International monetary and financial

Introduction Turkey suffered from financial and economic crisis twice during a very short period of time: the first crisis occurred in November 2000, while the second one took place in February 2001. The first crisis was primarily the crisis of private banking sector, when private commercial banks did not manage to meet their obligations and were destined to collapse. The second crisis was caused by disproportions in the state-owned banking sector. Both of these crises are very closely connected with the banking sector and they both are caused by inadequate regulation of this sector.

IMF played a very important role in Turkish economy during both the crisis of 2000 and 2001. During these years, it provided financial assistance to Turkey of $28 billion, as well as different kinds of recommendations. The stand-by agreement which was reached between IMF and Turkish government was in the heart of all of the reforms taking place in Turkey. The paper aims to investigate the major causes of Turkish crises of 2000 and 2001. In order to identify real causes of the crises, both official version and opinions of different economists are analyzed.

Major attention in the paper is devoted to the role of IMF in the crises and mistakes which its experts made when developing the program of reforms for Turkey. The paper touches upon potential threats of neo-liberalization monetary policy and its impact on the economies of middle level-countries. The paper provides the overview of the reforms which took place in Turkish economy prior to the crises and touches upon the negative impact of Turkish government on the country’s economy. 1. Overview of Turkey’s Financial and Economic Crises of 2000 and 2001

Turkey’s financial and economic crises of 2000 and 2001 have been one of the most powerful crises in the history of the country. The events of the crises have been widely discussed by different authors, including Gorvett (2001), Alper (2001), Ziya and Rubin (2003), Akyuz and Borata (2002), Yeldan (2001, 2002) and others. All of these researchers have conducted research on the major causes of Turkish crises and given their recommendation concerning how to avoid similar crises in future. Yeldan (2001, 2002) devotes particular attention to the analysis of causes of crises which disagree with official and media point of view.

Alper (2001) concentrates his attention on the connection of IMF to the crises and its major mistakes. As Yeldan (2002) marks, crises were not new for Turkey’s economy. Throughout the 90’s the country suffered from smaller-scale crises. However, the crises of 2000 and 2001 were exceptionally large by scale. For example, during that time Turkey’s GDP fell by 5%, which was one of the lowest indicators during the recent years. The brightest indicator of the crises though was rapid depreciation of Turkish Lira throughout 2001, increased cost of government borrowing and increase of imports by more than 24%.

“ As regards inflation, the further currency depreciation suggests that our end-year CPI inflation projection needs to be increased from 58 to 65 percent.... Finally, the economic slowdown and the depreciation of the Turkish lira have led to a marked turnaround in the external current account in 2001” (Akyuz Y_lmaz, Borata Korkut. The Making of the Turkish Crisis. Accessed on May 1, 2006 at URL: http://www. umass.

edu/peri/pdfs/fin_akyuz. pdf). The interest rates at Turkey's commercial banks increased dramatically during the period of crisis.

As Alper (2001) states, " during the November 20-December 5 2000 period only, US$6. 4 billion net foreign exchange outflow took place and the overnight inter-bank interest rates soared to 1, 700% on December 1. " Both financial crises in Turkey happened while the country was supported by IMF. The relationship of Turkey with the IMF has been very firm for many years, due to frequent macroeconomic crises in the country. This relationship started in 1958 and since then, Turkey frequently used IMF's support in many matters.

In 1990 Turkey applied at IMF for full convertibility of Turkish Lira. The support of the floating exchange rate of the currency was very successful until the end of 90's when it could not be managed efficiently anymore; at that time Turkey started implementing a stabilization program for its currency. In 1998, the program called Staff Monitoring Program was launched with the help of IMF; in 1999 it was followed by a large number of other agreements in the field of monetary regulation and reforms, and finalized by a stand-by agreement with the IMF.

This agreement aimed to cover a large number of macroeconomic problems and provide solutions to them. Some of thegoalsset by the agreement seemed very challenging, but the government was positive they all could be implemented in the shortest period of time. " The stand-by agreement was certainly ambitious: aiming to bring consumer price inflation down to 25 percent by the end of 2000, 12 percent by the end of 2001, and to seven percent by the end of 2002. ” (Ziya, Rubin, 2003, p. 9) There were other areas at which the agreement aimed, besides inflation decrease.

“ The program also tried to tackle fundamental structural problems in the key areas of taxation, privatization, banking regulation, and the reform of agricultural price support schemes. ” (Ziya, Rubin, 2003, p. 9) The program therefore was seeking to achieve very ambitious goals in all of the sectors of the country’s economy. The developers of the program believed that by targeting all of the sectors of the economy, they could successfully achieve the best results. Instead of success, the program had a financial crisis of 2000 as its result.

As it showed later, some of the goals of the program could not be achieved due to poor planning process of the program. It was very difficult for the officials involved in the process of implementation of the program to determine which actions had to be taken first. Another reason why the program failed was that the government did not have full commitment to the actions, which had to be taken according to the program. Members of thecoalitiongovernment which was ruling the country during the time prior to the financial crises had different goals, which did not always agree with all of the goals set by the program.

Even though government officials claimed that they were looking forward to implementing all of the actions planned by the program, in reality they turned out more interested in pursuing their own interests than the ones in the stand-by agreement. The fact that government problems caused major problems for the country’s economy was supported even by Turkish officials:

“ Prime Minister Bulent Ecevit stormed out of a meeting of the all powerful National Security Council and fronted the cameras.

" A major crisis," he said, had broken out between the government and the presidency. ” (Gorvett, 2001, p. 21). Besides government’s inability to carry out joint decisions, an important problem which threatened Turkish economy was connected with higher energy prices. As the result of increased energy prices, supply inflation started increasing rapidly because all of the industries which were using energy were forced to increase their prices. Supply inflation is very difficult to stop, and government of Turkey was not successful in that.

In addition to high energy prices, economy got weakened by an increased exchange of Euro, which had a direct impact on the cost of products imported from European Union. Despite the efforts of Turkish officials and officials from international organizations, the stand-by agreement signed with IMF did not have a positive impact on the economy. The consequences of Turkey’s financial crises were very severe. The first crisis of 2000 did not have a major impact on the economy and it was not even covered broadly in the media.

However, the second crisis of 2001 was a major blow because it greatly knocked down the country’s GNP. “ GNP in real terms declined by 9. 4 percent during the course of the year. The result was a dramatic drop in per capita income from $2, 986 to $2, 110 per annum and a massive increase in unemployment by 1 million people. ” (Ziya, Rubin, 2003, p. 12) The crisis of 2001 also had a major impact on the employment rate in the country. If in

2000 the crisis caused unemployment among unskilled workers, in 2001 all of the segments of the labor market were influenced.

Large numbers of people in highly-qualified jobs were fired. Small and middle-sized businesses also suffered greatly from the crisis of 2001. Many of them were driven into bankruptcy. The crisis had a deep impact on thepovertylevel in the country. “ The crisis also led to a major increase in the number of people living below the $400 per month poverty line and the $200 per month subsistence line. ” (Ziya, Rubin, 2003, p. 12). As the result of the crisis, many people stopped believing politicians because they considered bad politics the major cause of their hardships.

At the same time, the crisis of 2001 had some positive influence on the country’s economy. It served as a peculiar kind of shock for Turkey. As the result of this crisis, more reforms were conducted in the economy, and much faster than they otherwise would have been conducted. These reforms sealed Turkey’s place in the European Union. The same coalition government which drove the country’s economy into the major crises conducted a large number of reforms in Turkey during the following years, which contributed to Turkey’s stability and prosperity.