

# [Major causes of turkey’s financial and economic crises](https://assignbuster.com/major-causes-of-turkeys-financial-and-economic-crises/)

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Turkish crises of 2000 and 2001 had a very negative impact on the country’s economy. The research of the causes of the crises is very important, because it provides lessons for future development of economic policy in the country. The official version of the crises considers Turkey’s inability to conduct reforms efficiently the major cause of the crises. Surprisingly, there are some alternative versions which completely disagree with the official one.

Erinc Yeldan, professor of Bilkent University, Department of Economics in Ankara, Turkey has conducted a detailed analysis of causes and effects of Turkish crises and disagrees with the official version. “ The official stance is that the crisis was the result of thefailureof the public sector to maintain the austerity targets and the failure to fully implement the free market rationale ofglobalization” (Yeldan Erinc.

BEHIND THE 2000/2001 TURKISH CRISIS: Stability, Credibility, and Governance, for Whom? Retrieved on May 1, 2006 from URL: http://papers. ssrn. com/sol3/papers. cfm? abstract\_id= 290539) However, the author emphasizes that “ contrary to the official wisdom, the current economic and political crisis is not the end result of a set of technical errors or administrative mismanagement unique to Turkey, but is the result of series of pressures emanating from the process of integration with the global capital markets”. Yeldan believes that Turkey failed in the financial market because its financial system was not mature enough, similar to financial systems of other emerging economies.

According to Yeldan’s opinion, emerging markets are not able to retain their efficiency quickly after getting exposed to certain reforms in the economic sector. In case if these reforms are conducted too quickly and without the understanding of the specifics of the country, they can fail and lead to dangerous consequences. Yeldan opposes the traditional opinion which “ portrays Turkey as a misbehaved student in the global markets”. He argues that there was no Turkey’s fault in the crises.

It was just unable to react to the changes which took place in a short period of time due to the policy of neo-liberalization of financial markets. Yeldan points at the fact that, according to the official and media version, Turkish crises were the result of inability of Turkish government to implement reforms in a timely manner and follow the procedures which were marked in the program of economic reforms. Mr. Kemal Dervis, Vice-Chairman of the World Bank, who was forced to resign as the result of the Turkish crisis, stated that “ the main source of the Turkish crisis was the rapid widening of the current account deficit.

” This point of view is actually right to some extent, because all of the major economic indicators at the moment of the crisis displayed this tendency. At the same time, the author argues that Mr. Dervis refers to the effect but not to the cause of the phenomenon. According to Yeldan, current account deficit was an effect of a much more important factor, which in the final end contributed to the development of the crisis: “ the main issue here is to discuss the main reasons behind this deterioration, rather than highlighting the deterioration itself, which is merely an end-result!

” Yeldan disagrees with the opinion of Dervis that budget expenditures were much higher than revenues during the period and that this factor could be crucial in the development of the crisis. The researcher brilliantly points at the data describing consolidated budget revenues and expenditures during the analyzed period of time. Despite the official version that expenditures exceeded revenues, budget expenditures during the analyzed period did not exceed target levels, while levels of budget revenues were even higher than the target data. Therefore, Yeldan comes to a conclusion that the official version of the reasons of the crisis was false.

It stated that the major cause was account deficit, while this was just one of the consequences of the crisis. As Yeldan points, official version of the causes was used in order to hide the real mistakes made by IMF and other international organizations in handling the crisis. Instead of claiming that the crisis was caused not only by problems connected with Turkey’s economy but also by problems in the economic policy developed jointly by Turkish government and international organizations, officials chose to put all of the blame on Turkey alone, which was very convenient in the situation.

As the real major cause of the crisis, Yeldan cites neo-liberalization policy which became dominant in the markets and which led to several crises in different countries. Policy of liberalization is efficient for countries which have very strong financial systems and good monitoring mechanism. However, it is not acceptable for middle-income countries which have problems with control system. For example, famous Asian crisis of 1997 is the result of liberalization of financial markets.

In case of Turkey, the policy-makers simply did not anticipate such high volatility and change which were typical for globalized financial markets. With the new regulations governing the activity of Central Bank, the interest rates in the domestic market became subject to the changes in interest rates in the global markets, and stopped being dependent on the domestic asset market. Yeldan has also conducted observations of operations in the Turkish financial market prior to the crisis.

He came to some interesting results while analyzing monetary policy of Turkish government. Observations of the securities market showed that a large number of speculative operations were performed in the market prior to crisis. If in the past the world capital markets were not as easily accessible, they became fields of battle after roots of neo-liberalization policy got planted in Turkey. According to the research of Yeldan, the number of speculative operations increased dramatically in the Turkish market with neo-liberalization policy.

Operations of non-residents reached a particularly high level of increase. It is common truth that excessive volumes of speculative operations in the markets of middle-income countries can have a very dangerous effect on the financial markets. Experience of many countries shows that speculative operations can collapse financial markets; thus, some of these operations have to be prohibited until the market of the country reaches a certain level of maturity.

As Yeldan points, theenvironmentin which the reforms took place was therefore very fragile, and did not have a solid background. Yeldan also analyzes the situation with international reserves of the Central Bank in order to make a conclusion about external fragility of the country’s economy. According to many authors, one of the major indicators of upcoming financial crisis is the ratio of short-term foreign debt of the country to its international reserves.

This ratio shows the dependence of the country on the foreign debt in a short-term period of time, i. e. , its liquidity when it comes to paying for obligations denominated in foreign currency. Yeldan’s research has shown that this ratio did not go below the level of 100% in Turkey prior to the financial crisis, which means that there were no indicators of financial crisis in this department. The ratio of external fragility in Turkey stayed on a relatively high level for a long time. Therefore, there is no ground for identifying a cause of the financial crisis as the result of a negative value of external fragility ratio.

The real causes of the Turkish financial crises can be found in events which took place in the economy in 1989, when external transactions carried out by Turkey were liberalized to a maximum level. This policy led to increases in speculation in the Turkish financial market. The development of financial markets was not supported by adequate development of the market of real assets. Ziya and Rubin (2003) support Yeldan’s opinion that Turkish financial crises were not only caused by political mistakes, but also by financial liberalization. “ Domestic politics, then, was at the heart of the crisis.

Yet, an account of the crisis would be seriously incomplete if it failed to take into account the crucial role of external dynamics. ” (Ziya, Rubin, 2003, p. 10) The authors share Yeldan’s point of view that financial liberalization is oftentimes dangerous for countries which do not have strong and mature financial markets. It is impossible to make a final conclusion that neo-liberalization was the sole cause of financial crises in Turkey because there were lots of other causes. The crises were a result of a combination of certain factors.

However, it is important to emphasize that the lion’s share of blame for financial crises in Turkey should be placed on the shoulders of experts who conducted neo-liberalization policy in Turkey. The issue of financial liberalization has caused major discussions among world economists nowadays. On one hand, it can be regarded as a positive phenomenon due to the fact that financial institutions argue that strict regulation from the government does not let them operate to the fullest, and limits their opportunities not only to get profits but also serve the interests of their clients.

In some cases, this statement is actually true because oftentimes the government is too slow in updating the regulations for the present day needs of financial institutions. On the other hand, financial liberalization can lead to the destruction of the country’s financial system because liberal regulation environment motivates financial institutions take more risks than they would otherwise be taking and get engaged in activities which have a negative influence on their performance. In case of Turkey, liberalization brought more problems than positive consequences.