TURKEY'S UNHEARD VOICES

The Impact of Macroeconomic Policies on Socio-Economic Development in Turkey

POLITICS

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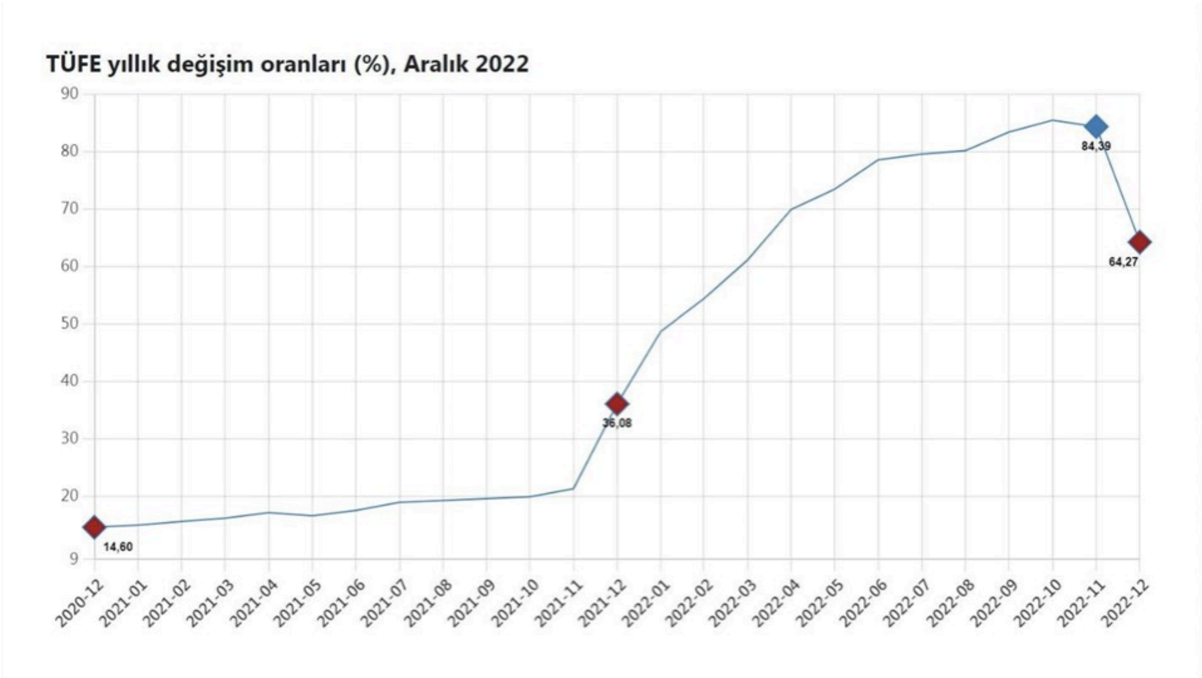
Abstract

This report analyzes the impact of macroeconomic policies implemented in Turkey between 2021 and 2024 on socio-economic development. Turkey's macroeconomic outlook has been shaped by global developments and government-driven policies. Key macroeconomic indicators include prices, national income, production, fixed capital investments, foreign trade, public finance, monetary banking, and the capital market. This report focuses in detail on prices and national income.

Inflation Dynamics in Turkey: Interest Rate Policies, Structural Factors, and Global Effects

Inflation rate calculations are based on the Consumer Price Index (CPI), which reflects the price changes of goods over a specific period. The CPI tracks the prices of various goods and services (e.g., food, transportation, housing, health, education) consumed by households over time. The inflation rate progresses in parallel with the price increases observed in the CPI.



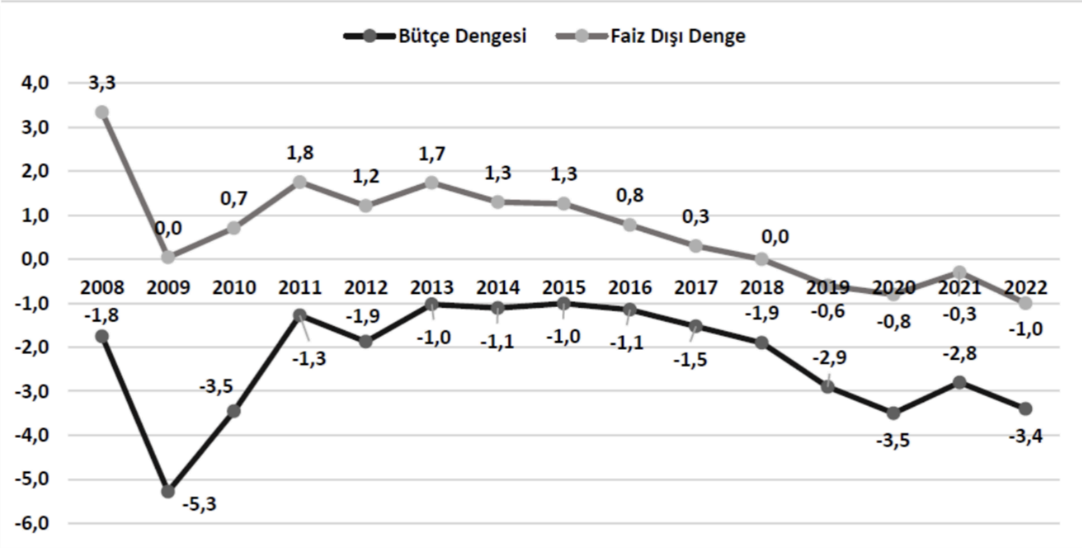
As shown in the table above, the average CPI rate for a product rose from 20% to 80% as of November 2021. This sudden change has multiple causes. Primarily, changes in monetary policy must be considered. At the end of 2021, the Central Bank of the Republic of Turkey (CBRT) decided to lower policy interest rates. Lower interest rates encouraged credit expansion, leading to increased demand and consequently a rise in inflation. This shift in monetary policy caused real interest rates to fall below inflation rates, resulting in negative real interest rates. Such a situation increased demand for foreign currency, causing the Turkish Lira to lose value. Thus, monetary policy changes played a critical role in rising inflation. According to many economists, the main trigger for the inflation crisis was the decision to lower interest rates in November 2021.

With the rise in inflation, purchasing power declined significantly. Purchasing power refers to the quantity of goods and services a person can buy with a certain income level. In other words, it indicates the value of a currency and how much can be acquired with it. A decline in the value of the Turkish Lira, coupled with a continuous rise in inflation, deeply affected the public. These effects are elaborated further in the report.

In addition to shifting monetary policy, deep-rooted structural problems and global developments also contributed to the rapid inflation increase. The Russia-Ukraine war, which began in 2022, caused major disruptions in global supply chains. Prior to the war, Ukraine was a critical raw material supplier for both Europe and the U.S., providing about 15% of the global grain supply. However, with Russia's seizure of Ukrainian Black Sea ports, exports from Ukraine were largely disrupted, leading to supply shortages and rising prices globally. Turkey's sensitive economy was particularly affected by these increases in raw material prices.

Looking at foreign trade, in 2024 Turkey's import value reached 344.1 billion USD, while exports totaled 261.9 billion USD. The country's import-dependent economic structure deepened its economic vulnerability. As previously mentioned, the change in interest rate policy increased demand for foreign currency, leading to a depreciation of the Turkish Lira. This depreciation significantly reduced the purchasing power for imported goods.
Another critical global development was the Covid-19 crisis. During the pandemic, many countries incurred significant budget deficits and rising public debts, leading them to quickly adopt fiscal policy tools. According to IMF data from 2020, Turkey implemented various spending supports such as cash assistance and unemployment benefits, along with numerous tax cuts. However, alongside tax reductions, government banks offered loans below market rates, and transfer expenditures increased. While these measures improved sectoral confidence indices initially damaged by the pandemic, they also placed additional burdens on the budget. The suspension of expansionary fiscal policies and the weakening of fiscal discipline were notable consequences. As a result, budget deficits and public debt burdens increased.
The combination of all these factors intensified inflationary pressures and led to economic fluctuations.

The second key indicator of macroeconomic policy is national income. While national income is usually assessed through indicators such as Gross Domestic Product (GDP), in Turkey, the primary balance is also frequently used in fiscal analyses. The primary balance refers to the difference between government revenues and expenditures, excluding interest payments. This indicator is commonly employed as a measure of fiscal sustainability and budgetary discipline.



When examining the primary balance, it is noteworthy that it remained above zero even during the 2008 global financial crisis, yet began to turn negative in 2019. A negative primary balance, which is a crucial indicator for the sustainability of public debt, signifies that the government is unable to finance its non-interest expenditures through public revenues, indicating difficulties in repaying the principal amount of debt. This fiscal strain gave rise to new financing needs. Starting from April 2020, a range of revenue-increasing measures were implemented, including hikes in customs duties, Special Consumption Tax (ÖTV), Banking and Insurance Transactions Tax (BSMV), and foreign exchange transaction taxes. In addition, public institutions introduced austerity measures to support these policies. However, the resulting economic burden on the budget led to deterioration in macroeconomic indicators. Low-interest credit policies carried out through public banks, in particular, triggered price increases in housing and automobiles, and thus further accelerated inflation.

Following the 2023 elections, a new economic policy called the "Gradual Interest Rate Hike Policy" was adopted to reduce inflation and alleviate financial vulnerabilities.

As part of this policy, the Central Bank raised the policy rate to 42.5% by the end of 2023 to limit exchange rate volatility and the rise in inflation. However, this increase failed to reduce the inflation rate to the expected level. Although the economic plan announced at the beginning of 2024 aimed to bring inflation down to 30%, the actual inflation rate by the end of the year was 49.25%. From a macroeconomic perspective, why did these policies—though theoretically sound—fail to produce the desired outcome in practice? The following sections of this report will explore this question from a sociological perspective.

The Role of Interest Rate Policies and Institutional Structures in Turkey’s Economic Performance

Although alternative policy tools have been utilized since the 2008 global financial crisis, central bank interest rate decisions continue to be the primary determinant of monetary policy stance. Interest rates play a key role in determining both the value of a country’s currency and the flow of international investments. Therefore, variations in central bank interest rate decisions are highly significant for the real and financial sectors through their impact on the relative value of national currencies.

As discussed in the introduction, one of the main reasons behind the rapid rise in inflation was the reduction in interest rates. Similarly, in an attempt to contain inflation, monetary policy was revised to increase interest rates. The main goal of these policies was to raise interest rates above the inflation rate, thereby encouraging individuals and investors to shift toward the Turkish Lira. On January 19, 2023, the interest rate was set at 9%, and by December 21, 2023, it had been increased to 42.5%.
However, the failure of this policy stems from the fact that Turkey’s social and economic structures did not adequately support the conditions necessary for its implementation. For economic policy changes to be effective and sustainable, they must not be limited to financial measures alone; rather, they must be supported by simultaneous reforms in political, social, and institutional structures. If these reforms do not complement one another, the economic measures taken will only offer short-term solutions and fail to create long-term, lasting impacts.

In the book Why Nations Fail, published by Professor Dr. Daron Acemoğlu, who was awarded the Nobel Prize in Economics in 2024, the main argument is that the key factor determining a country's economic success is its political and social institutions. The book divides institutions into two categories: inclusive institutions, which encourage broad participation, protect property rights, support innovation, and ensure economic growth; and extractive institutions, which concentrate power and wealth in the hands of an elite group, exploit resources, and increase inequality. It is also emphasized that political power should have a centralized structure but should not turn into excessive authoritarianism. Historically, how institutions evolve during "critical junctures" determines the fate of a nation. While inclusive institutions promote creative destruction, extractive institutions hinder it and lead to economic stagnation. The authors argue that geography, culture, or ignorance are not sufficient to explain a country's failure; instead, institutions are the determining factor. Ultimately, economic progress drives social development—and vice versa. A country cannot achieve meaningful social development without adequate economic infrastructure, and likewise, no country can attain sustained economic growth without the necessary social foundations.