

Step Up U.S. Involvement in Turkish Economic Crisis

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Brief Analysis

Turkey's economic near-meltdown last week — its second financial crisis in three months — was precipitated by political problems, not by narrowly economic issues. Until the political problems are addressed, the prospects for any new economic package will be questionable. With Turkish leaders and the International Monetary Fund (IMF) both seemingly floundering, Turkey likely would welcome suggestions on how to proceed, and the United States would do well to send a special high-level representative to Ankara for several days, as a source of informal advice and as a powerful symbol of U.S. support.

On February 19, Prime Minister Bulent Ecevit stormed out of a Turkish National Security Council meeting, claiming President Ahmet Necdet Sezer had insulted him. Ecevit described the situation as a "serious crisis." With investors still rattled by the liquidity crisis of last November, many mistakenly foresaw in Ecevit's words the imminent collapse of the government and of the IMF stabilization program that went into effect in January 2000. Further anti-Sezer charges by Ecevit two days later produced a near-collapse of the economy. Unable to defend its currency, Turkey had no choice but to float the lira, which immediately lost 36 per cent of its value. The stock market lost close to one-fifth its value, and interest rates soared into four digits.

The situation has now calmed somewhat: the stock market has crept back a bit and interest rates are just barely above 100 percent. Turks and IMF officials are now discussing terms of a revised program with more modest inflation targets. But even without further shocks, Turks likely will have to deal with new inflation and budgetary problems. Blue-collar workers — a core Ecevit constituency, who had been asked to be patient with the IMF program — and others on fixed incomes face serious increases in cost of living. Among the foreign policy implications, Turkey's latest economic problems increase doubts about its ability to meet European Union (EU) membership economic criteria and about its ability to pay for all its numerous contracted energy projects, including its pledge to pay for cost overruns on a prospective Baku-Ceyhan line.

Political Problems Plaguing the Economy Embodied in the crisis, in addition to economic fragility, are several structural problems now plaguing Turkish politics and not easily amenable to a short-term fix:

Corruption In both the November 2000 and February 2001 economic crises, corruption was an important precipitant. Part of the insult Ecevit bore at Sezer's hands was a lecture by the president accusing Ecevit of laxity in his approach to corruption. Ironically, as with the crisis in November, problems arose because of officials' expressed

concern about corruption, thereby bringing attention to the problem and frightening off investors. However, corruption as an issue has been picking up steam in Turkish public opinion for much of the past decade. Concern about corruption helped propel pro-Islamist Necmettin Erbakan to electoral victory in 1995; it did the same four years later for Ecevit and the surprise runner-up Devlet Bahçeli (now Ecevit's coalition partner and deputy prime minister), both of whom scored points for personal honesty. The issue is not about to disappear from public, or investor, consciousness.

Government Stalemate Public confidence in the government has been badly shaken, but it seems quite likely the government will indeed hold on for some time due to lack of alternatives. For a variety of reasons, it would be difficult to form any other government with the current parliamentary arithmetic. New elections are a possibility, but neither Ecevit nor his other coalition partner Mesut Yılmaz, leader of the Motherland Party, are eager to face the electorate. Less clear are the preferences of Bahçeli, now seen in many quarters as the political front-runner; for now, he insists the government should continue. It is not clear if a parliamentary majority could be mustered for new elections even with Bahçeli's support, however, as the opposition parties probably have their own misgivings about a near-term electoral contest. Thus, with elections not required until 2004, the government likely will continue for several months, if not longer.

Ecevit-Sezer Dispute Ecevit's nomination of then-Constitutional Court Chief Justice Sezer as president last spring was considered a political ten-strike at the time, particularly following the failure of Ecevit's effort to win a new presidential term for Süleyman Demirel. Sezer has proved to be immensely popular — according to polls, even more popular than the military, long Turkey's most venerated institution — thanks to his humility and fealty to rule of law. However, he and Ecevit have clashed repeatedly and publicly. Given their styles, personalities, and principles, further Ecevit-Sezer tensions are likely, even though both were probably stunned by the far-reaching economic effect of their latest spat. Moreover, public displays of tensions among leaders and institutions increasingly are becoming the norm in Turkey, as EU membership prospects force high-stakes decisions about Turkey's future political and economic structure.

Finding a Way Forward The economic crisis has left Turks, including officials, bewildered. Although Turkey had not fulfilled the IMF program perfectly — Ankara was lagging behind in its privatization timetable, for example — it was generally considered to have performed well. In January, the IMF official in charge of the program publicly praised the Ecevit government's record of compliance. The fact that a major part of the program collapsed over politics not directly related to economic policy will leave Turks, and foreign investors, questioning the IMF's understanding of Turkey and skeptical of any future IMF plan.

Turkey's emergence as a regional power in recent years has been possible thanks mainly to a perky economy that has seen sustained growth, with occasional interruptions, over the past two decades. During those twenty years, Turkey more than tripled its per capita income (from approximately \$1,000 to approximately \$3,300), surpassing neighbors it previously trailed, such as Syria, Iraq, Iran, and Russia. Turkey's uneven but overall highly successful economic performance, despite inflation that rarely dipped below 70 percent, defied conventional economic wisdom. Were the country to face long-term collapse, a less-confident Turkey might no longer be a forward-leaning supporter of U.S. interests in its mainly hostile region.

The Bush administration's professed preference for a non-interventionist approach in overseas economic crises may lead it to sit this one out. But with few of its officials experienced in international finance, the administration needs to demonstrate that it can contain financial crises so that they do not spread from one emerging market to others. The Argentine currency came under heavy pressure because investors were nervous Turkey's problems could spread to other emerging markets.

The United States has a key role to play, particularly in light of loss of confidence in the IMF. The near-euphoric

response of many Turks to President Bush's phone call of support to Ecevit last week — Treasury Secretary Paul O'Neill's supportive statement was also well received — was powerful testimony to the hopes Turkey now places in Washington. To boost Turkey's sagging spirits, and perhaps those of investors as well, Washington should designate a special representative to Ankara to advise Turkey on economic policy in the crucial days ahead. Whether such a representative is from inside or outside government, it is important that he be well connected in the international financial community.

The Personal Touch Turks would react well to such special attention from the United States, as they often do. In that respect, Secretary of State Colin Powell missed an opportunity to influence Turkey's wavering policy toward Iraqi sanctions by choosing to meet Turkish foreign minister Ismail Cem on the margins of the NATO meeting in Brussels rather than visiting him and other Turkish leaders in Ankara.

Turks bear primary responsibility for their economic woes and for finding the best remedies. Given Turkey's strategic importance and diminished confidence in the IMF, Washington needs to weigh in visibly and directly, rather than confine its involvement to phone calls and long-distance encouragement.

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