İZMİR CHAMBER OF COMMERCE

CUSTOMS UNION AND PERCEPTION OF THE SMES IN IZMIR

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ABSTRACT

This essay is prepared for the EU Training Programme, ran by EUROCHAMBRES and TOBB under the EU-Turkey Chambers Forum Project financed by the European Union.

The aim of my essay is to provide information to our members on the Customs Union and analyze its effects on Izmir's and Turkey's foreign trade. In order to make it more beneficial for our members, first I wanted to find out what the small and medium sized enterprises (SMEs) in Izmir know about the Customs Union and how they evaluate it. I gathered this information through a survey applied to the Professional Committee members of our Chamber.

As a result of my survey, I found out that 88% of the respondents say they have general information about the Customs Union and 12% say they do not know about it. In my survey I also asked from the respondents to list the advantages and/or disadvantages of the Customs Union according to them.

Although the percentage of the SMEs who say that they have general information about the Customs Union is high, most of them only consider it as abolishing the customs tariffs and quotas. However, the Customs Union is en economic integration model having a broader content.

Depending on the missing information of the SMEs in Izmir on the Customs Union and analyzing its effects on our foreign trade, I have prepared my essay.

CUSTOMS UNION AND PERCEPTION OF THE SMES IN IZMIR

European Integration has begun with the Treaty establishing the European Coal and Steel Community in 1952 and the six founding countries (Belgium, Netherlands, Luxemburg, Italy, France and Germany) has signed the Treaty of Rome in 1957, establishing the European Economic Community or namely the “Common Market”.

The European Economic Community changed into a political and economic union with the “Treaty of Maastricht on European Union” in 1993.

The main aim of the European Union has always been to have an economic integration between the Member States, which passes through the creation of an “internal market”. This integration means the unification of the economic activities of the Member States, and this is realized through four degrees. These are;

1) *Free Trade Area (FTA):* All customs tariffs and quotas that restrain trade between the members of the FTA are abolished, but the members are free to apply their national customs tariffs against import from third countries.

2) *Customs Union:* Besides abolishing all customs tariffs and quotas between the members, a common customs tariff is applied to third countries. It also includes adoption of a common trade policy. Within the EU, customs union in industrial goods began on January 1st, 1968 and customs union in agricultural goods began on January 1st, 1970.
   Customs Union brought abolition of customs duty and similar duties and brought free movement of goods.

3) *Single Market:* In addition to the free movement of goods provided by the Customs Union, it brings freedom of labor, services and capital.

4) *Economic and Monetary Union:* It covers common monetary and financial policies, once the Single Market is completed.

In this context, Turkey’s relation with the European Union (EU) has also begun in the economic aspect.

Turkey’s long marathon with the EU started in 1959 when Turkey applied to European Economic Community (EEC) for membership on July 31st, which led to the signing of the Ankara Agreement in 1963. The final aim of this agreement was the full membership of Turkey to the Union through the establishment of a customs union, which would bring the two sides closer in economic and commercial matters.

In 1987 Turkey applied for full membership to the EC. In 1989 the EC declared its decision as Turkey is eligible as a candidate; however the EC is not ready to consider any further enlargement in the establishment process of the single market and suggested to complete the Customs Union until 1995 in order to deepen relations.

In the Ankara Agreement, Turkey’s accession to the EU Internal Market was foreseen through three phases. These phases are:

1. Preparatory Phase (1964-1970): After the completion of the preparatory phase, an *Additional Protocol* was signed on November 13th, 1970 and it came into force in 1973.
2. Transition Phase (1973-1995): The provisions of this phase and the responsibilities of the parties were determined by the Additional Protocol. Completion of the Customs Union at the end of the transition phase was planned and it was achieved.
3. Completion Phase: This phase covers the period starting from 1996 until the full integration of Turkey to the EU Internal Market.

On September 1st, 1971 European Community abolished the customs duties on import of industrial goods from Turkey into the EC. This provided a striking increase in the export volume of Turkey. In 1972 export volume of Turkey increased 31% compared to 1971 and in 1973 the export volume increased 49% compared to the previous year.

At the EC-Turkey Association Council meeting on March 5th, 1995, the Decision no 1/95 on implementing the final phase of the Customs Union was taken and it came into force on January 1st, 1996.

Together with the completion of the Customs Union, the customs duties and charges having equivalent effect on the import of industrial goods from European Union and EFTA countries were abolished and the Common Customs Tariff of the EU began to be applied to the third countries.

This increased the import of Turkey from the EU and EFTA countries and their share in the total import volume of Turkey. On the other side the import of Turkey from the third countries has realized an important increase as well.

In the general aspect, customs union caused an increase in the foreign trade volume of Turkey with a higher increase in imports than exports. This is because Turkey needs to import the intermediate goods and machines for the production of industrial goods, which are than exported. So, as Turkey’s exports increase its imports increase more and this causes a higher foreign trade deficit.

Turkey’s export and import volumes since 1969 can be seen in the Table 1 below. It is possible to see the change before and during the three phases of the Customs Union.

Table 1: Foreign Trade of Turkey (1000$)

Years	Export	Import	Balance	Volume
1969	536.834	801.236	-264.402	1.338.070
1970	588.476	947.604	-359.128	1.536.080
1971	676.602	1.170.841	-494.239	1.847.443
1972	884.969	1.562.550	-677.581	2.447.519
1973	1.317.083	2.086.216	-769.133	3.403.299
1974	1.532.182	3.777.501	-2.245.319	5.309.683
1975	1.401.075	4.738.558	-3.337.483	6.139.633

1976	1.960.215	5.128.647	-3.168.432	7.088.862
1977	1.753.026	5.796.278	-4.043.252	7.549.304
1978	2.288.163	4.599.025	-2.310.862	6.887.188
1979	2.261.195	5.069.432	-2.808.237	7.330.627
1980	2.910.122	7.909.364	-4.999.242	10.819.486
1981	4.702.934	8.933.374	-4.230.440	13.636.308
1982	5.745.973	8.842.665	-3.096.692	14.588.638
1983	5.727.834	9.235.002	-3.507.168	14.962.836
1984	7.133.604	10.757.032	-3.623.428	17.890.636
1985	7.958.010	11.343.376	-3.385.366	19.301.386
1986	7.456.726	11.104.771	-3.648.045	18.561.497
1987	10.190.049	14.157.807	-3.967.758	24.347.856
1988	11.662.024	14.335.398	-2.673.374	25.997.422
1989	11.624.692	15.792.143	-4.167.451	27.416.835
1990	12.959.288	22.302.126	-9.342.838	35.261.414
1991	13.593.462	21.047.014	-7.453.552	34.640.476
1992	14.714.629	22.871.055	-8.156.426	37.585.684
1993	15.345.067	29.428.370	-14.083.303	44.773.437
1994	18.105.872	23.270.019	-5.164.147	41.375.891
1995	21.637.041	35.709.011	-14.071.970	57.346.052
1996	23.224.465	43.626.642	-20.402.177	66.851.107
1997	26.261.072	48.558.721	-22.297.649	74.819.793
1998	26.973.952	45.921.392	-18.947.440	72.895.344
1999	26.587.225	40.671.272	-14.084.047	67.258.497
2000	27.774.906	54.502.821	-26.727.915	82.277.727
2001	31.334.216	41.399.083	-10.064.867	72.733.299
2002	36.059.089	51.553.797	-15.494.708	87.612.886
2003	47.252.836	69.339.692	-22.086.856	116.592.528
2004	63.167.000	97.540.000	-34.373.000	160.707.000
2005	73.122.000	116.048.000	-42.926.000	189.170.000
2006	85.534.676	139.576.174	-54.041.498	225.110.850
2007	107.271.750	170.062.715	-62.790.965	277.334.465
2008	132.027.258	201.963.558	-69.936.300	333.990.816

Source: Turkish Statistical Institute (TURKSTAT)

During the 80s, especially after 1984 with the foreign expansion policy in the Turkish economy, foreign trade volume increased further. Turkey’s export growth rate was higher than the growth rate of imports, so the foreign trade deficit was lower during this decade. After 1990 foreign trade deficit continued to increase gradually, except the years of economic crises which are 1994, 1998-1999 and 2001-2002 depending on the devaluation of Turkish Lira.

In general, there is a negative perception of the Customs Union’s effects in Turkey mainly arguing the increasing foreign trade deficit and the Free Trade Agreements of the EU signed with third countries in which Turkey cannot become a party naturally.

However, the reason of the increasing foreign trade deficit is not the Customs Union alone itself, but the macroeconomic policies of Turkey mainly. For example the high unemployment and inflation rates and the low GDP growth rate, on the other side lack of industrial investment and technology transfer which still keeps imports higher than exports prevent the strengthening of the Turkish economy, thus its competitive power.

Turkey’s main foreign trade partners are the EU countries, respectively Turkey meets most of its import needs from the EU. That is why, the Customs Union is perceived as more beneficial for the EU rather than Turkey. In reality, the share of EU (27) in Turkey’s export increased since 1996, while its share in Turkey’s imports decreased.

When we look at the first 40 countries in our import and export lists prepared by the Undersecretariat of the Prime Ministry for Foreign Trade, we see that most of them are EU member states. According to the foreign trade statistics in 2008, there are 17 EU member states among both our first 40 export and import partners. In 1990, also there were 17 countries from the current EU-27 in our export partners list and 18 countries among our import partners.

Table 2: Foreign Trade with EU (27) ***Million $***

Years	Export	%	Import	%
1996	12.569	54,1	24.321	55,7
1997	13.435	51,5	26.119	53,8
1998	14.813	54,9	25.282	55,1
1999	15.424	58,0	22.530	55,4
2000	15.664	56,4	28.527	52,3
2001	17.546	55,9	19.823	47,9
2002	20.415	56,6	25.689	49,8
2003	27.394	57,9	35.140	50,7
2004	36.581	57,9	48.103	49,3
2005	41.365	56,3	52.696	45,1
2006	47.935	56,0	59.401	42,5
2007	60.399	56,3	68.612	40,3
2008	63.390	48,0	74.802	37,0

Source: Turkish Statistical Institute (TURKSTAT)

In the table above, our export and import volumes with EU (27) and its share in our total exports and imports can be seen. The high percentage decreases realized in both imports and exports in 2008 depend on the global economic crisis, as EU economy was highly affected by this crisis.

Taking these indicators into account, we can say that EU member states have always been the countries that Turkey trades the most, after the completion of the Customs Union the volume of our exports to the EU increased regularly and EU gained a stable position as our main trade partner with a percentage of 50% on average. Also, Turkey's trade with third countries has widened.

On the other hand, EU's high share in Turkey's foreign trade and the harmonization policies that started with the Customs Union process, increased competition in Turkey and thus the quality of the products. Besides that Turkey completed the harmonization with the related EU legislation even before the starting of the accession negotiations.

Customs Union tends to be known in Turkey by the SMEs, however it is only perceived as the abolishment of the customs tariffs and quotas. But, Customs Union is something more. The EC-Turkey Association Council Decision no 1/95 mainly covers the below stated areas;

- Free movement of goods,
- Technical harmonization of the legislation,
- Harmonization with the Common Trade Policy,
- Undertaking the preferential customs regimes,
- Harmonization with the Common Agricultural Policy and the preferential regime for the trade of agricultural products,
- Harmonization with the EU Customs Code,
- Harmonization of the legislation on protection of the intellectual, industrial and commercial property, competition rules of the Customs Union, means of commercial protection, public procurements, taxation,
- Institutional decisions; Customs Union Joint Committee, consultation and decision procedures, resolution of conflicts, safeguard measures.

In order to assure the free movement of goods and prevent trade deviation, EU Common Trade Policy, Competition Policy and standards and technical legislation should be adopted. Turkey has almost completed the necessary measures.

As stated before, Customs Union is mostly criticized in Turkey. The only criticism by the members of our Chamber has been about the Free Trade Agreements which EU signs with other countries until now. In order to learn what our members think about the Customs Union and to find out what they need to know about it, I have applied a questionnaire to our 400 Professional Committee Members, of whom 120 responded.

Like the general structure of the Turkish enterprises, more than 99% of our members are SMEs. The questionnaire is applied to SMEs who are engaged in trading.

55,8% of the respondents say that the Customs Union affected their trade activities positively, while 17,7% say they are affected negatively and 26,5% say their activities were not affected by the Customs Union.

Those who say that their trade activities are affected positively, state the advantages of the Customs Union as follows;

- With the Customs Union we can provide the inputs for our productions easier,
- When selling our products we can consider the whole Europe as a market,
- The general competition created by the Customs Union improves the standards and decreases the prices and these affect our business positively,
- Customs Union brought very positive results in exports. Any company in the EU can import from Turkey as if it purchases in its own country,
- We import with 0 customs duty,
- Standards, like CE, are common in the Customs Union partners so we do not need any additional documents,
- We can take out our imported goods from the customs faster and without any expense,
- Trade volume with the EU member states has increased. New taxation measures, free movement of goods, etc. increased both our imports and exports,
- With the Customs Union the procedures became easier and we have less work,
- Customs Union provides us freedom of import and export with the same conditions with EU,
- We can import intermediate goods from Europe easier, but the goods that our sector (chemicals) needs are mostly imported from Fareast,
- The Customs Union provided us price advantage, the customers in the EU prefer us rather than non-members of the Customs Union,
- Before the Customs Union we were importing from the USA and paying high duties. After the completion of the Customs Union, we started importing from EU member states and now we do not pay customs duties. This provided us a great advantage,
- With the Customs Union we import from the EU, so we can use higher quality products.

The disadvantages caused by the Customs Union and other opinions are stated as below,

- Customs Union restricts our agricultural products export,
- Lack of information on implementing the EU legislation at the customs offices,
- As we are not yet a member of the European Union, we cannot be a party in the Free Trade Agreements (FTA) that they sign with third countries and we do not have a right to make any recommendations about the FTAs,
- Realizing the Customs Union before becoming a member to the EU was a difficult process, if we had completed the Customs Union after becoming a member, it would have been more beneficial for our country.

We can export to and either import from the EU agricultural products. However, only processed agricultural products are covered by the Customs Union. Rest is subjected to customs duties.

"Lack of information on implementing the EU legislation" is a hindrance that should be solved by us. Staff of the customs offices should be well trained on the Customs Union rules and all the related procedures.

Free Trade Agreements of the EU with the third countries is the most criticized subject when considering the Customs Union.

From my survey, I reached the information that 61,8% of our members know the difference between a Free Trade Agreement and the Customs Union and 38,2% do not know the difference.

The difference between a Free Trade Agreement and the Customs Union is that parties of a FTA can apply their national regulations while trading with third countries, but the Customs Union requires adopting a common customs tariff policy towards third countries.

According to the Customs Union Decision, Turkey had to complete the undertaking of the preferential customs regimes of the EU until the end of the 5-year transition period (1996-2001). Preferential customs regimes include the Free Trade Agreements as well as the Generalized System of Preferences and Autonomous Regimes.

However, EU leaves Turkey to run FTA negotiations alone itself and does not provide the opportunity to put the FTA in force at the same time with the EU, although they involve Andorra and San Marino, which are partners of the Customs Union, in their FTAs with special articles in the agreements. On the other hand, after Turkey's efforts EU added a "Turkey Clause" in the FTAs. But, this clause is not binding and only invites the third country to sign a FTA with Turkey.

This situation causes trade deviation by providing the export of FTA partners into Turkey without any customs duties through the EU, although trade deviation tends to be prevented by the provisions of the Customs Union.

85,3% of our members think that Customs Union is not enough for Turkey-EU relations. Only 11,8% see Customs Union enough for the integration of Turkey with the EU. On the other hand, the percentage of the members who support Turkey's full membership to the EU drops to 76,5 and 23,5% do not support our full membership.

According to the results of the survey 64,7% of our members know where to find more information about the Customs Union, 26,5% say that they do not know and 8,8% did not reply to this question. This 8,8% is a part of the members who stated that they do not have a general knowledge about the Customs Union. The total who said they do not know about the Customs Union was 12%.

Turkish enterprises, so do our members, can find information from the below listed institutions;

- Delegation of the European Commission to Turkey
  http://www.avrupa.info.tr
  Tel: (+90) 312 459 87 00
  Fax: (+90) 312 446 67 37

- Secretariat General for EU Affairs, Department of Single Market and Competition
  www.abgs.gov.tr
  Tel: (+90) 312 218 1478
  Fax: (+90) 312 218 1471

- Undersecretariat of Customs, European Union General Directorate
  http://www.gumruk.gov.tr/TR-TR/ABDISILISKILER/Sayfalar/default.aspx
  Tel: (+90) 312 306 80 00

- Undersecretariat for Foreign Trade
  http://www.dtm.gov.tr/dtmweb/index.cfm?action=detay&dil=TR&yayinid=1130&icerikid=1236&from=home
  Tel: (+90) 312 204 75 00

- Economic Development Foundation
  www.ikv.org.tr
  Tel: (+90) 212 270 93 00
  Fax: (+90) 212 270 30 22

From the results of my survey, we can see that a high percent of the SMEs in Izmir are in favor of the Customs Union and they state more advantages than disadvantages.

When we look at the foreign trade figures of Izmir after 1996, we see that Izmir has an ascending trade volume, but in the years of economic crises trade volume falls and trade surplus increases. After 2004, Izmir starts to give trade deficits.

Table 3: Export and Import of Izmir between 1996-2008 (1000 $)

Years	Export	Import	Volume	Balance
1996	3.199.616	2.896.878	6.096.494	302.738
1997	3.240.787	3.172.446	6.413.233	68.341
1998	3.462.154	2.570.362	6.032.516	891.792
1999	3.194.430	2.207.865	5.402.295	986.565
2000	3.017.154	2.786.298	5.803.452	230.856
2001	2.740.576	1.715.470	4.456.046	1.025.106
2002	2.777.767	2.288.330	5.066.097	489.437
2003	3.473.936	3.306.953	6.780.889	166.983
2004	4.110.487	4.693.704	8.804.191	-583.217
2005	4.645.381	4.986.251	9.631.632	-340.870
2006	5.448.572	5.459.049	10.907.621	-10.477
2007	6.388.981	7.000.300	13.389.281	-611.319
2008	7.758.160	8.240.842	15.999.002	-482.682

Source: Undersecretariat for Foreign Trade

After 1996, Izmir's trade volume with the EU (27) follows the same progress with its total trade volume. Its trade relations with the EU show an irregular trend. Izmir has trade surplus mostly during the years 1996-2005, but it gives trade deficit in 1997, 2000, 2004 and 2005.

On the other side, the share of the EU-27 in the total trade volume of Izmir follows a descending trend since 1996. However, EU has the largest share in Izmir's trade every year. until 2000, its share is more than 60%, which reflects a very important amount. The average share of EU in Izmir's total trade volume is higher than its share in Turkey's total trade.

Table 4: Foreign Trade of Izmir with EU (27)

Years	Export	Import	Volume	Balance	Share in Total Volume
1996	1.962.044	1.895.880	3.857.924	66.164	63,3%
1997	1.908.554	2.059.421	3.967.975	-150.867	61,9%
1998	2.109.042	1.622.693	3.731.735	486.349	61,9%
1999	1.986.730	1.384.493	3.371.223	602.237	62,4%
2000	1.784.856	1.844.102	3.628.958	-59.246	62,5%
2001	1.550.129	1.036.269	2.586.398	513.860	58,0%
2002	1.636.345	1.312.048	2.948.393	324.297	58,2%
2003	2.045.498	2.002.135	4.047.633	43.363	59,7%
2004	2.337.740	2.790.318	5.128.058	-452.578	58,3%
2005	2.591.205	2.886.931	5.478.136	-295.726	56,9%

Source: Undersecretariat for Foreign Trade

Although, the share of the EU in Izmir's foreign trade volume decreases since the completion of the Customs Union, my survey results show that only 17,7% of the SMEs in Izmir say that they are negatively affected by the Customs Union. The change in the trade indicators cannot be explained only by the Customs Union, it is mostly affected by the macroeconomic situation in Turkey.

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