrait of the European Union. Brussels: Publication Office, 2004 P:4,22

### 3.2.1. Relations Between 1959-1969 (Ankara Agreement)

On July 1959 shortly after the establishment of the EEC, Turkey made her application to join. Turkey's application to an organization, which was newly established, had two reasons. First, Turkey did not want to be left outside of a political union in the long term. Second, Turkey did not want to let Greece enjoy all the economic benefits alone. This may explain why Turkey applied for membership only 16 days after Greece.<sup>24</sup> On 11 September of the same year, EEC Council of Ministers accepted both countries applications. Between 28-30 Septembers, the Commission and Turkey made first preparatory meetings.

The EEC's response to Turkey's application in 1959 was to suggest the establishment of an association until Turkey's circumstances permitted her accession. The negotiations resulted in the signature of the Agreement Creating an Association Between the Republic of Turkey and the European Economic Community, which is also called the Ankara Agreement, on 12 September 1963. The Ankara Agreement represented to GATT's approval on 12 February 1964. After the approval of Grand National Assembly of Turkey (TBMM) and member states entered into force on 1 December 1964. The Ankara Agreement consists of:

- i. Main Agreement 33 Articles,
- ii. Provisional Protocol 11 Articles,
- iii. Financial Protocol 9 Articles,
- iv. Final Act
- v. Provision

Among these documents Main Agreement covers the issues like aim of association and relationship, principles of customs union, free movement of persons, goods, services and

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<sup>24</sup> DTM, AB ve Türkiye. 5. Baskı. Ankara: 2002, P:310

capital, harmonization of technical legislation, economic and commercial policies, institutions of association and settling disputes.

The Ankara Agreement, which rests on article 238 of Treaty of Rome, sets fundamental principles of association. That is Ankara Agreement like funding treaties of the EU is a frame agreement. Details are to be set with protocols, which form an integral part to the Ankara Agreement.<sup>25</sup>

The principles of the Ankara Agreement are:

- i. To establish ever closer bonds between the Turkish people and the people in EEC,
- ii. To ensure a continuous improvement in living conditions in Turkey and in the EEC through accelerated economic progress and the harmonious expansion of trade and to reduce the disparity between the Turkish economy and the economies of the Member States of the Community,
- iii. To grant economic aid to Turkey during a given period,
- iv. To improve the standards of living of Turkish people, which will facilitate the accession of Turkey to the Community at a later date,
- v. To preserve and strengthen peace and liberty by joint pursuit of the ideals underlying the Treaty of Rome.

The objective of the agreement is to promote the continuous and balanced strengthening of trade and economic relations between the EU-Turkey while taking full account of the need to ensure an accelerated development of the Turkish economy and to improve the level of employment and living conditions of the Turkish people.<sup>26</sup>

In order to attain the objective a customs union will be implemented through three stages, preparatory stage, transitional stage, final stage. Preparatory stage, which was planned to last for 5 years, aimed to strengthen Turkish economy so that Turkey can fulfill her obligations in transitional and final stages. With the entry into force of the Additional Protocol in 1971, preparatory stage ended. Transitional stage, which was planned not to last longer than 12 years, aimed to establish progressively a customs union between

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<sup>25</sup> Ankara Agreement, Article 30

<sup>26</sup> Ankara Agreement, Article 2, Paragraph 1

Turkey and the Community and to align the economic policies of Turkey and the Community more closely in order to ensure the proper functioning of the association. Final stage was based on customs union and closer coordination of the economic policies of the EU and Turkey. There was not preset time limit; it was left to signing parties.<sup>27</sup>

Provisional Protocol detailed the exceptions applied to then four important Turkish exports; tobacco, dried grapes, dried figs and hazelnuts.

Financial Protocol was about the € 175 million loan that is agreed by the EEC Council to be given to Turkey to strengthen her economy.

The Ankara Agreement cannot be accepted only as a customs union agreement since it allows taking of all measures to form a common market between the parties, following the establishment of the customs union. Moreover, it revealed potential as a framework agreement for an association leading to full membership. In this context, the agreement goes beyond the level of commitments and it constitutes a reliable and effective basis for more than just cooperation, facilitating a partial integration of Turkey into the EU. The Ankara Agreement opens the way to full membership and does not have an annulment article. That means, agreement will be valid until its objectives are fulfilled.

On 9 December 1968, during the extended period of preparatory stage, negotiations on the Additional Protocol started. Negotiations lasted until 6 July 1969.

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<sup>27</sup> Ankara Agreement, Article 28

### 3.2.2. Relations Between 1970-1979 (Additional Protocol)

Negotiations ended successfully on 22 July 1970 and the Additional Protocol signed on 23 November 1970. Because the member states parliaments' approval is required commercial decrees were entered into force via a Provisional Protocol on 1 September 1971. This agreement closed the preparatory stage and started the transitional stage, yet it officially started on 1 January 1973 with the entry into force of Additional Protocol. The Additional Protocol approved in TBMM on 5 July 1971 and represented to GATT's approval on 30 September 1971. Composition of protocol is:

- i. Main Part           64 Articles,
- ii. Six Annexes       23 Articles,
- iii. Financial Protocol 13 Articles.

Main part of the Additional Protocol lays down conditions, arrangements and timetables for implementing the transitional stage referred to in Article 4 of the Ankara Agreement.<sup>28</sup> In other words, Additional Protocol established a timetable of technical measures to attain the objective of customs union.

Contrary to the Ankara Agreement, Additional Protocol has balanced characteristics. This means both sides, the Community and Turkey has mutual obligations in this period, although they are not in an equal weight. The development of the balanced and mutual relations, the strengthening of the customs union, the approximation of the economic policies between two sides and the development of the common activities are the most important principles of the Additional Protocol. The Protocol includes some implementation provisions about the policy approximation, establishment of a customs union for the industrial products, implementation of a preferential regime for the agricultural products, free movements of products, labor, services and capital within a

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<sup>28</sup> Additional Protocol, Article 1

specific time schedule, foreign investment, the right for residence, the coordination of economic policies, competition and state aids, economic aid and export subventions.<sup>29</sup>

The principles of the Additional Protocol in few words are:

- i. Mutual and balanced obligations,
- ii. The progressive establishment of a customs union
- iii. The closer alignment of the economic policies

Additional Protocol is an integral part of the Ankara Agreement and it is a practice agreement, which filled the frame, drew by the Ankara Agreement.

Ankara Agreement was signed with the ECC, just one of the communities. Some iron and steel products were within the authority of the ECSC and they were not covered by the Ankara Agreement. This is solved with an additional protocol, which anticipated establishment of a free trade area for those products.

Additional Protocol eliminated customs duties and quantitative restrictions between the EC and Turkey.<sup>30</sup> According to the related articles of agreement, the EEC accepted to abolish customs duties and charges having equivalent effect on imports from Turkey as from the day the Additional Protocol come into force with the exception of some petroleum and textile products.<sup>31</sup> Whereas Turkey would do the same within a timetable. First reduction would be made on the entry into force of the Protocol. Second and third reductions would be made in 3 and 5 years respectively, after first reduction. Fourth and subsequent reductions would be made each year in a way that final reduction would be made at the end of 12th year. For some products, Turkey would do the same reduction in 22 years instead of 12 years.<sup>32</sup> The timetable for these products would be a reduction of 5% on each duty on the entry into force of the Protocol, 3 further reductions each of 5% in 3, 6, 10 years later. It will be followed by eight more reductions each of 10% in 12, 13, 15, 17, 18, 20, 21, 22 years after the first reduction.

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<sup>29</sup> Rıdvan Karluk, Gümrük Birliği Dönemecinde Türkiye:Gümrük Birliği Ne Getirdi Ne Götürdü?. Ankara: Turhan Yayınları, 1997, P:29

<sup>30</sup> Additional Protocol, Articles 7-17 and 21-31

<sup>31</sup> Additional Protocol, Annex 1-2

<sup>32</sup> Additional Protocol, Annex 3

The obligations due to elimination of quantitative restrictions are similarly distributed. The EC would abolish all quantitative restrictions on imports from Turkey. On the other hand, Turkey would progressively abolish quantitative restrictions on imports from the Community not later than 22 years after the entry into force of the Protocol.

Turkey also accepted to apply the CCT until the end of transitional stage, which is 12 years from the entry into force of the Protocol.<sup>33</sup>

Agriculture is one of the important issues of the Protocol. According to the Protocol, there will not be free movement of agricultural products unless Turkey adjusts her agricultural policy to Common Agricultural Policy (CAP). In the meantime, the Council of Association would scope details of preferential treatment in trade of agricultural products between the EC and Turkey. Turkey's 76% of agricultural export benefited from preferential treatment whereas it is only 7% for the Community.<sup>34</sup>

Additional Protocol forced a wider integration beyond customs union. Because of this point of view not only free movement of products but also free movement of workers, capital and services are considered. However they were never backed up, expressions were far from binding, just intentions for the future.

The EC with some exceptions abolished all restrictions on imports from Turkey and let Turkish exported products to circulate freely in the Community market. However, the Community in 1976 and 1980 applied quotas to Turkish textile products. The share of textile products was 50% of the total exports. Therefore, it was a serious trade restriction against Turkey. The Community did not fulfill its obligations on the free movement of workers, which was supposed to be completed in 1986.

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<sup>33</sup> Additional Protocol, Articles 18-20

<sup>34</sup> DTM, AB ve Türkiye. 5. Baskı. Ankara: 2002, P:333-334



Turkey on the other hand was not more loyal to her obligations than the Community. After first and second reductions in 1973 and 1976 respectively, Turkey postponed the third reduction in 1978 referring to the Article 60 of the Protocol.<sup>35</sup>

Financial Protocol detailed provisions of the € 220 million loan given to Turkey through European Investment Bank (EIB).

The Protocol covered industrial products and processed agricultural products. Traditional agricultural products will be included in customs union after Turkey's adaptation of her agricultural policy to the Community's CAP. The EC and Turkey established a system for processed agricultural products in which parties differentiate between the agricultural and industrial components of the duties applicable to those products and abolished the duties for the industrial component.

### **3.2.3. Relations Between 1980-1989 (Application for Membership)**

The relations between Turkey and the EC stagnated following the military coup on 12 September 1980. On 16 September 1986, the EC-Turkey Association Council met after a long time. Relations started again. Turkey after a short time decided to apply for membership, based on EEC Treaty article 237, which gave any European country the right to apply. The Ankara Agreement and Additional Protocol's obligations were not fulfilled by both sides. Relations were still healing after a long period. Turkey's intention to apply for membership surprised the Community. Community asked Turkey to postpone her application and suggested that both sides should focus on customs union instead. The then West Germany Foreign Minister Mr. Genscher in a meeting expressed

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<sup>35</sup> First paragraph of Article 60 of the Additional Protocol states: "If serious disturbances occur in a sector of the Turkish economy or prejudice its external financial stability, or if difficulties arise which adversely affect the economic situation in a region of Turkey, Turkey may take the necessary protective measures."

Community's point of view: "*You are making very big mistake*".<sup>36</sup> Nevertheless, Turkey did apply for full membership on 14 April 1987. Turkey applied despite strong opposition of Community on the grounds of these major political and economic reasons.<sup>37</sup>

- i. Turkey's advantages from the Protocol turned to disadvantages in consequence of Community's actions like not including Turkey into Generalized System of Preferences (GSP) and making complimentary concessions to Mediterranean countries.
- ii. Community's first wave of enlargement was towards north and second one was towards south. First wave created the textile quota problem. Last wave affected Turkey more, because Turkey's and these countries export products are similar. It is unavoidable that this will affect Turkey's export performance and relations with the Community.
- iii. Turkey's level of relationship, association, with Community did not let enough financial aid transfer. Turkey wanted to enjoy the benefits membership, mainly Community funds.
- iv. When Greece applied for membership in 1975, Turkey did not move fast. It would have been different if Turkey had applied simultaneously with Greece. Despite the written guarantee, Greece tried much to block Turkey almost in everywhere.
- v. Every enlargement makes things difficult for Turkey and automatically hardens Turkey's membership.

The Council forwarded Turkey's application to the Commission for preparation of an opinion. The Commission adopted its opinion on 18 December 1989, 2.5 years after Turkey's application which is the longest among all similar. The Commission's opinion, 135 pages in total -10 pages of Opinion, 125 pages of the consequences and implications of Turkish accession-, which was endorsed by the Council underlined Turkey's eligibility

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<sup>36</sup> Mehmet Ali Birand, Türkiye'nin Gümrük Birliği Macerası 1959-1996. Dokuzuncu Baskı. İstanbul, Miliyet Yayınları, 1996

<sup>37</sup> Rıdvan Karluk, Gümrük Birliği Dönemecinde Türkiye:Gümrük Birliği Ne Getirdi Ne Götürdü?. Ankara: Turhan Yayınları, 1997, P:67-73

for membership, yet deferred the in-depth analysis of Turkey's application until the completion of Single Market in 1992. This is stated in the Opinion: "Commission is of the opinion that it would be inappropriate for the Community - which is itself undergoing major changes while the whole of Europe is in a state of flux - to become involved in new accession negotiations at this stage. Furthermore, the political and economic situation in Turkey leads the Commission to believe that it would not be useful to open accession negotiations with Turkey straight away."<sup>38</sup>

#### **3.2.4. Relations Between 1990-1999 (Customs Union Decision)**

On 7 June 1990, the Commission adopted a set of proposals, also called the Matutes Package. It included:

- i. Completion of the customs union,
- ii. The resumption and intensification of financial cooperation,
- iii. The promotion of industrial and technological cooperation and
- iv. The strengthening of political and cultural ties.

The Council due to the Greek veto never approved the package.

On 21 January 1992, EC and Turkey signed a Technical Cooperation Programme. On 28 September 1994, European Parliament (EP) froze the activities of EC-Turkey Joint Parliament, due to arrest of the DEP deputies. However, relations came back to normal less than a year. On 6 March 1995 the EU-Turkey Association Council took 1/95 decision, also known as customs union decision. Sometimes it is understood as a treaty like the Ankara Agreement or the Additional Protocol. However, this is a decision, an

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<sup>38</sup> Commission Opinion on Turkey's Request for Accession to the Community, Articles 10-11

implementation document of the legal conditions, which were defined earlier by the Additional Protocol.<sup>39</sup> This decision finished the transition stage and defined the conditions, timetable and methods for Turkey to align her legal infrastructure to the EU's commercial policy and competition policy. The aim of the Decision 1/95 is to bring free movement of industrial products and the processed agricultural products, equal conditions for trade and free competitive environment. The Customs union Decision composed of 66 articles, 17 statements and 10 annexes. It also included 2/95 Decision and a resolution about the improvement of the EU-Turkey relations and a protocol.

The first chapter of the Decision is about the free movement of goods and commercial policy. It covers the movement of industrial products in Articles 2-3, the elimination of customs duties and charges having equivalent effect in Article 4, the elimination of quantitative restrictions and measures having equivalent effect -including technical barriers- in Articles 5-11, the commercial policy in Article 12, the CCT and preferential tariff policies in Articles 13-16, and processed agricultural products in Articles 17-24. The second chapter is about the agricultural products covered in Articles 24-27. The third chapter is about the customs provisions covered in Articles 28-30. The fourth chapter is about the approximation of laws. This chapter covers the protection of intellectual, industrial and commercial property in Article 31, the competition rules of the customs union in Articles 32-38, the approximation of legislation in Articles 39-43, the trade defense instruments in Articles 49-51. The fifth chapter is about the institutional provisions, covering the EC-Turkey Customs union Joint Committee in Articles 52-53, consultation and decision procedures in Article 54-60, settlement of disputes in Articles 61-62 and safeguard measures in Articles 63-64. Last chapter -chapter six- is about the general and final provisions about the entry into force of the decision and the interpretation in the Articles 65-66.

The resolution is about the cooperation between the EU and Turkey on a wide range of issues, the macro-economic dialogue to provide an appropriate environment for the success of the customs union, cooperation on agriculture for a convergence between two

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<sup>39</sup> Haluk Günuğur, 6 Mart Kararı ve Gümrük Birliği, Gümrük Birliği Sürecinde Türkiye, İki Aylık Gümrük Birliği Dergisi. İstanbul: 1995, P:408

sides' implementations, cultural cooperation for the strengthening of ties and the improvement of mutual understanding, etc. Decision 1/95 covers a lot more comprehensive agreements than for seeded in the Ankara Agreement.<sup>40</sup>

The financial cooperation declaration is an integral part of the 1/95 Decision. According to this declaration, the EU will resume its financial support for Turkey to improve infra-structure linkages, to reduce the differences between the economies of the two sides and to help Turkey to adopt the Turkish industrial sector to the new competitive conditions and solve its problems in the way of the customs union where there is a possibility of facing with important social, as well as economic problems. The financial aid would depend on different sources among which the substantial budgetary resources for five years beginning from 1996, € 375 million; funds available under the 1992-1996 New Mediterranean Policy € 300 million; EIB loan for five years beginning from 1996, € 750 million and macroeconomic financial help in coordination with other international financial institutions.

Turkey in 1/95 Decision accepted the elimination of custom duties, quantitative restrictions and measures having equivalent effect in industrial products, special treatment for the processed agricultural products, adaptation of the CCT, customs provisions and the Common Commercial Policy (CCP) of the EU and alignment of its tariff in line with the EU's preferential trading regimes with certain third countries.

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<sup>40</sup> DTM, AB ve Türkiye. 5. Baskı. Ankara: 2002, P:347

**TABLE 2.1**  
**Customs Tariff Reduction of Turkey**

Year	12 Year List, %	22 Year List, %
1973	10	5
1976	20	10
1988	30	20
1989	40	30
1990	50	40
1991	60	50
1992	70	60
1993	80	70
1994	90	80
1995	95	90
1996	100	100

Source: Rıdvan Karluk, *AB ve Türkiye*, 5. Baskı.  
İstanbul: Emir Ofset, 1994, P:415

In terms of CCP, Turkey accepted to adopt the EU's CCP in five years from the entry into force of the Decision. The CCP of the EU emerged from the necessity to establish a single market depending on the common rules and policies with respect to foreign trade, where unified and common rules are valid for all countries. This policy aims at ensuring the free circulation of the products among the member states, the prevention of any possibility for traffic distortion and the implementation of the common rules within the EU.<sup>41</sup> In accordance with GATT Article 24 Turkey, from the entry into force of the Decision, accepted to apply the same commercial policy as the EU in the textile and clothing sector and the EU accepted to cooperate with Turkey to reach the objective. Both sides accepted the system of certificates of origin for the exports of textile and clothing from Turkey into the EU to remain valid until Turkey concluded the arrangements. Turkey started to apply exactly the same measures against 52 countries, as of those of the EU. This prevented trade deflection, caused by imports of goods from third countries into the area by a country that has a relatively lower external tariff than

<sup>41</sup> Rıdvan Karluk, *Gümrük Birliği Dönemecinde Türkiye:Gümrük Birliği Ne Getirdi Ne Götürdü?*. Ankara: Turhan Yayınları, 1997, P:195

the partner country, in order to re-export the goods to partner country. Therefore, unless these measures had been put into force trade deflection would have occurred. In 2004, the number of countries that these measures are applied is 38.<sup>42</sup>

The EU after establishing the customs union among them adopted the CCT in their trade relations. In addition, Turkey accepted the adoption of the CCT in her trade relations with third countries from the date of entry into force of the Decision. At the beginning, Turkey's average rate was about 40% where as the EU's was 7%, there was a gap between two parties.<sup>43</sup> The EU accepted to inform Turkey about the changes in CCT in sufficient time to make Turkey enable to align herself. If Turkey cannot align simultaneously, a period may be granted to Turkey. Turkey would not be allowed under any circumstances to apply tariff rates below the level of CCT. As derogations, Turkey, via the right regulated in article 19 of the Additional Protocol, may apply higher customs tariff than the CCT for five years. This will cover the products listed in Decision 2/95 and it will not exceed 5% of the value of the total import of Turkey in the year 1967. The timetable for the adoption of these products is; 10% in 1997, 10% in 1998, 15% in 1999, 15% in 2000, 50% in 2001. The average CCT rate for industrial products declined to 4.2% in 2004.<sup>44</sup>

According to Decision 1/95, Turkey accepted to align herself progressively with the preferential customs regime of the EU, which rests on the sets of autonomous regimes and preferential agreements, within five years from the entry into force of the Decision. These agreements as well as improving their access to Turkey, it will also improve Turkish exporters' access to these markets. During this period if a tariff rate other than the EU's is applied, products imported from third countries into the EU and released free circulation with preferential treatment because of their country of origin or of exportation will be subject to the payment of a compensatory levy.

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<sup>42</sup> Retrieved January 12, 2005 on the World Wide Web. URL:  
<http://www.foreigntrade.gov.tr/ab/ing/comtec.htm>

<sup>43</sup> Rıdvan Karluk, *Gümrük Birliği Dönemecinde Türkiye:Gümrük Birliği Ne Getirdi Ne Götürdü?*. Ankara: Turhan Yayınları, 1997, P:40

<sup>44</sup> Retrieved January 16, 2005 on the World Wide Web. URL:  
<http://www.foreigntrade.gov.tr/ab/TABgb/3.htm>

**TABLE 2.2**  
**CCT Adoption of Turkey**

Year	12 Year List, %	22 Year List, %
1989	-	20
1990	20	20
1991	20	20
1992	40	40
1993	60	50
1994	80	70
1995	90	85
1996	100	100

Source: Rıdvan Karluk, *AB ve Türkiye*. 5. Baskı.  
İstanbul: Emir Ofset, 1994, P:417

Turkey has signed 17 preferential trade agreements to date. The Free Trade Agreements (FTAs) Turkey concluded with Lithuania, Hungary, Estonia, Czech Republic, Slovakia, Poland, Slovenia and Latvia ceased by April 30, since these countries became full members of the EU on 1st May 2004. In addition, negotiations continue with Egypt, Lebanon, Albania and Faroe Islands. Turkey introduced her GSP scheme by taking account of the recent EU GSP Regime as of January 1, 2002 within the framework of 2002 Import regime, as regards 2.456 products. The product coverage of GSP increased to 2.884 in 2003. For 2004 in addition to the already existing 2.884 items, an additional 2.936 items are aligned.<sup>45</sup>

Turkey also accepted to change her customs code in a compatible way with that of the EU and the regulations of the Commission which include the origin of product, the customs value of the products, the entry of the products to the customs union area, free movement regime and customs procedure. New code entered into force on 5 February

<sup>45</sup> Retrieved January 18, 2005 on the World Wide Web. URL:  
<http://www.foreigntrade.gov.tr/ab/ing/comtec.htm>



2000. It simplified customs methods adapted to foreign trade and reduced the formalities and paper work in the import procedure.

**TABLE 2.3**  
**Free Trade Agreements**

Countries	Date of Signing	Date of Entry into Force
EFTA	10.12.91	01.04.92
Israel	14.03.96	01.05.97
Romania	29.04.97	01.02.98
Lithuania	02.06.97	01.03.98
Hungary	08.01.97	01.04.98
Estonia	03.06.97	01.07.98
Czech Republic	03.10.97	01.09.98
Slovakia	20.10.97	01.09.98
Bulgaria	11.07.88	01.01.99
Poland	04.10.99	01.05.00
Slovenia	05.05.98	01.06.00
Latvia	16.06.98	01.07.00
Macedonia	07.09.99	01.09.00
Croatia	13.03.02	01.07.03
Bosnia Herzegovina	03.07.02	01.07.03
Morocco	07.04.04	
Palatine	20.07.04	
Syria	28.08.04 initialed	
Tunisia	28.09.04 initialed	

Source: Retrieved January 20, 2005 on the World Wide Web. URL:  
<http://www.foreigntrade.gov.tr/ab/STA/bilesik.htm>

Alignment to EU legislation continued with these major adaptations:

- i. In order to approximate to legislation a decree on state aid compatible with the system in force in the EU and the relevant provisions of the World Trade Organization (WTO) Agreement subsidies and countervailing duties entered into force on 11 January 1995. This decree limits the scope of state aids to research and development (R&D), protection of environment, market research and promotion activities abroad.

- ii. In parallel to the Decision, to prevent the abuse of dominant power first, the competition law entered into force then the Board of Competition established on 6 March 1997.
- iii. The law on the monopoly of alcohol and alcoholic drinks and the tobacco law entered into force to make sure that there is no discrimination between state monopolies of Turkey and the EU companies.
- iv. Tobacco Products and Alcoholic Beverages Regulatory Board established on 20 July 2002 to draft the implementing rules in conformity with the 1/95 Decision's obligations.<sup>46</sup> In order to serve the protection of the intellectual rights, including patents, trademarks, geographical indications, industrial designs and copyrights Turkey participated in the related international conventions and signed important treaties.
- v. Another step in the approximation process is the decision of the standardization in the Foreign Trade, which entered into force on 8 April 1996, with the aim of making the quality control only for private security, environment protection, national security and consumer protection.
- vi. Furthermore, the decision for the establishment of Turkish Accreditation Body entered into force on 4 November 1999 with the aim of making standardization procedures compatible with the EU and the prevention of the technical barriers to which Turkish export may be subject.

The customs union decision did not cover agricultural products except the processed ones. As mentioned the free movement of agricultural products will be established after the adoption of the CAP. In the meantime, the EU and Turkey will implement a preferential regime, which includes tariff reductions, and tariff elimination for both sides.

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<sup>46</sup> Retrieved January 20, 2005 on the World Wide Web. URL: <http://www.foreigntrade.gov.tr/ab/ing/comtec.htm>

A free trade agreement signed with the ECSC and it entered into force on 1 August 1996. The treaty establishing ESCS ended on 24 July 2002 and rights and liabilities are transferred to the EU.

On 13 December 1995 the EP voted the 1/95 Decision and accepted with 343 yes votes, against 149 no votes. Finally, on 1 January 1996 with an 11 year delay in 12-year list, and a year delay in 22-year list customs union entered into force.

The customs union is important for Turkey for political reasons as well as economic reasons. Therefore, after the completion of customs union Turkey focused on membership. Turkey expected that customs union would ease the path to membership. However, things developed different. The commission excluded Turkey from the enlargement process in its report called Agenda 2000, On 16 July 1997. The report by conceding that the Customs Union was functioning satisfactorily did not referred to Turkey's full membership. On the same day the Commission reconfirmed Turkey's eligibility and brought a number of recommendations from liberalization of trade in services to consumer protection but also cited a number of political issues as pre-conditions in order to move forward. This provoked a frustration in Turkey in the political area. Turkey suspended political dialogue with the EU and turned down the invitations for participating conferences.

On 4 March 1998, the Commission published the European Strategy towards Turkey, which expanded the cooperation areas and sought to bring Turkey closer to the EU. Although the strategy did not contain new elements, it was a positive step taken towards Turkey. The Cardiff summit meeting on 15-16 June 1998 Turkey was included in the regular reports system like the other candidates. First regular report of Turkey was issued on 4 November 1998.<sup>47</sup>

The earthquake in 1999 brought the EU and Turkey closer. In addition to the two emergency humanitarian aid packages of €2 million, a consensus is reached for another

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<sup>47</sup> Rıdvan Karluk, Türkiye Ekonomisi Tarihsel Gelişim Yapısal ve Sosyal Değişim. Gözden Geçirilmiş 6. Baskı. İstanbul: Beta Yayınları, 1999, P:584-585

humanitarian aid package of €30 million for the reconstruction. Following the second regular report, which was issued on 13 October 1999, in the Helsinki summit held on 10-11 December 1999, Turkey was officially recognized without any precondition as a candidate country on an equal footing with the other candidate countries. Also according to the presidency conclusions and in parallel to the second regular report Turkey like other candidate countries will enjoy the benefits from a pre-accession strategy to stimulate and support its reforms.<sup>48</sup>

### **3.2.5. Relations Between 2000-2004 (Date to Start Negotiations)**

The Council approved the Accession Partnership on March 2001 and the Framework Regulation concerning EU's financial assistance to Turkey on 26 February 2001. The Accession Partnership document, the so-called road map from Turkey's accession, sets priority areas where Turkey is expected to further its alignment to EU acquis and determines EU's financial schemes that will support Turkey within the accession process. Turkey announced her own National Program for the Adaptation of the Acquis (NPAA) on 19 March 2001. According to the presidency conclusions of Copenhagen in December 2002, negotiations with Turkey will not start unless Turkey fulfills the Copenhagen political criteria. In March 2003, the Commission issued Strengthening the Accession Strategy for Turkey report, in which the Commission proposed a substantial increase in financial assistance for the period 2004-2006, that amount to €1.050 million in total. Financial assistance is set to be linked to the priorities defined in the Accession Partnership. The report also proposed enhanced cooperation in political dialogue, economic dialogue, justice and home affairs, maritime safety, extending the scope of the customs union. Accession Partnership is revised and adopted by the Council on 19 May 2003. NPAA is also revised on 24 July 2003. It set out how Turkey envisages dealing with the Accession Partnership, the timetable for implementing

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<sup>48</sup> Retrieved January 21, 2005 on the World Wide Web. URL: [http://www.mfa.gov.tr/MFA\\_tr/DisPolitika/AnaKonular/Turkiye\\_AB/](http://www.mfa.gov.tr/MFA_tr/DisPolitika/AnaKonular/Turkiye_AB/)

the Partnership's priority, and implications in terms of human and financial resources. On 5 November 2003, the Commission issued the sixth regular report on Turkey. It stated that the majority of the expectations in the revised Accession Partnership are fulfilled. On the other hand, it also stated that there are shortcomings in the implementation of the reforms. The Brussels European Council on 12 December 2003 concluded that due to considerable and determined efforts of Turkey to accelerate the pace of reforms the decision to open negotiations will be taken in December 2004 based on the report and recommendations of the Commission.

On 6 October 2004, the Commission based on its regular report recommended to start negotiations with Turkey. The Commission suggested a three-pillar strategy to approach the negotiations, first strengthened cooperation to reinforce and support the reform process in Turkey, second negotiations adapted to the specific challenges related to Turkey's accession and finally a substantially strengthened political and cultural dialogue bringing people together from EU Member States and Turkey. On 15 December, the European Parliament voted for Turkey. It is accepted to start negotiations immediately with 407 yes votes against 262 no votes. In the Brussels European Council on 16-17 December 2004, the European Council confirmed to open accession negotiations with Turkey without delay. The Council asked the Commission to prepare a proposal for a framework, with a view to opening negotiations on 3 October 2005, based on.<sup>49</sup>

- i. The negotiations will be conducted in an Intergovernmental Conference, decisions will require unanimity, and negotiations will be broken into chapters.
- ii. Long transition periods, derogations, permanent safeguards may be considered.
- iii. Negotiations can only be concluded after the establishment of the Financial Framework for the period from 2014.
- iv. Although the objective is accession, the outcome cannot be guaranteed and it is an open-ended process. If a candidate country cannot fulfill all the obligations then it will be anchored in the European structures through the strongest possible bond.

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<sup>49</sup> European Council 2004 Presidency Conclusions, Article 23

- v. Negotiations may be suspended upon the request of one third of the Member States in the case of a serious persistent breach of the principles of liberty, democracy, respect for human rights, fundamental freedoms and the rule of law, on which the Union is founded.
- vi. The Union will engage in an intensive political and cultural dialogue, with the aim of enhancing mutual understanding by bringing people together including the civil society.

### **3.3. Next Steps in EU-Turkey Relations**

Turkey's relations with the EU are based on one single aim, and it is Turkey's membership. Ankara Agreement and Additional Protocol with Customs Union Decision are just means that help Turkey to achieve the goal faster. Customs Union is also a step of the relationship. It will help Turkey to adopt economic aspects of membership faster. It will eventually turn to common market and monetary union between EU-Turkey.

Turkey has succeeded in getting a date for beginning negotiations in Brussels on December 2004. It is not wrong to say that this decision is the most important decision that has been ever taken in 45 years of EU-Turkey history. It was hard to imagine, just a couple of years ago that Turkey would complete preconditions for starting negotiations. In few years, Turkey abolished the death penalty, permitted to learn other local languages other than Turkish, and increased the role of civilian authority in government mechanisms. Turkey unlike most expectations, with a determined manner made very radical reforms.

On 11 April 2000 at the meeting of EU-Turkey Association council it was decided to setup 8 sub-committees (agriculture and fisheries, internal market and competition, trade, economic and monetary issues, innovation, transport-environment-energy, regional development-employment-social policy, customs-tax-drugs-money laundering) whose

work will be assessed a preparatory stage to the screening process. The Committees meet twice a year and are composed of representatives of the EU Commission and Turkey. Besides these sub-committee meetings, various committees and working groups were established within the EU Secretariat General in Ankara.

These meetings provided opportunities for both parties to be acquainted with issues other than customs union and with daily policies.<sup>50</sup> This is why, Turkish authorities claim that screening process will be easier than expected, because it has been already going on unofficially.

In first half of 2005, the Commission will set out in detail the process of negotiations particularly the implementation of the EU's rulebook, also known as the 'acquis communautaire'. The term 'negotiations' is often misunderstood in Turkey. The EU's common rules and policies were agreed between all the existing member countries long years ago, and the EU will not change them to suit a new member country, since it is joining the EU not the other way around. In addition, after Denmark and Britain experiences over the euro the EU will not grant any more permanent opt-outs. Therefore, negotiations are not about the content rather it is about the way and period of implementation. Negotiations will continue under 35 chapters that cover a wide range of the EU rules from health issues to defense. Following chapter will not be opened unless previous one is completed. The Commission will prepare non-papers, which inform the Council whether a chapter can be opened. The authority to open and to close a chapter belongs to the Council, with unanimous vote. After all the chapters are completed, the Accession Agreement will be finalized in Intergovernmental Conference and will be sent to the European Parliament and The Council's approval. The accession process will be completed after the approval of each member country's parliaments. However, for Turkey, the process may not end. France announced that it will leave the decision to French people and other member countries may follow footsteps of France, which may block Turkey's membership at the last stage.

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<sup>50</sup> TÜSIAD, Turkey-EU Relations: The Way Forward. İstanbul:2001, P:26

The negotiation process is long and complex. For example, Spain's negotiations lasted for 8 years, the period was 7 years for Estonia. Portugal applied for membership in 1956 yet become member in 1986. Turkey will have to adopt more than 80.000 pages of EU rules into national law. It is generally expected that Turkey's negotiations will last between 8-12 years, on an average a decade. Once negotiations start, it will develop a momentum of its own. Moreover, if Turkey like a unique body works towards to the objective of accession, negotiations may be completed before than expected.

The EU is has well prepared accession criteria and standard procedure as a result of previous waves of enlargement. However, Turkey is a much bigger and complicated candidate than the new 10 member countries. Therefore, the conditions may be stricter for Turkey. In the past decade, the EU has learned that it is not enough for a candidate country to change its legislation, because EU policies do not function properly without the implementation and enforcement.<sup>51</sup> For Turkey, the EU may take this lesson very seriously, and for this reason Turkey may have to prove she is implementing the relevant EU laws before each chapter is closed.

The way to the EU accession is also a public relations exercise. When the negotiations begin the EU may ask reforms in sensitive areas, parliamentarians and/or EU governments may also make new demands, such as a call to apologize for the treatment of Armenians in 1915-16 and better conditions for the Kurds. Here, Turkish Government should not meet criticism with prickliness and national rhetoric, but with modernation and coolness. Turkey should prove the EU members that she shares European values.

Turkey should win the hearts and minds of both Turkish public and European public. As the Czech Republic's former chief EU negotiator Pavel Telicka observed, "Accession negotiations are 80% in your own country, 15% in the EU member countries and only 5% in Brussels".<sup>52</sup> The new 10 members did not have to face a referendum on their membership in any of the existing member countries, but Turkey will. France

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<sup>51</sup> Heather Grabbe, When Negotiations Begin: The Next Phase in EU-Turkey Relations. London: Centre for European Reform, 2005, P:2

<sup>52</sup> Heather Grabbe, When Negotiations Begin: The Next Phase in EU-Turkey Relations. London: Centre for European Reform, 2005, P:5



already announced the referendum. Although EU leaders have to do much of the job of persuading the public, Turkey must contribute the process.

Turkey will find that membership of the EU's deeply integrated single market is qualitatively different. It involves vastly more legislation than the customs union, and the EU insists on much tighter implementation and enforcement of the rules. Under the single market, the EU will determine products standards for Turkish goods, health and safety regulations for Turkish factories and strict limits on the government's industrial subsidies. The EU will also take a keen interest in Turkey's budgetary and monetary policies. Turkey does not have to meet the Maastricht criteria for the euro, but she needs to show the EU that she can sustain single-digit inflation and steady growth. If economic conditions in Turkey steadily improve over the course of the negotiations, the incentive to migrate will be little<sup>53</sup>. People in the EU would start to see Turkey as an asset for the European economy, rather than a poor relation putting out the begging-bowl for EU transfers. For this reason, the Turkish government needs to explain the costs and benefits of accession in detail and publicize its timetable for implementing EU legislation.

The accession process is not about finding common interests between parties rather it is about agreeing a timetable for the candidate country to apply the EU's law at home. One of the Poland's negotiators in 2004 observed "Negotiations are a humiliating process. The EU makes it very clear that you are joining them, not the other way around."<sup>54</sup> Turkey will find out that the EU is not just a club based on a shared identity, but also a huge set of rules and regulations. European integration reaches deep into a country's policies and institutions. It affects not just high politics but daily life like how animals are slaughtered, what products can be advertised on billboards, etc. The EU covers foreign and security policies too, many of which are very sensitive in Turkey. Turkey may find it hard to accept such a strong external influence. The practical consequences of membership negotiations will be difficult, but the change in mentality required will be even harder.

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<sup>53</sup> Sübidey Togan, Turkey Toward EU Accession. Cairo:Economic Research Forum, 2003, P:18

<sup>54</sup> Heather Grabbe, When Negotiations Begin: The Next Phase in EU-Turkey Relations. London: Centre for European Reform, 2005, P:6

Turkey needs to be well prepared. The technicalities of preparing for EU membership will require an enormous effort. Nevertheless, the Turkish and EU governments also have to persuade the European public and the Turkish people that accession will benefit them in the end.

EU legislation harmonization is not completed. The reforms that have done in the last couple of years constitute an encouraging start for Turkey. 70.2% of the Turkish people are in favor of Turkey's membership.<sup>55</sup> This strong public support, may help Turkey to realize some complicated reforms.

### **3.4. The Institutions of EU-Turkey Association**

Turkey as an associate member cannot join EU Institutions. Because Turkey is not a member country and the EU does not let a non-member country to take part in its institutions and has right to effect decisions. To apply association regime and provide its progress three fundamental institutions founded by Ankara Agreement. These were, Association Council, Association Committee and Joint Parliamentary Commission. Eventually as relations develop, new institutions were established.

EU-Turkey Association Institutions did not meet regularly. Sometimes political climate sometimes other issues, like the free movement of workers, block meetings. For example, Customs Union Joint Committee is supposed to meet every month. However the Committee only met five times in 1996, met once or twice following years. Irregularity exists nearly for all the Association Institutions. It is inevitable that this decreases Institutions' efficiency, which in turn slows down Turkey.

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<sup>55</sup> DİE, Türkiye'de Bireylerin Avrupa Birliği'ne Bakışı. Ankara:DİE Matbaası, 2005, P:13

### **3.4.1. Association Council**

Association Council is established in accordance with the Article 22 of the Ankara Agreement in 1963. It is the main decision taking body of the association. Its main responsibility is to take decisions to reach targets of Ankara Agreement and Additional Protocol. It is composed of the Commission, Member States and Turkey's representatives, the presidency is held 6 months for each side. Decisions are taken with unanimity. Meetings are held at least once in 6 months at the level of ministers. Its decisions are binding for the parties. In addition, it has an important task in the settlement of disputes. Any disputes related with the agreements may be brought to the Council. The Council may solve the disputes. The Council prepares an activity report each year for the Joint Parliamentary Commission.

### **3.4.2. Association Committee**

Association Committee has been established by the decision number 3/64 of Association Council. The Committee prepares the agenda of Association Council, and evaluates the technical problems arising from Partnership Relations. The committee is composed of technicians from both sides. The chairperson and secretary of the Committee are appointed through the same procedure as applied for the Association Council.

### **3.4.3. Joint Parliamentary Commission**

Joint Parliamentary Commission has been established in accordance with European Parliament's decision on 14 May 1965, TBMM's decision on 22 June 1965 and decision of Association Council on 27 July 1965. The Commission is composed of 12 representatives from TBMM and 12 representatives from European Parliament. The Commission is responsible for the evaluation of issues stemming from the Ankara Agreement, with particular emphasis on the annual reports submitted by Association Council to the Presidents of TBMM and the European Parliament. The Commission meets twice a year.

### **3.4.4. Customs Cooperation Committee**

As a technical committee, the Customs Cooperation Committee has been established in accordance with the Article 6 of Ankara Agreement and under the Decision of Association Council No: 2/69 to ensure the implementation and development of the association common regime. Customs Cooperation Committee meets twice a year, one in Belgium and one in Turkey. The Committee is composed of the representatives of EU Commission and the Member States, and those of the Ministry of Foreign Affairs, Ministry of Justice, Ministry of Finance, Under Secretariat of Foreign Trade and State Planning Organization all of which form the Turkish Delegation presided by the Director General of EU and External Relations affiliated to the Under Secretariat of Customs of Turkey. The role of the Customs Cooperation Committee is to enhance the administrative cooperation between the contracting parties in order to implement the relevant provisions of the Agreement in an accurate and uniform way and conduct the work that will directly be assigned by the Association Council.

#### **3.4.5. Customs Union Joint Committee**

The Customs Union Joint Committee has been established in accordance with the Article 24 of Ankara Agreement and under the Decision of Association Council No: 1/95. It gives advices to the Association Council and it is responsible for the approximation of the Turkish legislation with that of the Union. The Committee is composed of two sides' representatives and meets once a month. It can establish sub-committees and workgroups to assist the Committees' responsibilities.

#### **3.4.6. Joint Consultative Committee**

Joint Consultative Committee has been established in accordance with the Article 24 of Ankara Agreement. It is composed of 18 representatives from the Economic Social Committee of the Union and 18 representatives from Turkey mainly members of economic and social interest groups. Its aim is to create a platform of mutual understanding and increase the level of knowledge.

### **3.4.7. ECSC-Turkey Joint Committee**

ESCS-Turkey Joint Committee has been established in accordance with the free trade agreement signed on 25 July 1996 to arrange the trade of products within the scope of free trade agreement. Presidency is held for 1 year for each side. Meetings are held in Brussels and Ankara once a year.<sup>56</sup>

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<sup>56</sup> Retrieved January 22, 2005 on the World Wide Web. URL: <http://www.dtm.gov.tr/abigm/>

## IV. THE EFFECTS OF THE CUSTOMS UNION

Customs Union integrated Turkish economy to one of the important trade blocks in the world. This integration led Turkey to access the EU market with more favorable conditions compared to other countries. On the other hand Turkey opened her market to the EU's and other countries' competition. It has been nearly 10 years that the Customs Union Decision was taken and more than 9 years since it has been entered into force. Within this period some positive and negative effects of customs union have been observed. There were and are severe arguments about the effects of the customs union. Rest of the paper aims to examine relatively observable and/or measurable results of the customs union from an objective aspect.

### 4.1. Foreign Trade Effects

The EU is the most third crowded land after China and India with 459 million population. The EU is also one of the biggest economies in the world. Its GDP in 2003 was €10.000 billion. The total intra trade volume in 2003 was €1.800 billion.<sup>57</sup> The EU had 20% in total world trade in 2002 sharing the first place with the US.<sup>58</sup>

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<sup>57</sup> The European Commission, Portrait of the European Union. Luxembourg: Office for Official Publications of the European Communities, 2004, P:14-22

<sup>58</sup> The European Commission, The Eurostat Yearbook 2004. Luxembourg: Office for Official Publications of the European Communities, 2004, P:163

The most important trade partner for Turkey is the EU, around 40-50% of share in total trade volume. This is not something new; the EU has been Turkey's most important trade partner not only after 1995, but more than 40 years. Table 3-1, shows the detailed trade figures of Turkey between 1967-1995. It shows a persistence increase in both exports and imports between the EU-Turkey. From 1967 to 1995 Turkey's volume of exports increased by 4.045%, whereas in the same period Turkey's exports to the EU increased by 4.634%. The situation for imports is 5.113% and 4.948% respectively. The average share of the EU in Turkey's exports and imports, and total volume of trade during the same period is 47%, 42% and 44% respectively.

**TABLE 3.1**  
**Foreign Trade of Turkey Between 1967-1995 (million USD)**

Years	Exports			Imports		
	Total	EU	EU Share	Total	EU	EU Share
1967	522	234	44,8%	685	334	48,7%
1968	496	226	45,4%	764	393	51,4%
1969	537	267	49,7%	801	393	49,1%
1970	588	294	50,0%	948	427	45,1%
1971	676	329	48,7%	1.171	582	49,7%
1972	885	428	48,4%	1.563	851	54,5%
1973	1.317	652	49,5%	2.086	1.161	55,6%
1974	1.532	761	49,7%	3.778	1.748	46,3%
1975	1.401	645	46,0%	4.739	2.378	50,2%
1976	1.960	1.017	51,9%	5.129	2.412	47,0%
1977	1.753	897	51,1%	5.796	2.559	44,1%
1978	2.288	1.127	49,3%	4.599	1.931	42,0%
1979	2.261	1.132	50,0%	5.069	1.940	38,3%
1980	2.910	1.300	44,7%	7.909	2.360	29,8%
1981	4.703	1.564	33,3%	8.933	2.633	29,5%



Years	Exports			Imports		
	Total	EU	EU Share	Total	EU	EU Share
1982	5.746	1.802	31,4%	8.843	2.566	29,0%
1983	5.728	2.066	36,1%	9.235	2.775	30,1%
1984	7.134	2.781	39,0%	10.757	3.314	30,8%
1985	7.958	3.204	40,3%	11.343	3.895	34,3%
1986	7.457	3.263	43,8%	11.105	4.565	41,1%
1987	10.190	4.868	47,8%	14.158	5.666	40,0%
1988	11.662	5.098	43,7%	14.335	5.895	41,1%
1989	11.624	5.408	46,5%	15.792	6.055	38,3%
1990	12.959	6.906	53,3%	22.302	9.328	41,8%
1991	13.593	7.042	51,8%	21.047	9.221	43,8%
1992	14.719	7.602	51,6%	22.871	10.050	43,9%
1993	15.348	7.376	48,1%	29.429	13.874	47,1%
1994	18.105	8.634	47,7%	23.270	10.915	46,9%
1995	21.636	11.078	51,2%	35.707	16.860	47,2%

Source: DTM, AB ve Türkiye. 5. Baskı. Ankara: 2002, P:444

There are some important subjects that must be taken into account seriously before going into details of the effects of the customs union on the foreign trade of Turkey. First, we cannot ignore the changes in Turkish and world economy. The 1994 crisis and the problems created by devaluation, Asia and Russia crises in world economy in 1997, the stagnation in Turkish economy in 1998, the earthquake in 1999, the crises on November 2000 and February 2001, the positive effects of decrease in inflation and interest rates on costs. All of these directly affect the performance of foreign trade. Second, the harmonization of technical procedure. The precondition of trading with the EU is to apply EU's rules, which covers standards, technical requirements, environment conditions etc. If related legislation is not applied then there is no reason to expect positive progress on trade relation with the EU. Third, it should not be forgotten that

Turkey started enjoying tariff free trade, except for some products, in 1971, however the EU started it in 1996 onwards. The amount of exports to the EU increased by 45,6% from 1970 to 1972 and by 158,8% from 1970 to 1974. Keeping in mind these will enable more accurate and objective analysis.

**TABLE 3.2**  
**Foreign Trade of Turkey Between 1995-2004 (million USD)**

Year	Total					EU					EU's Share		
	Exports	Chg.	Imports	Chg.	X/M	Exports	Chg.	Imports	Chg.	X/M	Exports	Imports	Total
1995	21.636	-	35.707	-	60,6%	11.078	-	16.680	-	66,4%	51,2%	46,7%	48,4%
1996	23.224	7,3%	43.626	22,2%	53,2%	11.549	4,3%	23.138	38,7%	49,9%	49,7%	53,0%	51,9%
1997	26.261	13,1%	48.559	11,3%	54,1%	12.248	6,1%	24.870	7,5%	49,2%	46,6%	51,2%	49,6%
1998	26.974	2,7%	45.921	-5,4%	58,7%	13.498	10,2%	24.075	-3,2%	56,1%	50,0%	52,4%	51,5%
1999	26.587	-1,4%	40.671	-11,4%	65,4%	14.348	6,3%	21.401	-11,1%	67,0%	54,0%	52,6%	53,2%
2000	27.775	4,5%	54.503	34,0%	51,0%	14.510	1,1%	26.610	24,3%	54,5%	52,2%	48,8%	50,0%
2001	31.334	12,8%	41.399	-24,0%	75,7%	16.118	11,1%	18.280	-31,3%	88,2%	51,4%	44,2%	47,3%
2002	36.059	15,1%	51.354	24,0%	70,2%	18.459	14,5%	23.321	27,6%	79,2%	51,2%	45,4%	47,8%
2003	47.253	31,0%	69.340	35,0%	68,1%	24.484	32,6%	31.696	35,9%	77,2%	51,8%	45,7%	48,2%
2004	62.774	32,8%	97.161	40,1%	64,6%	34.310	40,1%	45.373	43,2%	75,6%	54,7%	46,7%	49,8%

Source: Retrieved February 17, 2005 on the World Wide Web. URL: <http://www.die.gov.tr>

Table 3-2 shows the development of trade relations between the EU-Turkey after the customs union. From 1995 to 2004 Turkey's volume of exports increased by 190%, whereas in the same period Turkey's exports to the EU increased by 210%. Imports of Turkey and Turkey's imports from the EU increased by the same amount, which is 172%. The average share of the EU in Turkey's exports and imports, and total volume of trade during the same period is 52%, 48% and 50% respectively.

Total trade volume between the EU-Turkey increased from \$27.758 million in 1995 to \$79.683 million in 2004 with a 187% change. In 1996, the first year of customs union, the trade deficit between the EU-Turkey was \$11.589 million in favor of EU. In 2004, the deficit is \$11.063 million in favor of EU. Therefore, it is not correct to claim

that customs union created trade deficit over the time. However, the overall foreign trade balance of Turkey without counting the trade with EU, the deficit increased from \$8.469 million in 1996 to \$23.324 in 2004 with 165% change.

Exports of Turkey increased 190% between 1995-2004 from \$21.636 million to \$62.774 million, the highest amount of export of all times. Particularly from 2001 to 2004, Turkey increased the amount of exports by double. The increase in exports to EU is 210%, from \$11.078 million to \$34.310 million during between 1995-2004. The increase in exports to EU is 112,8% between 2001-2004. Like the general pattern in overall exports of Turkey, exports to the EU increase constantly.

The imports on the other hand do not have a regular pattern. There are harsh up and downs, imports decreased in 2001 by 24%, following year increased by 24%. The level of imports is very sensitive to economic situation. All of these are also true for the level of imports from the EU. The amount of imports during 1995-2004 increased to \$97.161 million from \$35.707 million, with a 172% change. Imports from the EU increased from \$16.680 million to \$45.373 million.

The X/M ratio in 2004 is 64,6% for total trade and 75,6% for trade with EU. The average X/M ratio for the period 1995-2004 is 62,6% and 66,8% respectively. Therefore, customs union did not create extra trade deficit so far; in fact, it improved the trade balance of Turkey.

The EU's imports from third countries decreased by 19% between 1995-2000. However, Turkey's share of 1.7% did not change. In 2003 Turkey was the seventh biggest exporter to the EU with a 2.7% share. In case of exports, Turkey was the sixth biggest market that EU exported with a 3.3% share.<sup>59</sup>

These figures show Turkey's exports to the EU increases constantly and rapidly than the general export trend of Turkey. Imports, on the other hand, are linked to the

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<sup>59</sup> The European Commission, The Eurostat Yearbook 2004. Luxembourg: Office for Official Publications of the European Communities, 2004, P:163

general economic conditions. There is no stable trend, it fluctuates with the economy. From EU's aspect, Turkey's role in overall EU trade seems to be settled. Import figures from Turkey, shows independent movement from the general economic conditions.

**TABLE 3.3**  
**Sectoral Breakdown of Turkey-EU Trade (million USD)**

Exports to the EU																
Year	Agriculture			Textile and Clothing			Iron and Steel			Chapter 84,85 and 87			Industrial Products			Total
	Value	%	Chg.	Value	%	Chg.	Value	%	Chg.	Value	%	Chg.	Value	%	Chg.	
1995	1.965	17,7	-	5.353	48,3	-	505	4,6	-	1.239	11,2	-	2.017	18,2	-	11.078
1996	1.854	16,1	-5,6	5.660	49,0	5,7	421	3,6	-16,7	1.505	13,0	21,4	2.110	18,3	4,6	11.549
1997	2.037	16,6	9,9	5.930	48,4	4,8	622	5,1	48,0	1.550	12,7	3,0	2.109	17,2	0,0	12.248
1998	1.941	14,4	-4,7	6.464	47,9	9,0	703	5,2	13,0	2.083	15,4	34,4	2.307	17,1	9,4	13.498
1999	1.901	13,2	-2,1	6.363	44,3	-1,6	818	5,7	16,4	2.705	18,9	29,9	2.562	17,9	11,0	14.348
2000	1.538	10,6	-19,1	6.469	44,6	1,7	908	6,3	10,9	2.865	19,7	5,9	2.730	18,8	6,6	14.510
2001	1.674	10,4	8,9	6.699	41,6	3,6	997	6,2	9,9	3.754	23,3	31,0	2.993	18,6	9,6	16.118
2002	1.632	8,8	-2,5	7.626	41,3	13,8	937	5,1	-6,0	4.924	26,7	31,2	3.340	18,1	11,6	18.459
2003	2.000	8,2	22,5	9.562	39,1	25,4	1434	5,9	53,0	7.099	29,0	44,2	4389	17,9	31,4	24.484
2003*	1.801	8,1	-	8.703	39,3	-	1.307	5,9	-	6.322	28,5	-	4.032	18,2	-	22.165
2004*	2.311	8,0	28,3	9.817	33,9	12,8	2.193	7,6	67,8	9.638	33,3	52,5	5.015	17,3	24,4	28.974

Imports from the EU																
Year	Agriculture			Textile and Clothing			Iron and Steel			Chapter 84,85 and 87			Industrial Products			Total
	Value	%	Chg.	Value	%	Chg.	Value	%	Chg.	Value	%	Chg.	Value	%	Chg.	
1995	790	4,7	-	828	4,9	-	1.852	11,0	-	6.617	39,2	-	6.774	40,2	-	16.861
1996	675	2,9	-14,5	1.379	6,0	66,5	2.081	9,0	12,4	10.155	43,9	53,5	8.848	38,2	30,6	23.138
1997	512	2,1	-24,1	1.611	6,5	16,8	1.873	7,5	-10,0	11.751	47,2	15,7	9.123	36,7	3,1	24.870
1998	477	2,0	-6,8	1.425	5,9	-11,5	1.466	6,1	-21,7	11.696	48,6	-0,5	9.011	37,4	-1,2	24.075
1999	489	2,3	2,5	1.318	6,2	-7,5	943	4,4	-35,7	10.428	48,7	-10,8	8.223	38,4	-8,7	21.401
2000	479	1,8	-2,0	1.411	5,3	7,1	1.332	5,0	41,3	13.694	51,5	31,3	9.694	36,4	17,9	26.610
2001	304	1,7	-36,7	1.280	7,0	-9,3	1.004	5,5	-24,6	7.736	42,3	-43,5	7.957	43,5	-17,9	18.280
2002	432	1,9	42,3	1.639	7,0	28,0	1.496	6,4	49,0	9.890	42,4	27,9	9.864	42,3	24,0	23.321
2003	564	1,8	30,6	1.806	5,7	10,2	2.407	7,6	60,9	13.987	44,1	41,4	12.931	40,8	31,1	31.695
2003*	463	1,7	-	1.610	5,8	-	2.191	7,9	-	11.793	42,7	-	11.535	41,8	-	27.592
2004*	550	1,4	18,8	1.825	4,8	13,4	2.502	6,6	14,2	17.786	46,6	50,8	15.471	40,6	34,1	38.134

\*January-November

Source: Retrieved February 17, 2005 on the World Wide Web. URL: <http://www.dtm.gov.tr>

Customs union revealed competition conditions and market entry benefits. This led to a change in production scales and production composition. Finally, these changed the composition of exports of Turkey. Table 3.3 shows the sectoral distribution of exports of Turkey to the EU and imports from the EU between 1995-2004.

The share of agriculture in exports is constantly decreasing. In 1995, the share of agriculture in Turkey's exports to the EU was 17,7% whereas the share was 8,2% in 2003. Although the share of agriculture is decreasing, the nominal gain from exports is around the same levels, \$1.965 million in 1995, and \$2.000 million in 2003. Agriculture is also a decreasing component in the composition of imports from the EU, even more severe than the decrease in exports. The share decreased from 4,7% to 1,7% during 1995-2003. The value of imports decreased too, from \$790 million to \$564 million in the same period.

Textile and clothing was biggest supporter of the customs union. Their expectation was that with the removal of quotas exports would accelerate. However, the sector disappointed. The share of textile and clothing went down dramatically from 48,3% to 39,1% between 1995-2003, although the value of exports increased from \$5.353 million to \$9.562 million. The increase in the exports of textile and clothing was a way below the level of increase in overall exports to the EU. The increase in exports of textile and clothing was 79% during 1995-2003, however the increase was 210% for overall exports to the EU. The level of imports in this sector is constant 5-7%, between 1995-2003, but the value is steadily increasing from \$829 million in 1995 to \$1.806 million in 2003.

Iron and steel sector's share in exports to the EU grew to 5,9% from 4,6%. This increase in the share also affected the value, which increased from \$505 million to \$1.434 million between 1995-2003. The Free Trade Agreement on products that are within the jurisdiction of ECSC entered into force in 1996. From 1996 to 2003 the exports of iron and steel to the EU increased by 184%. The share of iron and steel in imports is more moving. The level of share decreased from 11,0% to 4,4% in 1999 and

then started to rise, and in 2003, it was 8%. The value of iron and steel imports from the EU had a parallel move. It decreased to \$943 million from \$1.852 billion between 1995-1999 and became \$2.407 billion in 2003.

The exports of Chapters 84-85 (nuclear reactors, tools, boilers, machines with electric and equipments) and 87 (automobile industry products) increased by 423%, a lot higher than the overall 120% increase. The share of exports proportionally increased from 11,2% in 1995 to 29,0% in 2003. The value increased to \$7.099 billion from \$1.239 billion. The share of imports also increased. The level of share of Chapter 84, 85 and 87 was 44% in 2003, which was 39% in 1995. The value increased from \$6.617 billion to \$13.987 billion during the same period.

The changes in the share of industrial products in the composition of both exports and imports are minor. The share of exports of industrial products was 18,2% in 1995 and 17,9% in 2003. However, the value of exports, with constant growth, increased by 118%, from \$2.017 billion to \$4.389 billion. The value of imports of industrial products from the EU was \$6.674 billion in 1995, which increased to \$12.931 billion in 2003.

The sectoral composition of Turkey's exports to the EU changed in favor of chapter 84-85-87, iron and steel, and partly industrial products. The consequences are not favorable for agriculture and textile and clothing so far. This shows Turkey's exports' shift from labor intensive, less technological structure to capital intensive, high tech goods, which is favorable. This structural shift is the result of R&D activities parallel to technical harmonization and improvement in quality via the investments on electronics and automobile by foreign firms. Textiles and clothing is labor intensive, which means it is cost oriented. In addition, textile importers are very sensitive to pricing. These two factors make difficult for Turkish textile and clothing firms to achieve desired export level. Because of China and Asian countries, Turkish firms become uncompetitive and lose markets, which in turn decrease the level of potential

exports. The revaluation of YTL is also often indicated as one of the reasons that blocks textile and clothing sector.

Competitiveness figures support the structural change in Turkey's trade. Turkey's competitiveness improved after the Customs Union especially in easily imitable research-oriented goods and difficult imitable research-oriented goods on the other hand worsened in labor-intensive goods and raw material intensive goods, between 1996-2000.<sup>60</sup>

**TABLE 3.4**  
**EU-Turkey Trade (Commodity Groups) (million USD)**

Exports										
Year	Investment			Intermediate			Consumption			Total
	Value	%	Chg.	Value	%	Chg.	Value	%	Chg.	
1995	318	2,9	-	3.528	31,8	-	7.232	65,3	-	11.078
1996	396	3,4	24,5	3.727	32,3	5,6	7.425	64,3	2,7	11.549
1997	423	3,5	6,8	4.105	33,5	10,1	7.721	63,0	4,0	12.248
1998	489	3,6	15,6	4.612	34,2	12,4	8.397	62,2	8,8	13.498
1999	631	4,4	29,0	4.981	34,7	8,0	8.737	60,9	4,0	14.348
2000	666	4,6	5,5	5.203	35,9	4,5	8.631	59,5	-1,2	14.510
2001	960	6,0	44,1	5.751	35,7	10,5	9.359	58,1	8,4	16.118
2002	1.274	6,9	32,7	5.834	31,6	1,4	11.330	61,4	21,1	18.459
2003	2.077	8,5	63,0	7.431	30,4	27,4	14.929	61,0	31,8	24.484
2004	3.776	11,0	81,8	10.772	31,3	45,0	19.759	57,4	32,4	34.417

<sup>60</sup> Bahri Yılmaz & Selim Jürgen Ergun, The Foreign Trade Pattern and Foreign Trade Specialization of Candidates of the European Union. Berlin: Ezoneplus Working Paper No:19, 2003, P:8-13

Imports										
Year	Investment			Intermediate			Consumption			Total
	Value	%	Chg.	Value	%	Chg.	Value	%	Chg.	
1995	4.831	28,7	-	10.539	62,5	-	1.491	8,8	-	16.861
1996	7.388	31,9	52,9	12.880	55,7	22,2	2.870	12,4	92,5	23.138
1997	7.327	29,5	-0,8	14.009	56,3	8,8	3.535	14,2	23,2	24.870
1998	7.182	29,8	-2,0	13.270	55,1	-5,3	3.622	15,0	2,5	24.075
1999	6.069	28,4	-15,5	11.823	55,2	-10,9	3.525	16,5	-2,7	21.401
2000	7.254	27,3	19,5	14.116	53,0	19,4	5.114	19,2	45,1	26.610
2001	4.317	23,6	-40,5	11.168	61,1	-20,9	2.595	14,2	-49,3	18.280
2002	5.361	23,0	24,2	14.417	61,8	29,1	3.196	13,7	23,2	23.321
2003	6.999	22,1	30,6	19.233	60,7	33,4	5.147	16,2	61,0	31.695
2004	10.672	23,5	52,5	26.819	59,0	39,4	7.613	16,8	47,9	45.434

Source: Retrieved July 29, 2005 on the World Wide Web. URL: <http://www.dtm.gov.tr>

Table 3.4 shows the distribution of commodity groups in EU-Turkey trade. According to this table, the only group that made a major change in exports is the investment products. The share of investment products in Turkey's exports to the EU increased from 2,9% in 1995 to 11,0% in 2004, in terms of value from \$318 million to \$3.776 million, a 1.087% increase. Intermediate products on the other hand had a 32,5% share in 1995, which decreased to 31,3% in 2004. The value gained from intermediate products' exports raised from \$3.528 million to \$10.772 million. The share of consumption products was 57,4% in 2004, which was 65,3% in 1995. However, value of exports raised \$7.232 million to \$19.759 million during the same period. The increase in exports of investment products shows that Turkish firms gained a constant share in the market of high value added products.<sup>61</sup>

<sup>61</sup> TÜSİAD, *Avrupa Birliği'ne Uyum Sürecinde Gümrük Birliği'nin Dış Ticaretimize Etkileri*. İstanbul: Lebib Yalkın, 2003, P:87



In case of imports, the distribution of commodity groups shows a change in favor of consumption products. Investment products share in imports from the EU decreased to 23,5% in 2004 from 28,7% in 1995, the value increased from \$4.831 million to \$10.672 million. Import of intermediate products' share also decreased. It was 62,5% in 1995, which decreased to 59,0% in 2004, the value of imports raised from \$10.539 million to \$26.819. The share of consumption products increased to 16,8% in 2004 from 8,8% in 1995. The value of imports increased by 411% between 1995-2004. It rose from \$1.491 million to \$7.613 million. The average share of commodity groups in Turkey's imports from the EU between 1995-2004 is 26,5% for investment products, 58,3% for intermediate products, 15,2% for consumption products. The import of investment and intermediate products provides input to the economy. These products create contribution to the economy. The sum of investment and intermediate products is 85%, which is very positive. The average share of consumption products is 15,2%. The increase in import of consumption products is mainly due to low interest consumption loans and high internal demand caused by revalued TL. The consumption products imported from the EU, makes Turkish people conscious of quality, standards and consumer rights. As Turkish people gain conscious, they demand same standards from the domestic producers. As domestic producers provide same level, of quality and standards, they can supply it to Turkish people or they can export it to the EU. One other thing is the negative effects of import of consumption products may be balanced with the high taxes levied on luxurious products.<sup>62</sup>

Table 3.5 shows the distribution of Turkey's trade by selected country groups for selected years. In terms of exports, only Organization of Islamic Conference and EFTA countries lost 2,5% and 1,6% of share respectively when compared to 1990 figures. When 1996 figures are compared to those of 2004, the picture looks different. Organization of Black Sea Economic Cooperation and New Independent States' shares decreased by major degrees up to 7,1%. The Russian economic crisis was one of the main reasons of decrease in the share of New Independent States'. Organization of Islamic Conference's share is stable and EFTA countries' share decreased by 0,6%. It can

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<sup>62</sup> İKV, Gümrük Birliği'nin Türkiye Ekonomisine Etkileri. İstanbul:N/A, 2004, P:20

be derived that Turkey's exports after customs union, with the help of global crisis, shifted to the EU. The increase in the level of exports to the EU despite global crisis, like Russia and Asian, proves that Turkey gained a level of stability in terms of exports.

**TABLE 3.5**  
**Turkey's Trade by Country Groups**

Year/Country	Exports				Imports			
	1990	1996	2000	2004	1990	1996	2000	2004
EU	55,4%	49,7%	52,2%	54,7%	44,4%	53,0%	48,8%	46,7%
OECD Countries	68,0%	59,3%	68,4%	64,3%	63,8%	71,3%	65,4%	61,2%
Org. of Blacksea E.Co.	1,8%	14,6%	8,5%	10,4%	1,6%	8,9%	12,3%	15,6%
New Independent St.	N/A	13,4%	5,9%	6,3%	N/A	7,0%	10,4%	13,2%
Org. of Islamic Conf.	18,7%	16,0%	14,1%	16,2%	17,2%	12,8%	13,5%	10,9%
EFTA Countries	2,6%	1,6%	1,2%	1,0%	2,7%	2,5%	2,1%	4,0%

Source: February 17, 2005 on the World Wide Web. URL: <http://www.dic.gov.tr>

Distribution of imports favored Organization of Black Sea Economic Cooperation and New Independent States by major degrees, from 8,9% and 7,0% share in 1996 to 15,6% and 13,2% in 2004 respectively. The share of Organization of Islamic Conference decreased by 1,9% and 6,3% in 2004 and 1990 respectively. The EFTA countries increased their share to 4,0% in 2004 from 2,5% in 1996. There are also decreases in shares of the EU and the OECD countries. The EU's share decreased from 53,0% in 1996 to 46,7% in 2004 and the OECD's share decreased to 61,2% in 2004 from 71,3% in 1996.

According to Table 3.5, contrary to the general expectation that trade diversion effects will be appeared -via a serious shift in favor of EU because of the elimination of duties for the goods coming from the EU- no such effects appeared to be seen between 1996 to 2004, except the Organization of Islamic Conference.

Therefore, it is obvious that customs union shifted trade ways to the EU. EU's share in total trade of Turkey increased slightly from %48,4 in 1995 to %49,8 in 2004. However, as Table 3.5 shows there is no dramatic concentration on EU, in other words there is no dramatic reduction in any country groups. Even if there was major concentration on the EU, it should be accepted normal. As Turkey get more and more involved with EU, trade between them will increase involuntarily. For example, the share of the EU in Portugal's total trade after 10 years of membership was 75%. In the same period Spain's exports to the EU increased by 404% and imports from the EU increased by 505%.<sup>63</sup>

#### **4.2. Foreign Direct Investment Effects**

Turkey offers a huge and dynamic domestic market to foreign investors with a population of more than 70 million people and a Gross National Product (GNP) of 251 billion USD for 2004. Approximately 63% of the population in Turkey is below the age of 35. Turkey enjoys a unique location bridging Europe and Asia. With working average for an employee of 280 days per year and 9 hours per day, Turkey ranks third hardest working country in the world.<sup>64</sup>

However these positive facts do not change Turkey's unsuccessful performance of Foreign Direct Investment (FDI). Customs Union did not able to reverse it either. Table 3.6 shows FDI inflows to Turkey from 1980 to 2003.

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<sup>63</sup> DTM, AB ve Türkiye. 5. Baskı. Ankara: 2002, P:436

<sup>64</sup> Retrieved February 22, 2005 on the World Wide Web. URL: <http://www.yased.org.tr/>

**TABLE 3.6**  
**FDI Inflows to Turkey (million USD)**

Years	Authorized FDI	Foreign Capital Companies No	Realizations
1980	97	78	35
1985	234	408	99
1990	1.861	1.856	684
1995	2.938	3.161	934
1996	3.836	3.582	914
1997	1.678	4.068	852
1998	1.646	4.533	953
1999	1.700	4.950	813
2000	3.477	5.328	1.707
2001	2.725	5.841	3.288
2002	2.243	6.280	1.042
2003*	1.208	6.511	150

\*Authorized FDI as of June 30, 2003, Realizations as of January 31, 2003.

Source: Retrieved February 22, 2005 on the World Wide Web. URL:

<http://www.hazine.gov.tr/english/ybs/geneling.htm>

FDI inflows to Turkey increased by 31% in 1996, the highest of all times, followed by decreases of 56% and 2% in 1997 and 1998 respectively, via the global economic crisis. In 1999, there was a 3% increase. Year 2000 was the year of second highest FDI inflow, \$3.5 billion, mainly generated by the 3rd GSM network. The following years' figures decreased by 22% and 18% in 2001 and 2002 respectively. The trend of global inflows of FDI is also decreasing. The total global inflows of FDI in 2003 were \$560 billion, declining from its historical peak of \$1.1 trillion in 2000. The decrease in global FDI inflows, also decreased FDI's coming to Turkey. This is the one of the reasons why FDI did not increase after customs union.

A report prepared by the State Planning Institute (DPT) on the basis of the data provided by various international organizations states that capital flow is prevented by bureaucratic obstructions and poor legislation, and the real cause for direct investment oriented foreign capital not entering Turkey at the expected level is economic and political instability.<sup>65</sup> After Turkey entered in to customs union, Turkey had 3 major economic and 2 major political crises. There were other negative effects like instable and high inflation, interest rates and lack of proper legislation. These all created an unfavorable environment for potential investors.

However, the picture has begun to change. Improving macroeconomic indicators are backed-up with political stability. One of the biggest problems was the legislation. A new FDI law (Law 4875) was enacted in June 2003 to replace the old one (Law 6224), dating back to 1954.

The new law replaces the old FDI approval and screening system with a notification and registration system, bans nationalization without fair compensation, guarantees national treatment to foreign investors, eases restrictions on FDI, eliminates the minimum capital limit, grants foreign investors full convertibility in their transfers of capital and earnings, allows them to own property without any restrictions and recognizes foreign investors' right to international arbitration. The creation of the Investment Advisory Council in March 2004, aimed at increasing Turkey's attractiveness for FDI, is another example of the importance given to foreign investment

The EU's share in FDI's coming to Turkey is 78%, between 1995 and 2002. The instability between EU-Turkey relations and uncertainty of Turkey's candidate status until 1999, then uncertainty of date for negotiations affected FDI inflows into Turkey.

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<sup>65</sup> Muzaffer Dartan, Turkey-EU Relations With Particular Reference to the Customs Union, Muzaffer Dartan&Çiğdem Nas (ed.s), The European Union Enlargement Process and Turkey. İstanbul:Libo, 2002, P:297

**TABLE 3.7**  
**FDI Inflows to CEE Countries Compared With Turkey (billion USD)**

Country	1995	1998	1999	2000	2001	2002	2003
CEE countries acceded to EU	12,2	16,7	18,6	20,3	18,4	22,6	11,5
Czech Rep.	2,6	3,7	6,3	5,0	5,6	8,5	2,6
Hungary	5,1	3,8	3,3	2,8	3,9	2,8	2,5
Poland	3,7	6,4	7,3	9,3	5,7	4,1	4,2
Slovakia	0,3	0,7	0,4	1,9	1,6	4,1	0,6
Turkey*	2,9	1,6	1,7	3,5	2,7	2,2	1,2
World	335,7	690,9	1.806,8	1.388,0	817,6	678,8	559,6
EU-15	114,6	249,9	479,4	671,4	357,4	374,0	295,2

\*As of 30 June, 2003

Source: UNCTAD, World Investment Report 2004. New York: UN, 2004, P:72

Table 3.7 shows FDI inflows to Central and Eastern European (CEE) countries that acceded to the EU in 2004 compared with Turkey. Poland, Czech Republic and Hungary received enormous amounts of FDI compared to Turkey. Is it because they provide better conditions to foreign investors than Turkey. The answer is composed of different parts. First of all, the main difference between these countries and Turkey is that these countries have started negotiations much before. Starting negotiations is stepping into the EU, which is a way better than being candidate. The amount of FDI one country receives when starts negotiations with the EU are always higher than the amount it received during the candidacy.

Second point is the political will. The importance of political will on FDI is clearly observed during last wave of enlargement. Poland, the membership of which is evaluated as the most problematic among the candidate countries, except Turkey, received a total of \$51 billion FDI during twelve-year period, until 2003. Germany's political will to see Poland as a member, is one of the main reasons why Poland received

that much FDI. Turkey, unfortunately, did not enjoy this kind of political will. Yet Turkey suffered from political unwillingness. Third point is the costs. The labor, energy, land costs of these countries are below than those of Turkey's. For example per hour labor cost in textile sector in Poland was \$1,36 whereas the per hour labor cost in Turkey is \$5,90 in 2002. Industrial electricity cost was \$0,05 in Poland and was \$0,09 in Turkey in 2002.<sup>66</sup>

Turkey is spending a lot of efforts and resources to attract FDI inflows into the country. On the other hand, Turkey exports FDI to third countries. Turkey's FDI outflows between 1997-2004 are reached to \$7 billion.<sup>67</sup> Three out of first four countries that Turkey exports FDI are the EU countries, which are Holland, England and Germany. These are also the countries that Turkish people live most.

Beside everything, one thing is certain. Turkey does not receive enough FDI that she is supposed to. The reasons are various and some are beyond Turkey's influence, like the lack of political will. Turkey's share in world FDI is only %0.278.<sup>68</sup> The amount of FDI inflows amounts less than 1% of GDP so far, which is up to 7,9% for CEE's. Table 3.8 shows ratio of FDI to GNP for selected new member CEE countries for the periods before and after negotiations start.

Table 3.8 shows clearly how starting negotiations affected the FDI inflows. Czech Republic's FDI/GNP ratio increased from 2,6% in 5 years average before negotiations start to 7,9% in 5 years average after negotiations start. The case is even better for Slovakia, whose FDI/GNP ratio increase to 6,4% from 1,2%. These figures support the claim that Turkey's unfortunate destiny in attracting FDI, ceteris paribus, will end eventually by the time negotiations start.

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<sup>66</sup> İKV, Gümrük Birliği'nin Türkiye Ekonomisine Etkileri. İstanbul:N/A, 2004, P:24

<sup>67</sup> Dünya Gazetesi, 21 February 2005, P:10

<sup>68</sup> UNCTAD, World Investment Report 2004. New York: UN, 2004, P:288

**TABLE 3.8**  
**FDI/GNP Ratio for Selected CEE Countries**

Country	Period of Negotiations (5 years average)		
	Before	After	Change
Bulgaria	3,0%	5,0%	67%
Czech Rep.	2,6%	7,9%	204%
Poland	1,9%	2,8%	47%
Slovakia	1,2%	6,4%	433%
Average	2,2%	5,5%	150%

Source: Retrieved December 08, 2004 on the World Wide Web. URL:  
[http://www.tekstilmenkul.com.tr/Arastirma/ozel\\_raporlar.aspx](http://www.tekstilmenkul.com.tr/Arastirma/ozel_raporlar.aspx)

Because of reasons explained above customs union did not have major effect on FDI inflows. However, recent developments in both political and economic area, new FDI legislation and starting negotiations for membership in 2005 are all promising factors for the progress of FDI. If things go in the way that has been going for last 2 years, it is unavoidable that Turkey will meet new peak FDI inflows figures.

#### 4.3. Financial Aid Effects

Turkey's financial relations ties with the EU began with the Ankara Agreement's Financial Protocol. It provided an amount of € 175 million loan for the period 1964-1969. Turkey used € 105,9 million for financing infrastructure projects and € 69,1



million for financing other investment projects. The loan financed 44 projects, 11 public and 33 private sector projects.

Second Financial Protocol is signed with the Additional Protocol in 1970. Protocol supplied Turkey a total of € 220 million loan, € 195 million from the Community budget and € 25 million from EIB for the period of 1971-1977. Turkey used this loan to finance € 175 million worth public sector projects and € 45 million worth private sector projects. When Britain, Ireland and Denmark joined the Community, a Additional Protocol to second financial protocol is signed, which provided an extra € 47 million loan to Turkey.

Third Financial Protocol is on May 12, 1977 and entered into force on September 01, 1979. This protocol provided Turkey € 310 million loan, € 90 million from the EIB and € 220 million from the Community budget for the years between 1979-1982. By the time December 1982, € 220 million was assigned to infrastructure and public sector projects and € 90 million was assigned to private sector projects. In 1980, because of the particularly difficult situation in Turkey, the Community granted a special aid package of € 75 million, grants for eleven projects, mainly in the energy, health, environment and education sectors.

The details of the Fourth Financial Protocol was decided in the meeting of Association Council on June 30, 1980. This protocol supplied Turkey € 600 million for 5 years between 1982-1986. Of this amount, € 325 million loan and € 50 million grant was assigned from the Community budget and rest was from the EIB. Negotiations on the protocol was completed on the first half of 1981 and initialed by the parties on June 19, 1981. However due to political reasons, mainly because of Greek veto, it did not entered into force.

In 1993 and in 1995 Turkey received twice a sum of € 3 million for administrative cooperation measures.

**TABLE 3.9**  
**Financial Support of the EU 1963-1995 (million)**

	Period	Loan	Grant	Total
I. Fin. Protocol	1964-1969	€ 175	-	€ 175
II. Fin. Protocol	1971-1977	€ 220	-	€ 220
Additional Pro.	1971-1977	€ 47	-	€ 47
III. Fin. Protocol	1979-1981	€ 310	-	€ 310
Special Aid	1980-1982	-	€ 75	€ 75
IV. Fin. Protocol	1982-1986	€ 550	€ 50	€ 600
Gulf War Aid	1991	€ 175		€ 175
Adm. Cooperation	1993-1995	-	€ 6	€ 6
<b>Total</b>		<b>€ 1.477</b>	<b>€ 131</b>	<b>€ 1.608</b>

Source: DTM, AB ve Türkiye. 5. Baskı. Ankara: 2002, P:445

Table 3.9 shows the financial support of the EU between 1963-1995. The EU allocated €1.608 million to Turkey in 32 years. Out of €1.608 million, Turkey could use only €1.008 million. The fourth Financial Protocol was not entered into force due to political reasons. Without any doubt, this amount is very small, especially when compared with the countries who receive financial aid from the EU and who do not have any association ties with the EU. For example, Yugoslavia between 1958-1993 received € 1.607 million from the Community. Egypt in the same period enjoyed € 1.463 million.<sup>69</sup> These countries did not have any obligations to fulfill against the Community like Turkey. The objective of financial aids is stated in the Financial Protocol of Additional Protocol as “promote an accelerated development of the Turkish economy in order to facilitate the pursuit of the objectives of the Agreement establishing an Association between the European Economic Community and Turkey” .

<sup>69</sup> Nurettin Bilici, *Avrupa Birliği Mali Yardımları ve Türkiye*. Ankara; Akçağ, 1997, P:136

Therefore, instead of being favored by the Community, Turkey unfortunately did not seem to have any special treatment from the Community before customs union.

The purpose of the financial aids was to prepare uncompetitive Turkish economy to the effects of customs union. Within this framework, before the customs union entered into force, financial cooperation between EU-Turkey started again. In the first half of 1995, the EU detailed principles of a new financial cooperation. The plan foresees these steps:<sup>70</sup>

- i. There will be important amount of budget resources supplied to Turkey in 5 years time starting from 1995,
- ii. Turkey will continue to enjoy from New Mediterranean Policy like the period 1992-1996,
- iii. After the beginning of customs union, in order to increase the competitiveness of Turkish economy, the EIB loans will be supplied,
- iv. From 1996 Turkey will benefit all the financial means that the EU provides to Mediterranean countries,
- v. Upon the request of Turkey, possibility of providing extraordinary macro economic aid for implementing International Monetary Fund (IMF) programmes

This financial cooperation has never been implemented due to Greek veto.

Table 3.8 shows clearly how starting negotiations affected the FDI inflows. Czech Republic's FDI/GNP ratio increased from 2,6% in 5 years average before negotiations start to 7,9% in 5 years average after negotiations start. The case is even better for Slovakia, whose FDI/GNP ratio increase to 6,4% from 1,2%. These figures support the claim that Turkey's unfortunate destiny in attracting FDI, *ceteris paribus*, will end eventually by the time negotiations start.

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<sup>70</sup> Retrieved March 12, 2005 on the World Wide Web. URL:  
<http://www.deltur.cec.eu.int/default.asp?lang=0&ndx=12&mnID=3&ord=5&subOrd=1>

**TABLE 3.10**  
**Financial Support of the EU 1996-2000 (million)**

	Period	Loan	Grant	Total
MEDA I	1995-1999	-	€ 376	€ 376
Budget	1996-2000	-	€ 375	€ 375
Misc. Aids	1992-1999	-	€ 14	€ 14
EIB	1996-2000	€ 750	-	€ 750
New Medit. Policy	1992-1996	€ 340	-	€ 340
MEDA II	1997-1999	€ 205	-	€ 205
Risk Capital	1999	€ 12	-	€ 12
Macro Eco. Aid	-	€ 200	-	€ 200
Total		€ 1.507	€ 765	€ 2.272

Source: DTM, AB ve Türkiye. 5. Baskı. Ankara: 2002, P:450

The EU assigned only €2.272 million to Turkey for 5 years, yet it did not let Turkey to use it all. These financial supports should be linked to economic conditions and reasons; unfortunately, the EU did the reverse. For example, Spain received € 6 billion, € 3 billion as grants from the EU in 1996. Greece enjoyed € 4,5 billion, and € 4 billion as grants. This country received € 44,2 billion financial aids from the EU between 1981-1996.<sup>71</sup> “These countries receive more because they are member countries is inadequate to explain this inequality.” There is clear political bias in favor of member countries. Turkey, without any authority in decision-making mechanisms accepted to join customs union yet the EU makes discrimination.

After the earthquake disaster in 1999, the EU immediately provided € 35 million grants to Turkey. The EIB also gave €600 million loan under Turkey Earthquake Relief and Rehabilitation Aid (TERRA). The EU’s earthquake aid totaled to € 635 million.

<sup>71</sup> Onur Öymen, Türkiye’nin Gücü. İstanbul: AD Yayıncılık, 1998, P:200

Turkey used € 125 million, € 35 million as grants, and € 90 million as loans, of this amount.

Following the Helsinki European Council in 1999, a pre-accession strategy was introduced to the financial assistance programmes with Turkey. Assistance continued to be available for structural adjustment, in co-ordination with the international financial institutions, in addition assistance also began to focus on institution building, investment, and supporting the participation of Turkey in Community programmes and agencies. The Council adopted on December 17, 2001 a regulation concerning pre-accession financial assistance for Turkey. In its Strategy Paper of 2002, the Commission envisaged that total assistance should be substantially increased, taking into account Turkey's needs and absorptive capacity. The Copenhagen conclusions confirmed that from 2004 this assistance would be financed under the pre-accession expenditure heading of the 2000-2006 financial perspectives. The Commission has adopted on February 12, 2003 a proposal and transmitted it to the Budget Authority. In this respect, pre-accession financial assistance for Turkey will be € 1.050 million between 2004-2006. Turkey will receive € 250 million, € 300 million and € 500 million in 2004, 2005 and 2006 respectively.

**TABLE 3.11**  
**Financial Support of the EU 2000-2006 (million)**

	Period	Loan	Grant	Total
MEDA II	2000-2006	-	€ 1.659	€ 1.659
Euro-Med II	2000-2006	€ 1.470	-	€ 1.470
Pre-Acce. Strategy	2000-2002	-	€ 15	€ 15
Pre-Acce. Strategy	2000-2002	-	€ 135	€ 135
Customs Union	2000-2004	€ 450	-	€ 450
Pre-Acce. Fin. Asis.	2004-2006	€ 1.050	-	€ 1.050
<b>Total</b>		<b>€ 2.970</b>	<b>€ 1.809</b>	<b>€ 4.779</b>

Source: DTM, AB ve Türkiye. 5. Baskı. Ankara: 2002, P:452

Table 3.11 shows the financial assistance of the EU for Turkey between 2000 and 2006. In the framework of Meda II, during the 2000-2006 periods, € 889 million was allocated to Turkey. This amount is increased to € 1.659 million with the Commission's proposal on February 12, 2003. The proposal also provided Turkey accession financial assistance, € 1.050 million, between 2004-2006. Turkey will receive a total of € 1.470 million from the EIB Euro-Med II facility. The Commission adopted two draft regulations to support financially the European strategy for Turkey. A first regulation reinforcement of customs union of € 15 million over a three-year-period. A second regulation economic and social development foresees € 135 million over a three-year-period, 2000-2002. The EIB loan of € 750 million could not be supplied to Turkey due to political reasons. Because of this, a € 450 million EIB loan is allocated for the period 2000-2004. Turkey used € 759 million, € 669 million as grants and the rest as loans.<sup>72</sup>

**TABLE 3.12**  
**EU-Turkey Financial Aids 1963-2006 (million)**

	Period	Loan	Grant	Total Allocated	Total Used
Association	1953-1995	€ 1.477	€ 131	€ 1.608	€ 1.008
Customs Union	1996-2000	€ 1.507	€ 765	€ 2.272	€ 755
Earthquake	1999	€ 600	€ 35	€ 635	€ 125
Pre-Acce. Strategy	2000-2006	€ 2.970	€ 1.809	€ 4.779	€ 759
<b>Total</b>		<b>€ 6.554</b>	<b>€ 2.740</b>	<b>€ 9.294</b>	<b>€ 2.647</b>

Source: Compiled from several sources

<sup>72</sup> İKV, Gümrük Birliği'nin Türkiye Ekonomisine Etkileri. İstanbul:N/A, 2004, P:58

Table 3.12 shows the financial support of the EU in the past 42 years. This table proves two important points. First, without any doubt, not enough sources are allocated to Turkey. Second one is about the usage; EU does not even let Turkey to use this minimum amount of support. So far, Turkey was able to use only 28% of sources allocated. This situation leads to the fact that Turkey faced the economic burden without much support of the EU.

#### **4.4. Competition Effects**

Regulations concerning competition in the Europe date back to the 1958. The reason was the cartels, which emerged between two World Wars led to a need for making competition regulations in Europe. During this period, intense emergence of cartels in Germany particularly and their support for National Socialists aroused the opinion that cartels had played a central role in the development of totalitarian regimes pushing the world into war, and caused a strong tendency in Europe against cartel formations. Germany being in the lead, by 1958 the German Cartel Act, competition acts commenced to be passed in many European countries, which adopted democratic order. However, the real important development began with the process initiated by the European Coal and Steel Community Agreement signed on April 18, 1951, the Rome Treaty establishing the European Economic Community entered into force in January, 1958. The ECSC Agreement exclusively directed at coal and steel sectors involves two important articles (articles 65 and 66) in terms of competition regulations. The provisions of the articles also pioneered the competition system envisaged in the Rome Treaty.

Article 2 of the Rome Treaty set the main goal as "the creation of a common market between the member states", and "the establishment of a system that would

ensure that competition is not distorted in the internal market" embodied in article 3 (g) was considered as a means aimed at this goal. Within this framework, the Rome Treaty included a separate section entitled "Competition Policy". Competition rules were provided by articles 85 and 86<sup>73</sup>, which, respectively, regulate practices restricting competition between enterprises, and prohibit the abuse of dominant position by dominant enterprises. However, due to the conditions of the period it was signed, the Rome Treaty lacked a regulation concerning mergers and acquisitions. This shortcoming was eliminated 1990. Hence, the EU's competition policy covers antitrust and cartels, merger control, liberalization, and lastly the state aids. The Commission has wide powers to make sure fair trade is applied.

Article 16 of the Ankara Agreement envisaged that principles referred to in the provisions of the Rome Treaty concerning competition, tax and the alignment of legislation is applicable within the association relationship. The first actions in Turkey aimed at the protection of competition were in 1971 and 1975. Article 167 of the 1982 Constitution imposed on the state the task and responsibility of "taking measures ensuring and improving the sound functioning of markets for money, loan, capital, goods and services", and "preventing, in markets, de facto monopolization and cartelization or those, which shall arise by agreement".

The most important legal development was the Act on the Protection of Competition No. 4054, which was adopted in the end of 1994. This act largely sources from articles 85 and 86 of the Rome Treaty. Furthermore, it is required to mention that the favorable atmosphere created by the Customs Union and by the requirements in the Decision 1/95 has undoubtedly played an important role during the adoption process of the Act.

The purpose of the Act on the Protection of Competition No. 4054 is detailed in Article 1 as, to prevent agreements, decisions and practices preventing, restricting or

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<sup>73</sup> In accordance with article 12 of the Amsterdam Treaty, which entered into force on May 01, 1999, new article numbers of articles 85 and 86 of the Rome Treaty have been changed as 81 and 82.



distorting competition in the markets for goods and services and the abuse of dominance by the firms dominant in the market, and to ensure the protection of competition by performing the necessary regulations and supervisions to this end. It is possible to gather under three main headings the provisions in the Act, aimed at realizing this goal:

- i. Provisions related to agreements, decisions and practices, which prevent, distort or restrict competition, concluded between any undertakings operating in or affecting the markets for goods and services within the boundaries of the Republic of Turkey.
- ii. Provisions related to the abuse of dominance by the undertakings dominant in the market.
- iii. Provisions related to any kind of legal transactions and behavior having the nature of mergers and acquisitions which aim at creating a dominant position or strengthening an existing dominant position, and which shall consequently decrease competition to a significant extent.

On November 04, 1997, the Turkish Competition Board, with 11 members, was set up. The most important responsibilities of the Board are:

- i. To make examination, research and investigation, upon application or on its own initiative, regarding the prohibited activities; and take necessary measures for the termination of such infringement, and impose administrative fines on those responsible for it,
- ii. To assess the exemption and negative clearance requests of those concerned, grant an exemption and negative clearance certificate to appropriate agreements,
- iii. To follow up continuously the markets with which the exemption decisions and negative clearance certificates are related, and in case changes are determined in these markets or the conditions of parties, to reassess the applications of those concerned,
- iv. To allow mergers and acquisitions,
- v. To opine, directly or upon the request of the Ministry, regarding necessary changes to be made to the legislation on competition law,

- vi. To follow up the legislations, practices, policies and measures of other countries in respect to the agreements and decisions restricting competition,
- vii. To negotiate and resolve about the recommendations in issues of purchasing, selling or hiring such as the purchase of movable and immovable goods and fixture, and make necessary relevant arrangements.

In 1995, as a result of Decision 1/95 the Act on the Protection of Consumers was entered into force.

Although Turkey made a major progress in the harmonization of competition laws there is still a way to go. The legislation on antitrust and cartels and merger control is largely aligned with that of the EU's. The areas that need improvement are:<sup>74</sup>

- i. Effective coordination between the Competition Board and sectoral regulatory authorities in order to promote competition -like the protocol with Telecommunication Authority-, in regulated sectors such as the Energy Markets Regulatory Authority and the Banking Regulatory and Supervisory Agency.
- ii. Adaptation of state aid legislation, to provide an operationally independent state aid monitoring authority. Currently, State Aid Monitoring and Supervising Board, along with DPT render judgments on the propriety of particular state aid programs.<sup>75</sup>
- iii. Improvement in competition conditions in the alcoholic beverages sector. Transfer of the regulatory power from state monopoly to Tobacco and Alcoholic Beverages Board is not satisfactory because of the provisions that stem from the legislation in 2001, which are in contradiction with the Customs Union.
- iv. Alignment in the adjustment of state monopolies and companies having exclusive and special rights.

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<sup>74</sup> The Commission's 2004 Regular Report on Turkey's Progress Towards Accession, P:91-94

<sup>75</sup> OECD, Peer Preview of Turkey's Competition Law and Policy. Paris: OECD, 2005, P:17

The issue of state aids has been on the agenda since the beginning of customs union. Unlike its counterparts in the EU, Turkish Competition Board was not granted with the authority on state aids. Unfortunately, Turkey still not completed the infrastructure for the harmonization of state aid laws and the organization of the independent authority to control state aids.

Free market economy is often said to be the best way of utilizing resources. However free market economy does not always lead to the optimum, sometimes markets fail. Here competition authorities come into play when market fault emerge, and play a dominant role in practicing the policies aiming both an effective allocation of resources and an increased efficiency. Today there is no argument on the importance of competition. What is more, researches conducted indicate that in countries where there is an increase in competitive density, national income per capita increases as well.<sup>76</sup>

Competition leads to low prices and high quality, brings freedom of choice, encourages technological development, and increases efficiency in resource allocation. Turkey enjoyed most of these after customs union. There are numerous examples. For example, sectors that did not support customs union and promote closed economy now become the leading exporters. Another example related with the technological development is, some sectors now have a major market share in European markets. Turkish consumers' choices increased which led to prices decrease. Therefore, the Turkish consumers' utilization improved.

Customs union effected Turkey in terms of competition very positively. The more Turkey aligns her laws with that of the EU, the more benefits she will enjoy in both the short and long run.

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<sup>76</sup> Retrieved March 20, 2005 on the World Wide Web. URL: <http://www.rekabet.gov.tr>

## 4.5. Other Effects

### 4.5.1. Effects on the way to membership

Customs Union decision included wide areas for mutual movement. It did not only bring arrangements on tariff rates or customs code but also brought arrangements for the development of further cooperation. This aimed to bring Turkey closer to the EU. Customs Union decision reaffirmed the significance of the objective of the Ankara Agreement and of its Article 28, which provides for the accession of Turkey to the EC “as soon as the operation of the Agreement has advanced far enough to justify envisaging full acceptance by Turkey of the obligations”. One of the reasons Turkey accepted to take place in this formation where she cannot affect the decision-making mechanisms is that Turkey saw customs union as a softener on the way to membership. As a result, Turkey became the sole country who applied customs union before membership. Besides all negative parts, there are also positive consequences of this.

Through all those years, Turkey gained a great experience of working with the EU institutions. Even this is a great opportunity for Turkey in the sense that it can be used to ease the negotiation process. Secondly, Turkey has been making adjustments since 1963 to align her law to those of the EU’s. This is in a way implicit harmonization, which Turkey will begin officially after October 3, 2005. Therefore, Turkey will not start from 0% harmonization of the ‘acquis communautaire’. Most of the harmonization in these chapters is completed:<sup>77</sup>

- i. Chapter 1: Free Movement of Goods
- ii. Chapter 5: Corporate Law

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<sup>77</sup> TÜSİAD, Avrupa Birliği’ne Uyum Sürecinde Gümrük Birliği’nin Dış Ticaretimize Etkileri. İstanbul: Lebib Yalkın, 2003, P:73

- iii. Chapter 6: Competition
- iv. Chapter 23: Rights and Health Protection of Consumers
- v. Chapter 25: Customs Union
- vi. Chapter 26: External Relations
- vii. Chapter 30: Corporate Structure

According to the negotiation periods of 10 new members of the EU, average days to close these chapters are:<sup>78</sup>

- i. Chapter 1: 353 days
- ii. Chapter 5: 610 days
- iii. Chapter 6: 989 days
- iv. Chapter 23: 60 days
- v. Chapter 25: 523 days
- vi. Chapter 26: 346 days
- vii. Chapter 30: 364 days

Therefore, unlike other candidate countries Turkey will start negotiations with two important inputs: the experience with the EU and the progress that has been done until now. Turkey can use these throughout the negotiation process.

#### **4.5.2. Effects on Technical Barriers to Trade**

Article 8 of the 1/95 Decision stated that: “Within five years from the date of entry into force of this Decision, Turkey shall incorporate into its internal legal order the Community instruments relating to the removal of technical barriers to trade”. According to this article, Turkey was supposed to align with the *acquis* on removal of technical barriers to trade, within the free movement of goods, by the end of 2000.

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<sup>78</sup> Retrieved March 25, 2005 on the World Wide Web. URL: [http://www.maoner.com/ab\\_muzakere\\_sure.htm](http://www.maoner.com/ab_muzakere_sure.htm)

However, the alignment is not completed yet. There are still around 500 directives to implement to reach full harmonization.<sup>79</sup>

Customs Union decision particularly focused on standardization, the process by which product standards and regulations are developed and adopted.<sup>80</sup> Turkish Standards Institute (TSE), established in 1960, is the centerpiece organization responsible to prepare and publish Turkish standards for all types of materials, products and services. TSE has full memberships in the International Standardization Organization (ISO) and International Electrotechnical Commission (IEC) and affiliate memberships in the European Committee for Standardization (CEN) and European Committee for Electrotechnical Standardization (CENELEC). TSE is adopting CEN/CENELEC standards. At the end of 2004, the number of mandatory standards to be adopted was around 500.

All imported products that are subject to mandatory standards must hold a Certificate of Conformity (TSE mark) and a quality Conformance Certificate (TSEK), produced by the TSE prior to importation. This creates an environment in which Turkey is the one to continue barriers. Recently, on February 2004, the procedure is simplified for products bearing Conformance European (CE) marking. Delays and unnecessary documentation act as a technical barrier against foreign producers, placing them in an unfavorable position in the domestic market.

In the area of accreditation, Turkish Accreditation Authority (TÜRKAK) is established in 1999. The role of this independent authority is to accreditate bodies, which will assess suitability of products to technical laws. TÜRKAK has accredited 24 bodies. However because a multilateral agreement with the European Cooperation for Accreditation multilateral agreement is not signed yet, TÜRKAK's accreditations are not recognized in the EU. Therefore, TÜRKAK should become a signatory and with

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<sup>79</sup> The Commission's 2004 Regular Report on Turkey's Progress Towards Accession, P:77

<sup>80</sup> Article 8, Paragraph 4 of the 1/95 Decision: "The Parties stress the importance of effective cooperation between them in the fields of standardization, metrology and calibration, quality, accreditation, testing and certification"

cooperation conformity, assessment bodies' difficulties in achieving acceptable traceability and reliability should be removed.

Removing technical barriers to trade is Turkey's obligation not only because of CU but also because of WTO's regulations against technical barriers to trade agreement. In order to reach the goal of free movement of goods Turkey should complete harmonization, which was supposed to be completed at the end of 2000, as soon as possible. What has been done, in the sense of harmonization, made the free movement of goods chapter relatively easy one to complete in the negotiations and represent an important step forward in Turkey's integration with the EU Single Market.

#### **4.5.3. Effects on Intellectual Property Rights**

In Article 31 of the Customs Union Decision, the EU and Turkey re-confirmed the importance they attach to the obligations arising the agreement on trade related aspects of intellectual property rights (TRIPs) concluded in the Uruguay round of multilateral free trade negotiations. Turkey was required to adopt and implement, the provisions of the WTO TRIPs until 1999, accede by 1996 to the Paris Act (protects library and artistic works), Rome Convention (protects performers, producers of phonograms and broadcasting organizations), Stockholm Act (protects industrial property) and Nice agreements (concerns the international classification of goods and services for the purposes of the registration) and adopt by 1996 domestic legislation on the protection of intellectual property rights (IPRs) that is compatible with EU directives.

Turkey has made considerable progress in the area of IPRs. Major steps are: Turkish Patent Institute's legal certainty increased, having full responsibility for the registration and administration of patents and IPRs on November 2003; Turkey ratified

and acceded to the European Patent Convention on November 2000; Specialized courts to handle cases related to IPRs are established in 2001.

However, despite the positive position there is still much to do. Piracy and counterfeit is a serious problem. The International Intellectual Property Alliance (IIPA) estimated that the total trade loss due to piracy reached \$131.5 million in 2002. The loss between 1999 and 2002 is \$794.2 million. Although the figures are decreasing still the IIPA describes Turkey as “one of World’s worst book piracy market”.<sup>81</sup> In March 2004, exclusive investigation and enforcement police teams for IPRs crimes are established in major cities.

Turkey has not yet joined the World Intellectual Property Organization (WIPO) Copyright Treaty or the WIPO Performances and Phonograms Treaty. Furthermore, in the area of industrial property rights, Turkish law on the legal protection of designs is not fully compatible with the EU.

Neither the number of specialized IPR courts nor the number of trained judges and prosecutors are yet sufficient considering the huge number of IPR infringement cases.

Improvement in IPRs is important. Because they may act as a powerful signaling mechanism for potential investors. By acquiring a sound set of IPR rules and a transparent and reliable monitoring system, Turkey will provide a better environment for strengthening FDI.<sup>82</sup>

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<sup>81</sup> Retrieved March 25, 2005 on the World Wide Web. URL: <http://www.iipa.com/rbc/2004/2004SPEC301TURKEY.pdf>

<sup>82</sup> Sinan Ülgen, Yiannis Zahariadis, *The Future of Turkish-EU Trade Relations*. Centre For European Studies, P:21 (Retrieved March 25, 2005 on the World Wide Web. URL: <http://www.ceps.be>)



#### 4.5.4. Effects on Public Income

One major principle of customs union is abolishing tariffs for intra trade, and applying a common tariff rate for trade with third countries. These directly affect government revenue from customs. When government loses revenue from customs, it has to compensate the loss from somewhere, for example by raising taxes.

The same course was also expected for Turkey. Studies estimated that Turkey would lose tariff revenue equal to 1.4% of GDP.<sup>83</sup> However, figures did not support this expectation. The share of customs revenue in GNP was 2,31% in 1994. In 1996, the ratio was %2.61. In addition foreign trade revenues increased by 134% in 2000 when compared to 1999. These figures prove that Customs Union did not cause revenue loss in fact created a minor increase.<sup>84</sup>

### 4.6. Effects on Automobile Sector and Textile Clothing Sector

#### 4.6.1. Automobile Sector

Automobile sector was known to be one of the least supporters of customs union. They argued that sector is not mature enough to face a severe competition from the EU,

<sup>83</sup> Glenn W. Harrison, Thomas F. Rutherford, David G. Tarr, Economic Implications for Turkey of a Customs Union with the European Union. The World Bank International Trade Division, Policy Research Working Paper, No:1599, 1996, P:3

<sup>84</sup> TÜSİAD, Avrupa Birliği'ne Uyum Sürecinde Gümrük Birliği'nin Dış Ticaretimize Etkileri. İstanbul: Lebib Yalkın, 2003, P:89

so the government should continue to protect the sector. The Customs Union entered into force as it is supposed to be. Today automobile sector is one of the biggest gainers from the customs union.

After 90's foreign automobile companies' interest in Turkey increased. This resulted by their investments. Today the 15 largest companies are established by foreign investment and out of these 8 companies are EU original. In Turkey 80% of production in the sector is exported. The 70% of total exports are exported to the EU.<sup>85</sup> The share of the sector in Turkey's total exports to the EU increased from 4,5% in 1994 to 15% in 2002. The share in total imports from the EU increased to 14% from 9% in the same period.

Automobile products export recorded continuously increasing trend. Non-EU original automobile companies aimed to benefit from quota and tariff free environment that Turkey provides to access the EU market. Investments of foreign automobile companies to Turkey, increased the quality of infrastructure. Some EU companies shifted production of some types to Turkey. It started with Fiat's Tempra and continued with various types like Renault Megane and Fiat Doblo. Sector is mainly composed of EU original companies. This led to fast harmonization of EU standards compared to other sectors. In addition, relatively low cost and qualified Turkish labor and Turkey's geographical location, which formed benefits to EU companies for exports to Middle and Far East markets, helped an export focused production understanding to settle. The supplier industry did not compete with the competition after the customs union. They then turned to export. Therefore, increase in supplier industry export also increased the automobile sector total exports.

Imports also increased after customs union. However, the import figures, like Turkey's general import trend, are directly affected from the global or local economic situation. For instance, in 2000 imports increased by 68% and in the severe economic

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<sup>85</sup> Retrieved March 26, 2005 on the World Wide Web. URL: <http://www.osd.org.tr/disticaret2003.pdf>

crisis in 2001 decreased by more than 65%. The reasons of increase are mainly due to increase in the consumer quality consciousness and interest decrease in consumer loans. The supplier industry imports also increased. The imports of supplier industry from the EU were around 15% before the customs union, however after customs union the rate increased to around 60%. This is due to uncompetitive ness of domestic supplier industry.<sup>86</sup>

The aquis adaptation was more rapid than other sectors. The labor is qualified, young and cost low in Turkey. R&D studies and exclusive production of some types created know-how. These gave Turkey an opportunity to enjoy, which is a chance to become production base. Today there are around 30 brands in the automobile sector. The internal market becomes competitive after customs union. The local producer share decreased to 15% from 45%.

Therefore, automobile sector gained from customs union. Sector is R&D and technology based, Turkey's progress is very hopeful and has potential future earnings. The internal market opened to competition, the quality and after sales services improved whereas prices decreased, which in turn increased consumer utility. Sector learned export based production, and isolated itself from domestic economic fluctuations as possible as they can. Therefore, it continued to grow independent of economic crises.

#### **4.6.2. Textile and Clothing Sector**

Turkey is the World's sixth biggest textile and clothing exporter. This is enough to mention the importance of the sector for Turkey. There was an expectation that with the completion of customs union Turkey's share will increase in EU textile and clothing market. It is based on the Article 60 of the 1/95 Decision which eliminates quotas in 14

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<sup>86</sup> İKV, Gümrük Birliği'nin Türkiye Ekonomisine Etkileri. İstanbul:N/A, 2004, P:68-70

product groups, that had been applied since 1982. Because of this very reason, textile and clothing sector strongly defended completion of customs union. Yet the expectations are not fulfilled at the desired level.

Before the customs union the share of EU in Turkey's total, textile and clothing sector was 64,3% in 1995. After the customs union although the value of exports increased, the total increase in the sector was higher. Because of this, the share of EU in Turkey's total textile and clothing sector began to decrease. It decreased to 62% in 1998, then increased to 66% in 2003. The reason is the competition that Turkey faced from CEEC and North African Countries on the labor costs particularly in the clothing sector.<sup>87</sup>

The textile and clothing sector's import from the EU is also decreased. In 1996, the share increased to 46,5% from 30,9%. This was due to CCT, that is applied to 24 countries, and which created a benefit for EU to access Turkish market. The share then started to decrease, and went down to 37,7% in 2003.

There was no major *acquis* adaptation that changed the way of doing business. Although textile and clothing is an important sector for Turkey, quality or efficiency improvements were not done before customs union. The cost is paid by low exports. In addition, the sector is mainly labor intensive, not technology intensive like the electronics sector. Therefore, besides the cost of sources like land and energy, the cost of labor is very important. It directly effects total cost, so the price, competitiveness and export ability. The quality and time elasticity of production are important factors but clearly not important as cost of labor is. Turkey's export composition is changing from labor intensive to technology intensive products, where the value added is high and export capacity is greater. The CEEC's are Turkey's one of the important competitors in the EU market. Now they are members and have the authority in the decision-making mechanism but Turkey does not. Moreover, from the beginning of 2005 the textile and clothing trade is subject to WTO rules and regulation, which means free trade for the

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<sup>87</sup> İKV, Gümrük Birliği'nin Türkiye Ekonomisine Etkileri. İstanbul:N/A, 2004, P:79-82

sector. So Turkey loses her beneficiary position in the EU and maybe elsewhere. China and India are the most important suppliers of the World. With free trade because of highly low labor costs, they surely will win a great market share.

Therefore, Turkey's expectations from the customs union on textile and clothing sector did not realize fully. In addition, even if it were realized in a liberalized market with severe competition Turkey may not have enjoyed the benefit as much as she wanted.

## V. CONCLUSION

Customs union is a type of integration that participating countries not only remove tariff and quantitative restriction on their internal trade but also introduce a common external tariff on trade with third countries. Although there are plenty examples of customs unions there is no consensus whether customs unions makes participant countries and/or third countries better off or worse off.

Theorists evaluate the effects of customs union according to its effects on welfare. Viner, most known theorist of customs union, argues that welfare effect can be measured by the balance between the trade creation and trade diversion. If trade creation outweighs trade diversion customs union results in welfare increase. If trade diversion exceeds trade creation customs union leads to welfare decrease. Lipsey criticized Viner's argument that trade creation to be that efficient and trade diversion to be that inefficient. He argued that a simple conclusion that trade creation is efficient and trade diversion is inefficient may not be valid and a country may gain welfare by forming a customs union that creates trade diversion. Cooper and Massell, on the other hand, argued that unilateral tariff reductions are better than the customs union, since this kind of policy lead to trade creation effects without any trade diversion. Meade, similar to Viner, makes a distinction between trade creation and trade diversion effects and accepts the privileged positions of the member countries at the expense of others by saying that trade diversion leads to a decrease in welfare. Kemp and Wan argued that participating countries may increase their benefits without deteriorating the welfare levels of the third countries. Therefore, since customs union leads to a net welfare increase for both sides, it is possible to increase the scope of the customs union by covering the entire world.

The EU is the world's largest and most sophisticated example of customs union formation. In 2003 the total volume of trade in EU was \$7.438 billion with a 40% share of total world trade. The volume of intra-EU trade was €1.800 billion. Customs union is one the most important principles on which EU are established. Article 3 of the Treaty of Rome clearly says that member states must eliminate customs duties and quantitative restrictions and all other measures having equivalent effect on the import and export among themselves.

Turkey's way crossed with EU more than 45 years ago. Since the proclamation of the Turkish Republic, Turkey aligned herself with the West. Turkey was either a founding member or among the first members of organizations like NATO and OECD. As a result of Turkey's willingness to align herself with the west, Turkey applied to EEC, shortly after its establishment in 1959. The negotiations resulted in the signature of the Ankara Agreement on 12 September 1963. The objective of the agreement is to promote trade and economic relations between EU and Turkey by developing Turkish economy and welfare. In order to attain the objectives, a customs union is set to be implemented through three stages, preparatory stage, transitional stage and final stage. Additional Protocol signed on 23 November 1970, started transitional stage. It is a practice agreement and filled the frame drew by Ankara Agreement. Turkey's application for full membership 1987 resulted to accelerate the establishment of customs union. On 6 March 1995 EU-Turkey Association Council took the 1/95 decision, which is also known as Customs Union Decision. On 1 January 1996 customs union between EU and Turkey entered into force.

According to Customs Union Decision Turkey had to eliminate customs duties, quantitative restrictions and measures of equivalent effect on trade of industrial goods, including processed agricultural products, adopt measures equivalent to the EU's common commercial policy, align tariffs in line with the EU's preferential trading arrangements with certain third countries, adopt customs provisions in line with those of the EU, adopt competition rules and align legislation in this area with that of EU, adopt legislation in the field of intellectual property protection to secure a level of protection equivalent to that in the EU.

The debate on whether Customs Union with the EU is necessary and/or efficient for Turkey or not has been going on for decades. There were and still are severe criticisms against the Customs Union Decision. According to Erol Manisalı, mostly known with his views against Customs Union Decision, customs union between EU and Turkey does not consider mutual interests, and includes fundamental political, economic and legal imbalances. Unlike rest of the business world representatives Sinan Aygün, President of Ankara Chamber of Commerce, is persistently opposed to customs union. He has been claiming that, it will be more rational for Turkey if she makes a free trade agreement rather than customs union with the EU.

As mentioned at the beginning, Customs Union with the EU varies from the similar ones in the sense that it is beyond an agreement of abolishing tariff and quotas. Therefore, it directly or indirectly affects a lot of parameters. This thesis aimed to study only the parameters that are mostly known or that has enough data.

Turkey has entered into the Customs Union with EU before becoming a full member of the EU. All the other countries that established a customs union with the EU, first became a full member then entered the customs union. Article 16 and 64 of Customs Union Decision stipulates Turkey to comply with the EU in customs union related issues. On the other hand, Turkey is not represented in the decision making mechanisms of the EU. An alternative consultative mechanism is established, yet it does not work properly. So Turkey has to fulfill obligations which are dependent on unilateral decision of the EU, even if they are against Turkey's national interests. This is creating problems in WTO meetings, EU's trade agreements with third countries and so on. The absence in decision making mechanisms did not let Turkey to represent and influence the decisions taken on customs union related issues. If Turkey had taken place in decision making process, the outcome of Customs Union with the EU would have been definitely better.



Turkey's foreign trade benefited from customs union. The trade deficit with the EU was \$11.589 million in 1996. The deficit for 2004 is \$11.063. Turkey's foreign trade balance within the same period, excluding the trade with EU, increased by 165%. The X/M ratio for the period 1995-2004 is 62,6% for Turkey's total trade and 66,8% for Turkey's trade with EU. Therefore customs union did not create trade deficit, it improved the trade balance of Turkey. Turkey's exports to the EU increases constantly then the general export trend. The composition of exports change from labour intensive and less technological structure to capital intensive and high technological structure. The share of investment and intermediate goods, which provide input to the economy, in the total value of imports from the EU between the period 1995-2003 is 27% and 58% respectively. Whereas the share of consumption goods is just 15%. What is more, the customs union did not seriously reduced Turkey's trade with any other country groups.

Turkey did not received the FDI, she expected after customs union. The amount of FDI inflows amounts less than 1% of Turkey's GDP, where as this ratio is up to 7,9% for CEE's. However Turkey's situation, with 3 major economic and 2 major political crises, was not welcoming during the first 6 years of customs union. The legislation changed in June 2003. New FDI law become one of the most modern among other examples.

Unfortunately, Turkey did not take enough financial aid from the EU. The amount that is budgeted for Turkey after 1995 is €7.686 million. Turkey used 21% of this amount, which is €1.639 million. It is not that Turkey did not want to use, but vetoes do not let Turkey to use. This leads to a conclusion that Turkey worn the costs of customs union without much support the EU.

Customs Union with the EU brought obligations related to competition. Competition leads to low prices and high quality, brings freedom of choice, encourages technological development and increase efficiency in resource allocation. Turkey enjoyed most of them after customs union. On the consumer side, Turkish consumers' choices increased which led to prices decrease and improved utilization. On the producers' side, technology intensive production increased, which increased efficiency

and decreased unit costs. Today some sectors have a major market share in EU market via competition.

In the area of technical barriers to trade Turkey made a serious progress after the customs union. Turkey was supposed to remove all the technical barriers to trade until the end of 2000. The removal is not completed yet. The harmonization is made, in order to abolish all the double processes that foreign or domestic firms have to face during exporting or importing. This will decrease the bureaucracy, the paper work, transactions costs and time wasting.

Customs union makes Turkey's IPRs consciousness to improve. Turkey took major steps in order to align her legislation with those of the EU. However the alignment is not completed yet. Development in the IPRs environment is also an important criteria for FDI inflows.

The amount of public income was expected to decrease after the customs union, due to the reduction in tariffs. The outcome was not what is expected, the customs revenue was 2.31% in 1994, the ratio was 2.61% in 1996. The decrease in tariff rate is compensated with the increase in imports.

Turkey's ultimate aim is to become a full member of the EU. Turkey entered customs union with some political expectations. These expectations are rarely met. Nevertheless, Turkey gained experience of EU legislation. What is more, all the harmonisation done so far, will shorten the negotiation period. In this sense Turkey benefited from customs union.

Consequently, Turkey gained economically rather than politically from the customs union. There is no serious evidence among the topics discussed above that customs union hurt Turkish economy. However in the political sense, some negative issues such as no representation in the decision-making mechanisms, aid blockings,

absence of political willingness exist. Nevertheless it seems that economic benefits outweigh results raised from political issues.

Further studies will be useful to detail every parameter discussed in this thesis and to reach more accurate conclusions.

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## APPENDICES

### Appendix A

#### Chronology of EU-Turkey Relations

<b>1959</b>	
31 July	Turkey applies to join the EEC.
11 September	The EEC Council of Ministers accepted Turkey's and Greece's applications for associate membership.
<b>1960</b>	
27 May	EEC-Turkey relations were frozen due to the military coup in Turkey.
<b>1963</b>	
12 September	EEC and Turkey signed an Association Agreement (Ankara Agreement) to take Turkey to Customs Union and finally to full EEC membership. I. Financial Protocol was signed.
<b>1964</b>	
1 December	Ankara Agreement came into force.
<b>1966</b>	
16-17 May	First EEC-Turkey Joint Parliament meeting was held.
<b>1968</b>	
9 December	Negotiations on the Additional Protocol started.
<b>1969</b>	
6 July	Transition period negotiations started.
<b>1970</b>	
22 July	The Additional Protocol that includes the necessities of transition period was accepted.
26 October	First Customs Cooperation Committee meeting was held.
23 November	The Additional Protocol was signed. II. Financial Protocol was signed.
<b>1971</b>	
5 July	The Additional Protocol was approved by TGNA

<b>1972</b>	
13 January	EEC-Turkey negotiations that would make the Association Agreement accepted by new members of the Community started.
20 July	The period of Intermediate Agreement was extended by Association Council.
<b>1973</b>	
1 January	The Additional Protocol entered into force. A step to lowering customs duties and harmonization of the consolidated liberation list started.
30 June	First Complementary Protocol was signed.
<b>1974</b>	
1 January	Complementary Protocol went into force.
<b>1976</b>	
1 January	Turkey lowered customs duties and harmonized the consolidated liberation list according to the Additional Protocol
<b>1977</b>	
12 May	III. Financial Protocol was signed.
<b>1979</b>	
1 May	III. Financial Protocol went into force.
<b>1980</b>	
12 September	Military coup in Turkey
<b>1982</b>	
22 January	The relations between EC and Turkey stagnated following the military coup on 12 September 1980
<b>1986</b>	
16 September	EC-Turkey Association Council met. Relations that were frozen since 1980 September started again.
<b>1987</b>	
14 April	Turkey applied for full EC membership.
<b>1989</b>	
18 December	EC Commission as an answer to the application Turkey declared that Community cannot accept any new member before concluding its internal market integration in 1992, and recommends further political, economic, and social reforms in Turkey before opening accession negotiations.
<b>1991</b>	
30 September	Association Council met for the first time after 1986.

<b>1992</b>	
21 January	EC and Turkey signed a Technical Cooperation Programme.
<b>1994</b>	
28 September	European Parliament froze the activities of EC-Turkey Joint Parliament.
<b>1995</b>	
6 March	EU-Turkey Association Council took the decision of customs union.
16 November	EC-Turkey Joint Commission became active again.
13 December	1/95 Decision (Customs Union Decision) of Association Council was approved by European Parliament.
21 December	Free Trade Agreement including ECSC goods was signed between EU and Turkey.
<b>1996</b>	
1 January	Turkey concluded transition period of European integration, which lasted 22 years and entered to the last phase in full membership process with the Customs Union coming into force.
19 February	EU-Turkey Customs Union Joint Committee met for the first time.
25 July	EU-Turkey ECSC Agreement was signed in Brussels and came into force after its publication in the official gazette.
<b>1997</b>	
16 July	European Commission excluded Turkey from Agenda 2000.
12-13 December	Luxembourg European Council reconfirms Turkey's eligibility for EU membership and calls for a European Strategy to bring Turkey closer to the EU.
<b>1998</b>	
3 March	European Commission proposed European Strategy for Turkey
4 November	European Commission adopted I. Progress Report for Turkey.
<b>1999</b>	
13 October	European Commission adopted II. Progress Report.
10-12 December	Helsinki European Council confirms Turkey is an official candidate country.

<b>2000</b>	
17-18 October	EU and Turkey started Services and Public Procurement negotiations.
8 November	European Commission adopted III. Progress Report.
<b>2001</b>	
8 March	EU formally agrees to the text of the Turkish Accession Partnership.
19 March	EU Council of Ministers approved Turkey's National Programme for the Adaptation of the Acquis.
13 November	European Commission adopted IV. Progress Report.
<b>2002</b>	
21-22 June	EU declared that the decisions to take Turkey to the next step in the process of full membership can be made in the Copenhagen Presidency Council.
3 August	Turkey amended its constitution bringing it closer to meeting the Copenhagen criteria.
9 October	European Commission adopted V. Progress Report.
<b>2003</b>	
19 May	Revised Accession Partnership adopted by the Council.
24 July	Revised National Programme for the Adaptation of the Acquis adopted.
5 November	European Commission adopted VI. Progress Report.
<b>2004</b>	
6 October	European Commission adopted VII. Progress Report.
15 December	European Parliament approved to start accession negotiations with Turkey.
17 December	Brussels European Council took the decision to open negotiations with Turkey on October 3, 2005.

**Appendix B**  
**Ankara Agreement**

Principles	Article 2	<p>1. The aim of this Agreement is to promote the continuous and balanced strengthening of trade and economic relations between the Parties, while taking full account of the need to ensure an accelerated development of the Turkish economy and to improve the level of employment and the living conditions of the Turkish people.</p> <p>2. In order to attain the objectives set out in paragraph 1, a customs union shall be progressively established in accordance with Article 3, 4 and 5.</p> <p>3. Association shall comprise:</p> <p>(a) a preparatory stage;</p> <p>(b) a transitional stage;</p> <p>(c) a final stage.</p>
	Article 3	Preparatory stage
	Article 4	Transitional stage
	Article 5	Final stage
Implementation of the Transitional Stage	Article 10	Customs Union
	Article 11	Agriculture
Other Economic Provisions	Article 12	Free movement of workers
General and Final Provisions	Article 22	Association Council
	Article 28	As soon as the operation of this Agreement has advanced far enough to justify envisaging full acceptance by Turkey of the obligations arising out of the Treaty establishing the Community, the Contracting Parties shall examine the possibility of the accession of Turkey to the Community.
Provisional Protocol		
Financial Protocol		

**Appendix C**  
**Additional Protocol**

Free Movement of Goods	Article 2	Free movement of goods shall apply: (a) to goods produced in the Community or in Turkey, including those wholly or partially obtained or produced from products coming from third countries which are in free circulation in the Community or in Turkey; (b) to goods coming from third countries and in free circulation in the Community or in Turkey.
Customs Union	Article 7	The Contracting Parties shall refrain from introducing between themselves any new customs duties on imports or exports or charges having equivalent effect and from increasing those already applied, in their trade with each other at the date of entry into force of Protocol.
	Article 9	On the entry into force of this Protocol, the Community shall abolish customs duties and charges having equivalent effect on imports from Turkey.
	Article 11	Turkey shall progressively abolish, over a period of twenty-two years the basic duties in respect of the Community on the products listed in Annex 3
Common Customs Tariff	Article 17	The Turkish Customs Tariff shall be aligned on the Common Customs Tariff during the transitional stage on the basis of the duties actually applied by Turkey in respect of third countries.
Elimination Of Quantitative Restrictions	Article 21	Quantitative restrictions on imports and all measures having equivalent effect shall be prohibited between the Contracting Parties
	Article 24	The Community shall, on the entry into force of this Protocol, abolish all quantitative restrictions on imports from Turkey. This liberalization shall be consolidated in respect of Turkey.
	Article 25	Turkey shall progressively abolish quantitative restrictions on imports from the Community
Agriculture	Article 33	Over a period of twenty-two years Turkey shall adjust its agricultural policy with a view to adopting, at the end of that period, those measures of the common agricultural policy which must be applied in Turkey if free movement of agricultural products between it and the Community is to be achieved.
	Article 35	Community and Turkey shall grant each other preferential treatment in their trade in agricultural products.

Free Movement of Workers	Article 36	Freedom of movement for workers between Member States of the Community and Turkey shall be secured by progressive stages in accordance with the principles set out in Article 12 of the Ankara Agreement between the end of the twelfth and the twenty-second year after the entry into force of that Agreement.
Right Of Establishment, Services And Transport	Article 41	Parties shall refrain from introducing between themselves any new restrictions on the freedom of establishment and the freedom to provide services.
Competition, Taxation And Approximation Of Laws	Article 44	Neither Contracting Party shall impose, directly or indirectly, on the products of the other Party any internal taxation of any kind in excess of that imposed directly or indirectly on similar domestic products. The Contracting Parties shall, not later than the beginning of the third year after the entry into force of this Protocol, repeal any provisions existing at the date of its signature which conflict with the above rules.
Economic Policy	Article 52	The Contracting Parties shall avoid introducing any new foreign exchange restrictions on the movement of capital and current payments connected therewith between themselves, and shall endeavour not to make the existing arrangements more restrictive.
Commercial Policy	Article 53	The Contracting Parties shall consult each other in the Council of Association in order to achieve, during the transitional stage, the coordination of their commercial policies in relation to third countries.
General And Final Provisions	Article 58	In the fields covered by this Protocol: The arrangements applied by Turkey (Community) in respect of the Community (Turkey) shall not give rise to any discrimination between Member States, their nationals or their (Turkish nationals or Turkish) companies or firms.
	Article 60	If serious disturbances occur in a sector of the Turkish economy or prejudice its external financial stability, or if difficulties arise which adversely affect the economic situation in a region of Turkey, Turkey may take the necessary protective measures.
	Article 61	Without prejudice to the special provisions of this Protocol, the transitional stage shall be twelve years.
	Article 62	This Protocol and the Annexes shall form an integral part of the Ankara Agreement.
Financial Protocol		



**Appendix D**  
**Customs Union Decision**

Free Movement Of Goods	Article 2	<p>1. Free movement of goods shall apply to goods: Produced in the Community or Turkey, including those wholly or partially obtained or Produced from products coming from third countries, which are in free circulation in the Community or in Turkey, coming from third countries and in free circulation in the Community or in Turkey.</p> <p>2. Products from third countries shall be considered to be in free circulation in the Community or in Turkey if the import formalities have been complied with and any customs duties or charges having equivalent effect which are payable have been levied in the Community or in Turkey, and if they have not benefited from a total or partial reimbursement of such duties or charges.</p>
Elimination Of Quantitative Restrictions Or Measures Having Equivalent Effect	Article 5	Quantitative restrictions on imports and all measures having equivalent effect shall be prohibited between the Parties.
	Article 6	Quantitative restrictions on exports and all measures having equivalent effect shall be prohibited between the Parties.
	Article 8	Within five years from the date of entry into force of this Decision, Turkey shall incorporate into its internal legal order the Community instruments relating to the removal of technical barriers to trade.
Commercial Policy	Article 12	In conformity with the requirements of Article XXIV of the GATT Turkey will apply as from the entry into force of this Decision, substantially the same commercial policy as the Community in the textile sector including the agreements or arrangements on trade in textile and clothing. The Community will make available to Turkey the cooperation necessary for this objective to be reached.
Common Customs Tariff And Preferential Tariff Policies	Article 13	Upon the date of entry into force of this Decision, Turkey shall, in relation to countries, which are not members of the Community, align itself on the Common Customs Tariff.
	Article 15	Turkey may retain until 1 January 2001 customs duties higher than the Common Customs Tariff in respect of third countries for products agreed by the Association Council.

	Article 16	Turkey shall align itself progressively with the preferential customs regime of the Community within five years as from the date of entry into force of this Decision. This alignment will concern both the autonomous regimes and preferential agreements with third countries.
Agricultural Products	Article 26	The Community and Turkey shall progressively improve, on a mutually advantageous basis, the preferential arrangements, which they grant each other for their trade in agricultural products.
Protection of Intellectual, Industrial and Commercial Property	Article 31	The Parties recognize that the Customs Union can function properly only if equivalent levels of effective protection of intellectual property rights are provided in both constituent parts of the Customs Union.
Competition	Article 32	The following shall be prohibited as incompatible with the proper functioning of the Customs Union decisions by associations of undertakings and concerted practices which have as their object or effect the prevention, restriction or distortion of competition, and in particular those which: (a) directly or indirectly fix purchase or selling prices or any other trading conditions; (b) limit or control production, markets, technical development or investment; (c) share markets or sources of supply; (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage; (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations, which, by their nature or according to commercial usage, have no connection with the subject of such contracts.
	Article 42	Turkey shall progressively adjust, in accordance with the conditions and the time-table laid down by the Association Council any State monopolies of a commercial character so as to ensure that, by the end of the second year following the entry into force of this Decision, no discrimination regarding the conditions under which goods are procured and marketed exists between nationals of the Member States and of Turkey.

Taxation	Article 50	Neither Party shall, directly or indirectly, impose on the products of the other Party any internal taxation of any kind in excess of that imposed directly or indirectly on similar domestic products. Neither Party shall impose on the products of the other Party any internal taxation of such a nature as to afford indirect protection to other products.
Institutional Provisions	Article 52	EC-Turkey Customs Union Joint Committee
Consultation And Decision Procedures	Article 55	Wherever new legislation is drawn up by the Commission of the European Communities, it shall informally consult Turkish experts.