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Trade Relations between China and Turkey: A Comparison with the European Union

Could China be an alternative to Turkey's trade relations with the European Union?

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Introduction

In recent days, think tanks and media in the European Union (EU), Germany as well as the United States (US) have begun to raise questions about China's trade and investment offensive with Turkey and its economic and political consequences for Europe and the US. One of the most common questions is whether Ankara would change its Western orientation towards the EU and the US through a new strategic partnership with China.
This development is closely monitored in the EU, and especially in Germany. Cost-benefit analyses are carried out as to whether China can replace the EU countries economically and whether Turkey's departure from the West will be dependent on the Chinese economy in the coming years.

It is a fact that economic relations between Turkey and China have intensified very quickly. Since 2010, there has been a sharp increase in Chinese exports, investment (FDIs) and loans to Turkey. In contrast, Turkey's exports and investments in China developed at an insignificant low level. It means that there is an asymmetric economic relationship and a one-sided dependency between both countries.

The main objective of the working paper is to examine Turkey's trade relations with China in the context of relations between Turkey and the EU. We will analyse the advantages and disadvantages of Turkey's trade with China and the EU. The first part of the study provides a brief overview of trade relations, in particular trade flows between Turkey and China. Then Turkey's trade relations with the EU will be examined. In a final step, we will draw the consequences for the Turkish economy.

Political Relations

An important milestone in the political and diplomatic relations between Turkey and China was the signing of a friendship agreement between Turkey and the Republic of China on 4 April 1934.[2] Turkey recognized the People's Republic of China (PRC) on 5 August 1971[3]. Relations between Turkey and the PRC have been advanced since the 1980s throughout the establishment of a consultation mechanism between both countries. Bilateral relations were improved to a level of “strategic cooperation" in 2010[4]. As a NATO member, Turkey has become a "dialogue partner" of the Shanghai Cooperation Organization, in which China is a founding and leading member along with further member states India, Kazakhstan, Kyrgyzstan, Pakistan, the Russian Federation, Tajikistan and Uzbekistan[5].

[2]T.C. Resmî Gazete, “Türkiye Cumhuriyeti ile Çin Cumhuriyeti arasında 4 Nisan 1934 tarihinde Ankarada İmza edilen dostluk muahedesinin tasdikına dair kanun”, 9 June 1934, No. 2722, <https://www.resmigazete.gov.tr/arsiv/2722.pdf>. See Necati Demircan, “Interactions between Two Republics: The Republic of Turkey and the Republic of China (1923-1949)”, *BRIQ* 3, no. 1 (2021/2022): 26-39.

[3] Embassy of the People’s Republic of China in the Republic of Turkey, “China, Turkey issue joint declaration on establishing strategic relationship of cooperation”, 9 October 2010, <https://www.mfa.gov.cn/ce/cetur//eng/ztgx/t759783.htm>.

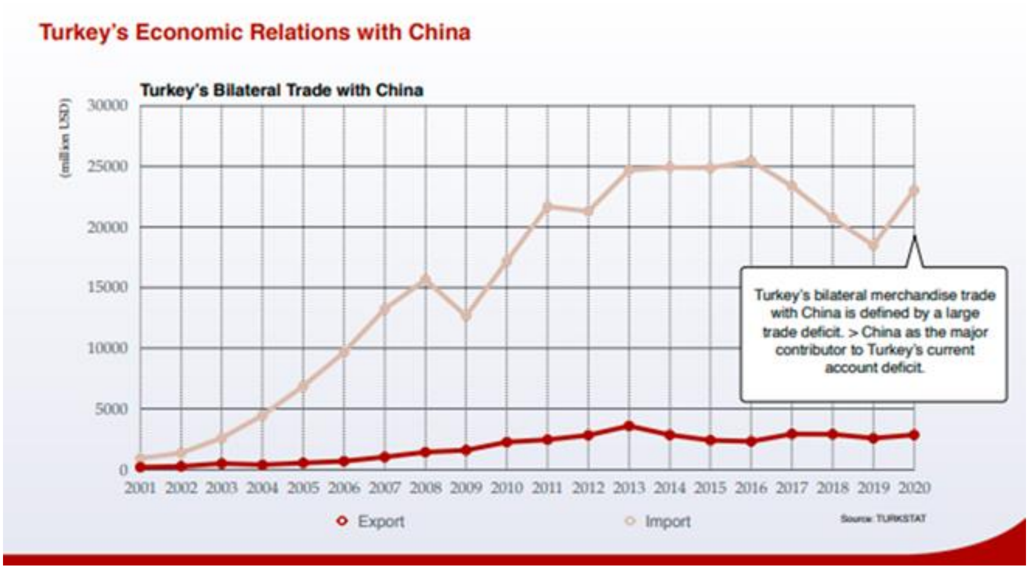
[4] Ministry of Foreign Affairs Republic of Türkiye, “Relations between Türkiye and People's Republic of China”, <https://www.mfa.gov.tr/relations-between-turkey-and-china.en.mfa> (accessed 7 February 2022). See also Chinese Embassy in Turkey, »China, Turkey issue joint declaration« [as in Fn. 3].

[5] The Shanghai Cooperation Organisation, “About SCO”, <http://eng.sectsco.org/about_sco/> (accessed 7 February 2022).

Bilateral Trade of Goods between Turkey and China

Diagram 1 shows the development of bilateral trade between Turkey and China from 2001 to 2020. Obviously, the difference between import and export has widened over the last twenty years at the expense of Turkey. Although the trade deficit has narrowed in the period 2016 to 2019, the future development of Turkey's trade deficit with China suggests that the gap between import and export of goods will not be balanced in the coming years.

Diagram 1[6]



According to the International Trade Center statistics[7], a total of USD 8.506 billion was exported from Turkey to China in three years (2018-2020), compared to USD 62,888 billion

[6] Source: Altay Atlı "China's Rise: Challenges and Opportunities", Sabancı University and Konrad Adenauer Stiftung Turkey, 30 March 2021 (Power Point Presentation); see also Ministry of Foreign Affairs Republic of Türkiye, "Türkiye-People's Republic of China Economic and Trade Relations", <https://www.mfa.gov.tr/turkey_s-commercial-and-economic-relations-with-china.en.mfa>.

[7] "Trade Map", *International Trade Center* (ITC), <https://www.trademap.org/Index.aspx>.

in imports from that country in the same period. China is not one of Turkey's most important export markets, but after Russia it is the country with the most imports.[8]

For Turkey, China is one of the countries with the most destabilizing trade balance. From 2018 to 2020, Turkey's trade deficit with China was around USD 57.4 billion, equivalent to 2.8% of Turkey's GDP in 2020.

Turkey's USD 20.2 billion deficit with China in 2020 amounts to 41.5% of the country's total trade deficit. In other words, almost half of Turkey's trade deficit comes from China. In 2020, the ratio of exports to imports in Turkey's total foreign trade was 77.2%, while in trade with China it was only 12.4%. In plain language: Turkey has a competitive disadvantage in trade with China.[9]

The most interesting feature of trade with China lies in the breakdown of trade in production sectors. It is a fact that the main products exported from Turkey to China are low added value: primary products, natural resources, raw materials, mineral ores come to the fore; whereas main products imported from China are largely of high added value and high-tech raw materials.

The share of the top 10 products in total exports to China was 75.6% in the same period. It is interesting to note that the group of SITC 25 and SITC 26 products covers around 47.3% of the exported goods. The main exports from Turkey are marble and travertine, chromium, copper, lead, iron, natural borate, boron oxide, boric acid.[10]

Looking at imports from China by commodity, the share in total imports from China of the two main commodities - SITC 85 and 84 - is 51.6%, mainly in manufacturing and high-tech products.[11] If we compare the export and import figures of trade with China, it is obvious that trade in goods between China and Turkey is largely characterized by *inter-trade specialization.*

In other words, both countries export and import completely different types of goods. Turkey mainly exports agricultural raw materials, minerals and labor-intensive goods, and imports largely capital-intensive and high-tech products from China, as if trade relations between developed and undeveloped countries were taking place. The trade figures clearly show that Turkey's trade relation with China is asymmetric. Even though future development of trade between both countries seems to be improving, it is at the expense of the Turkish economy.

[8] Ibid.

[9] The export-to-import ratio, the value of the export of goods divided by the imports of goods. Values above one indicates a positive trade balance, while values less than one indicate a negative trade balance. Turkey's imports from China are compared to exports to that country.

[10] SITC 25: Salt; sulfur; earth and stone; cleaning agents, lime and cement and SITC 26: Ores, slags and ashes.

[11] SITC 85: Electrical machinery and equipment as well as parts thereof; sound recording and playback equipment, television, and SITC 84: Machinery, mechanical equipment, nuclear reactors, boilers; parts of it.

Turkey's Trade with the European Union

As a next step, let us briefly focus on the trade relations of Turkey with the EU. We then will compare it with the trade relations of Turkey with China. Finally, we will come to the question: What are the costs and benefits of trade relations between Turkey and China as well as Turkey and the EU?

Trade in Goods and Services

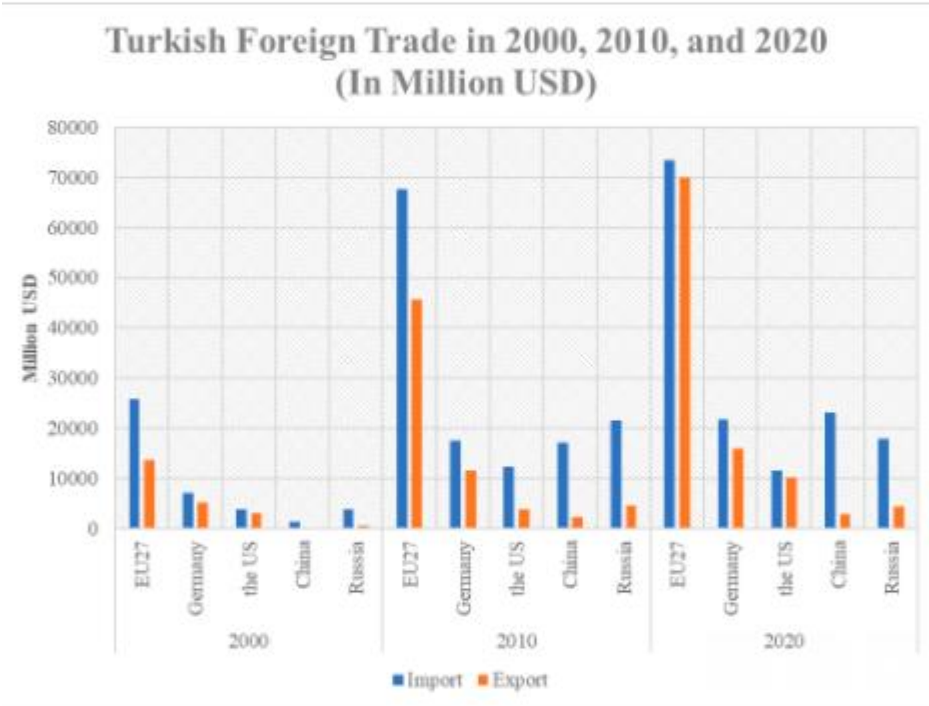
The trade relations of Turkey with the EU can be summed up as follows:

- "Turkey is EU's 6th biggest trade partner, representing 3.6% of the EU's total trade in goods with the world in 2020."[12]
- "The EU is by far Turkey's largest import and export partner, as well as its main source of investments. In 2020, 33.4% of Turkey's imports came from the EU and 41.3% of the country's exports went to the EU."[13]
- Diagram 2 shows total trade in goods between the EU and Turkey in 2020 amounted to EUR 132.4 billion. While EU's imports from Turkey were worth EUR 62.6 billion[14], EU's exports to Turkey totaled EUR 69.9 billion. It can be easily seen that trade in goods and services between the EU and Turkey is largely characterized by *intra-trade specialization.* It means that both sides export and import mainly manufacturing goods.
- Thus, trade deficit in 2000 was EUR 7.3 billion in favour of the EU (2018: EUR 2.3 billion) and in 2019 EUR 1.5 billion in favour of Turkey. The same diagram demonstrates two-way trade in services in 2019 between the EU and Turkey amounted to EUR 26.5 billion; of those EU imports of services representing EUR 13.9 billion and exports EUR 12.6 billion. It is interesting to note that Turkey had a positive trade surplus in the trade of services in the period of 2017-2019. The trade surplus in services in favour of Turkey was EUR 1.2 billion in 2017, EUR 0.7 billion in 2018 and EUR 1.3 billion in 2019.

[12] European Commission, "Turkey – Trade Picture", <https://ec.europa.eu/trade/policy/countries-and-regions/countries/turkey/> (accessed 7 February 2022).
[13] Ibid.
[14] Ibid. Turkey's export to the EU's were worth €62.6 billion and were led by machinery and transport equipment (€24.1 billion, 38.5%), clothing (€8.3 billion, 13.3%), and agriculture and raw materials (€5.3 billion, 8.5%). Turkey's import from the EU were led by machinery and transport equipment (€24.1 billion, 38.5%), clothing (€8.3 billion, 13.3%), and agriculture and raw materials (€5.3 billion, 8.5%).

Diagram 2: EU-Turkey Trade in Goods and Services[15]

Diagram 3: Turkish Foreign Trade[16]



[15] Source: European Commission, "Turkey – Trade Picture", <https://ec.europa.eu/trade/policy/countries-and-regions/countries/turkey/>.
[16] Source: Table was updated to include the year 2020 from: Ziya Oniş and Maimaiti Yalikun, "Emerging partnership in a post-Western world? The political economy of China-Turkey relations", *Southeast European & Black Sea Studies* 21, no. 4 (2021), <https://doi.org/10.1080/14683857.2021.1981624>.

- Diagram 3 shows the distribution of Turkish foreign trade by country and region from 2000 to 2020. By closer examination, Turkey's foreign trade volume increased from USD 82 billion to USD 390 billion over the past 20 years. The importance and weight of the EU/27 countries in Turkey's foreign trade have not changed at all in its distribution of countries and regions in 2020. In the same year, Turkey's EU/27 exports account for 41.3%. In contrast, China and Russia together share 3.7%. In other words, China and Russia have no importance in Turkish exports. In terms of import figures, China and Russia account for 20% of total imports. This remained unchanged in 2020. This means that Turkey constantly has a trade deficit with these two countries and a comparative disadvantage.[17]

- Among the EU/27 Member States, Germany is now Turkey's most important economic partner for Turkey's traditional market, which has not changed for decades. There is no question that Germany today plays an enormously important role in Turkey's foreign trade relations. In 2020, Germany's share of Turkey's export and import markets were around 9% and 11% respectively. Germany is Turkey's third largest import partner after China and Russia. Turkey has exported to the value of about USD 16 billion to Germany and imported USD 22 billion from Germany in 2020, trade deficit was USD 6 billion (2019: 2.6 billion). In the same year, however, the trade deficit with China recorded USD 20.2 billion and with Russia USD 18.6 billion in 2019.[18]

Conclusion

To sum up, we can draw the following conclusions from Turkey's trade relations to both countries, China and the EU:

- Turkey's trade deficit with the EU is significantly smaller than its deficit with China. This means that Turkey's export-import ratio of goods with the EU (95.5%) is closer to unity in 2020, whereas the export-import ratio in trade in goods with China was 12.4% in the same year. In addition, trade with China in 2020 covers almost 41.1% of Turkey's foreign trade deficit. But trade relations between the EU and Turkey are almost balanced. When it comes to export and import of services, Turkey has comparative advantages over the EU.

- Turkey's trade in goods with China is characterized by inter-trade specialization between trade transactions. Turkey mainly exports agricultural products, raw materials, minerals and labour-intensive goods to China and imports largely capital-intensive and high-tech products from China. The trade figures clearly show that Turkey's trade relations with China are asymmetric and expanding to the detriment of the Turkish economy.

- By contrast, trade relations between Turkey and the EU are based on intra-trade specializations. Both sides export and import similar commodities such as SITC 6-7-8 and mainly processed products, which indicates that Turkey can compete with the EU in these advanced and capital intensive sectors.

[17] Turkish Statistical Institute, "Foreign Trade Statistics, December 2020", Press release (29 January 2021), <https://data.tuik.gov.tr/Bulten/Index?p=Foreign-Trade-Statistics-December-2020-37412&dil=2>.
[18] Ibid.

- As China has done under the "Made China 2025" label, Turkey needs to change its industrial and export strategy and evolve from low-cost and labor-intensive products to high-tech industry. Instead, the share of goods produced with advanced technology based on education and innovation should be increased in the manufacturing industry. The ratio of high-tech manufactured products makes up only 3.8% of Turkey's exports and 13% of its imports in 2020 respectively.[19] In 2020, high-tech products represented 20% of total EU imports and 18% of total exports.[20] To produce advanced technological goods, Turkey needs to have a high-level human capital, outstanding educational institutions and well-equipped research centers first.[21]

- Our trade analysis reveals that Turkey has been an integral part of the European market and a member of the European Customs Union, without becoming a full member of the EU, for decades. Turkey's foreign trade policy depends on the EU's foreign trade policy. In this regard, trade relations and disputes between the EU and China are seen as part of their own affair and have a rather indirect impact on Turkey's trade relations with China.

- Turkey's trade with the EU is in balance and dominates, in comparison to trade with China, in terms of size as well as in terms of structure of exports and imports. We conclude that China's trade cannot replace the importance of EU trade for Turkey.

- It seems clear regardless of the direction of Chinese-Turkish relations: Turkey should continue to explore options for full integration into the European single market. The trade figures clearly show that Turkey's trade relations with China are considerably asymmetric and the future development of trade between both countries seems to be improving at the expense of the Turkish economy.

- Most important international concerns focus on the fact that in China's economic model, based on state capitalism, market forces do not determine the production of goods produced by state owned enterprises (SOEs). The overinvestment by Chinese state-owned enterprises to stimulate economic growth leads to overcapacity and the need for China to find new export markets in order to sell the surplus of products created by the infant industries, in general below market prices. An import of goods without market principles would be beneficial in the short term, but carries the risk of price deterioration and a fall in domestic production in the long run.[22]

- It is an obvious fact that China, with its current trade surpluses over the past years, finances its investments in Turkey and grants funds (loans) to commercial banks who

[19] Ibid.

[20] China was the EU's main partner for high-tech imports and the United States for high-tech exports. See Eurostat, "Production and international trade in high-tech products", *Statistics Explained*, <https://ec.europa.eu/eurostat/statistics-explained/index.php?title=Production_and_international_trade_in_high-tech_products&oldid=541231> (accessed 7 February 2022).

[21] For a more detailed analysis of the Turkish Economy see Bahri Yilmaz, *Turkish Economy: Where does this Road Lead?* Country Report (Ankara: Konrad-Adenauer-Stiftung, 12 February 2014), <https://www.kas.de/en/web/tuerkei/laenderberichte/detail/-/content/in-welche-richtung-entwickelt-sich-die-tuerkische-wirtschaft->.

[22] Directorate-General for External Policies, Policy Department, *EU-China trade and investment relations in challenging times*, Study (Brussels, May 2020): 44, <https://www.europarl.europa.eu/thinktank/en/document/EXPO_STU(2020)603492> (accessed 2 February 2022).

signed swap agreements with the Central Bank of Turkey (CBT). In other words, regarding trade deficits with China, Turkey itself is financing its current account deficits.

- This unfavorable evidence should be a wake-up call for Turkey's policy makers as China's unilateral influence expands. To make up for its trade deficit with China, Ankara should take China's trade offensive more seriously, and it is best advised to pursue a selective trade and investment policy against China.

Turkey’s Financial Dependency on China Increasing

Finally, we will address the question of what are the driving economic factors behind the rapprochement between Beijing and Ankara. Why does Turkey become more financially dependent on China?

Since 2018, Turkish economy has been facing very serious economic problems and is once again experiencing a severe debt and currency crisis. The crisis is due to excessive government spending as well as excessive debt in foreign currencies, connected with high inflation and depreciation pressures.

The depreciation of the national currency is likely to exacerbate price inflation. A weaker currency induces further inflation in Turkey due to imports priced into hard currencies. Thus, it is likely to lead to a vicious circle for price inflation. That unpredictable policy pursued by the Central Bank of Turkey (CBT) left a heavy burden behind:

High inflation (49%)[23], a weak currency, and rising national debt. Turkey's total outstanding sovereign debt is estimated at around USD 450 billion in 2021.[24]

The Turkish government aims to close its current account deficit and finances the repayment of foreign debts through foreign direct investment and loans (fresh money) from everywhere including China and, interestingly, from Qatar. Because of all these facts, the economy urges capital inflows and remains strongly dependent on "hot" money from abroad, mostly in the form of short-term capital.

Under these circumstances, there are two main reasons why Turkey intensifies its economic relations with China, which is acting as a main creditor: One is that due to the political and security issues arising in its relations with the US, it is difficult to obtain direct monetary financing from the US. Moreover, the Turkish government does not want to be involved into negotiations with the International Monetary Fund (IMF). As far as Turkey’s relation with the EU is concerned, Brussels has already frozen accession negotiations with Ankara. Apart from the refugee issue, interest in Turkey has declined dramatically. In sum, at this stage of relations with the US and the EU, it seems difficult to get the much-needed funds from them.

Second, Turkey has been a subject to the Chinese government's interest in recent years due to its geographical and strategic location in the Eastern Mediterranean region, its proximity to the European market, intensification of economic relations with the Middle

[23] Official declared annual inflation rate in January 2022. See Natasha Turak, “Turkey’s inflation hits nearly 50%, highest in two decades”, *CBNC* (online), 3 February 2022, <https://www.cnbc.com/2022/02/03/turkeys-inflation-hits-nearly-50percent-highest-in-two-decades-.html>.

[24] External Debt in Turkey increased to 453,463 USD Million in the third quarter of 2021 from 446,439 USD Million in the second quarter of 2021. See “Turkey Total Gross External Debt”, *Trading Economics* (online), <https://tradingeconomics.com/turkey/external-debt> (accessed 30 January 2022).

East, including with Israel, Egypt, and Greece[25], and the importance to the Belt and Road Initiative (BRI) – Middle Corridor – for Chinese investors.

Therefore, in recent years, China has improved its trade and investment relations to win Turkey's favour, amid Turkey's serious problems with the West. For all of these reasons, Beijing has increased its financial grip in the form of swap agreements and loans; although it is not at the level Turkey is currently in need of. China is not only expected to fill in the investment gap, but also the looming foreign exchange gap. Some economists have warned Turkey that China's plan to finance and build an infrastructure around the world could lead to a debt trap that creates a dependency on Beijing or its strategic gain.[26] The infrastructural investments are made through loans from the Chinese banks and financial institutions and should be paid on time.[27]

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doi: 10.18449/2022WP03

[25] Jean Bastian, *Expeditionary Capital in the Eastern Mediterranean: Why Turkey Matters to China and Vice Versa*, Berlin: Stiftung Wissenschaft und Politik, October 2021 (Centre for Applied Turkey Studies [CATS]), WP 04: 7, doi: 10.18449/2021WP09.
[26] "'Debt Trap Diplomacy' is the accusation that China uses Belt and Road as part of a manipulative global strategy (…) The accusation was sparked by projects such as the Hambantota Port Development in Sri Lanka. The Sri Lankan government was unable to service the Chinese loans which funded the project, and the port was handed over to the Chinese under a 99-year lease in 2017 – echoing tactics employed by 19th century European Imperialists against Qing Dynasty China." Yu Jie and Jon Wallace, *What is China's Belt and Road Initiative (BRI)?* (London: Chatham House, 13 September 2021), <https://www.chathamhouse.org/2021/09/what-chinas-belt-and-road-initiative-bri>.
[27] George Marshall Lerner, "China to the Rescue in Turkey?", *The Diplomat* (online), 3 July 2020, <https://thediplomat.com/2020/07/china-to-the-rescue-in-turkey/>; Nicholas Lyall, "China in Postwar Syria", *The Diplomat* (online), 11 March 2019, <https://thediplomat.com/2019/03/china-in-postwar-syria/>; Guy Faulconbridge, "Montenegro Close to Deal on Lifting Chinese Debt Burden – Minister", *Reuters* (online), 7 July 2021, <https://www.reuters.com/world/exclusive-montenegro-close-deal-lifting-chinese-debt-burden-minister-2021-07-07/>.