



OECD Territorial Reviews: Istanbul, Turkey

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Introduction

Istanbul, the demographic and economic heart of Turkey, has gone through enormous changes over the past century. This mega-city of about 15 million inhabitants has seen its population increased more than tenfold since 1950. It has benefitted from a favourable national economic environment, triggered by a broad and continuous reform process, strengthening its position on the international marketplace. Over time, Istanbul has established itself as the industrial, financial and logistics centre of the country, producing almost one-third of the national output and absorbing the bulk of foreign direct investment. Though it ranks low among OECD metro-regions in terms of gross domestic product (GDP) per capita, Istanbul has registered one of the highest output growth rates since the mid-1990s.

Istanbul however faces challenges that could hamper its ambition to become a hub for finance, logistics, culture and tourism in the Euro-Asia region, as well as its development in general. It is changing from an economy driven by labour-intensive activities to one based on knowledge industries, while traditional and labour-intensive sectors (*e.g.*, textiles and its supply chain) are shifting only gradually and slowly to other complementary industry segments. Constraints on human capital development and the informal sector have hindered productivity levels and increased income disparities. Over-migration is putting a burden on Istanbul's transport, public infrastructure and housing, and earthquake risk management. The scale and variety of these challenges necessitates improving the overall planning system, local public management and implementing a national strategy to reduce regional disparities and limit migration flows.

This *Policy Brief* looks at some of the challenges facing Istanbul and at the possible solutions. ■

What are the main trends?

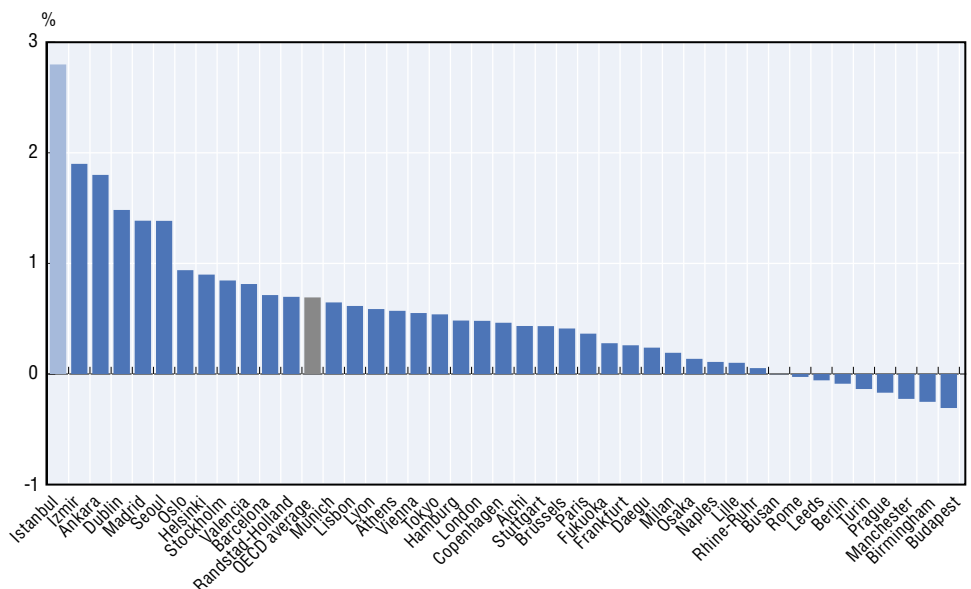
With around 15 million inhabitants, Istanbul metro-region has become a mega-city, ranking eighth out of 78 OECD metro-regions in terms of population size and first for population growth since the mid-1990s (Figure 1). Istanbul concentrates almost 20% of the national population versus 5% in 1950. Istanbul is also the leading economy in Turkey. It produces almost 27% of national GDP, 38% of total industrial output and more than 50% of services, and generates 40% of tax revenues. Its GDP per capita exceeds the national average by more than 70%, i.e., the third highest level among the largest 78 OECD metro-regions (Figure 2). With a stronger specialisation in higher-value-added activities, Istanbul's productivity level also exceeds the national average by almost 50%. Not surprisingly, Istanbul gets the lion's share of total FDI and generates half of total exports in Turkey (being the OECD country with one of the highest trade-to-GDP ratios).

Yet, emerging cities in China, Eastern Europe and other Asian countries are threatening Istanbul's economic base. Despite a structural change in the industrial mix, Istanbul maintains a sizeable low value-added and labour-intensive manufacturing sector, i.e., mainly textiles and supply chain. This sector represents 37% of the total labour force and 26% of GDP and around 80% of total exports. A productive restructuring has been ongoing in textile and specialisation is apparent in some high-value-added activities such as pharmaceuticals and to a lesser extent in electronics but this overall process is taking place slowly. ■

What are the future challenges?

Economic growth has resulted in it attracting dramatic waves of migrants from other parts of Turkey as well as from neighbouring countries at one of the fastest paces in the world. Such inflow of migrants has put the city's physical infrastructure under considerable strain and led to sizeable congestion costs and pollution issues. The two bridges crossing the Strait of

Figure 1.
AVERAGE ANNUAL POPULATION GROWTH RATES AMONG A SELECTION OF OECD METRO-REGIONS (1995-2002)



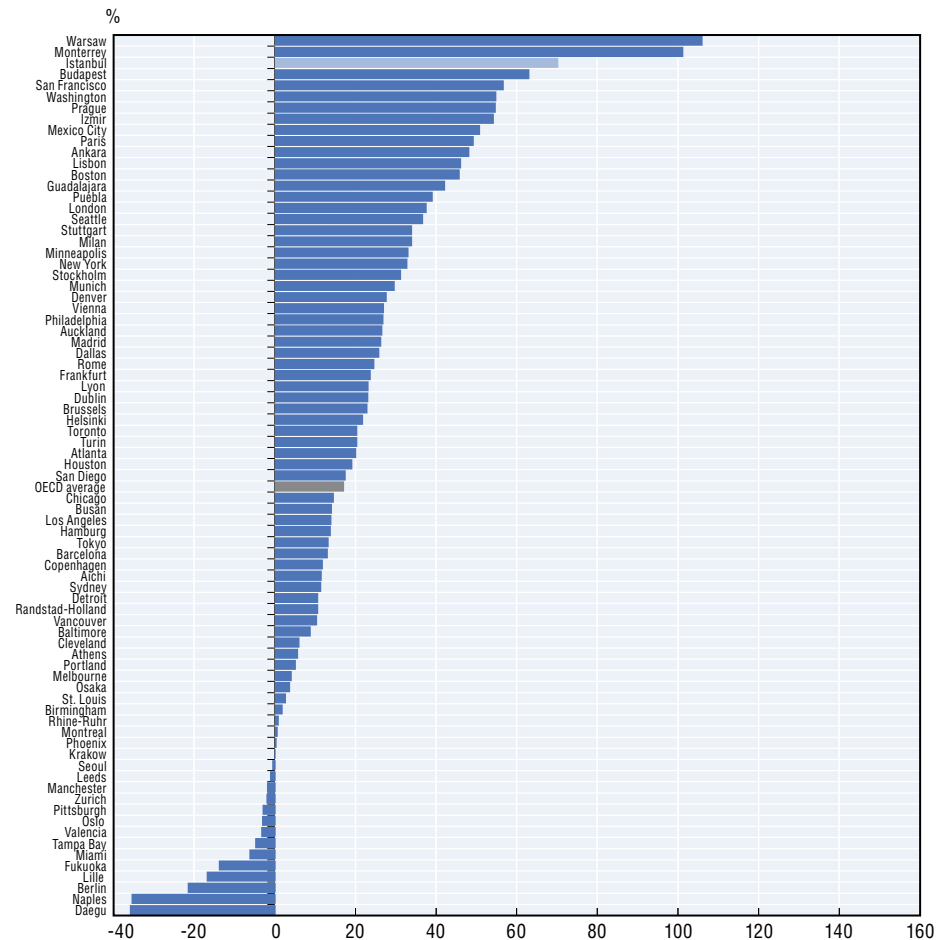
Note: OECD average refers to the average of OECD metro-regions.

Source: OECD Metropolitan Database.

Istanbul (the Bosphorus) run above capacity and the newly developed public transport systems (tramways, light rail and metro) is by far too limited. Informal settlements, housing around 50% of the population, have proliferated, sprawling towards water reserves and preserved forest areas. The Strait of Istanbul is considered one of the most crowded and potentially dangerous waterways in the world. The 1999 earthquake, one of the most damaging earthquakes in the world, and the threat of another major earthquake in the next 30 years make addressing these issues even more pressing.

Migration has also spurred the informal sector of the economy (around 30% of the city’s working labour force) as economic growth has been insufficient in providing jobs for a large number of newcomers into the labour market. The large number of small firms that make up the informal sector has helped to relieve urban employment tensions during the economic downturns. However, it also explains the low activity rate due to less employee access to adult education, on-the-job training, and other means of human capital development; all necessary for upgrading skills and increasing the innovation capacity and productivity of firms.

Figure 2.
DIFFERENCES IN PER CAPITA GDP OF METRO-REGIONS AND THEIR NATIONAL LEVEL (2002)
Sample of 78 metro-regions in the OECD



Note: OECD Average refers to the average of OECD metro-regions.

Source: OECD Metropolitan Database.

Increasing competition from low-labour-cost countries has impacted the real income of workers in labour intensive activities. Rapid economic growth has been insufficient in creating jobs for newcomers to the labour market (unemployment rate stand at 11.4%). Income disparities have increased with the new, highly educated and high-wage group working in more advanced and services oriented activities. This process is common in economies experiencing a major shift in industrial mix, but the effects in Istanbul have been magnified, with the large influx of low-skilled migrants over a relatively short period. ■

How to upgrade the economy?

To face international competition and becomes an innovation hub in Turkey capable to generate positive spillovers in the rest of the country, Istanbul needs to accelerate the positive trends in restructuring towards complementary segments. This includes Istanbul's activities to progressively upgrade towards higher technology content activities (*e.g.*, chemical, pharmaceuticals and medical devices, and electrical equipment and devices) and continued restructuring in the textile industry, expanding employment in apparel linked to global markets and contracting in knit fabrics. A lack of microeconomic adjustments and institutional bottlenecks are however slowing the pace of industrial transformation. Many of the actions to be taken are related to national macroeconomic policies, products and labour market regulations, tax and national sectoral policies (*e.g.*, education, labour markets, etc.). At the regional level, actions could aim at strengthening the networks between firms, encouraging links up and down supply chains, and facilitating the insertion of small firms into the wider processes of technological and managerial change.

Current policies to foster regional innovation and productivity could be further strengthened including those targeting Technoparks, technology development in logistics and textile and managerial and technological modernisation of SMEs. Such initiatives could be complemented by specific policies to tap all the potential of FDI in technology transfer. A cluster policy would be relevant to exploit specific niches for instance in design and fashion. Pharmaceutical manufacturing, medical and surgical equipment, and soap and detergents (18% of the total Istanbul's value added) also have the potential to trigger positive technological externalities on other sectors like biotechnology. Other promising sectors include the chemical and medical sectors, which have shown recent growth patterns and the prospect of health tourism.

A main priority for upgrading Istanbul's economy is to address the informal sector. This will require a long-term strategy that includes broad-based and integrated reforms, with a particular focus on creating a legal framework for micro-firms. Local government could promote formalisation through incentives like reducing local red tape, simplifying export rules and regulations. Connecting small firms and the sector of internationally competitive, export-oriented firms would contribute to bridging the technology gap due to lack of information about production methods and processes. The policy challenge is to reach these firms and provide access to financing and to create venture capital systems along with complementary actions (capacity building, micro-credit). ■

Can Istanbul become a hub in the Euro-Asia region?

The public authorities in Turkey see Istanbul as a regional centre for finance, logistics and tourism and culture between Europe, Asia, the Middle East and the former East European countries. Istanbul does benefit from important assets in these three areas but reforms and strategies are needed:

- In *logistics*, Istanbul has a long experience as the node of Turkey's international transportation corridors, processing 60% of the country's total trade volume, more recently strengthened by major transnational transport infrastructure projects, expansion of the modal transport and improved port management systems. It is however crucial to take environmental concerns into account, especially related to over-use of the Strait of Istanbul, and avoid a fast track implementation of specific projects.
- Istanbul's historical heritage makes it an attractive *tourism* destination and its recent nomination as the "2010 European Capital of Culture" has led to a series of renovation, restoration and demolition projects, complemented with financial incentives to increase the capacities of hotel, museums and other cultural amenities. The implementation phase, however, suffers from limited capacity, infrastructure deficiencies, cumbersome administrative procedures and limited access to financial resources. More attention could be put to attract repeat visitors and cultural events, or promote competitive creative industries linked with traditional industries.
- In *finance*, the Istanbul Stock Exchange (ISE) has witnessed a dramatic increase and the banking sector is more experienced than other places in the Euro-Asia region. Weaknesses include a low capitalisation rate and the capital markets being dominated by public securities over stocks. Reforms are needed to reduce high transaction and intermediary costs, and the financial intermediary institutions' high dependency on the stock exchange. ■

What about social and spatial development?

Going beyond a mere pro-growth strategy is crucial for Istanbul as rapid urbanisation growth and a large influx of domestic and foreign migrants to Istanbul in a relatively short period of time have raised major development issues threatening its social and environmental sustainability.

Several new projects are ongoing to address transport congestion, including the Marmaray project, an undersea rail tunnel across the Strait of Istanbul, the relocation of workshops off of the peninsula and the introduction of an efficient integrated tariff management to promote mass transportation. These efforts remain however by far limited compared to that needed to address the scale of the issue. A main obstacle to improvement is the highly fragmented decision-making process characterised by a large number of actors. The former Transportation Master Plans (last one enacted in 1996) have not been implemented, and the proposed shift in the modal split, away from cars towards the railway system, has not yet materialised. Similarly in urban planning, the system critically lacks implementation capacity accommodating projects already in progress and leading to an unsustainable pattern of urban growth.

Promoting a more environmental approach is even more pressing in such a congested and at-risk region as Istanbul. Remarkable achievements have been made in water management and adopting a wider concept of the environment, one which includes air pollution caused by transport, the use

of coal (or brown coal) for heating and, to a lesser extent, from unregulated industrialisation. More efforts need to be made to reduce traffic congestion. The Istanbul Earthquake Master Plan should be implemented, although individual elements are being adopted including major projects for seismic reinforcements and of law enforcement on illegal occupation.

Further incorporating social development concerns in current economic and urban policies is essential not only to deal with – and cushion against – eventual macroeconomic shocks but also to provide the social capital necessary for a long-term competitiveness strategy. At the local level, current urban regeneration policies, in particular the relocation policies for families and small-scale industries, needs to be implemented without disrupting socio-economic ties and community relations, and with sufficient infrastructure to support the newly planned neighbourhoods. Mass production of low-income housing and specific mortgage programmes, like those implemented recently in other parts of Turkey, could be complemented with actions to upgrade and regulate squatter settlements to reinforce local economic development and social capital in these areas. ■

What governance system for Istanbul?

The implementation of a competitiveness strategy, along with the necessity to deal with issues related to migration, congestion, social polarisation and environmental concerns make governance of the mega-city region especially challenging. Governance in Istanbul has undergone a major transformation. The planning responsibilities previously under the central government's responsibility have been transferred to the Istanbul metropolitan municipality since 2004 and the recent expansion of the municipality boundary which coincides which covers a large part of the functional economic area presents an opportunity to formulate a good strategic framework. New concepts are being introduced in the planning exercise such as urban regeneration, earthquake and tourism, environmental and transport.

Despite these improvements, Istanbul's governance system remains too complex and fragmented. Conflicts often arise because of a strong control of the central government and the provincial authorities over local matters as well as overlapping responsibilities. Several ministries intervene in infrastructure and land-use development, sometimes in contradiction with urban plans. Istanbul would benefit from a less iterative planning process and a clearer implementation programme. There is still a multitude of plans that involve a large number of actors with ill-defined competences leading to a diluted global vision and focus on the principal priorities. This is particularly apparent in transport and land-use planning.

Endowed with a large administration, Istanbul could well consider improving its local management through a modernisation reform like in Madrid or Seoul. These reforms introduce greater transparency in urban decision making and further accountability, a rationalisation of the local administrative framework, measures to enhance the local workforce capacity, new rules in human resources management, nomination procedures based on competition and transparency, and control and audit procedures on the allocations of resources to various extra-municipal actors including for the attribution of public works contracts. Enhancing the role of civil society in the local decision-making process, through better access to information, and

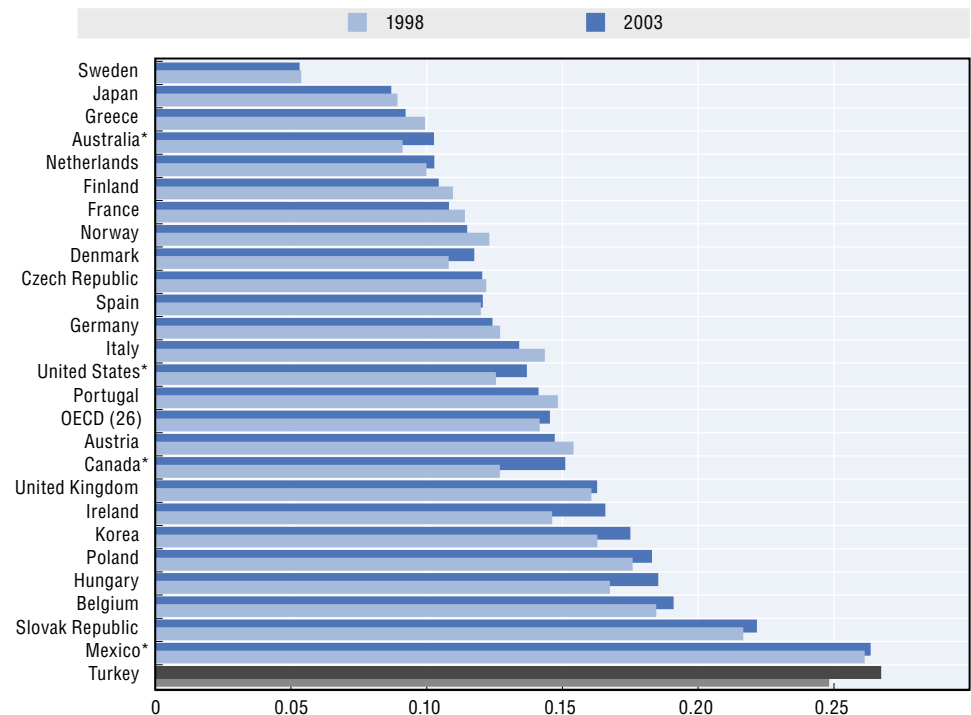
more involvement in municipal decision-making structures, would contribute to creating a more consensus-oriented approach.

Since the early 2000s, decentralisation of public administrations has been a key government priority in Turkey. Laws have been enacted or are under discussion, but changes are taking time to implement. One priority area in this process will be to ensure that lower level authorities have the local capacity to carry out their new duties. An interesting step in the decentralisation process – that will provide an additional institutional tool for governance in Istanbul – is the establishment of development agencies (DA) on a country-basis in 26 regions. The DAs have a number of broad objectives as they combine the functions of an investment promotion agency with that of a regional development agency. Whilst the DAs appear as a promising and necessary addition to the Istanbul region’s institutional structure, it is still unclear to how the DAs will fit into the existing structure and networks. ■

What about the central government?

Looking forward, the challenges facing the Istanbul metropolitan region cannot be tackled without considering the *national context of huge regional disparities* (the largest among OECD countries) (Figure 3). The central government understands the importance of fostering the economic development of its major metropolitan area and dealing with the major urban issues: Istanbul is a national pole of growth that needs to be sustained. However, the increasing challenges faced by the mega-city will constantly be

Figure 3.
COMPARISON OF REGIONAL DISPARITIES IN OECD COUNTRIES
Gini index for GDP per capita



Note: The Gini index looks not only at the regions with the highest and the lowest values but also at the differences among all regions. It ranges between 0 and 1 with the higher the value, the larger regional disparities. The Gini index for GDP per capita is obtained from the *OECD Regions at a Glance 2005*. And the regional population figures are collected from Statistics Sweden.

Source: OECD (2007), *OECD Regions at a Glance*.



threatened so long as the rest of the country is lagging behind. The resulting over-concentration in Istanbul has reached its sustainable limit, necessitating a national strategy for managing future growth. It is urgent for this process to be expedited not only for the development of the country, but also for the success and the sustainability of Istanbul under the continuous threat of increasing pressures from inward migration. ■

For further information

For further information about the *OECD Territorial Reviews of Istanbul* and the series of *OECD Territorial Reviews* on metropolitan regions, please contact Lamia Kamal-Chaoui, tel.: +33-1 45 24 16 73, e-mail: Lamia.Kamal-Chaoui@oecd.org.

For further reading

OECD (2006), **Economic Survey of Turkey**, Volume 2006, ISBN 978-92-64-02916-3, € 45, 196 pages.

OECD (2008), **OECD Territorial Reviews: Istanbul, Turkey**, ISBN 978-92-64-04371-8, € 40, 276 pages.

OECD (2006), **OECD Territorial Reviews: Competitive Cities in the Global Economy**, ISBN 978-92-64-02708-4, € 37, 446 pages.

OECD (2006), **OECD Territorial Review: Seoul, Korea**, ISBN 978-92-64-01300-1, 170 pages.

OECD (2007), **Regions at a Glance 2007**, ISBN 978-92-64-00987-5, € 50, 252 pages.

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Where to contact us?

OECD HEADQUARTERS

2, rue André-Pascal
75775 PARIS Cedex 16
Tel.: (33) 01 45 24 81 67
Fax: (33) 01 45 24 19 50
E-mail: sales@oecd.org
Internet: www.oecd.org

GERMANY

OECD Berlin Centre
Schumannstrasse 10
D-10117 BERLIN
Tel.: (49-30) 288 8353
Fax: (49-30) 288 83545
E-mail:
berlin.centre@oecd.org
Internet:
www.oecd.org/berlin

JAPAN

OECD Tokyo Centre
Nippon Press Center Bldg
2-2-1 Uchisaiwaicho,
Chiyoda-ku
TOKYO 100-0011
Tel.: (81-3) 5532 0021
Fax: (81-3) 5532 0035
E-mail: center@oecdtokyo.org
Internet: www.oecdtokyo.org

MEXICO

OECD Mexico Centre
Av. Presidente Mazaryk 526
Colonia: Polanco
C.P. 11560 MEXICO, D.F.
Tel.: (00.52.55) 9138 6233
Fax: (00.52.55) 5280 0480
E-mail:
mexico.contact@oecd.org
Internet:
www.oecd.org/centrodemexico

UNITED STATES

OECD Washington Center
2001 L Street N.W., Suite 650
WASHINGTON DC. 20036-4922
Tel.: (1-202) 785 6323
Fax: (1-202) 785 0350
E-mail:
washington.contact@oecd.org
Internet: www.oecdwash.org
Toll free: (1-800) 456 6323

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