

Turkey: A Business Perspective of Election Outcomes Nov. 3, 2015

StratejiCo. explains what AKP's electoral victory means for political and economic environment and what kind of strategies businesses should develop to stay afloat.

1. The Political Outcome

Turkey's re-election on Nov. 1 ushered in the fourth term of AKP (Justice and Development Party) government, with the ruling party surprisingly regaining a comfortable parliamentary majority it lost five months ago. AKP swept Turkish votes by 49.4%, ending a period of hung parliament after 13 years of single-party rule. The outcome marked a dramatic change in Turkish voting behavior compared with the previous election. AKP leadership, including its founder Turkish President Recep Tayyip Erdogan, managed to successfully appeal to mostly conservative voters during the summer and increased its votes from 40.8% amid increasing militancy and stagnating economy. Opposition parties lost ground against AKP, which either increased or maintained its electorate in virtually every electoral district of Turkey. While CHP made slight increase in the number of parliamentary seat, pro-Kurdish/socialist HDP and nationalist MHP lost one fourth and one third of their supporters respectively. The biggest winner of the election is obviously President Erdogan, who makes his ambition to boost executive powers of presidency as the number one policy target. His successor Prime Minister Ahmet Davutoglu has also assured his political power by replicating AKP's success back in 2011.

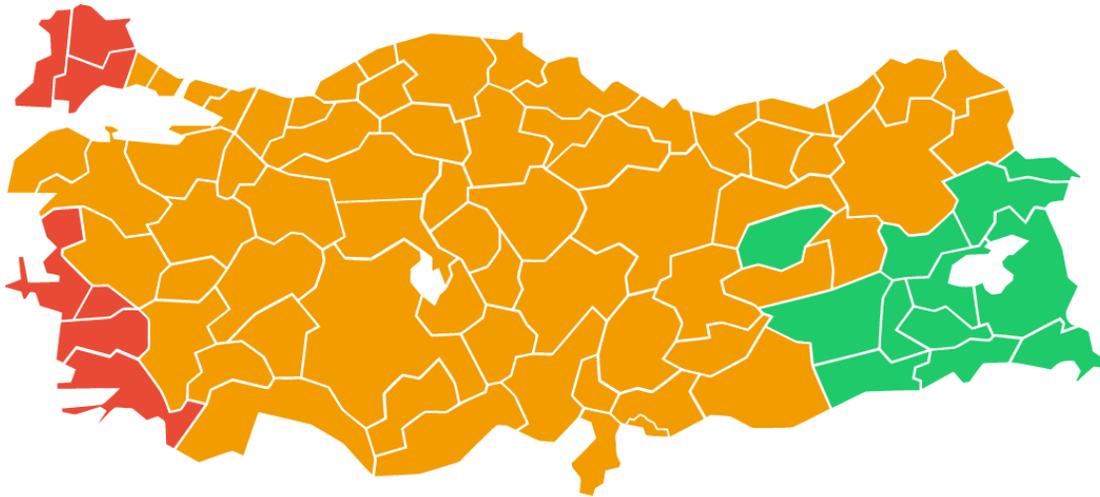
The main reason behind AKP's electoral success is without doubt the inability of four political parties to form a coalition government in the aftermath of June 7 elections. Since then, Turkish people have witnessed violence between the Turkish state and Kurdish PKK militants, as well as suicide attacks by Islamic State inside Turkish borders. Amid increasing uncertainty and insecurity, Turkish voters appear to have preferred single-party stability for another four-year. The outcome, however, does not allow AKP to change the constitution on its own, for which at least a supermajority of 330 seats is required.

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Now that AKP has a comfortable majority in the parliament, Turkish business people and foreign investors try to gauge whether AKP will demonstrate its capacity

to find solutions to country’s long-lasting challenges. There are plenty, and it will be interesting to watch how AKP’s leadership will tackle them.

Vote distribution



Comparisons of Election Results

	2011	June 2015	November 2015
AKP	% 49 👤 332	% 40.87 👤 258	% 49.34 👤 315
CHP	% 25 👤 138	% 24.95 👤 132	% 25.42 👤 134
MHP	% 12 👤 50	% 16.29 👤 80	% 11.96 👤 41
HDP	% 0 👤	% 13.12 👤 80	% 10.77 👤 60

2. Economy: Reform or Stagnation

Turkish Lira and markets jump in response to AKP’s election victory. The lira was up more than 5% against US Dollar, the biggest gain since May 2015. Istanbul stock index increased by a similar amount, giving a strong message that markets function

better under stable conditions.

Lira Spikes After AKP Election Win

Clear victory sparks biggest rise against USD since May



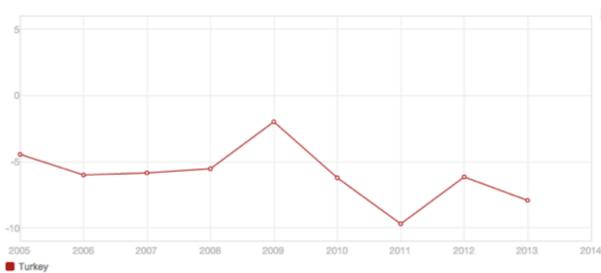
Source: Bloomberg

Bloomberg

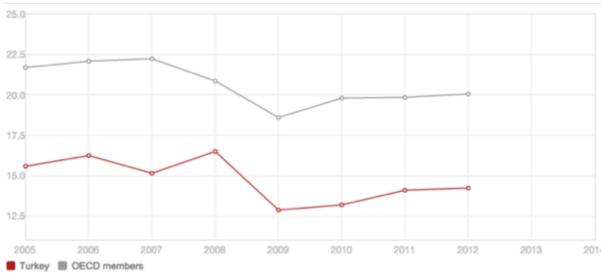
More important than the short-term indicators, however, Turkey's future economic stability will be determined by the long-term policies that the AKP government will adopt. Turkey has long been stuck in middle-income trap, being unable to increase GDP per capita above \$10,000 since 2010. Unemployment rate has risen above 10%, with young unemployment being around 25% as one of the most burning social and economic issue. Turkey's current account deficit, an indicator that demonstrates the amount of foreign-borrowed money against country's national savings, is still a major source of vulnerability.

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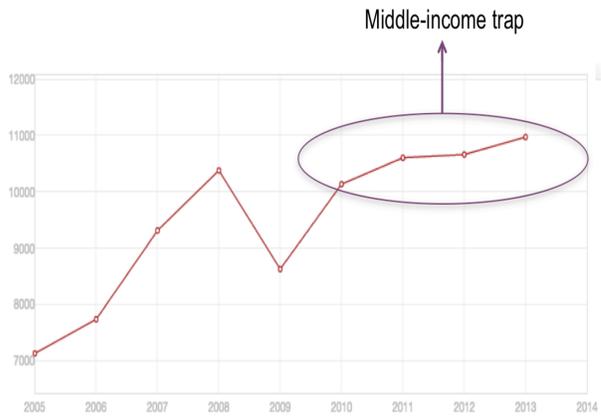
In the face of economic challenges, AKP management so far has not appeared to create a common front. Erdogan-led group of decision-makers argued for low-interest rate policy to boost economic growth and incentivize giant infrastructure projects, while country's longest serving economy chief Ali Babacan and Finance Minister Mehmet Simsek adopted a more dovish policy and defended independence of Central Bank. Now that AKP's experienced economy chiefs are back in the game, it remains to be seen which camp will have a greater say in economic policies. Markets and investors will anxiously watch for signs of reconciliatory policies, while remaining cautious of geopolitical risks surrounding Turkey.



Current account balance %GDP



National savings %GDP (OECD members vs. Turkey)



Turkey - GDP per capita / Source: World Bank

The AKP government has two main options. The first one is going to back to reformist policies it had adopted during its first term, namely accelerating the EU accession process, implementing structural reforms, increasing independence of judiciary and creating a business-friendly environment. The other path that AKP leadership could choose is further polarizing the society with the goal of constraining its opponents in politics, media and business, as well as increasing Erdogan’s executive powers without changing the constitution. The sudden plunge of shares by Koza-Ipek and Dogan Groups, which both are perceived as opponents of the government, demonstrates the extent to which business environment is vulnerable to political power.

3. The Business Environment

Both foreign investors and Turkish firms have a lot to keep in mind when developing business strategies in the new era of Turkish politics. As an early indicator, two giant business organizations TOBB (Union of Chambers and Commodity Exchanges) and TUSIAD (Turkish Business and Industry Association) called for an urgent agenda to normalize the business environment and implement acutely needed reforms.

While anxiously waiting for government’s next step, business leaders should also

get prepared to tackle upcoming challenges that private firms will face. We analyze such challenges in three parts: labor relations, social movements and government relations.

1. Labor Model and Business Strategy

Labor wages in Turkey are expected to increase in the medium-term. The chart below demonstrates that nominal unit wages index has remained below consumer prices index so far. But with the goal of not to be outdone by its rivals, AKP has increased expectations of its voters by promising a dramatic increase in minimum wage (from 1000 TL to 1.300TL) and gradual abolishment of sub-contractor system. This means Turkey will cease to be a cheap labor country, and will have to transform itself into a value-added economy. This is, however, easier said than done. Business will have to develop strategies to strike the right balance between volume and value in production, and adjust their labor models accordingly. Such strategic choices call for carefully crafted change management programs, because deep-rooted habits of Turkish culture are unlikely to be replaced quickly. Managers will need to make right decisions and some tough trade-offs, while also convincing their organizations to comply and cooperate with the new principles. Short-term costs may seem daunting, but embracing them seems to be the only viable way to remain sustainably profitable in Turkey.



2. *What to Expect From Local Communities*

Business lives and operates in communities, which they are expected to contribute by increasing socio-economic conditions. Recently in Turkey, environmental movements have become stronger in response to giant energy and infrastructure projects. This is especially the case in Turkey's western regions, where support to AKP government is the lowest. Given the inability of opposition parties in keeping AKP's power in check, such communities are likely to create stronger social movements to assert their demands. Therefore, businesses in Turkey and in the region specifically should be careful about understanding and engaging local communities, and creating a balance between making feasible investments and local demands regarding social life, environment and respect for cultural habits.

3. *Building Relations With the Government*

With AKP reassuring its supremacy in Turkish political life, firms in Turkey and those who are considering Turkey as a primary target are now expected to seek right interlocutors to understand policy and business environment.

It is no secret that the Turkish government is a key stakeholder in Turkey's private sector, and businesses should engage in corporate political activity to help shaping the rules of the game in their favor. With AKP reassuring its supremacy in Turkish political life, firms in Turkey and those who are considering Turkey as a primary target are now expected to seek right interlocutors to understand policy and business environment. It would be a mistake to rule out the need to develop a sound engagement strategy, and rely on the so-called dealmakers who claim to provide privileged relationship with the government in exchange of grasping some share of the deal. This is not to say that relationships do not matter. On the contrary, they play a key-role in Turkish market. However, foreign investors need assistance of culturally savvy professionals who can bridge international and Turkish perspectives and turn relationships into constructive business deals.

4. *Summary*

Turkey has entered a new period of single-party rule as a result of the Nov. 1. re-election. However, whether the short-term positive environment will transform itself into a long-term political and economic stability will depend on the policy choices by the AKP government. For the moment, Turkey is still in the league of fragile countries due to macro-economic indicators, deep societal divisions and

geopolitical risks. In order to overcome this challenge, Turkey should urgently end social polarization, bring the Kurdish militancy to a peaceful end and engage in structural reforms to revitalize the economy. Whether the incumbent government will be able to carry out these huge tasks will depend on the alignment among its leaders. Therefore, businesspeople should closely monitor the interplay between policy and business environment, develop and implement agile strategies to tackle issues especially labor, community and governmental matters.

About StratejiCo.

StratejiCo. is a strategic consultancy company headquartered in Istanbul. Since 1987, StratejiCo. serves multinational companies that operate in Turkey and in the region by providing knowledge, relations and communication. We use an engagement-based approach to develop and execute corporate and public affairs strategies.

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