Box 4.2

Structural Policy Measures to Reduce the Current Account Deficit

After reaching 6.5% in the first half of 2018, the ratio of the current account to gross domestic product (CA/GDP) decreased to 5.5% in the third quarter with the recovery in exports. In November, the 12-month cumulative current account deficit fell l to USD 34 billion, with a reduction of USD 5.5 billion from the previous month. The improvement in the current account is expected to continue considering the recovery in exports and slowdown in imports. Meanwhile, as the literature states, improvements in the current account in the medium/long run will call for reforms on the structural side . Accordingly, multiple measures to contain the current account deficit have recently been taken in Turkey. The main structural problems in the current account and policy measures to contain them are discussed in this box under five headings.

Savings-Investments Gap

The saving-investment gap fluctuating around 4-5% is higher than in peer countries. Accordingly, a number of policy measures increasing the diversity of financial instruments to encourage domestic savings have recently been put into effect. For example, funds accumulated in the automatic enrollment pension system are expected to reach 3.5% of GDP at the end of 2020. Similarly, gold-backed bond issues aimed at bringing the under-the-mattress gold into the economy and the dowry and housing accounts facility introduced in 2016 increased the household savings significantly.

An increase in the household saving rate rests on a higher income as well as a healthy income distribution. Other long-term solutions include changing consumption habits by reducing waste and taking cognizance of ecologic sustainability as well as maintaining a rate of population increase compatible with long-run sustainable growth.

The household debt in Turkey is relatively lower than its peers. Nonetheless, the connection between the household debt and a balanced current account emphasized by the literature calls for the capacity to implement macro-prudential policies in coordination with different institutions when necessary. Accordingly, the recently established Financial Stability and Development Committee plays an important role in detecting the risks accumulated in financial system in advance and coordinating the management of such systemic risks. The amendments to Decree no. 32 and the establishment of the initiative at the CBRT to manage the exchange rate risk, and the foreign exchange borrowing regulation addressing small-scale firms with no foreign exchange are all expected to help attaining a healthy saving structure .

Foreign Direct Investments

Policies aiming at increasing Foreign Direct Investments (FDI) should be designed in tandem with the industrial policies. The motivation of foreign firms investing in the manufacturing sector is generally to raise the efficiency of a part of the production chain while the motivation of foreign firms investing in the services sector is to increase their market share . The incentive programs that are conducted in different sizes and scopes can assist FDI that will increase the production capacity through positive externalities. Accordingly, domestic partnership can be encouraged and the FDI incentives can be designed with the intention of increasing the capacity and skills of domestic suppliers. These programs should be designed to serve the purpose of developing knowledge-based capital; should be supported by long-term education policies aiming at increasing R&D; should be more-broad based and easily understood and implemented by investors.

Investments in Sectors with High Productivity and Added Value

It should be considered that the main prerequisites of production in high value added sectors are the production experience, technical infrastructure, business environment, R&D and human capital. Hence, sources of investment should be channeled to areas that will develop technical infrastructure and education system should be designed in a way to ease the transition of employment towards productive areas.

Import Dependency of Exports

Policies aimed at producing high value added and technological products domestically as an alternative to imported inputs can help contain the current account. Accordingly, to reduce dependency on imported intermediate inputs and sustainability of input supplies the Input Supply Strategy (GITES) and Action Plan was put into effect and the Committee for Domestic Production was established. On the other hand, it should be emphasized that the use of imported intermediate inputs is not entirely unfavorable given cognizance of the internationalization of production. The sustainability of imported inputs, especially for producers that are a part of global chains is essential.

Energy Imports

The primary policy to reduce the demand for imported energy is the shift towards renewable energy. Reducing natural gas imports will affect the current account directly. Energy investments should be designed in view of the natural resources of the country and should be dispersed across the country. Incentives for domestic hardware, training the technical staff that can use this technology, and undertaking energy saving policies can all contribute to the efforts to meet the energy demand through domestic resources. Moreover, efforts to change the energy consumption behavior should also be supported.

To sum up, it is important to support the cyclical improvement in the current account with structural policies in order to attain a balanced current account in the long run. To this end, efforts to increase savings for a balanced current account financing structure and to sustain financial stability will be conducted in hand with efforts to increase the total productivity in an era of internationalization of the production.

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