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Abstract: Turkish economic growth depends on capital inflows and access to cheap credit sources. Once the global financial conditions tightened in 2018, Turkey was among the emerging markets that suffered the most. This article analyses the making of Turkey's economic crisis in 2018-2019, while elaborating the phases of Turkish financialisation. It locates the slow-motion drift of Turkish economy within the context of dependent financialisation and argues that a long-term account is needed to grasp the economic turmoil of recent years.

JEL code: E44, E52, E6, F31, G01,

Keywords: Turkey, Dependent Financialisation, Economic Crises, Crisis Management

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Introduction

The global financial tightening in 2018 hurt emerging markets and Turkey was among the most notable victims, as it suffered from a currency crisis followed by a recession. The Turkish Lira (TL) lost 31 per cent of its value against the US Dollar (USD) in 2018, depreciating much further in the first eight months and then appreciating after the sharp interest rate hike that September. Since then, a bankruptcy wave has drowned hundreds of firms while the official unemployment rate has reached record levels, unseen since the 2008 collapse. The debt restructuring framework of the banking sector, revised in October 2018, helped banks restructure loans worth 20 billion USD in the following months and new securitization campaigns followed suit.[1] However, the efforts of policymakers to contain the spillover effects were not enough to revitalize the credit market as of early March 2019. According to the latest available data, the Turkish economy slipped into recession in the second half of 2018, although the average annual growth rate was still positive at 2.6 per cent.[2] The Turkish economy is expected to grow only slightly in 2019 if a recovery occurs in the second half of the year. Thus, we suggest that it would be appropriate to call Turkey's current turmoil as the 2018-2019 economic crisis.

It seems to be a textbook example of an economic crisis in an emerging market in the late 2010s. Yet again, the policy response of economic managers relies on a fundamentally market-oriented perspective, in which monetary policy is prioritized in crisis management while securitization is portrayed as the remedy for the credit crunch. We argue that Turkey's current crisis should be located within the context of dependent financialization. The development and management of the 2018-2019 crisis reveal that once a peripheral country is locked into dependent financialization, it becomes much harder to escape from those mechanisms that themselves provoke economic crises.

The major contribution of this paper is providing a critically informed analysis of Turkey's 2018-2019 economic crisis by contextualizing the currency crisis of August 2018 as part of dependent financialization. To support our argument, we first explain the concept of dependent financialization following the heterodox literature on the financialization experiences of Emerging Capitalist Countries (ECCs). Second, we review financialization in Turkey in four phases to explain the key dynamics of each. Third, we focus on the crisis tendencies of dependent financialization, which have intensified in the post-2013 period. Finally, we analyze the policy responses of Recep Tayyip Erdoğan's administration and the Central Bank (CBRT) to the currency crisis. Drawing on a qualitative and case-based enquiry, we rely on both first-hand statements and secondary writings on Turkish political economy, and the official data at hand. To substantiate our argument and delineate changes between different phases and periods, we present the data in time series and tables.

[1] Banks Association of Turkey chair Hüseyin Aydın's statement in Dünya Gazetesi, 'TBB Başkanı Aydın: Yapılandırılan Kredi 118 milyar lira', https://goo.gl/JHrULi, 10 January 2019 (accessed on 15 February 2019).

[2] Turkish Statistical Institute, 'Quarterly Gross Domestic Product, Quarter IV: October-December, 2018', http://www.turkstat.gov.tr/PreHaberBultenleri.do?id=30886 (accessed on 13 March 2019)

Dependent financialization and its limits

Financialization is an uneven and combined process in the sense that the global financial flows affect credit expansion and financial deepening in emerging capitalist countries (ECCs), while the forms it takes in the global South are mediated by various factors, such as the balance of class forces in a particular country or the fragilities of particular economies stemming from accumulated vulnerabilities. There is no single universal indicator of financialization. Relying on stylized measures, such as stock capitalization/Gross Domestic Product (GDP) ratios or the financial income of non-financial corporations, may lead to viewing it as something peculiar to advanced capitalist countries.[3] The unprecedented levels of transformation in peripheral countries in the last three decades remain under-analyzed from such a perspective.[4] Since, however, financialization depends on capital inflows to ECCs, it also has limits. Global financialization itself is an open process and despite its penetrating force, is a crisis-ridden transformation with discontinuities that should not be 'regarded as a temporary blip that will be ironed out as the logic and power of finance is furthered'.[5] Peripheral or dependent financialization, however, has extra limits due to its dependence on policy responses and ensuing USD glut or capital flows from advanced capitalist countries (ACCs).

Drawing on Marxist, Post-Keynesian or Regulationist approaches, the heterodox literature on financialization in the global South tends to use 'subordinated financialization'[6] or 'peripheral' or 'semi-peripheral financialization'[7] concepts to analyze both the peculiarities and common properties of various financialization experiences in ECCs. In line with the burgeoning literature, and following Becker,[8] we suggest that *dependent financialization* is more suitable for ECCs, especially for those with high rates of dollarization (or euroization) and large current account deficits, whose domestic production is highly dependent on imported goods, and where economic growth mostly relies on capital inflows.

On a theoretical level, dependent financialization can be derived from the dependency school and the regulation approaches. Becker and Weissenbacher suggest that 'the two approaches

[3] See E. Stockhammer, 'Financialisation and the slowdown of accumulation', *Cambridge Journal of Economics*, 28 (5), pp. 719-741.

[4] For a detailed review of literature on financialisation in ECCs, see B. Bonizzi, 'Financialization in developing and emerging countries', *International Journal of Political Economy*, 42(4), 2013–14, pp. 83–107.

[5] P. Langley, 'Uncertain subjects of Anglo-American financialization' '*Cultural Critique*', 65, 2007, pp. 67-91, p. 86.

[6] C. Lapavitsas, 'The financialization of capitalism: 'Profiting without producing'', *City*, 17(6), 2013, pp. 792-805; J. Powell, *Subordinate Financialisation: A Study of Mexico and its Non-Financial Corporations*. PhD dissertation, SOAS, University of London, 2013; P. G. Bortz and A. Kaltenbrunner, 'The international dimension of financialization in developing and emerging economies', *Development and Change* 49(2), 2017, pp. 375–393; A. Kaltenbrunner and, J. P. Painceira, 'Subordinated financial integration and financialisation in emerging capitalist economies: The Brazilian experience', *New Political Economy*, 23(3), 2018, pp. 290-313.

[7] J. Rodrigues, et al., 'Semi-peripheral financialisation: the case of Portugal', *Review of International Political Economy*, 23, 2016, pp. 480–510; J. Becker et. al., 'Peripheral financialization and vulnerability to crisis: a regulationist perspective', *Competition & Change*, 14, 2010, pp. 225–247; A. C. Santos, et al., 'Semi-peripheral financialisation and social reproduction: the case of Portugal', *New Political Economy*, 23(4), 2018, pp. 475-494.

[8] J. Becker, 'Financialisation, industry and dependency in Turkey' *Journal Für Entwicklungspolitik*, XXXII 1/2, 2016, pp. 84 –113.

share some key features: Both of them emerged at least partially out of Marxist debates, both operate with an intermediate level of abstraction and both are explicitly historical and geographical'.[9] Dependent financialization also refers to the hierarchical character of the global economic and financial system. In abstract terms, it refers to the dependency of financialization's unfolding and financial deepening on capital inflows. In many ECCs, financialization shapes capital accumulation and dominates political economic transformation through these flows.[10]

Regarding the dependency school, we do not argue that all premises of the 1960s' dependency school has been validated, so we do not intend to apply the original framework to current financialization. Rather, we claim that the concept is useful for explaining the hierarchical character of the international financial system in which financialization takes place. There are two implications of this hierarchical system. First, ECCs structurally have higher interest rates than ACCs. The primary effect of this is a tendency for ECC currencies to appreciate, leading to what is sometimes referred to as the 'financial Dutch disease'.[11] Two consequences of structurally higher interest rates are premature deindustrialization[12] followed by increasing dependency on imports. Second, many corporations in ECCs have to take USD or Euro-denominated loans due to the hierarchical character of the international monetary system because the convertibility of ECC currencies in international markets is more limited than that of hegemonic currencies.[13] In short, corporations in ECCs face both more expensive borrowing and being forced to do so in other nations' currencies. This dependent structure makes ECCs more crisis prone and vulnerable to the monetary policy decisions of ACC central banks. Regarding the forms of financialization, structurally higher interest rates do not necessarily hinder financialization itself in ECCs but can determine its forms. For instance, higher interest rates were the main driver of state-centred financialization in Turkey during the 1990s in the early phases of financialization, when the management of the public debt was the key for financial stability.[14] Lower interest rates, however, have been the main driver for more inclusive financialization, where private debt – including household debt and

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[9] J. Becker and R. Weissenbacher, 'Changing development models: dependency school meets regulation theory', *Coloque International Recherche & Regulation*, 2015, Paris. URL: https://www.eiseverywhere.com/retrieveupload.php?c3VibWlzc2lvbl84NTg3OF83NTYyMzIucGRmKmVzZWxlY3Q=, (accessed on 20 October 2018), p. 2.
[10] Becker, 'Financialisation, industry and dependency in Turkey', op. cit.
[11] P. G. Bortz and A. Kaltenbrunner, 'The international dimension of financialization in developing and emerging economies', *Development and Change*, 49(2), 2017, pp. 375–393.
[12] D. Rodrik, 'Premature deindustrialization', *NBER Working Paper No. 20935*, 2016, https://www.nber.org/papers/w20935 (accessed on 5 January 2019).
[13] R. P. Andrade and D. N. Prates, 'Exchange rate dynamics in a peripheral monetary economy', *Journal of Post-Keynesian Economics*, 35(3), 2013, pp. 399-416
[14] G. Yalman, T. Marois and A. R. Güngen (eds.) *The Political Economy of Financial Transformation in Turkey*, Routledge: London, 2019; A. R. Güngen, 'Hazine Müsteşarlığı ve Borç Yönetimi: Finansallaşma Sürecinde bir Kurumun Dönüşümü', *Amme İdaresi Dergisi*, 47(1), 2014, pp. 1-21.

new forms of fictitious capital – has become more prominent in the lending preferences of the domestic financial system.[15]

As for the regulation school, we argue that a more innovative approach is required to adapt its merits to the concept of dependent financialization. The current state of the art in this school also encourages us to explore new dimensions because attempts to explain the current phase of capital accumulation in both ACCs and ECCs need to be improved, i.e. go beyond the framework revolving around discussing 'post-Fordist accumulation regimes'. One of the key merits of the regulation school is its holistic approach, enabling the analysis of economic and financial dynamics in relation to social classes, vertical and horizontal class struggles, and their reflections on the political, labor and capital accumulation regimes.[16] Although we do not analyse the political regime and labour policies in Turkey here, we believe that elaborating the connections between the monetary and the labour regimes as components of the 'mode of regulation' in dependent financialization could enrich comprehensive analyses.

In this study, we will not only elaborate the characteristics of Turkish financialization but also point out the limits of dependent financialization. Indeed, one may ask how financial deepening can even be possible for ECCs if higher interest rates are structural components of dependent financialization. The answer relates to changes in the international economic conjuncture and the forms of financial transformation. Structurally higher interest rates are the main driver of the underdevelopment of financialization in ECCs. Nevertheless, the implementation of neoliberal economic policies, which have resulted in constant austerity since the crisis of the 1970s in ACCs, has brought about a lower inflation conjuncture. The reduction of borrowing costs in international markets in tandem with domestic monetary reforms and implementation of disinflationary programmes in ECCs in the 1990s and early 2000s created an opportunity for these countries to join inclusive financialization processes. Furthermore, especially after the Great Recession, when interest rates were negative in most ACCs, we witnessed a new financialization wave in ECCs, which were able to both reduce interest rates and avoid a devaluation of the national currency thanks to the ACCs' quantitative easing programs. Therefore, the ACC central banks' interest rate decisions and the hierarchical nature of the international monetary system, which can be seen as a mirror image of state hierarchies in the international system, are the ultimate limitations to dependent financialization.

Before extending the discussion to Turkey's financial transformation and the 2018-2019 economic crisis, we would like to further clarify the criteria used by Becker[17] to delineate peripheral characteristics of financialization. Having shown that financialization is not a linear process in peripheral countries, Becker[18] mainly emphasized the role of interest-bearing

[15] E. Karacimen, 'Interlinkages between credit, debt and the labour market: evidence from Turkey', *Cambridge Journal of Economics*, 39(3), 2014, pp. 751-767

[16] R. Boyer 'Marx's legacy, régulation theory and contemporary capitalism', *Review of Political Economy*, 20(3), 2018, pp. 284-316.

[17] Becker, 'Peripheral financialization'.

[18] Ibid.

capital (i.e. credit money) in the initial phases of financialization. Accumulation of fictitious capital, in that context, was shown to be the outcome of further regulations and reforms, such as privatizing pension systems. Rather than employing rigid categories for classification, we would like to underline how fictitious capital accumulation is always intertwined with the circulation of credit money. That is, periodization of peripheral financialization should not rest on clear-cut distinctions between private credit money and fictitious capital, identifying one period solely with the dominance of one form of capital or an accumulation strategy focusing on one form. Rather, a subtler analysis should be able to identify continuities and complexities in peripheral financial transactions, such as the interconnections between state fictitious capital, credit expansion, new forms of fictitious capital and financial deepening in various forms.[19] We will focus on the ramifications of financialization in this sense and integrate our clarification into the analysis of financial transformation and Turkey's latest currency crisis of 2018.

Financial transformation in brief and phases of financialization in Turkey

Capital inflows, and their pace and reversals have dramatically affected the mechanisms of economic growth and recession in Turkey. This has been the primary feature of dependent financialization and the outcome of three decades of financial liberalization and deepening. Despite the shallow nature of Turkish financial markets compared with those of ACCs, financial flows and standards have influenced policymaking processes. We argue therefore that dependent financialization, as a result of Turkey's economic structure, has characterized the country's capital accumulation.

Dependent financialization developed in four distinct phases in Turkey. The first phase between 1989 and 2001 was characterized by liberalization of capital movements, which is an integral part of the generic neoliberal project.[20] During this period, however, high public debt became one of the most pressing economic issues. As in many peripheral countries, Turkey's financialization was shaped by the accumulation of fictitious capital issued by the state, with the banking system mediating between international financial markets and the Turkish Treasury, thereby benefiting from interest rate arbitrage between international and domestic markets.[21] The issue of rolling over public debt in the 1990s not only provided gargantuan revenues for Turkish capital groups but also made the Turkish economy more crisis-prone.[22] The policy responses to these crises, and particularly post-2001 restructuring, led to a change

[19] By state fictitious capital, we refer to government debt instruments traded in the secondary markets. By new forms of fictitious capital, we refer to various derivatives that proliferated in the post-Bretton Woods era. For a similar use, see T. Marois, 'Historical Precedents, Contemporary Manifestations: Crisis and the Socialization of Financial Risk in Mexico', *Review of Radical Political Economics*, 46(3), 2014, pp. 308-330.
[20] Y. Akyüz, 'Internationalization of finance and changing vulnerabilities in emerging and developing countries', *South Center, Geneva,* Research Paper No: 60, 2014.
[21] Ü. Akçay, *Para, Banka, Devlet: Merkez Bankası Bağımsızlaşmasının Ekonomi Politiği*, [Money, Bank, State: The Political Economy of the Independence of Central Bank]. İstanbul, SAV Press, 2009.
[22] E. Voyvoda and E. Yeldan, 'Managing Turkish debt: an OLG investigation of the IMF's fiscal programming model for Turkey', *Journal of Policy Modeling*, 27(6), 2005, pp. 743–765.

in the form of financialization. The predominance of state fictitious capital in the financial markets did not end abruptly in the post-2001 years. On the contrary, declining interest rates between 2002 and 2005 enabled bondholders to benefit from holding such capital. Given the primary surpluses of the state and a declining public sector borrowing requirement, the new focal point became the consumer credit market. In short, high interest rates, high-inflation and volatile capital flows characterized the first phase, during which banks accumulated extraordinary revenues through speculation on state fictitious capital.

The second phase, which began after the 2001 crisis, was characterized by the growth of household indebtedness, a new phenomenon in Turkey, even though the ratio of household debt to disposable income was still lower than in most ACCs.[23] The key developments of the post-2001 crisis period were the establishment of an inflation targeting system and the CBRT's gaining independent status from the government[24] while cutting direct borrowing lines between the CBRT and the Treasury was another crucial policy innovation in the second phase. Finally, restructuring the banking sector and establishing new regulatory institutions were complementary components of the post-2001 policy framework, which was installed under the auspices of an IMF stand-by program.[25] These reforms coincided with a very positive international economic conjuncture of declining borrowing costs. In addition to the IMF program, the new financial reforms were anchored by Turkey's official European Union candidacy status. Consequently, capital inflows skyrocketed during this period, which was mainly characterized by increasing household and nonfinancial corporate debt followed by baby steps to deepen financial markets and enable the issuance of new forms of fictitious capital[26] (see Figure 1).

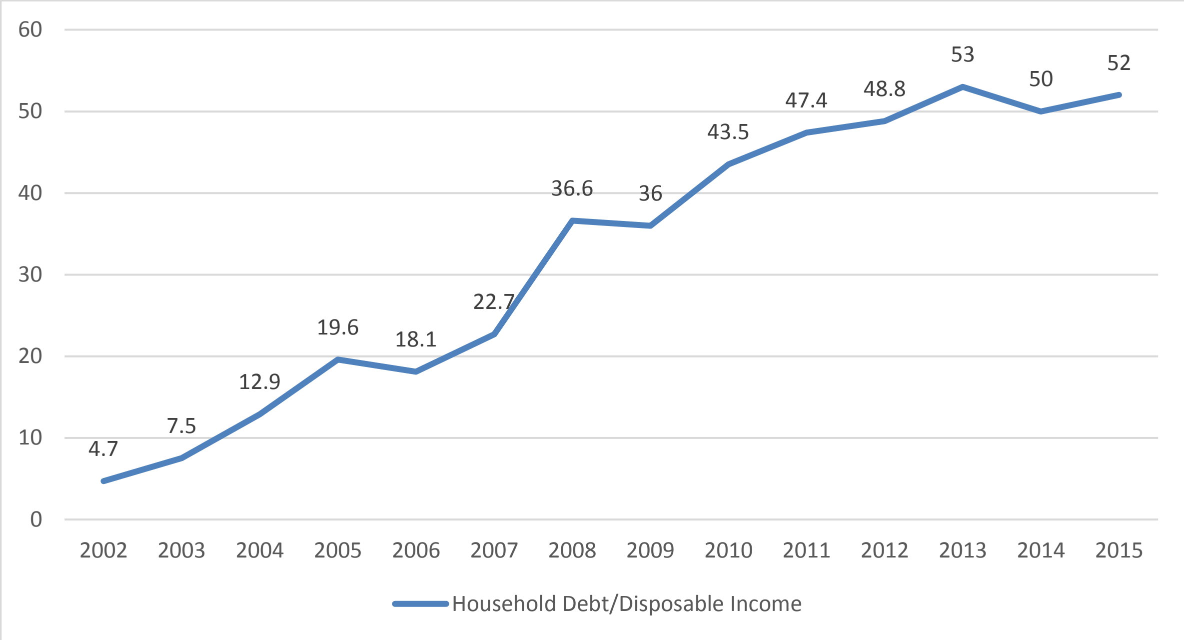
[23] E. Karaçimen, 'Financialization in Turkey: the case of consumer debt' *Journal of Balkan and Near Eastern Studies* 16(2), 2014, pp. 161-180; A. R. Güngen, 'Financial Inclusion and Policy-Making: Strategy, Campaigns and Microcredit a la Turca', *New Political Economy*, 28(3), 2018, pp. 331-347.

[24] N. Ergüneş, 'Transformation of the Turkish banking sector within the financialisation process of Turkish economy', *IIPPE Financialisation Working Paper No. 4,* 2010, http://www.iippe.org/wiki/images/8/8c/Transformation_of_the_Turkish_Banking_Sector.pdf (accessed on 18 January 2019).

[25] IMF, *Turkey Letter of Intent and Memorandum on Economic Policies*, 3 May 2001, https://www.imf.org/external/np/loi/2001/tur/02/#mep (accessed on 12 January 2019).

[26] Ü. Akçay, 'Die Krise der türkischen Wirtschaft und die Grenzen abhängiger Finanzialisierung', *PROKLA*, 48(4), 2018, pp. 617 – 639.

Figure 1. Increasing household indebtedness ratio in Turkey (2002-2015).



Source: Compiled by authors from CBRT Financial Stability Reports (various years)

The diminishing public sector borrowing requirement following the 2001 restructuring pushed Turkish banks to pursue new outlets for profitable lending. Domestic mergers and acquisitions that produced sectoral consolidation and the internalization of foreign finance capital gave way to changes in bank assets control and diversification of financial products attracting households.[27] Explicit state support for the development of the corporate bond market and increasing stock market trading volumes were notable features of this phase. Although Turkey's neoliberal governments have supported deepening of financial markets since the 1980s, more decisive steps were only taken following the 2001 crisis and the subsequent banking sector restructuring.[28]

While real interest rates remained high during the second phase, they were declining thanks to favorable international economic conditions. This enabled successive Justice and Development Party (AKP) governments to implement a neoliberal populist governance strategy, which consisted of an orthodox neoliberal recipe with two compensation mechanisms: (i) social inclusion by increasing social spending compared to previous decades and (ii) financial inclusion thanks to falling interest rates.[29] However, relatively high - albeit

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[27] T. Marois and A. R. Güngen, 'The Neoliberal Restuercuting of Banking in Turkey Since 2001' in G. Yalman, T. Marois and A. R. Güngen (eds.), *The Political Economy of Financial Transformation in Turkey*, London: Routledge, 2019, pp. 135-162

[28] A.R. Güngen, 'The neoliberal emergence of market finance in Turkey', in G. Yalman, T. Marois and A. R. Güngen et al. (eds.), *The Political Economy of Financial Transformation in Turkey*, London: Routledge, 2019, pp. 162-184.

[29] Ü. Akçay, 'Neoliberal populism in Turkey and its crisis' *Institute for International Political Economy Berlin, Working Paper, No 100*, 2018, http://www.ipe-berlin.org/fileadmin/downloads/working_paper/IPE_WP_100.pdf (accessed on 18 January 2019).

declining - interest rates coupled with huge capital inflows resulted in an appreciation of the TL. The overvalued currency was also crucial for taming inflation since Turkey's production structure is mainly dependent on the imports. However, an overvalued TL also dramatically increased the current account deficit as well, which became a structural component of dependent financialization during this phase.

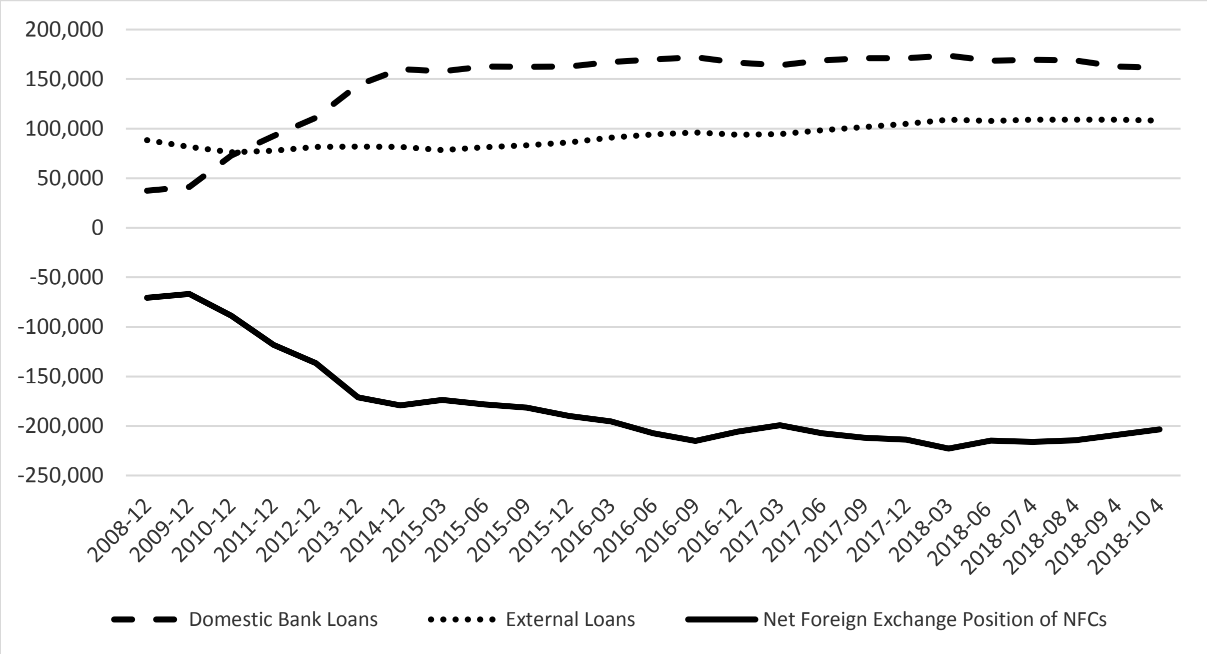
The third phase, which began after the 2008 global financial crisis, lasted until 2013. Throughout the post-2001 years, policymakers and neoliberal gurus had voiced concerns about creating alternative financing mechanisms for corporations. Since resolving the public debt rollover in the post-2001 period did not satisfy 'crowding out thesis' proponents by providing cheap and accessible resources to capital groups, securitization and development of the corporate bond market became a hot topic in 2006-2007. Given this background, reinforcing securitization and strengthening market (non-bank) finance characterized the post-2008 medium-term government responses to Turkey's 2008-2009 crisis. Reinforcing market finance in Turkey was a spillover from intensified international financial integration, confirmed by official state agendas, such as the 2009 Istanbul International Finance Centre strategy[30] and capital market regulations that adopted EU standards, reaching their peak in the new capital market law of 2012.[31] These renewed attempts were also responses to the fact that economic internationalization had not yet radically changed the financial architecture in Turkey. Thousands of Turkish firms, had to resort to bank finance as in previous decades. In June 2009, amidst a year-long collapse of the Turkish economy (4Q of 2008 to 4Q of 2009), the Council of Ministers made it easier for corporations without foreign exchange revenues to borrow in foreign currencies.[32] Hence, during the height of the global financial crisis, policy makers decided to liberalize regulations on borrowing in foreign exchange-denominated loans, especially for non-financial corporations in Turkey. This move had two results: (i) a sharp increase in foreign exchange-denominated debt levels of private non-financial companies and (ii) further mutation of the role of the banking system.

Policymakers' main motivation for this liberalization was to benefit from positive international financial conditions and provide a breathing space to non-financial corporations. As a direct result of the policy responses to the Great Recession in the ACCs, it was becoming easier to obtain cheap USD loans. Figure 2 shows the banking system's new intermediary role, which was an effect of liberalizing borrowing schemes for non-financial companies in Turkey. Following this step, non-financial corporate debt increased from 66 billion USD to 177 billion USD between 2009 and 2013. Furthermore, non-financial corporations, some of which lacked the capacity to borrow in international financial markets, borrowed more and more USD-denominated loans from Turkish banks. This became significant particularly in the latest economic turbulence in 2018, when the banking system as a whole became extremely

[30] Devlet Planlama Teşkilatı, İstanbul Uluslararası Finans Merkezi Stratejisi Eylem Planı, 2009, DPT: Ankara.
[31] Güngen, 'The neoliberal emergence of market finance in Turkey'.
[32] TC Başbakanlık, 'Türk parası kıymetini koruma hakkinda 32 sayılı kararda değişiklik yapılmasına dair karar', *Resmi Gazete*, 16 April 2009, http://www.resmigazete.gov.tr/eskiler/2009/06/20090616-1.htm (accessed on 15 January 2019).

vulnerable to currency shocks, precisely because it had facilitated the borrowing schemes of non-financial companies and was exposed more than ever to a sudden depreciation of TL.

Figure 2. Changing roles of domestic banks in Turkey (2008-2018)

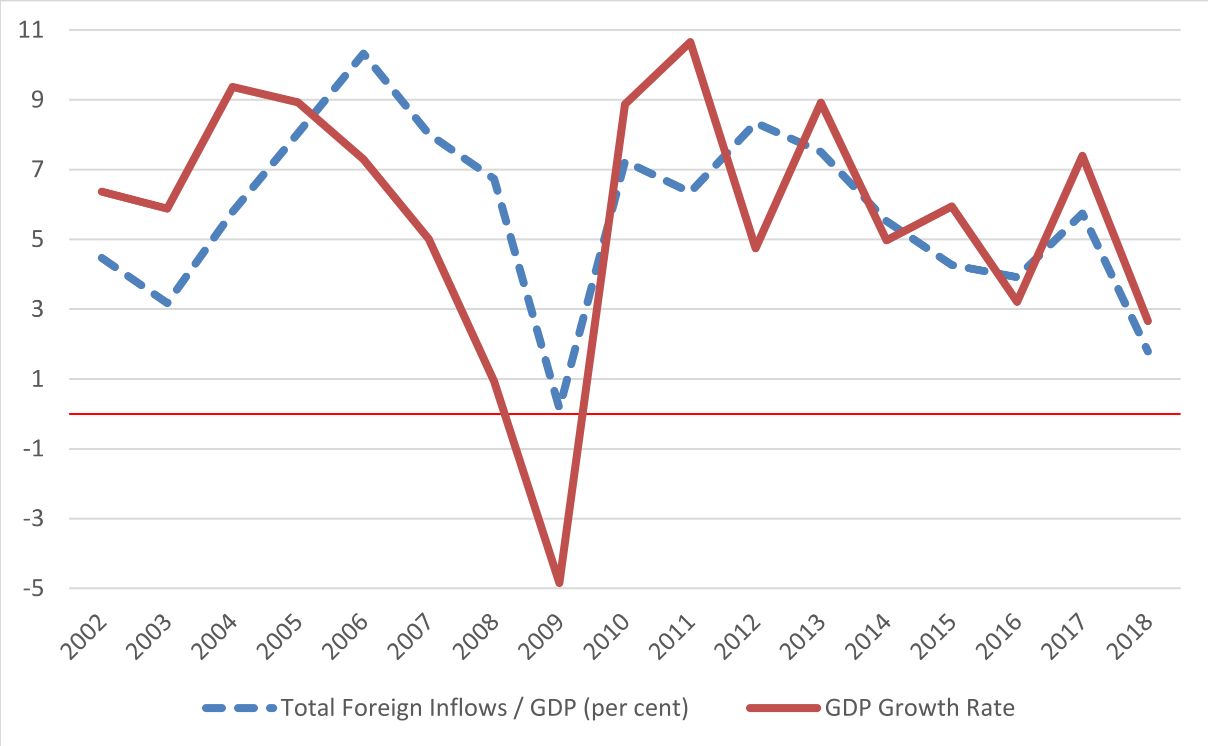


Source: Prepared by the authors based on CBRT database, https://evds2.tcmb.gov.tr/ (10.01.2019)

The striking parallelism between net capital inflows and GDP growth in Turkey in the aftermath of capital account liberalization persisted in the third and fourth phases (elaborated below). As Figure 3 shows, the 2008–2009 financial crisis generated rapid outflows from Turkey.[33] Soon after the ACC central banks created massive amounts of money via quantitative easing from 2009 onwards, these capital flows reversed to boost the Turkish economy. Turkish policymakers did not take measures to prevent a sharp increase in the non-financial sector's foreign exchange debt. Despite attempts by the CBRT and Banking Regulation and Supervision Agency (BRSA) to prevent rapid credit expansion and an explosion in household debt in 2010-11, there was no significant policy change. On the contrary, as capital market regulations and state-level strategies to deepen the market based finance imply, the AKP cadres hoped for a qualitative break in the near future, with significant increases in private sector debt securities, deepened Islamic bond markets and new financial instruments.[34]

[33] For the framework we use in calculating net foreign flows, see Boratav, K. (2006) 'Yabancı Sermaye Girişlerinin Ayrıştırılması ve Sıcak Para: Tanımlar, Yöntemler, Bazı Bulgular', A. H. Köse, F. Şenses and E. Yeldan (eds.) *İktisadi Kalkınma, Kriz ve Olasılıklar: Oktar Türel'e Armağan*, İstanbul: İletişim, pp. 17-31.
[34] Güngen, 'The neoliberal emergence of market finance in Turkey'.

Figure 3. Foreign inflows and economic growth in Turkey (2003-2018)



Source: Prepared by the authors based on CBRT data and Turkstat

The fourth phase of dependent financialization covers the post-2013 period, when the slow-motion drift began. The 2018 currency crisis and ensuing recession are the latest parts of this drift. Household indebtedness peaked in 2013 before declining due to increasing interest rates resulting from adverse international financial conditions after the Fed's tapering announcement. That is, the dependent nature of ECC financialization became apparent through the channel of higher borrowing costs when ACC interest rates were increasing. Despite the increasing indebtedness of the corporate sector, crisis tendencies were evident in 2015, pushing large conglomerates to keep their short-term foreign exchange liabilities below their short-term assets. The long-term liabilities of non-financial corporations exceeded their assets by 190 billion USD in late 2015 and continued increasing until the abortive coup attempt of 2016.[35] Thus, Turkey's interest rate hikes were not due to the 30 per cent nominal increase in the 2016 minimum wage but to the dire financing needs of the private sector and the increased risks. Since the industrial structure is highly dependent on the imported inputs, depreciation of the TL pushed inflation higher on the one hand while not providing competitive advantages to the extent desired by large conglomerates on the other. Post-2016 Turkey therefore became more vulnerable to capital flows. The share of portfolio flows in the financing of the current account deficit increased further after the 2016 coup attempt, to reach 51 per cent in 2017. The TL was losing ground faster than other emerging market

[35] CBRT publishes monthly statistics regarding the liabilities of non-financial corporations. The total liabilities of NFCs only started to decline after the 2018 currency shock.

currencies in 2017 while both inflation and interest rates were much higher than in other middle-income countries.

This summary shows that financialization in Turkey has reflected the country's mode of integration with global capital accumulation processes. We claim that, to understand Turkey's current economic turmoil, which has developed in three phases over the last five years, it is particularly valuable to refer to the dependency of both Turkish economic activity and the expansion of financial markets to capital inflows. In other words, the fourth phase of the dependent financialization had three distinct episodes during which crisis tendencies intensified. The main characteristic of the last six years has been adverse international financial conditions for the ECCs, which put an additional depreciation pressure on TL and exposed the inner contradictions of dependent financialization.

Slow-motion crisis of dependent financialization in Turkey

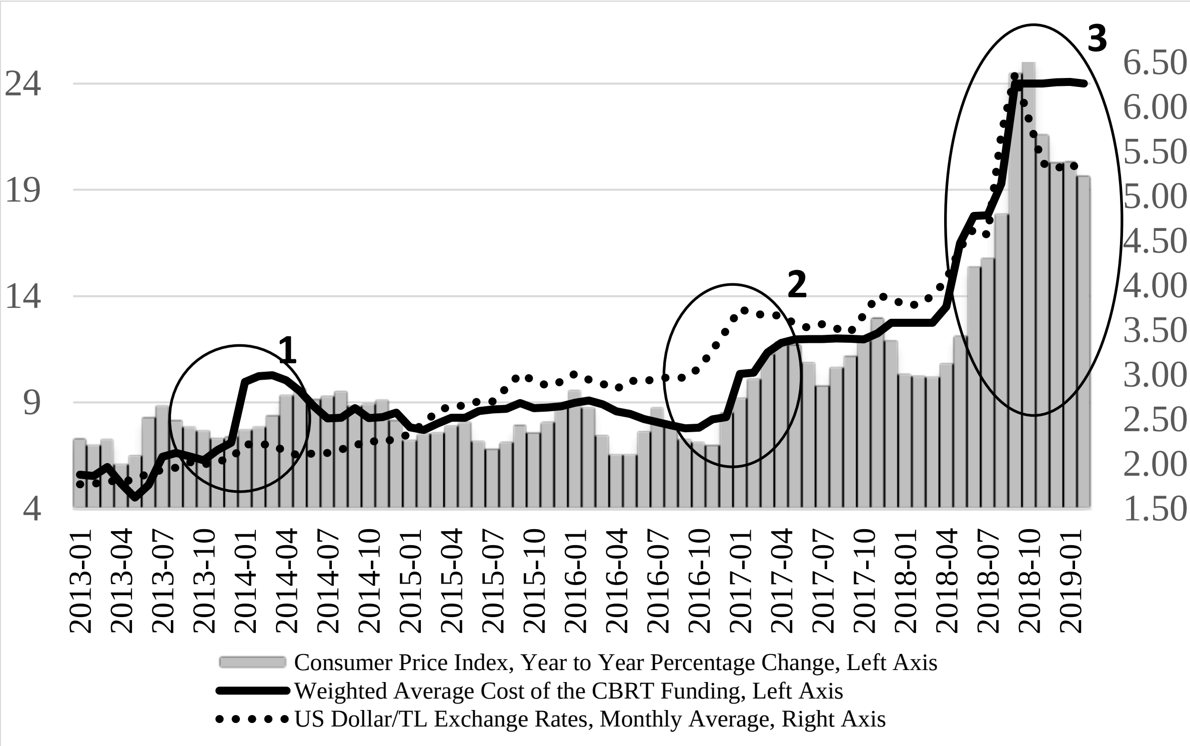
The final phase of dependent financialization is marked by three episodes of intensifying crisis tendencies. Policymakers successfully postponed the first two, but not the final one. AKP governments developed this strategy of postponing crises in response to intensified political pressure, which manifested itself in the five elections (one local, three parliamentary and one presidential) and the referendum held between 2013 and 2018. Even though the AKP and Erdoğan gained majorities in all these elections, the contradictions of dependent financialization have become increasingly harder to contain on each subsequent occasion. Before going into the details, it is worth reminding ourselves of the main contradiction in the Turkish economy, though similar to other cases of dependent financialization, amidst a depreciation of the nation's currency. On the one hand, policymakers have sought to sustain a lower interest rate policy even though international financial conditions, which had previously made lower rates possible, were changing. On the other hand, insisting on a lower interest rate policy for the sake of strong economic growth triggered currency shocks. Furthermore, these currency shocks boomeranged and raised inflation, which put pressure on policymakers to increase interest rates further. This contradiction also caused a dilemma for them between lower interest rates and currency shocks, which characterized crisis management in Turkey during the post-2013 period. Thus, over the last five years, the lower interest rates are, the greater has been the risk of a currency crisis.

The first episode of intensifying crisis tendencies happened between 2013 and 2014. Policymakers avoided increasing interest rates until 27 January 2014, although there were negative developments in both international financial conditions and Turkey's political stability. The Fed's tapering announcement was the key international change in 2013[36] while the Gezi Park events and the collapse of the informal ruling coalition between AKP and the

[36] B. Bernanke, 'The economic outlook', *Board of Governors of the Federal Reserve System*, 2013, https://www.federalreserve.gov/newsevents/testimony/bernanke20130522a.htm (accessed on 15 January 2019)

Gülen organization[37] were two aspects of the political crisis inside Turkey. Ultimately, the CBRT increased the policy rate by more than 4 per cent to control rising inflation as shown in Figure 4, area #1. While the liquidity provided by ACC central banks was falling, it still provided enough space to not only avoid a recession but also gradually decrease the cost of CBRT's funding rate in 2014 and 2015. Thanks to capital inflows, therefore, the AKP government was able to overcome the first economic bottleneck of the post-2013 period, even though there was a contraction of GDP on quarter-to-quarter change in the second quarter of 2014, as shown in Figure 5.

Figure 4. Three episodes of intensifying crisis tendencies in Turkey (2013/1 - 2019/2)



Source: Prepared by the authors based on CBRT database, URL: https://evds2.tcmb.gov.tr/ 12.03.2019

The failed coup attempt provoked the second episode of the intensification of crisis tendencies in mid-2016. To counter the impact of a small currency shock and interest rate hike, policymakers resorted to state-sponsored credit expansion from late 2016 onwards. The aim was not only to avoid economic recession but also to consolidate political support before the critical 2017 referendum on political regime change. The economic strategy to overcome crisis tendencies in this second episode was based on tremendous support to the small and medium-sized enterprises by providing three-year loans with no payments in the first year.

[37] For a comparative analysis of the political crisis see C. Tuğal, *The Fall of the Turkish Model: How the Arab Uprisings Brought Down Islamic Liberalism*, Verso: London, 2016.

Policymakers also revitalized the Credit Guarantee Fund (CGF) mechanism, which is based on reducing the amount to be allocated by commercial banks for collateral. The Turkish Treasury pledged 25 billion TL in 2017 as collateral, implying 250 billion TL in fresh loans (8 per cent of Turkish GDP at that time) to Turkish firms.[38] In case of default, the losses would be partially absorbed by the Turkish state while creditor banks would attempt to sell the non-liquid collateral of the borrower.[39]

In short, the CGF was used to partly socialize the financial risks of these loans. Nominal credit volume expansion, with the help of the CGF mechanism, amounted to 21 per cent, implying that the AKP government overcame this second economic bottleneck by state-sponsored credit expansion.[40] However, despite all the government's efforts to sustain lower interest rates, a sharp interest rate increase occurred in 2017, as shown in Figure 4, area #2. Boosting the credit market also had the cost of a greater current account deficit and higher inflation rates in 2017. Despite currency stabilization in the first half of 2017, the TL depreciated 20.5 per cent against the USD from mid-2016 to the end of 2017.[41] Figure 5 reflects the consequences of policy responses for GDP growth. The sharp contraction in the third quarter of 2016 was an alarming sign for the AKP. Its strategy of postponing the crisis before the crucial constitutional referendum for regime change (held on 16 April 2017) resulted in a strong recovery, albeit very short lived.

The third episode resulted from both global financial tightening in 2018 and the protracted impact of the ways in which previous episodes had been overcome. Prior to the 24 June 2018 presidential and parliamentary elections, political uncertainty increased and became uncertainty over the new political and economic structure since the long process of change in the political regime was to be completed after the elections of June 24 if Erdoğan and his alliance with the far-right Nationalist Movement Party (MHP) won. The peak of the currency crisis came when political tension between Turkey and the USA escalated in August 2018 (the TL lost 23 per cent of its value against the USD in August alone and volatility ensued)[42] and the CBRT had to increase its weighted average cost of funding from 12.75 per cent in January to 24 per cent in September, as shown in Figure 4, area #3. While the August 2018 currency crisis was definitely a strong catalyst, the Turkish economy was already cooling. GDP growth on a quarter to quarter basis, shown in Figure 5, indicates that there was zero growth in the second quarter of 2018, prior to the currency crisis.

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[38] TC Başbakanlık, 'Kredi Garanti Kurumlarına Sağlanan Hazine Desteğine İlişkin Kararda Değişiklik Yapılmasına Dair Karar', *Resmi Gazete*, 10 March 2017, http://www.resmigazete.gov.tr/eskiler/2017/03/20170310-11.pdf, (accessed on 12 March 2019)

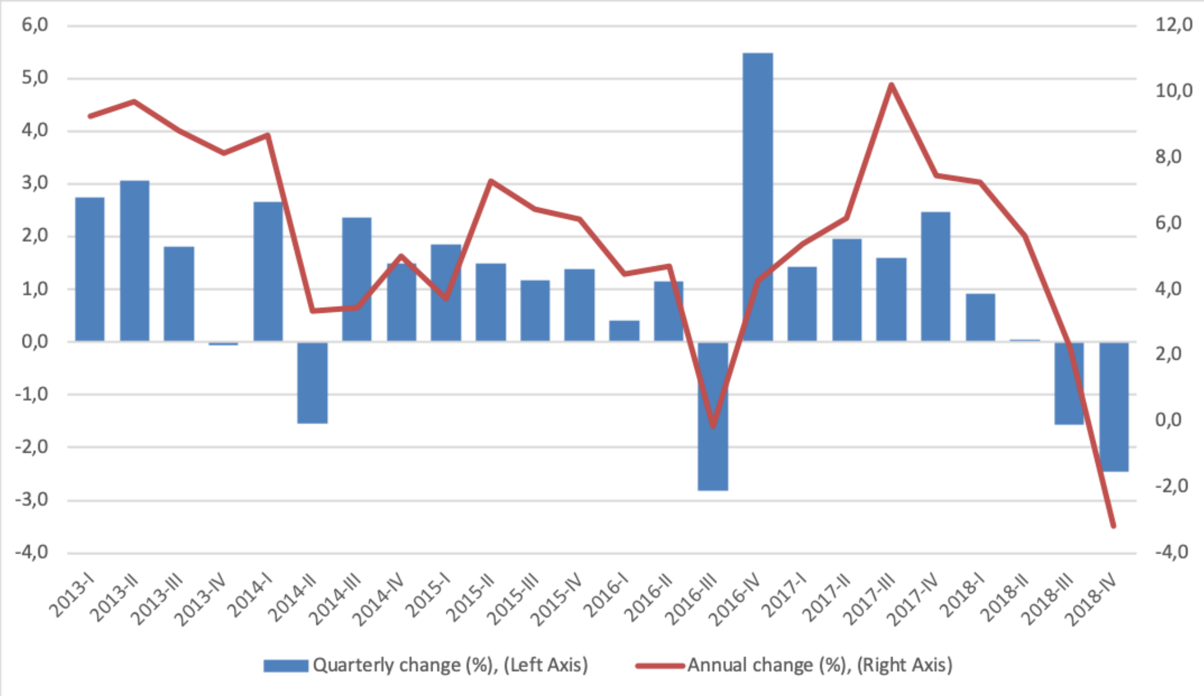
[39] A. R. Güngen, 'Vom Regen in die Traufe? Die wirtschaftspolitischen Präferenzen der AKP und ihre Auswirkungen seit dem Putschversuch', İ. Ataç, M. Fanizadeh and V. Ağar (eds.) *Anthologie: Nach dem Putsch. 16 Bemerkungen zur 'neuen' Türkei*, Vienna: Vienna Institute for International Dialogue and Cooperation (VIDC), pp. 124-138.

[40] Statistics on credit volume can be accessed *via* the bulletins of the Banking Regulation and Supervision Agency (http://ebulten.bddk.org.tr/haftalikbulten/).

[41] We used CBRT data for USD/TL to calculate TL depreciation.

[42] Ü. Akçay and A. R. Güngen, 'Lira's downfall is a symptom: The political economy of Turkey's crisis', *Critical Macro*. 18.08.2018, https://criticalfinance.org/2018/08/18/liras-downfall-is-a-symptom-the-political-economy-of-turkeys-crisis/ (accessed on 23 December 2018).

Figure 5. Turkey's Gross Domestic Product (percentage change between 2013 and 2018)



Source: Prepared by the authors based on the Turkish Statistical Institute database using seasonally and calendar-adjusted data, URL:

http://www.tuik.gov.tr/PreHaberBultenleri.do?id=30886 12.03.2019

The balance of payments data indicate that net capital inflows dropped significantly in 2018 before turning negative in both March and June. It is however, important to underline that the portfolio outflows of non-residents in March, May and June would still have been less damaging for the economy given their small amounts relative to the portfolio outflows by residents in the same months. According to CBRT data, residents not only continued to invest in foreign stocks and bonds in a similar tempo to previous months but also transferred abroad massive amounts of their savings through banks. Between May and August 2018, residents transferred 17.4 billion USD of their savings abroad, aggravating Turkey's financial slide while investing in foreign bonds and stocks and depositing their savings abroad.[43] From the beginning of financial tightening for Turkey in March to October 2018, residents' portfolios and other investments abroad reached 17.8 billion USD (see Table 1 below). This phenomenon is reminiscent of the residents' responses back in 2008-09, when the waves of the financial crisis hit the Turkish economy hard. The amounts are however unprecedented when considered on a monthly basis and add a relatively new dimension to the existing correlation

[43] This amount is the sum of residents' investments into foreign bonds and stocks, and their savings deposited abroad, which actually comprised the lion's share of the 17.4 billion USD, according to CBRT data.

between net foreign flows and GDP growth observable across the board following capital account liberalization.

While net foreign inflows into Turkey may have slowed due to global financial conditions, net resident money outflows have aggravated the dire financing needs of the economy. Thus, the Turkish currency crisis of 2018 differs from the 2001 and 2008-09 crises. The sudden stop scenario highlights the importance of capital flows for emerging markets. As Eichengreen and Gupta note, the mechanism of a sudden stop functions as follows: "The exchange rate depreciates, reserves decline, and equity prices fall. GDP growth then decelerates, investment slows, and the current account strengthens."[44]

Table 1. Change in Capital Flows, Reserves and Net Errors and Omissions

Change in Capital Flows, Reserves and Net Errors and Omissions			
Million USD	**2017 (March - October)**	**2018 (March - October)**	**Difference (+, -)**
Net Foreign Direct Investment	8630	9345	(+) 715
Net Foreign Portfolio Investment	22346	-6532	(-) 28878
Residents' Direct Investment Abroad	1583	2060	(+) 477
Residents' Portfolio and Other Investments Abroad	-1409	17892	(+) 19301
Change in Reserves	5993	-19284	(-) 25277
Net Errors and Omissions	3297	17188	(+) 13891

Source: Prepared by the authors based on the CBRT data, 14.3.2019

In the 2018 currency crisis, the sudden stop in spring 2018 was accompanied by radical increases in resident money outflows. Notably, total capital outflows in August mainly stemmed from money transferred abroad by Turkish citizens. Having said this, we should add that the remaining parts of the mechanism continue. Despite a 13 per cent appreciation of the TL against the USD from early September to early December, Turkish reserves were depleted, economic stagnation turned into recession in the second half of 2018 and the current account balance strengthened rapidly. Unregistered capital inflows in the financial account reached their highest annual level in Turkish history in 2018, avoiding further collapse of the currency.[45]

[44] B. Eichengreen and P. Gupta, 'Managing sudden stops', *World Bank*, Policy Research Working Paper 7639, 2016, URL: http://documents.worldbank.org/curated/en/877591468186563349/pdf/WPS7639.pdf, (accessed on 18 September 2018), p. 3.

[45] CBRT, 'Balance of Payments Analytic Presentation', https://evds2.tcmb.gov.tr/index.php?/evds/serieMarket (accessed on 13 March 2019)

Responses to the currency crisis: the government's so-called 'rebalancing' narrative

Turkish policymakers framed the current economic turmoil with reference to a narrative stressing the 'rebalancing of the economy', which implies that economic difficulties can largely be attributed to business cycles and international economic imbalances. According to this official framework, positive developments in the current account are a sign of rebalancing rather than economic recession. However, this framework is supported by neither a theoretical approach nor empirical data. Instead, used as propaganda material by the Erdoğan administration before the local elections of 31 March 2019, rebalancing became a buzz word for policymakers. In reality, policymakers adopted three responses to contain the crisis and its spill-over effects.

The first was stabilization of the TL, which consisted of a dramatic increase in interest rates in September 2018 and the announcement of the New Economic Programme (NEP) as the key document outlining the main roadmap of policy responses. According to the NEP, the Turkish economy would not experience a recession; rather it would grow 2.3 per cent in 2019 while 2018 to 2020 would be 'rebalancing' years during which fiscal discipline would accompany economic advances. However, it has since become clear that the NEP's prediction for 2018 GDP growth was wrong as TURKSTAT reported 2.6 per cent official year-on-year growth for 2018, well below the NEP's prediction of 3.8 per cent. The NEP also foresaw a transformation in manufacturing and export sectors towards increasing 'value added' production in the Turkish economy, notwithstanding the ongoing radical decline in gross capital formation.[46] However, the major importance of the NEP resides in its explicit commitment to fiscal discipline and its portrayal of the deepening of financial markets as a remedy.

The second response consisted of various debt restructuring schemes. The process for corporations started before the currency crisis before spreading across almost all sectors, including construction, shoemaking, energy, and transportation. The Banks Association of Turkey published a debt restructuring scheme in October 2018 to smooth the process while Turkish banks entered into negotiations with corporations, resulting in restructuring worth 20 billion USD in 2018. Legal complexities and the rush for concordat and restructuring, however, made it necessary to revise the legal framework in December. Minister of Trade, Ruhsar Pekcan, stated that a striking number of 856 firms applied for concordat in 2018,[47] but the number of applicants should have been much higher since the legal change in December (via Law no 7155) made it much harder for corporations to benefit from concordat opportunities. Consequently, non-performing loans increased rapidly in the first months of 2019.

Policymakers also converted the Turkey Development Bank, which is a state-owned development bank, into a financial institution exempt from banking regulations. While this might prove handy in socializing new financial risks in the near future, its main use in the post-crisis months was the securitization of housing loans in December 2018. This endeavor, though

[46] Hazine ve Maliye Bakanlığı, Yeni Ekonomi Programı, 2019-2021 (Orta Vadeli Program), HMB: Ankara.
[47] Ruhsar Pekcan's statement in Dünya Gazetesi, 'Konkordato ilan eden şirket sayısı açıklandı', https://goo.gl/U8Xh9t, 13 December 2018, (accessed on 1 February 2019).

limited in scope (with a volume of 3.15 billion TL), revitalized the asset-backed securities market while securitization helped state-owned banks postpone liquidity problems to keep extending loans despite high interest rates.[48] Since the credit crunch could not be overcome by late 2018 and households were cutting down on spending, the BRSA also revised credit card instalment regulations to allow households to have more instalments. The main intervention in the household debt market, however, was the use of Ziraat (Turkey's biggest state-owned commercial bank) to restructure household credit card debt with interest rates below the market average. While there is no data regarding the amount of debt restructured by Ziraat in the first months of 2019, comparing the monthly income loss payments transferred to the bank from the Treasury with previous amounts will provide clues in the upcoming months.

The third policy response was a temporary reduction of taxes for sectors experiencing economic difficulties. In reducing tax rates in the automotive, furniture and household appliances sectors for the last 3 months of 2018 (then extended further until local elections), government policymakers pushed for discounts and tried to stimulate the domestic market.[49] As can be seen clearly, the policy responses had two main aims: (i) containing the spill-over effects of the currency crisis prior to the local elections set for 31 March 2019 and (ii) recovering economic growth as fast as possible. Additional notable aspects are the use of securitization mechanisms to fight the credit crunch and recurrent emphases on further financial deepening. Despite previous discussions within the Erdoğan administration regarding Turkey's economic model and development trajectory,[50] crisis management in the second half of 2018 revealed a persistent hegemony of market-oriented perspectives and, despite rhetorical animosity, a renewed commitment to dependent financialization.

Conclusion

Dependent financialization in Turkey can be summarized in terms of the emergence of an economic structure in which the economic activity increasingly depends on capital inflows. While money lent from international financial markets mainly financed state borrowing in the 1990s, these inflows helped TL to appreciate and eroded the competitive power of many corporations in the longer term. Credit expansion in Turkey, starting in the early 2000s, brought formerly excluded segments of society into the loan market. While the state decision in 2009 to make it easier to borrow in foreign exchange terms boosted USD-denominated debts of non-financial corporations, there were increasing attempts to deepen the financial

[48] Ministry of Finance and Treasury's announcement in Anadolu Ajansı, 'Türkiye'nin en büyük VDMK ihracına büyük talep', https://www.aa.com.tr/tr/ekonomi/turkiyenin-en-buyuk-vdmk-ihracina-buyuk-talep/1332141, 7 December 2018, (accessed on 13 March 2019).

[49] Berat Albayrak's statement in Anadolu Ajansı, 'Bakan Albayrak vergi indirimi paketini açıkladı', https://www.aa.com.tr/tr/ekonomi/bakan-albayrak-vergi-indirim-paketini-acikladi/1299002, 31 October 2018, (accessed on 13 March 2019).

[50] A. R. Güngen and Ü. Akçay 'Türkiye'de Ekonomi Politikasında Arayışlar, Çıkmazlar ve Alternatifler', in T. Tören and M. Kutun (eds.) *Yeni Türkiye? Kapitalizm, Devlet ve Sınıflar*, İstanbul: SAV, 2016, pp. 246-279.

markets throughout the AKP period. AKP supported a deepening of the corporate bond market, revised its decision-making processes and legal framework regarding the financial sector and explicitly pushed for further securitization in the post-2008 period. Though financialization in Turkey in the post-2001 period was based on an increased borrowing capacity of both households and corporations, increasingly coupled with the new forms of fictitious capital devised in the last decade, there were limits to financialization in Turkish context.

Interest rates, higher relative to the ACCs, may not impose barriers against financial deepening and more inclusive forms of financialization in the ECCs, as long as capital inflows continue. If, however, global financial conditions tighten, making it harder to access cheap sources of finance, ECC economic actors start to face limits. While the ECCs, under such circumstances, need to offer increasingly higher interest rates to attract capital, it becomes more difficult for households and corporations to roll over their debt. Against a backdrop of a credit squeeze, maturity mismatches in both the financial and non-financial corporations become more obvious. Allowing the currency to depreciate amidst financial tightening does not necessarily provide a route for quick recovery, since many products have lost their competitive edge during the previous period. Dependent financialization leads to boom-bust cycles in ECCs and may cause prolonged recessions depending on global liquidity conditions and the ability of policymakers to make people pay for the cost of economic busts.

For many scholars of Turkey, re-institutionalization and regulations in the post-2001 period promoted rapid economic growth while policy choices in the last couple of years have caused an ominous economic collapse. Our perspective on the other hand, provides a longer-term account underlining the fragility of the economy throughout the neoliberal financialization period. We argue that this dependent financialization framework provides a better understanding of the recurrent nature of economic turmoil over the last couple of years. We also suggest that the currency crisis of 2018 should be seen as a catalyst for Turkey's 2018-2019 economic crisis. The 2018 currency crisis did indeed prove to be the final act in the slow-motion drift that began with the first signs of change in global liquidity conditions. Dependent financialization may have institutionalized the social power of finance capital in Turkey but the growth of market finance and drawing more people and corporations into the financial markets inevitably created greater volatility. The government's response to the 2018-2019 crisis, however, indicates the continuing commitment of Turkey's policymakers to the model that led to the crisis in the first place.

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