

# International Financial Crises and the Political Economy of Financial Reforms in Turkey: 1994-2009

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**Abstract**—This study<sup>1</sup> holds for the formation of international financial crisis and political factors for economic crisis in Turkey, are evaluated in chronological order. The international arena and relevant studies conducted in Turkey work in the literature are assessed.

The main purpose of the study is to hold the linkage between the crises and political stability in Turkey in details, and to examine the position of Turkey in this regard. The introduction part follows the literature survey on the models explaining causes and results of the crises, the second part of the study. In the third part, the formations of the world financial crises are studied. The fourth part, financial crisis in Turkey in 1994, 2000, 2001 and 2008 are reviewed and their political reasons are analyzed. In the last part of the study the results and recommendations are held.

Political administrations have laid the grounds for an economic crisis in Turkey. In this study, the emergence of an economic crisis in Turkey and the developments after the crisis are chronologically examined and an explanation is offered as to the cause and effect relationship between the political administration and economic equilibrium in the country. Economic crises can be characterized as follows: high prices of consumables, high interest rates, current account deficits, budget deficits, structural defects in government finance, rising inflation and fixed currency applications, rising government debt, declining savings rates and increased dependency on foreign capital stock. Entering into the conditions of crisis during a time when the exchange value of the country's national currency was rising, speculative finance movements and shrinking of foreign currency reserves happened due to expectations for devaluation and because of foreign investors' resistance to financing national debt, and a financial risk occurs.

During the February 2001 crisis and immediately following, devaluation and reduction of value occurred in Turkey's stock market. While changing over to the system of floating exchange rates in the midst of this crisis, the effects of the crisis on the real economy are discussed in this study. Administered politics include financial reforms, such as the rearrangement of banking systems. These reforms followed with the provision of foreign financial support. There have been winners and losers in the imbalance of income distribution, which has recently become more evident in Turkey's fragile economy.

**Keywords**—Economics, marketing crisis, financial reforms, political economy

## I. INTRODUCTION

MANY financial crises started in the international financial system repeatedly from the 1990s on. European Monetary Crisis (1992-93), Latin America "Tequila Crisis" (1994-95), Turkey Crisis (1994), South East Asian Crisis (1997-98), Russian crisis (1998), Brazil Crisis (1999), Turkey Crisis (2001), Argentine Crisis (2002), Global Crisis (2008) are just some of these crises to name. As number, frequency and devastating impact the global financial crises increased in a world where international capital movements

are free, they took greater place in economics literature. The main discussion takes around whether they take place because of the changes in market expectations or weakness in basic economy indicators.

## II. LITERATURE REVIEW

Latest crises are tired to be explained by new crises models as the economic crises emerged and new cases come to the agenda. Traditional theories of financial crises were developed for the explanation of crises took place in Latin American countries in 1980 and held for the inconsistency between national economic policies and the exchange rate [1]. This theory remained inadequate to explain the crisis in the European monetary system in the early 1990s. Theories emerged to explain new crises, argued that negative expectations on sustainability of the stable exchange rate in the developed economies have led to the crises [2].

Unlike others, theories explaining Southeast Asian crisis emphasized the government guarantees against losses of banks and companies [3]. According to this approach, the government guarantees led to increase in stock prices thus led to crisis. This approach differs from others as it also explains bank crises. Crisis started as banks borrow from abroad and decrease the yield of capital (decrease in yield of capital means decrease in assets quality and thus decrease in their net value. The mechanism can be expressed as follows: As liabilities increased because of increase in interest rates, returns on assets were unchanged therefore net value of bank capital was decreased), thus led to increase of bank losses and resulted in banks recall of commercial loans. National banks recalled domestic credits in order to pay their debts to abroad. Crisis became inevitable as capital outflow followed that case. Therefore it was argued that the basis of crisis was banking and financial sector problems especially balance sheet problems.

Different studies were conducted for different countries starting from above mentioned crisis theories. Some of those studies are reviewed as follows.

Banking system was determined as the primary factor for the basis of crisis in the study of Eichengreen and Bordo [4] conducted for 1975-1997 term on 21 developed and developing countries. Banking system became more fragile especially due to the bank panic withdrawal of deposits from the banking system rapidly in that period.

In cross sectional data analysis of 65 developed and developing countries Demirgüç and Detragiache [5] obtained results in their study similar with Eichengreen and Bordo [4] study. In addition, the importance of inadequate regulation and supervision in the banking system and macroeconomic imbalances in the banking crisis were emphasized.

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Kregel [6] on the other hand argues that causes of the crisis are different for Southeast Asian crisis in 1997 and Latin America countries in the 1990s and 1980s. According to Kregel [6], crises in Latin American countries in 80s and 90s are because of excessive budget deficits and balance of payments problems. Southeast Asian crisis is largely due to the short term speculative capital movements. International capital movements in a positive conjuncture emerged in Asian countries led to crisis due to excessive market optimism and reduced perceived risk in the banking thus led to excessive credit growth. On the other side, Asian countries started to experience debt-and-deflation process based on reversal of positive expectations.

Alves, Ferrari and Paula [7] suggested in one of their study that monetary crisis for Brazil in 1998-1999 is due to lack of confidence based on the defendable foreign exchange rate and foreign liabilities sustainability of government where capital movements are fully liberal.

Demirgüç and Detragiache [5] and Rossi [8] highlighted in their studies that deposit insurance together with financial liberalization increase the probability of banking crisis. Similarly, Arestis and Glickman [9] and Kregel [10] argued that financial liberalization applied additional pressure on the financial system and cause deepening of the crisis in the 1997 Southeast Asian crisis.

On the other side López-Mejía [11] asserted that excessive capital flows adversely affect the banking system especially in developing countries by causing a mismatch between maturity of banking credits and liabilities together with a credit quality degradation in the 1990s. Increased bank loans depending on the capital flows led to increase in financial asset prices and fragility of the banking system and therefore financial crises emerged.

Hardy and Pazarbaşıoğlu [12] suggested based on their study carried by using a large number of macroeconomic variables that the amount of credit, capital inflows and an increase in interest rates, the reduction in growth rate could increase the risk of the crisis.

Gavin and Hausman [13] emphasized the importance of the increase in the amount of debts in the occurrence of crises. Accordingly, the increase in the amount of the debt is the main reason of crisis in Latin America. Then, Kaminsky [14] made the same analysis by extending the sample size and found a positive correlation between the banking crisis and excessive credit expansion. These results are in a position of support for arguments put forward that the fragile structure of the banking system is one of the main causes of the crisis. The study held by Chang and Velasco [15] concludes that the financial crisis as a side effect of the bank panic. According to Chang and Velasco [15] as central bank prevents crisis by acting like the last credit resort in a closed economy, and it cannot prevent crisis since international reserves are limited in an open economy following the policy of fixed foreign exchange rates. Likewise, Sachs and Radelet [16] suggested also that crises are caused by the bank panic. Especially in Asia crisis, the bank panic and financial fragility that started by the effect of international investors' pessimistic behaviours those recall one

each other led to a crisis although all the related countries had no mistaken policies.

Many studies made on the formation of the financial crisis experienced in Turkey. Some of the works done on the crisis of 1994 crisis in Turkey are depicted below.

Celasun [17], similar to Özatay [18], suggests that besides the wrong management of public debt, the excess liquidity in the market as a result of instabilities in fiscal policies is the cause of crisis in 1994. In their study where they analyzed the crisis in 1994 by using a large number of macroeconomic variables Uçer, Van Rijckeghem and Yolalan [19] argued that the systematic deterioration in the basic macroeconomic indicators have played an important role in emergence of the crisis. In conclusion, common feature of these studies is that they emphasize the budget deficits and unsustainable external deficits as the main reasons for crisis in 1994. In the studies of Boratav [20], Uygur [21] and Yeldan [22] crisis is held with the mechanism explained below. The main reason of the crisis in 1994 is the budget deficits. The budget deficits led by insufficient domestic savings were compensated by capital movements as a result of financial liberalization. In this context, capital movements under budget deficits and external deficits have created a temporary equilibrium in the form of high interest-and-low exchange rate. The studies of Boratav [20], Uygur [21] and Yeldan [22] of the crisis use the following mechanism to explain. The main reason for the budget deficit is the 1994 crisis. Domestic savings in the budget deficits caused by insufficient, as a result of financial liberalization of capital movements has been corrected. In this context, capital flows and external deficits of the budget deficit while continuing to occur, in the form of high interest-and-low exchange rate has created a temporary equilibrium. The financial crisis is triggered by on the one hand the high interest-and-low exchange rate policy accelerates the entry of capital movement, on the other hand doubts of market players for the reliability of implemented policies grow. As a result, the deficits (budget deficits and external deficits) called twin deficits in economics literature led to the financial crisis in Turkey in 1994.

Unlike the 1994 crisis, November 2000 and February 2001 financial crises are subject of many more studies emphasizing the formation of crisis and the fragility of banking system [23], [24], [25], [26], [27], [28], [29], [30], [31], [32], [33], [34].

Özatay and Sak [27] suggests that February 2001 crisis would not occur if the banking system has not been fragile in spite of poor macroeconomic indicators of the year 2000 (excessive public borrowing requirement, the public debt to GNP ratio, the current account deficit, high ratios of inflation rate and financial sector foreign liabilities to exchange reserves, and excessive exchange rate value). The primary reason behind the February 2001 crisis was the fragility of the banking system based on excessive public borrowing requirement and mistakes done in financing it. In that study, the November 2000 and February 2001 crises have occurred in Turkey because of the fragile structure of the banking sector. Increased open positions of the banking system with increased

duty losses of public sector banking led to interest rates increase and increased the doubts over the sustainability of debt.

Fisher (IMF chief economist during February 2001 Turkey crisis) argued that current account deficit is the most prominent source of crisis indicator, and the banking sector crisis with high current account deficit caused the crisis in Turkey in 2001 November [26].

Karabulut [30] found in his study on exchange rate crises in Turkish economy covering the 1989-2001 period that the financial crisis came out when the difference between the official real exchange rate and the current exchange rate is highest at two points (March 1994 and February 2001). The importance of the study comes from its using the concept of foreign currency crisis rather than using the concept of financial crisis for 1994 and 2001 crises in Turkey. According to Karabulut [30], the root cause of foreign currency crisis is the currency exchange rate policy that represses foreign exchange rates thus led to overvaluation of domestic currency. In addition, he argues that crises in Turkish economy verify the Krugman theory based on the view that likelihood of foreign currency crisis increases as the budget deficit increases. Another aspect of the model is that it explains the crises in Turkish economy with the banking system and the budget deficit in spite of explaining them in other developing countries with basic indicators for foreign. Karabulut [30] suggests that the most basic feature of the crisis in Turkey is overvaluation of the domestic currency through repressing foreign exchange rate.

Togan [34] asserts that the main reasons of financial (foreign currency) crisis in April 1994 and February 2001 are corrupt financial discipline and excessive real foreign exchange rate.

Akyüz and Boratav [23] explains the role of the fragility of banking system in February 2001 crisis that any person who knows the structure and the weaknesses of Turkish banking system and dynamics of stability policy using foreign currency anchor should also know problems may arise in attaining the targeted drastic decrease in nominal interest rates and how Turkish economy is fragile before the risks of drastic changes in capital flows. Uygur [26] on the other hand emphasizes the effect of a fragile banking system on the banking crisis by arguing that in case the risky banking system borrows from abroad and Central Bank omits sterilization, any disruption in foreign capital movements (in-and-out) disables money-and-interest accordance capability of the economy.

Alper [28] suggests that the fragile banking system combined with negative external factors (oil prices, international interest rates and the dollar-to-euro parity increased) and mistakes in the program design of IMF makes February 2001 crisis is inevitable. Işık [29] emphasized the fragility of banking system by arguing that the external financial fragility indices for Turkish economy increased rapidly before April 1994 and February 2001 financial crises and this led to pessimistic expectations on repayment capacity of the economy for external financial liabilities and thereby cause a financial crisis.

### III. FORMATION OF FINANCIAL CRISIS

There exist heterodox approaches to explain crisis besides traditional approaches in economics literature. According to the heterodox approach to the crisis financial crisis, in a capitalist economy, financial instability and speculative attacks are seen as a natural result [29]. According to this approach, finance-and-expenditure relation, in a capitalist economy, is itself a source of instability beyond being a factor to increase instability. Excessive indebtedness status arising as a result of excessive accumulation of debt, financial fragility in the banking sector, debt deflation, concepts such as systemic risk are basic elements of these approaches.

Rapidly increasing bank credits and debt accumulation in non finance sectors based on market behaviours through excessive optimism in economic growth (expansion) periods also increase credit risks of banks and fragility of financial system. In other words, the basic causes of the crisis are excessive optimism of market players in their instinctive behaviours and credit boom it led.

Prior to analyze financial crisis in economics literature it is observed that concepts like financial instability, financial irregularities, financial fragility and systemic risk are used interchangeably [31]. These concepts generally described as occurrence risk or the probability of deviations (deteriorations) caused by unexpected changes in prices and amounts of assets in financial markets. In some cases, these concepts do not remain limited to financial markets only and cover all the destructive effects in other sectors of the economy.

In this context, these concepts could also be used in place of financial crisis in economics literature. Financial crisis concept is generally used for the result of negative effect of deteriorations in financial markets disrupting performance of financial institutions those are spread into entire economy consequently lead to degradation of payment systems and prevention of effective allocation of resources. Mishkin [32] defines financial crisis based on imperfect information theory as financial crisis is deterioration in financial markets in increase of adverse selection and moral risk problems. This deterioration in financial markets makes investment funds ineffective to turn into most productive investment possibilities. So the financial crisis is defined as incompliance of financial markets to function effectively resulting in a significant contraction in economic activities.

Schwartz [33] differentiates the actual real financial crisis and real non financial crises. Real nonfinancial crises only lead to loss of wealth by turning initial optimistic expectations into uncertainties. Schwartz puts forward that this loss of wealth does not mean the financial crisis. Schwartz does not take the bank panics and financial proceedings without the potential to decrease in money supply as a crisis although it may lead to excessive drops in asset prices and increased number of bankrupts.

The meaning of the term financial crisis and its corresponding status in economics is problematic. However in general it is argued that there are four types of crises [34]: (a) Currency crisis, (b) Banking crisis, (c) Systemic financial crisis and (d) External debt crisis. In case a speculative attack

on the exchange value of the currency yields in devaluation of the currency or great decrease in foreign exchange reserves in order not to let that devaluation or hyper increase in interest rates, this case is then called currency crisis. Banking crisis occurs when actual or potential bank failures may prevent banks in fulfilment of their obligations or the government may be forced to intervene to avoid that failures. Systemic financial crises are financial deteriorations with important negative consequences on real economy through preventing effective functioning of financial markets. External debt crisis happens when the debt of a country could not be paid by either the government or private sector. As a result, common features of all types of financial crisis are their having unsustainable economic imbalances and important fluctuations in financial asset prices (or foreign exchange rate).

#### IV. FINANCIAL CRISIS IN TURKEY

##### *a) 1994 Crises*

Macroeconomic management policies have not been implemented properly in Turkey in liberation of capital flows upon 24 January 1980 decisions. The inflow of external resources was wrapped into a short term structure under the market uncertainty through high inflation. The share of state in external debt has declined the shares of bank sector and private sector has expanded where system is shackled by short term capital in-and-out flows.

Decrease in interest rates when public debt requirement was increased started a rally for foreign currency and disfavour for domestic currency in 1994 crisis. Thus, domestic currency is vastly devaluated against foreign currencies. The foreign exchange rates increased 230% within three months and a negative economic growth is experience although it was around 7% previously. Interest rates began to climb to 1000% from 100%.

Expectations factor was affected negatively because of various reasons in this period; short term capital in-and-out flows upset the economy. Besides all, it was known that the real problem was related with the financial deficits of public. Economy was over forced and sound resources could not be provided.

A banking crisis accompanied 1994 crisis. A rush for excessive borrowing caused by financial deficits of public affected banking system in great extends also. Banking system got used to live on interest rate difference in external and domestic market and trading on treasury bills instead of providing credits to the system.

There were 44 banks with 5769 branches in 1979. That quantity was doubled in 1994. After the crisis new banks are not permitted and new branches are strictly limited. Later, a real increase in all of those was observed. It is worth to dig that in search of the cause of the crisis.

Banks are inspected by their own inspectors and controllers besides Ministry of Finance, independent auditors, Supreme Audit Board, chartered bank controllers. It is impossible not to detect the failures of system up to that time in spite of all those inspections.

Failures of financial system, deficits of each and every bank and inconsistencies with the established rules of procedure were all known. However they were not yet confronted sufficiently. In the root of that insufficiency there lays dealing with number of banks exceeding 80 each. All numerous banks are not in accordance with the realities of the country. Decrease in that quantity became possible with new arrangements upon the crisis. Personal rights, third person interest and unlawful interventions should be restrained.

Bank confiscating articles of Bank Law of 1994 were applied mistakenly and untimely. During the crisis 10 banks in difficult position were confiscatable. However three of them were confiscated prior to completion of procedures. When it is understood that the panic was inevitable deposit guarantee was announced and other banks were saved temporarily. If deposit guarantee would be announced earlier then no banks would be confiscated.

##### *b) November 2000 and February 2001 Crises*

Upon getting late in settling down the economy, an IMF standby program put into operation in December 1999 aiming to reduce the rate of inflation into one digit figure, to drop rate of interest into a reasonable level and to efficient use of resources in the economy.

Targets of the program in regard of rate of inflation were almost caught and improvements were observed in public financial balance in 2000. Some structural reforms were put into operation. IMF diagnosed the crises as a liquidity jam in Turkish banking sector shake the confidence of both foreigner and gradually national investors and led to serious liquidity crisis in November.

The crisis was triggered by first closing foreign credit channels and later closing credit channels of two big Turkish banks for one of the medium size Turkish banks (Demirbank) which undertook an active role in government securities market.

That bank had to liquidise some part of the government securities its portfolio in second hand market. This transaction raised interest rate and led foreign investors and other national banks to tend to sell the same and to close their positions in order to minimize their losses. Outflows were accelerated by concern of foreign investors for open positions of Turkish banks in foreign currency and their transactions in order to close them. Although the tension is dropped by provision of liquidity into the market by the Central Bank, continuing outflows increased the doubts on sustainability of the regime for the foreign exchange rates. Meanwhile, the Central Bank cut the liquidity provision to the market and the overnight interest rates jumped over 2000%.

The underlying fundamental factors beneath the April 1994 and February 2001 crises in Turkey are currency substitution, the banking system's tendency to open positions, rising conjuncture and political instability. These four factors marked high rise in peak times of both crises.

Crises were inevitable for Turkish economy as currency substitution was accelerated, tendency for open positions in banking system was increased, and demand was boosted

through rising conjuncture. Rapid demand rise and economic growth pumped by excessive optimism in a full financial liberation attained economy bring self instability and fragility. As everything is going well (except some macroeconomic indicators) in rising economic conjuncture, the risks unperceived by both private sector and public sector made the economy fragile against possible shocks (like rise in oil prices, increase in external interest rates, sensitive coalition structure).

Currency substitution accelerated by pessimist expectations triggered the crisis in Turkish economy that became instable by rising economic conjecture and tendency of open positions in banking system.

Especially duty losses of public banks estimated 20 billion dollar besides public deficits were in fact the massagers of the February 2001 crisis.

Although poor public fiscal discipline caused by populist policies during 1990-2001 was usual, high public deficit to GNP ratios (12% and 12.5% respectively for April 1994 and February 2001) were the signs for oncoming demand boom derived by rising conjuncture.

Other sign in regard of demand boom prior to April 1994 and February 2001 crises is rapid increase in the current account deficits based on overvalued domestic currency against dollar. Thus current account to foreign currency reserve ratios of both the Central Bank and the banking system were increased. On the other hand, the open accounts to GNP ratios were high in both crises.

Demand boom especially in public sector but in economy in general led banking system to borrow in foreign currency in short term and lend in domestic currency in long term as a result of high interest rate-and-fixed foreign currency rate policy. Banking system financed the budget deficits in a growing economy in one side and met the credit inquiries especially consumer credits in the other side. In other words, the banking system financed the aggregate demand by short term speculative capital movements (April 1994 and February 2001 crises should be discriminated in terms of increased budget finance. Budget deficits before April 1994 crisis was financed through the Central Bank resources but budget deficits before February 2001 crisis was financed through domestic borrowing and short term speculative capital movements provided by the banking system).

Ratios of open accounts (Open accounts in the banking system is estimated 17 billion dollars approximately ) and liquid liabilities to foreign currency reserves increased rapidly with the effect of excessive indebtedness because of tendency of open positions of the banking system. The indicators of international liquidity concern and fragility of the banking system especially liquid liabilities/foreign currency reserves ratio, foreign currency assets/foreign currency liabilities ratio, total credits/foreign currency reserves ratio all increased before crises. Therefore the possibility for self actuating crises is increased as argued by traditional theories through fragility of the banking system and risk of foreign exchange rate those are taken as indicators of financial crises. In other words, sensitivity of the banking system towards the speculative capital outflows has increased in both crises (Net capital

outflows is 19 billion dollars in 1993-1994 periods where it is 12.4 billion dollars in January-October 2000 and 13.6 billion dollars in November 2000-September 2001).

Foundation for financial crisis were prepared by excessive optimism in the banking system, insufficient inspection, increase in short term liquid liabilities (maturity mismatch), financial management in public sector, deformity in financial structure (duty losses of public banking, holding banking, inadequate capital stock) and deposit guarantee application. As a result, although converting short term foreign liabilities into long term credits in domestic currency could finance the rising economic conjuncture by the banking system but financial fragility through this way increased the risk of crisis.

Currency substitution was increased by public budget deficit, fragility of the banking system and especially by lack of households' confidence for policies in use in prior to April 1994 and February 2001 crises. Liquidity in the economy was increased by the repression of the interest rate and the attempt to change the structure of public debt by the government thus devaluation expectation in the market increased and led to boom the demand of foreign currency. Crisis of confidence was run by policies for repressing the interest rate in order to reasonably meet budget deficits thus the interest rate was increased. Serious doubts arose on using the foreign currency as an anchor depending on high inflation rate (contrary to expectations), over valuation of domestic currency, increase in current account deficit and failure in budget stability although there were improvements in interest rate, stock exchange and economic growth, all are basic macroeconomic variables in prior to February 2001 crisis. As a result, the over valuation of foreign exchange rate and the continuous increase of foreign exchange accounts of citizens made the sustainability of the program impossible and the crises rose from that process.

Other economic indicator before April 1994 and February 2001 crises in regard of demand boom is rapid increase in current account deficits because of over valuation of domestic currency against dollar. On the other hand, current account deficit to GNP ratios in both crises increased drastically.

#### *c) Effects of 2008 Global Crisis in Turkey*

Global crisis is triggered by the bankrupt of Lehman Brothers on 15 September 2008 (who had wealth of 691 billion dollars at the end of 2007) and the domino effect among financial institutions who lend to Lehman Brothers within international credit chain. Collapse of Lehman Brothers force the global investment banks to decrease their debt portfolios reached to high amounts and made up derivative products mostly. Banks were obliged to shrink their credits in order to meet their immediate losses and this situation became one of the basic reasons for credit jam jump to Europe and Turkey.

Decrease of interest rates (since it was not sustainable after a point) by FED and increased world trade volume and non increased inflation all because of China would not helped the case. World annual trade volume was 6 trillion dollars in period of 1994-1999 and a recession together with a correction is experienced in 1999-2000 and trade volume did not change

in that period. Another recession for the world annual trade volume became inevitable as it was raised to 14 trillion in period of 2001-2007.

Current deficit of Turkey stayed sustainable in spite of it was increased with inflows by direct and indirect investments. Current deficit was realized as 32.7 billion dollars in 2007, as 41.4 billion dollars in 2008. It is expected to be 51 billion dollars for 2009.

Current deficit of 2007, 32.7 billion dollars was met by 45 billion capital inflow (20 billion dollar part is permanent capital) so 13 billion dollar is excess. These inflows are due to privatization revenues happened to be only once. It is clear that current deficit should be met with one way or another. It does not seem be sustainable easily because of the reasons as follows:

- Privatization revenues will not be always so much more,
- Annual growth may not be high every year,
- Direct investment inflows may not be that high every year.

Turkey needs to find precautions necessary to meet its current account deficit because of reasons depicted above.

It should be noticed that the probability of a new crisis in the world is high, countries like Turkey with high current account deficits can be affected from that crises in greater extend, a new balance could be formed (USA and EU in one side and China, Russia, India and some other Asian countries on the other side) and Arab capital with increasing possibilities that ready to take part in that balance. It could be expected that disputes that may arise in economic context may lead to political disputes after a certain extend.

It was the Arabs who provided the fund for saving Citygroup that announced its largest loss by 18 billion dollars. Likewise, many giant China funds can be suitor for American companies. And now Americans are not pleased at all with that. Therefore, new processes seem to be more complex than of today.

#### *d) Role of political factors in crises*

There are political factors for crises to occur besides internal factors. It is almost impossible to foresee them and take necessary precautions. In a globalized world, crises are globalized as well. There occurred so called (in general features) financial crises in various places of the world in last ten years.

Some of the political factors as causes of crises are as follows:

- Excessive price increase of raw materials and meanwhile fluctuations in oil prices.
- Turkey's Cyprus concern based on embargo in terms of economic embargo formerly a military embargo due to Cyprus Peace Operation of Turkey. Its effect is continued till (first 1980s then) the present.
- The war as a consequence of invasion of Kuwait by Iraq so shutting down Iraqi border cost to Turkey around 50 billion dollars currency lost.

- Liberty concept is misunderstood and misapplied. Liberty is a limited concept even in the most liberal countries and is rule based. Application of "laissez faire laissez passer" is experienced in most destructive way.

- Liberal interest rate policy is carelessly applied even infrastructure for fiscal sector is not prepared.

- Unrealized fiscal reforms (although they are announced in government programs) led to negative expectations.

- Unreal statements in search of excuse because the expectation factor is not comprehended, led to mistrust in the society.

- Tool and purpose are mixed up and money policy is started to be seen as a tool.

- Start and stop the credits totally and lack of selective policy in application of credit policies adversely affected production.

- Public deficits could not be prevented. These deficits force the emission volume on one hand and increase the aggregate demand in an unwanted direction on the other hand.

- Necessary steps were not taken to generate sound resources necessary for economic growth. On contrary, the taken precautions for tax system led to loss of sources.

Self created crises in Turkey are turned into economic crises by combining them with external factors those repeat every ten years.

#### V. CONCLUSION AND RECOMMENDATIONS

Turkey faces today serious structural problems in economic, political and human resource context same as autocratic and totalitarian countries in Latin American and Asia do. It is difficult to say Turkey has the ability to overcome these problems in a short and medium term. If it could be so, a society struggling to change and transform since a century should have succeed it up to date. April 1994 and February 2001 crises in Turkey occurred because of currency substitution, open positions tendency in the banking system, the boom in demand through conjuncture, and most importantly, political instability. The 2008 crisis is a global originated crisis.

An unstable economic growth has emerged excessively depending on speculative capital movements as the boom in demand led by populist policies of 1990-2001 was combined with the open positions tendency in the banking system. The currency substitution was accelerated and the crisis was triggered as doubts of financiers of economic growth and households on sustainability of economic policies in use were combined with fragility of the banking system.

The reality reveals itself that factors (rising economic conjuncture, the fragile banking system and currency substitution) played role in occurrence of the crisis in April 1994 and February 2001 were raised up during an economic context with policies depended on fixed (or repressed) foreign currency although Turkish economy had structural macroeconomic problems all the 90s.

As a result, crises in Turkey occurs because of the fragile banking system that depends on short term speculative borrowing and the currency substitution that depends on lack

of confidence for economic policies in use in raising economic conjuncture likewise emphasized in empirical studies for other countries as well. This means Turkish economy that becomes unstable with rapid economic growth and fragile banking system, may tumble in crisis with even a small deterioration in expectations.

Some recommendations those may contribute to overcome crisis by enhancing economic potential yet in medium term are given below:

- The most important concern is foreign currency reserves could not meet foreign currency expenses. Sound commercial networks should be established among Turk and Arab counties.
- It does not seem possible to sustain and transform the economy with existing urban-rural population structure and agricultural status.
- Direct incentives should be provided for foreign exchange earning activities.
- Transfer of labour savings in foreign currency and tourism income are in vital importance for Turkey to overcome bottlenecks easily. Therefore, bringing the savings of Turks abroad to the country should be promoted, cared and monitored seriously.
- Economic development is finance with the banking system in Turkey as it is the case for European countries and Japan as well because economic organization is constituted accordingly. However banks in Turkey tend to be in the position of an entity that lives on income from securities as they finance state deficits with high interest rate.
- Road to tax base expansion passes through lowering tax rates. Therefore, tax rates should be reduced and tax system should be made transparent and simple at possible extend.
- It seems difficult to make domestic currency valuable especially when its scale is considered. Therefore it is required to anchor it to a foreign currency or a package like SDR or Euro to make its value more stable.

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